

**BANKING  
THAT  
WORKS.**

# HSH NORD- BANK GROUP AT A GLANCE.

## INCOME STATEMENT in (€ m)

	2016	2015
Net income before restructuring	445	954
Net income before taxes	121	450
Group net result	69	98

## BALANCE SHEET in (€ bn)

	31.12.2016	31.12.2015
Equity	5.0	4.9
Total assets	84.4	97.0
Business volume	93.2	106.2

## CAPITAL RATIOS<sup>1)</sup> & LEVERAGE RATIO (%)

	31.12.2016	31.12.2015
CET1 ratio	14.1	12.3
Tier 1 capital ratio	18.7	16.4
Regulatory capital ratio	24.8	20.6
Leverage ratio	7.0	6.3

## EMPLOYEES (computed on full-time equivalent basis)

	31.12.2016	31.12.2015
Total	2,164	2,384
Germany	2,068	2,264
Abroad	96	120

## LONG-TERM RATINGS

	Unguaranteed liabilities	Guaranteed liabilities <sup>2)</sup>	Public-sector Pfandbriefe	Mortgage Pfandbriefe	Ship Pfandbriefe
Moody's	Baa3 dev. <sup>3)</sup>	Aa1 stable	Aa2	Aa 3	Baa 2
Fitch	BBB- neg.	AAA stable	-	-	-

<sup>1)</sup> According to the same period calculation under the CRR rules.

<sup>2)</sup> Liabilities covered by guarantor's liability (Gewährträgerhaftung).

<sup>3)</sup> dev.: Developing



# GOOD WORK. GOOD FIGURES.

Successful for and with our clients, further improvement in our own structures, substantial wind-down of legacy assets and certainty about the privatisation process due to the final EU decision – 2016 was eventful as well as pointing the way for **HSH NORDBANK**. It was a year during which we gave an impressive demonstration of our new operational strength – new business totalling €8.9 billion is no mean feat in a demanding setting. And this was without breaching our own quite strict risk parameters. Which shows: our Core Bank is healthy and full of vitality. In short: Good work – which is why this is the heading of our 2016 annual report.

But of course, we know that although 2016 was an important year, the decisive event will be the change in ownership scheduled for 2018. One thing is clear: in 2017 we will again do all it takes to make the change a success – among other things, by proving just how good HSH Nordbank is at doing their business. Among our clients we stand for competence, reliability and speed – in short: for **GOOD WORK**.

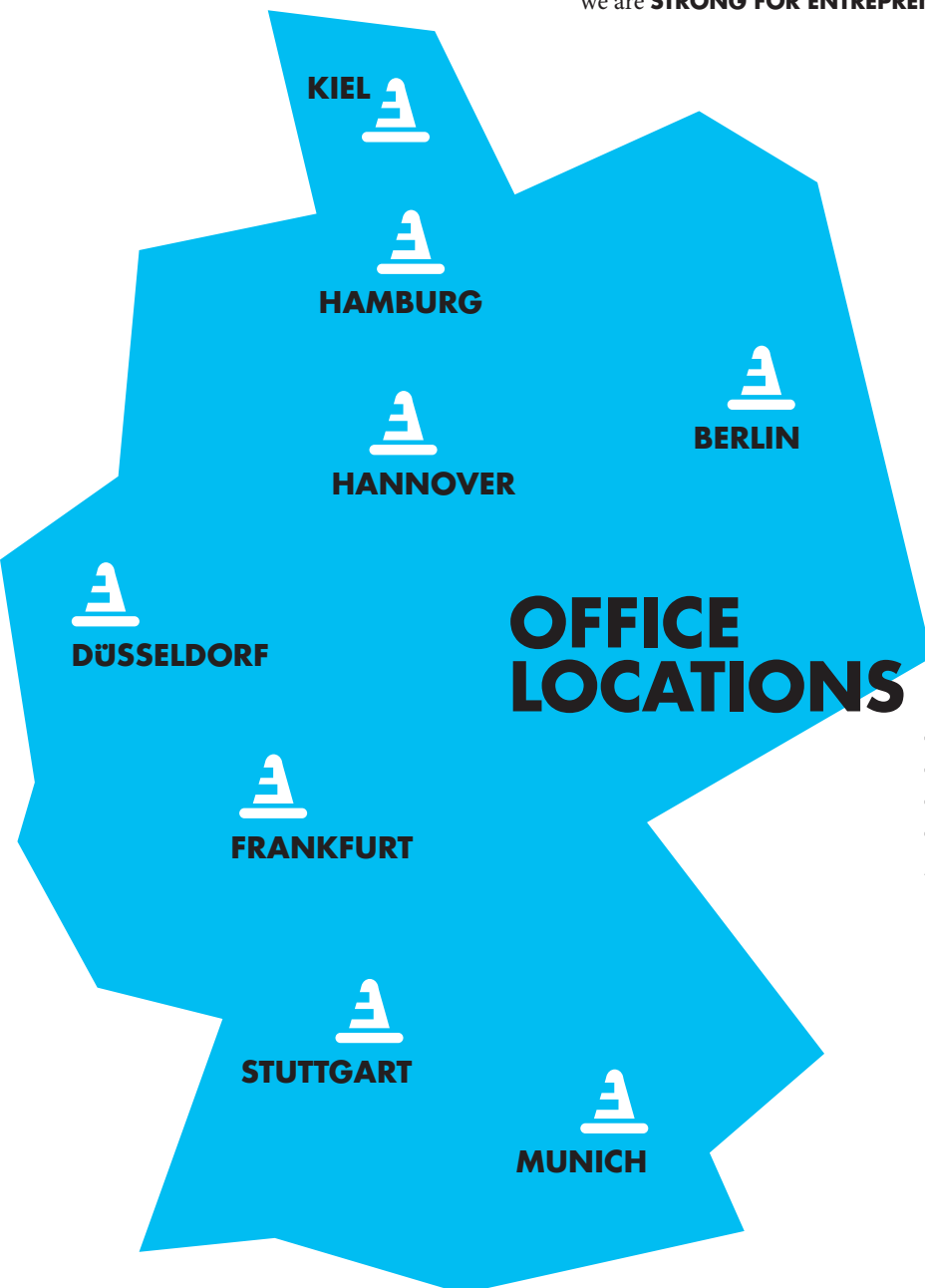
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# ROLLING UP OUR SLEEVES FOR ENTREPRENEURS

We are the 'Bank for entrepreneurs' – the Bank for people with foresight, passion and initiative. We are where our clients are: in our home region of North Germany, in the metropolitan regions of Germany and in selected foreign locations. Here we offer companies tailor-made finance solutions and assist them with our broad-based sector expertise. **HSH NORDBANK** is one of the leaders in Germany for real estate financing. We are among the top players in Europe when it comes to realising renewable energy projects, while we have a long tradition of expertise in the maritime industry. The Corporate Client business is an important pillar of our Bank, which we aim to strengthen further: through commitment, single-minded determination and reliability. We seek to convince through performance because we are **STRONG FOR ENTREPRENEURS**.



- + LUXEMBOURG
- + ATHENS
- + HONG KONG, SINGAPORE
- + NEW YORK\*

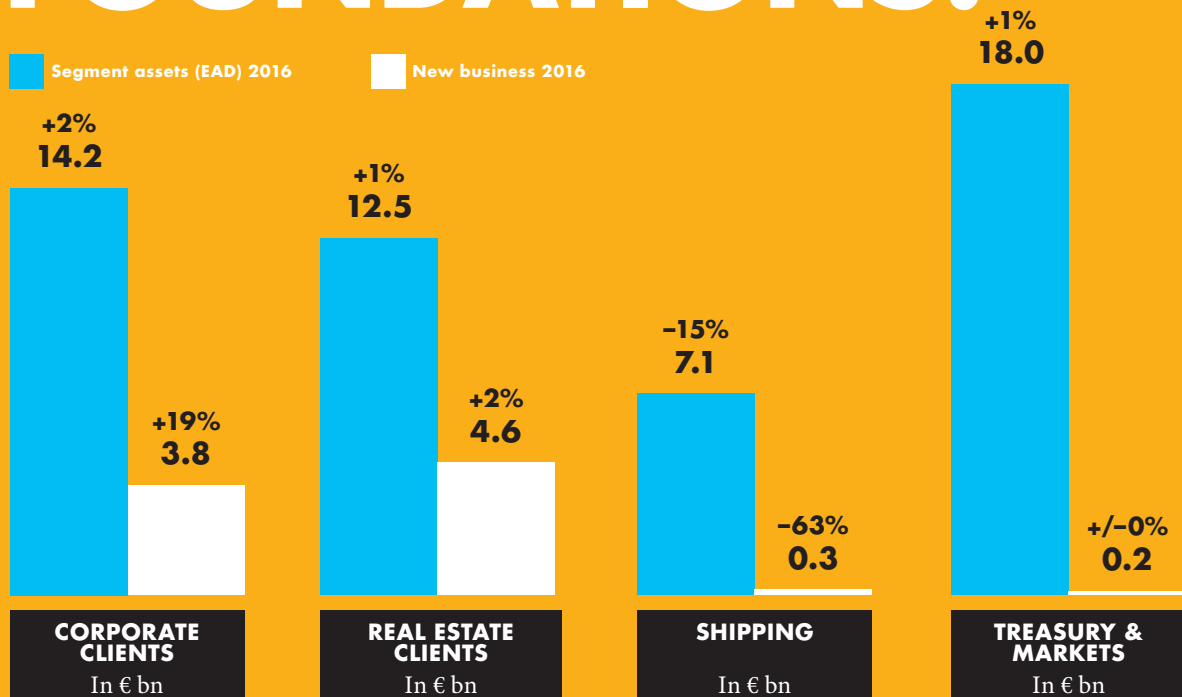
\* Representative office since the end of 2015

# R SLEEVES FOR

## OPPORTUNITIES UP, RISKS DOWN.

- ◆ **CLEARER OUTLOOK FOR THE FUTURE:** Following the EU Commission’s final decision in the state aid proceedings, the underlying conditions of the change in ownership, scheduled to take place in 2018, have now been set.
- ◆ **STRUCTURES FURTHER IMPROVED:** We are systematically working to improve our internal structures. Our aim has been to become more reliable, faster and more accurate, all the while maintaining clear cost control. We have succeeded in doing so.
- ◆ **OPERATIONAL STRENGTH DEMONSTRATED:** New business worth €8.9 billion demonstrates our competitiveness and shows that our business strategy is working.
- ◆ **LEGACY ASSETS REDUCED:** In 2016, we wound down legacy assets amounting to about ten billion euros in EAD (exposure at default), with five billion euros through the portfolio transfer agreed with the EU to the AöR (Anstalt des öffentlichen Rechts, institution under public law) of the federal states. And roughly as much again through our ongoing wind-down programmes.

# HSH NORDBANK’S FOUNDATIONS.



# FOUR ME ONE FOR

**LADIES AND GENTLEMEN,** 2016 was marked by further strengthening of our operational business, the final decision in the EU proceedings and preparations for the planned change of ownership in 2018. At the same time, we have systematically improved our internal processes. This includes readjusting our Risk department and combining market departments to form one potent unit. As a result, our Management Board has become leaner. Furthermore, we have enhanced the transparency and availability of our market and risk data – the keywords are: overall bank management system and ‘transparent bank’.

More than ever we see it as our task to adapt the organisation within our Bank continuously to meet the mounting challenges. This is necessary not only to survive in what is an intense competitive setting, but also to lay the foundations for a positive development of our Bank over the long term.

In 2016, we demonstrated once again that our Core Bank is full of vitality and that it enjoys an excellent position in the market. Our net income for the year impressively underscores this point: at €639 million, our Core Bank’s pre-tax profit – before consolidation effects – was more than three times the 2015 figure, while Group earnings before taxes came to €121 million. New business totalled €8.9 billion and matched the previous year’s strong level. The Corporate Clients business area stood out as it expanded its new business by around 20 per cent. We are among the top three providers of commercial real estate finance in Germany and rank among the top five in Europe when it comes to financing alternative energy sources, specifically wind farms and solar parks. HSH Nordbank has also made further progress in terms of capital and liquidity: our Com-

# EN, REWORD.

mon Equity Tier 1 (CET1 phased in) ratio totals a solid 14.1 per cent, meeting the market participants' expectations and contributing to the stability of our rating. Another important point: in 2016, we made further progress in winding down legacy loans dating from 2009. All told, we have wound down ten billion euros (EAD) – five billion euros through the transfer to the institution under public law (AöR) of the federal states and an additional five billion euros as part of our day-to-day business. This wind-down will continue within the narrowly defined limits of the guarantee. We are very aware of how heavily these legacy

assets in conjunction with the guarantee will still weigh on our Company going forward.

On termination of the EU proceedings, HSH Nordbank was able once again to make greater use of its operational strength in 2016. The combination of sector knowledge, good processes and excellent contacts with the players in growth industries has created good opportunities for the Bank, despite all the uncertainties that need to be considered. The new shareholders will boldly take advantage of these opportunities after 2018.

Yours sincerely



Stefan Ermisch  
Chief Executive Officer



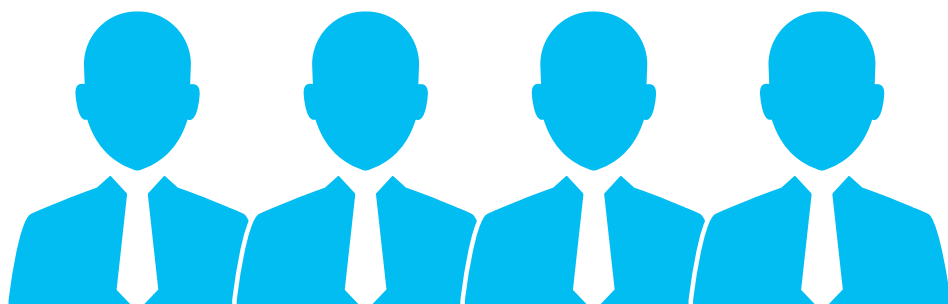
Oliver Gatzke  
Chief Financial Officer



Ulrik Lackschewitz  
Chief Risk Officer



Torsten Temp  
Board member for Markets





# TARGETS REACHED. KEEP GO- ING.

**HSH Nordbank closed out 2016 with a Group profit of €121 million. How do you rate the year?**

**Stefan Ermisch:** 2016 was a good year for the Bank. This is not only due to the fact that we can be pleased with our result as a whole. More importantly, perhaps, we have managed to make the Bank as a whole more effective and more competitive.

**What does this mean specifically?**

**Stefan Ermisch:** The work of a bank now needs to be efficient, fast, neat and low-cost. This is something we have been working on for years; it's an ongoing process. Those who don't stay with it get ruled out. The competition in our industry is very tough. Hence permanent improvement and change are fundamental requirements for success. At the same time, we have shown that our Core Bank is able to hold up excellently in a heavily contested market, not only in our northern German home region but also beyond. This is an important message that is reflected in the results: in 2016, our Core Bank generated earnings before taxes of €639 million. This good result was possible only because our colleagues worked with a great deal of commitment. All in all, we laid the foundations for long-term success in 2016.

**How did new business go?**

**Stefan Ermisch:** All told, we concluded new business with a volume of €8.9 billion and are thus on a par with last year's strong figure – but this time with a smaller team. The existing volume in the Core Bank remained largely constant in 2016: the Corporate Clients business area generated 14.2, Real Estate Clients 12.5 and Shipping 7 billion euros.

**What impact did the emphasis on focal industries have on new business?**

**Stefan Ermisch:** A consistently positive one. In many areas, we continued to expand or consolidate our position in the market. In the real estate segment, we generated new business worth €4.6 billion and thus slightly exceeded the the previous year's strong figure. Here we are among the top 3 in Germany. In our Corporate Clients business area, we increased new business by 20 per cent to €3.8 billion. In renewable energies, we are among the top 5 in Europe; our new business in this area in 2016 was well in excess of €1 billion.

**May 2016 saw the EU's final decision in the state aid proceedings. A change in ownership is planned by the end of February 2018. What does this mean for the Bank?**

**Stefan Ermisch:** We see this major change as an opportunity. The banking sector is undergoing fundamental change. The industry has to deal not only with strict regulatory requirements, but also with the strain resulting from the setting of low interest rates. At the same time, traditional business models need to be transposed to the digital world. New owners will understand the opportunities that this setting offers and make bold use of them. On top of this with HSH, they will be able to take possession of a bank well established in the market with an excellent organisational structure. But just so we can get this right: the sale scheduled for 2018 is being managed by the federal states of Hamburg and Schleswig-Holstein. But of course, we as the Bank will support them to the best of our ability.





Stefan Ermisch,  
Chief Executive Officer

CORE BANK PRE-TAX INCOME OF  
**€639 MILLION**

**Is the Bank to be sold as a whole?**

**Stefan Ermisch:** That is the aim. But syndicates may also be formed.

**Who might be interested in HSH Nordbank?**

**Stefan Ermisch:** At present, investors have the opportunity to acquire a well-established commercial bank in a region and country with a strong economy. This Bank provides future and growth prospects. Of course, investors will take a very close look because it is not every day that such an offer comes up. For us, it is important not to let up in our day-to-day operations – quite the opposite. We must continue to honour our service promise to the market and to our clients on an everyday basis. And that is what we will do. Our colleagues have always demonstrated their ability to not only keep on top of business in turbulent times, but also to rise to peak form. We stand for the ability to handle new challenges successfully time and time again.

**The Core Bank is profitable, but the new owners also have to contend with the Non-Core Bank.**

**Stefan Ermisch:** That's true. Even though we have made genuinely good progress when it comes to reducing our legacy assets, past mistakes made pre-2009 continue to weigh very heavily, particularly so because the shipping sector has been in the throes of a historical crisis ever since. Furthermore, the guarantee dating from 2009 defines very narrow limits for economic scope for action. Both these factors weigh

on us. The entire shipping sector is severely shaken. This is hitting us very hard – like all banks exposed to shipping. Put simply, the Non-Core Bank pools the past mistakes in the form of non-performing loans that to date have been wound down insufficiently, due also to the guarantee. This is not ideal; nevertheless, all parties involved have a duty to find a good solution to these problems in the course of privatisation. We know this, the owners know this, the EU Commission knows this, as does the European Central Bank.

**Are there any parties interested in non-performing loans?**

**Stefan Ermisch:** Yes, they are investors who have specialised in the liquidation of critical portfolios. They take on risks and hope for promising returns. Given the fact that the shipping market has hit absolute rock bottom, this may be a good time to enter it. But these investors have certain prices in mind. Here, it will be important to find an economically feasible path for all involved. Everyone will have to push themselves to their limit to achieve a good result. I am confident that this will be possible.

STRONG  
STRONG





*Stefan Ermisch,  
Chief Executive Officer*

**ONG IN A  
REGION.**

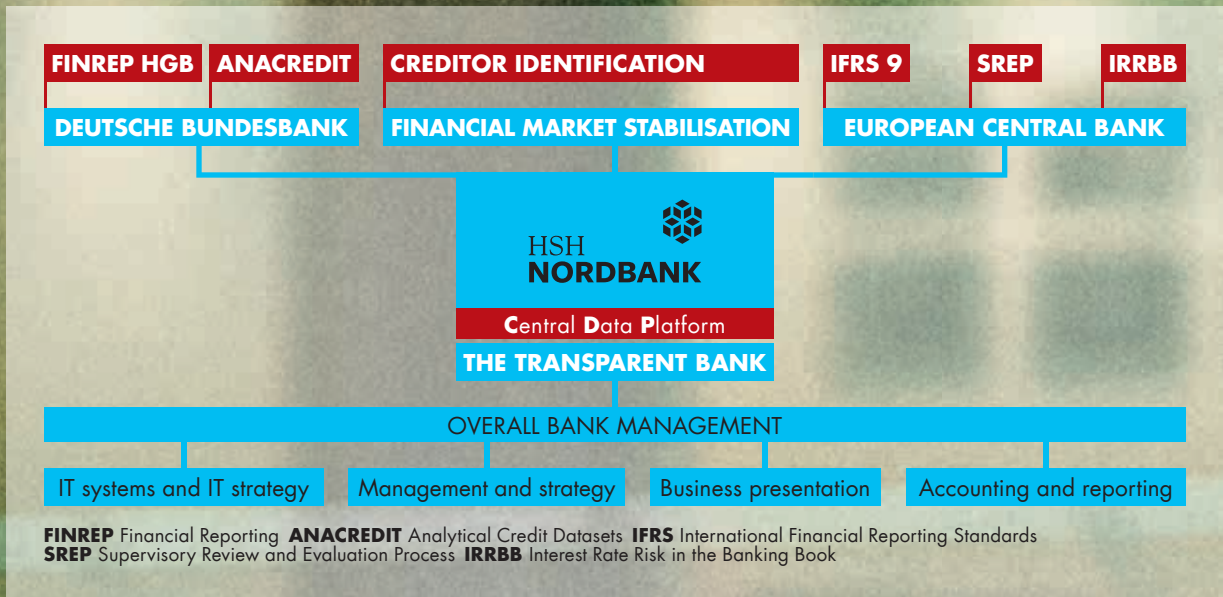




*Oliver Gatzke,  
Chief Financial Officer*

# TRANSPA B





**The regulatory requirements for banks tightened substantially in the wake of the financial crisis. What does this mean for the management of our Bank?**

**Oliver Gatzke:** One main difference is that we no longer look at and manage income, costs, risks, liquidity and capital separately from each other. Now there is an integrated performance and risk management approach. We have a uniform view on all financial, risk and business data. Although this entails considerable effort, it also results in significantly greater transparency. We thus meet our own management requirements as well as those of national and European regulatory authorities. This is designed to avoid a repeat of what happened during the financial markets crisis, when the financial institutions under stress conditions were not always able to manage their risk exposures appropriately.

**What does this management approach mean specifically?**

**Oliver Gatzke:** We work on the basis of the principle of a ‘transparent bank’. This means that we meet the management requirements and the many different regulatory requirements of the European Central Bank and the national regulatory authorities from a single, central data platform. This is a key point, as it allows us to manage all processes from a single source. This way of working combines the entire IT with the strategic management, the business presentation, the accounting and reporting of our Bank. What this means in practical terms is that we are able to obtain financial and risk figures, for example on equity, liquidity or asset quality, virtually in real time and in many cases to pass them on to the management team and the regulatory authorities as part of an automated process, with speed and transparency.

**Do the changes in bank management provide opportunities for our Company?**

**Oliver Gatzke:** Yes, because we will not only become more transparent, but also faster. Also, this integrated view provides a substantially better basis for making decisions. This means that it contributes to solutions that are viable in the long term as well as being forward-looking.

**Why is data procurement and data preparation in the banking business, in particular, so complex?**

**Oliver Gatzke:** The complexity is due to the fact that banks have their eye on three control sets. First, the external accounting data for the balance sheet and preparation of the income statement. Secondly, we report in depth on the business areas, client relationships and individual transactions managed by internal accounting. And finally, there is the supervisory law view of risk and, in tandem with this, the liquidity and capital position. Data from all control sets needs to be brought together. This is most successful if all control sets are fed from the same data platform, as is the case with our Company.

# THE TRANSPARENT BANK.

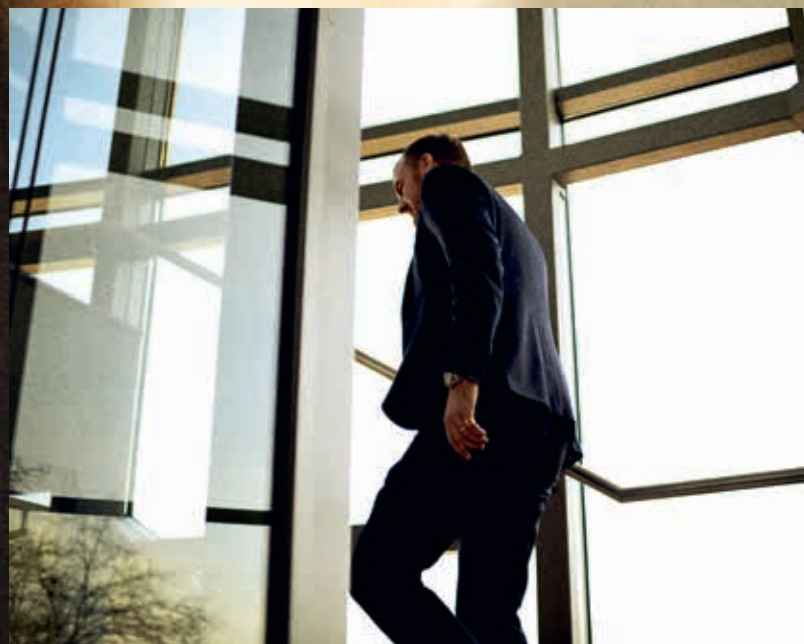
# A CLEAR PICTURE

**Effective 1 November 2016, the former Restructuring Unit (RU) was integrated into the Risk department that you manage. Why?**

**Ulrik Lackschewitz:** The RU was virtually a bank within the Bank, with its own processes, own procedures. There may have been reasons for this structure at the time this unit was set up. But over the long term and in the current situation it was not suitable because it provided no integrated view of the risks. This is something we changed. Integration of what is now the Non-Core Bank means that there are now uniform processes and lending standards; everything is now connected.

**What has changed as a result of the integration?**

**Ulrik Lackschewitz:** Previously, the RU, which by the way did good work, handled everything: analysis, advisory and processing. Now the tasks have been separated: analysis is handled by Credit Risk Management under Jan Lührs-Behncke. The Special Loan Management unit of Jan Erik Groß is responsible for assisting exposures. We no longer have a situation where some colleagues perform analysis and advisory at the same time. This clear separation was also important from MaRisk aspects. All told, this was a major restructuring and one we completed well internally – among other things thanks to the flexibility and strong commitment of our colleagues.



**€10 BILLION (EAD)  
IN LEGACY ASSETS WOUND DOWN**



**How are we dealing with the loans, most of which are non-performing, that are bundled together in the Non-Core Bank?**

**Ulrik Lackschewitz:** We have made major progress when it comes to winding down non-performing loans. We achieved this thanks to our professional management of these portfolios. In some cases, we restructured exposures while in others, we sold off portfolios. All in all, we wound down around ten billion euros (EAD) in this way. We transferred five billion euros to the AöR of the federal states and reduced a further sum of around five billion euros in our day-to-day business. This wind-down process continues; it also includes the sale of our market portfolio.

**What does the pooling of non-performing loans in the Non-Core Bank mean for relationships with our clients?**

**Ulrik Lackschewitz:** We are consistently speaking with one voice. All this leads to more exacting access to our clients. I expect this approach to yield major benefits.



*Ulrik Lackschewitz,  
Chief Risk Officer*



# EXCELLENCE EFFORT WILL



*Torsten Temp,  
Management Board member for Markets*

# EXCELLENT TEAM TALK STRONG TO SELL.

**The market units can look back on 2016 as a good year. What was the decisive factor in this success?**

**Torsten Temp:** We are now characterised by the fact that we provide excellent team service and have a strong will to sell – even under demanding conditions. In 2016, the leadership within the sales department changed and I am now the sole person responsible. And there was the final EU decision in the state aid proceedings, after which we began preparations for the selling process. For the Bank the change in ownership is an opportunity. From a pure sales perspective, however, such changes are usually not an ideal starting point. Nevertheless, we not only achieved, but even exceeded the results we targeted for 2016. And new business worth about €8.9 billion is a strong performance. Our good results are especially gratifying because we had a weak start to 2016. I enjoyed following the catch-up charge. All in all, you are looking at a satisfied head of sales – something you don't see very often.

**What do companies today expect from their bank?**

**Torsten Temp:** The most important issues are speed, competence in the structuring of a loan and reliability. Clients take a good product selection as a given. Our aim is to provide our clients with something akin to a one-stop shop.

**Are you succeeding?**

**Torsten Temp:** I think so, otherwise we would not have gained more than one hundred new clients in the Corporate Clients business area alone. Our clients are rewarding our good performance – this is the feedback we are receiving in conversations. It is also demonstrated by our client surveys.

**Interest rates are low at the moment, while commodity prices and currencies are fluctuating considerably. How important is it to help clients minimise uncertainty factors?**

**Torsten Temp:** For years we have successfully been working to improve the interplay between client relationship managers and product specialists from the capital market. As a result, our clients can hedge interest rates and currencies straightforwardly for their benefit – and we improve our cross-selling ratio.

**Many banks have recently discovered the German SME sector for themselves. What does this mean for HSH Nordbank?**

**Torsten Temp:** The German SME sector has been highly competitive among banks for decades, so this in principle is nothing new. But in the past two years a few non-German banks have joined the fray, quite aggressively, because their home markets tend to still be rather affected by the crisis.

**Does tougher competition mean that banks are prepared to accept greater risks in order to get a look-in?**

**Torsten Temp:** In some areas that is certainly what we are seeing. But we do not do unreasonable business. We apply clear, strict risk standards. And we stick to them. Over the long term this is the right strategy.

Strong for entrepreneurs  
**REAL ESTATE CLIENTS**

**UNDERSTAND** It takes expertise and experience to correctly assess the potential of a location or a property.

**RECOGNISE** As one of the leading banks specialising in real estate, we set up tailored finance in close collaboration with you: from the project idea through to disbursement.

**SHAPE** Rely on one of the top names: together we will lay foundations you can absolutely trust.

**TACKLING  
IS THE OR  
THE DAY.**





Peter Axmann,  
Head of Real Estate Clients

# ISSUES DER OF





# GERMAN AN ATTRACTIVE REAL ESTATE LOCATION



*Lothar Schubert,  
managing partner of  
DC Developments GmbH & Co. KG*



*Peter Axmann,  
Head of Real Estate Clients*

**ART COMES FROM EXPERTISE.** Developing high-quality real estate is an art that Hamburg-based company DC Developments has mastered to perfection. For the past ten years the project development company has realised buildings that have generated a great deal of enthusiasm through their architecture, location and quality. Indispensable building blocks: the individual wishes of owners and users, striving for innovation and an eye for details. Be they residential, real estate, office or commercial buildings; hotels or neighbourhood developments, the 40 staff at DC Developments are passionate about creating values that enrich the environment and the cityscape.

“With the ‘KPTN’ we are developing a mixed-use neighbourhood in Hamburg’s most recent district, which will enthruse not only the Hafencity residents but also any visitors. Many companies from our city are on board with the realisation of the entire project and it is no coincidence that HSH Nordbank is our financing partner,” said Lothar Schubert, Managing Director of DC Developments GmbH & Co. KG. “The HSH team has experience of handling complex project developments of this size; it is very familiar with its home market and has convinced us with its Hanseatic courtesy many times before.”



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Projekt KPTN,  
HafenCity Hamburg



**TRANSPARENT, FAST, COURTEOUS** – with specialist knowledge, experience and well-functioning processes we have advanced to an excellent position in CRE financing in Germany and are among the major providers of finance. We are successful not only in our northern German home region, but also in other German federal states where we have in the past established ourselves with offices in Berlin, Düsseldorf, Frankfurt, Stuttgart and Munich. Moreover, we assist foreign investors in their transactions on the German real estate market. For them, in particular, Germany is viewed as an especially solid market that promises stability even in unsettled times and thus provides auspicious investment opportunities. Our clients include, in particular, professional real estate investors, project developers and development companies. We offer them tailored financing solutions that are geared to their business plan. Our clients appreciate not only the transaction security we provide, but also our solution-oriented way of working – right from the initiation of business and over the entire loan term.

Our range of services includes traditional mortgage loans as well as structured financing for existing properties, commercial project developments and residential property development projects. We always have the sector cycle firmly in our sights and pay particular attention to ensuring that risks are manageable and predictable – such caution is important to ensure long-term success.

**THE MARKET IN A NUTSHELL.** Real estate in Germany has been in high investor demand for years. With a volume of more than €53 billion, 2016 was once again among the richest in transactions on the commercial real estate markets. The drivers of this vigorous upturn are the low interest rates and the substantially better economic performance in Germany compared to other countries since the economic crisis of 2008/09. Both domestic and international investors are looking for opportunities to invest their money at a profit. In this process, flourishing real estate markets promising high rental and value growth are sought after. Thanks also to the positive trend of the job market over the past few years, big German cities, in particular, are perceived as being attractive. While the number of those out of work has fallen by 18 per cent since 2009, the number of those employed in office jobs has risen by about ten per cent. Population numbers have also grown by around six per cent while the purchasing power of private households is up by just under 17 per cent. All this prompted foreign retail chains to move to prime locations in German cities because they hope for growth prospects outside their often stagnating home markets. The positive sales trend in turn benefits the booming online retail trade, which in itself entails the extensive build-up of logistics centres. Investors have moreover shown heightened interest in hotel properties because the mounting political uncertainty in some countries is making Germany more attractive as a holiday destination. All these factors have led to a sharp rise in real estate prices in Germany. Nevertheless, investor demand remains high, also because real estate remains attractive due to the lack of other investment opportunities that promise high returns. This goes not only for office and commercial real estate, which is always sought-after by institutional investors, but increasingly also for logistics, hotel and residential real estate. It is due solely to the stable economic setting that investors and developers will probably continue to keep an eye on the German real estate markets over the coming years.

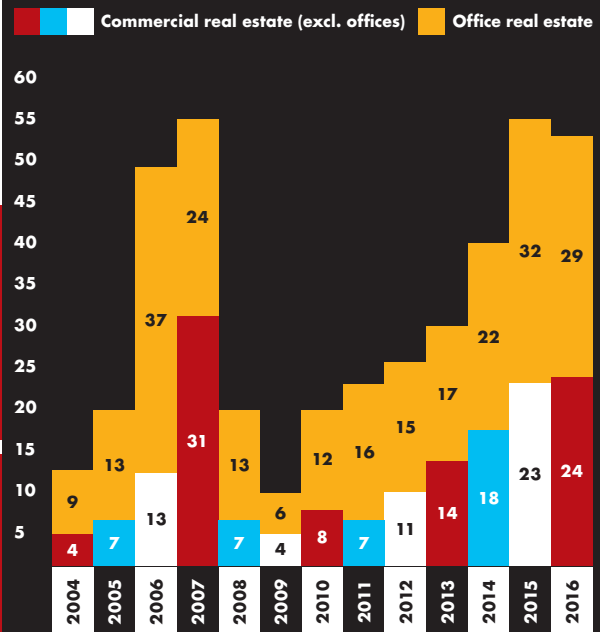
Source: HSH Nordbank Research

**€12.5 BILLION  
LOAN PORTFOLIO**

**€4.6 BILLION  
OF NEW BUSINESS IN 2016**

**COMMERCIAL REAL ESTATE TRANSACTIONS  
IN GERMANY**

(in € bn)







*Patrick Miljes,  
Head of Corporate Clients*

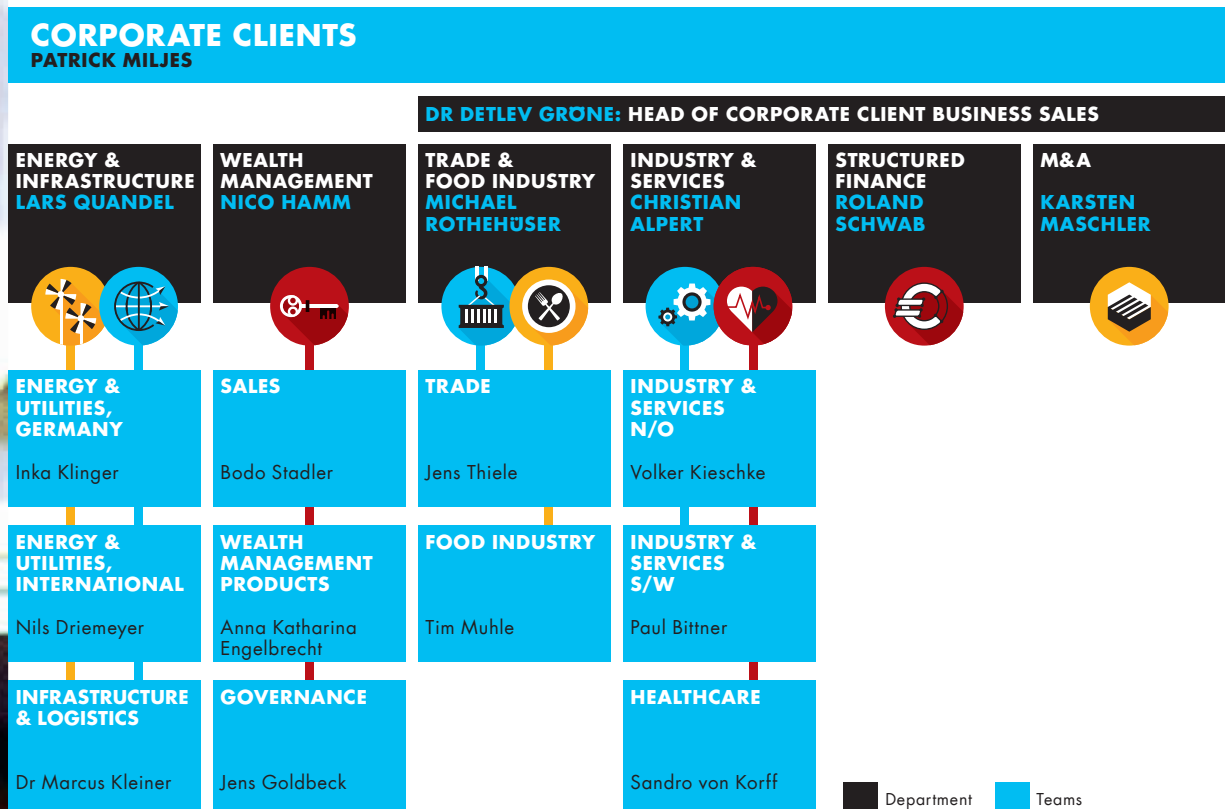
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**YEAR-ON-YEAR INCREASE IN  
NEW BUSINESS IN 2016?  
AROUND 20%  
TO €3.8 BILLION**

# OUR WORK PAYING OFF.

**WE CAN SEE THIS IN THE RESULTS** that rate the realignment of the Corporate Client business area and the strengthening of sales as being profitable. Thus we increased new business in 2016 by around 20 per cent over the previous year to about €3.8 billion. We achieved this because we gained around 100 new clients – not only in our northern German core region, but also in other strong economic regions such as the Rhineland and south-west Germany. Given the persistently competitive market setting, we can be proud of these successes – they are the result of our systematic work. Work that we are continuing.

Our specialists advise and support their clients with in-depth knowledge; especially in the focal sectors of Energy & Utilities, Infrastructure & Logistics, Industry & Services, Healthcare, Food Industry & Trade and Wealth Management, Structured Finance and M&A. Thanks to this broad range of deep knowledge, we are able to develop solutions together with our clients that fit in perfectly with their business. And it takes competence, flexibility, speed and reliability to offer these solutions – characteristics that our clients appreciate. And with which we will continue to be successful in 2017.







*Matthias Munniger,  
Energy & Utilities, Client Relationship Manager*

# WORKING TOGETHER FOR ENERGY





Strong for entrepreneurs  
**ENERGY & UTILITIES**

**UNDERSTAND** The markets are characterised by technical, legal and structural changes.

**RECOGNISE** You can depend on our experience as pioneers in the sector and on our keen sense for trends. We will deploy our expertise and comprehensive financial solutions in the execution of your projects.

**SHAPE** Whether your business is a utility focusing on solar, hydro or wind, offshore or onshore, we support you with all our energy.



*Knud-Erik Andersen,  
CEO European Energy A/S*

NG TOGETHER  
OR A NEW  
SYSTEM.



A photograph of two men standing in front of a large array of solar panels. The man on the left is wearing a dark brown coat and glasses, while the man on the right is wearing a dark blue jacket. They appear to be in conversation. The ground is covered in snow, and the sky is clear and blue.

**RENEW  
ENERGIES.  
WRITE A  
SUCCESS  
STORY.**



**RENEW ENERGIES. WRITE A SUCCESS STORY.**

In the renewables sector, we are among the top 5 European finance providers and thus in the premier league. We see the fact that even in 2016 we were able to exceed our ambitious new business targets as an incentive to remain at the top over the coming years. In 2016, our new business exceeded **€1 BILLION FOR THE FIRST TIME.** In the projects business we are active across Europe in the asset classes of ‘wind onshore’, ‘wind offshore’, ‘solar’ and ‘hydroelectric power’. We have been financing wind and solar projects for the past 25 years and thus rank among the pioneers in this sector. It is precisely for this reason that our clients – producers, project developers, investors and utilities – benefit from our know-how that is recognised in the market and from our wealth of experience. Our existing loan portfolio currently has a volume of around five billion euros and comprises some 240 projects. We offer our clients long-term project finance as well as working capital lines, liquidity management and various products to manage risks. We support them in import and export business and offer them services in conjunction with the sale and purchase of projects and shareholdings. Our expertise in this area is documented regularly in various publications – our tenth Wind Study was recently published on the occasion of the WindEnergy Hamburg Fair (September 2016).

**EUROPEAN ENERGY.** The Danish project developer and operator of solar and wind farms also offers the technical and commercial management of the farms. Since the company’s establishment in 2004, European Energy A/S has developed a total of 65 wind farms and 29 solar projects in six different European countries. All plants together have a total rated output of around 800 megawatts (MW). The investment costs for the project total more than one billion euros. European Energy developed the biggest solar park in northern Europe at a decommissioned air force site in southern Denmark, where 300,000 photovoltaic modules on an area of around 108 hectares generate nominal output of 50.4 MW.

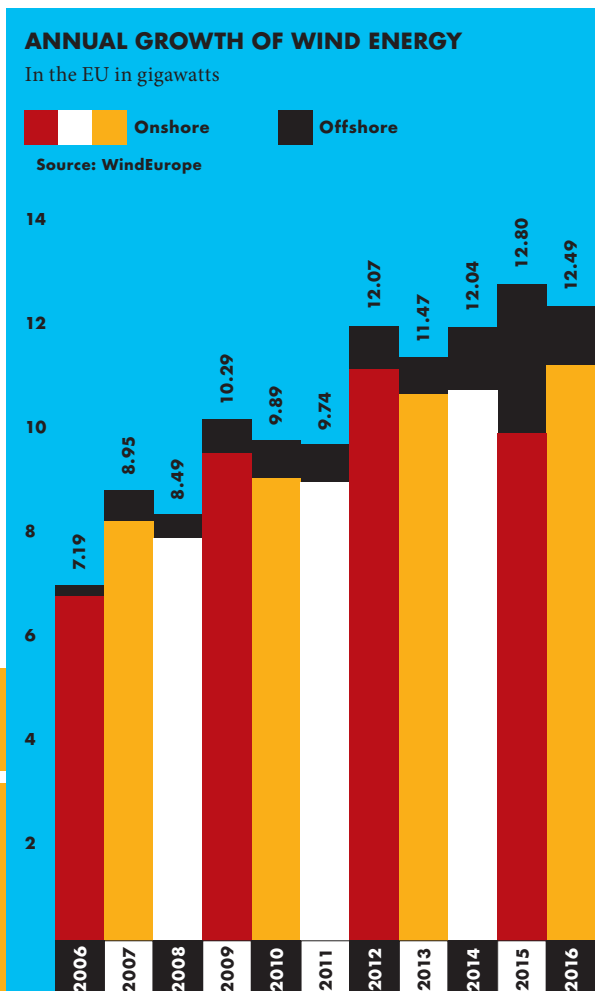
CEO Knud-Erik Andersen: “In HSH Nordbank we have found a financing partner who understands our particular needs as a project developer and assists us across national borders in a professional manner and with a great deal of expertise.”

**PREMIERE:  
NEW BUSINESS > €1 BILLION**

**OUR EXISTING LOAN PORTFOLIO  
CURRENTLY HAS A VOLUME OF AROUND  
€5 BILLION  
AND COMPRISES AROUND 240 PROJECTS**

**THE MARKET IN A NUTSHELL.** The expansion of renewable energies (RE) continues to progress apace in Europe – particularly thanks to the boost provided by the Paris UN Climate Agreement of 2015 and the commitments made by the EU for the period up to 2030. According to industry association WindEurope, 86 per cent of all power plant capacity newly installed in 2016 within the EU was based on RE technology. The increase in wind energy plants accounted for an aggregate rated capacity of 12.5 gigawatts (GW) or around 51 per cent of the total increase in capacity. A further 27 per cent (6.7 GW) was contributed by photovoltaic plants. As in the previous year, Germany was by far the biggest sub-market in Europe for new wind farms, both onshore and offshore, with a capacity increase of 5.4 GW. Capacity growth was one of the main factors in renewable energies now accounting for just under 30 per cent of electricity consumption in the EU. The increase in RE power plant capacity is likely to continue over the long term, but will have to be interlinked to a greater extent with the expansion of the power grid. Although growth will weaken in individual markets, the further expansion of renewable energies will now make it possible to achieve the substitution of climate-damaging fossil fuels that is envisaged over the long term. National development schemes and expansion plans offer project developers and investors in the EU countries sufficiently reliable underlying conditions to push ahead with the capacity increase over the coming years – despite the move towards capacity auctions with amounts of remuneration that are to be established through competition.

Source: Research HSH Nordbank





*Britta Kanzelmeyer,  
Infrastructure & Logistics,  
Client Relationship Manager*

**WE GIVE  
IT A  
PUSH.**





*Torsten Lehmert,*  
*Managing Director of RAILPOOL*



## Strong for entrepreneurs **INFRASTRUCTURE & LOGISTICS**

**UNDERSTAND** The pace of this globalised world needs flexible logistics chains and a reliable infrastructure.

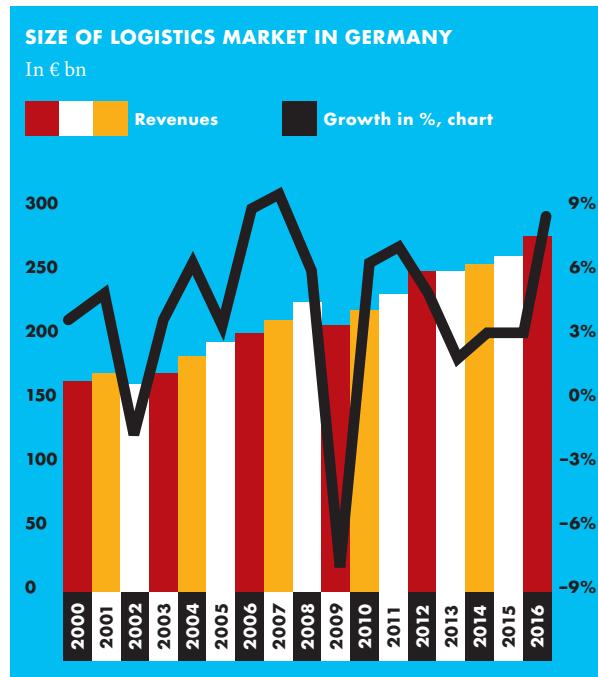
**RECOGNISE** Our extensive experience allows us to support you when it comes to investing, hedging economic risks or executing your payments.

**SHAPE** From transport management on road and rail, from the airport through to the harbour terminal, together we set the course for the success of your enterprise.

**FINANCING, DONE WELL.** From a locomotive weighing tons to the last byte – we ensure connection. Be it in road or rail-based transport, supply companies and supply networks or energy and telecommunications. With innovative financing solutions for data centres, smart meter and broadband projects we are a sought-after contact partner for financing. The financing of infrastructure projects on the European market – they are of our focus and the core area within which our experienced team is able to offer attractive solutions to our clients. For instance, in greater Berlin we helped more than 100,000 households connect to the German fibre-optic network in 2016. Going beyond project financing, we assist clients with company finance as a sector specialist with a wealth of detailed knowledge and long-standing experience in the areas of logistics, locomotive and coach manufacture as well as building construction.

At the same time, we assist our clients in the financing of plants and projects right from the start – be it in the selection of the investment, the offer as part of a concession, a bidding procedure right through to successful completion.

**MORE THAN  
100,000 HOUSEHOLDS**  
CONNECTED TO THE GERMAN FIBRE-OPTIC NETWORK



**THE MARKET IN A NUTSHELL.** Logistics is one of the most important areas of Germany's economy. It includes the transport of goods, their storage and the management of goods and information flows. And although global growth has slowed down, the logistics sector is continuing to increase. In this sector, which is dominated by SMEs, around 60,000 companies offer their logistical services. This is due, not least, to the booming online trade and the increasing service offerings of e-commerce providers. According to the German Logistics Association (Bundesvereinigung Logistik, BVL), cross-sector sales in 2016 came to around €258 billion – equivalent to more than 25 per cent of the European logistics market. This is due to the high competitiveness of domestic logistics companies, Germany's good geo-strategic position and the quality of the German transport infrastructure. Regular public-sector and private investments in roads, tunnels, bridges, railways, ports and airports are necessary in order to maintain these standards. Accordingly, the German government has been using its good budget situation to ramp up infrastructure spending considerably.

Spending totalling €13.7 billion is planned for 2017. Compared to 2014, this is equivalent to an increase by more than one-third. Further substantial spending is planned beyond 2018. The projects of the German Plan for Federal Traffic Routes 2030 alone are worth more than €67 billion. The Hamburg metropolitan region will also be able to benefit. For example, the harbour link road for the A1 and A7 motorways is due to be expanded, as well as linking these two motorways in the south of Hamburg. Together with the deepening of the river Elbe and the widening of the Kiel Canal, this will create the basis for an enduring dynamic growth of the northern German economy.





# THE CONNECTION HAS BEEN ESTABLISHED!

**RAILPOOL** is among the biggest lessors of rolling stock in Europe. Most recently, we signed a lighthouse transaction for our long-standing client and for DB Cargo AG through the bilateral financing of around 200 second-hand locomotives. As part of the transaction, DB Cargo AG sells the used electric locomotives to a consortium led by RAILPOOL, with Toshiba and others also participating. In return, DB Cargo AG will be able to use the rolling stock for a period of eight years as part of a capacity reduction model. Through this tailored financing with a volume of a high eight-digit euro amount, HSH Nordbank is assuming a pioneering role on the competitive rail market.

At the same time, this transaction enables RAILPOOL to assume a clear strategic positioning on the market. RAILPOOL was established in 2008 as a joint venture between HSH Nordbank and KfW IPEX Bank; the Munich-based company now has operations in 20 European countries. Following the successful development phase the company passed into the hands of the private equity fund of Oaktree Capital Management in 2014. GIC, a major investment fund in Singapore, now also holds an equity stake. In addition, the founding banks have involved further reputable European banking firms in the financing as part of the expansion of RAILPOOL. Torsten Lehnert, Managing Director of RAILPOOL: "A special kind of partnership connects us with HSH Nordbank – together we have decisively shaped the locomotive leasing market."



**WE TRADE CHALLENGES.** Of course, trade has always been a core business area for us. It would be difficult for it to be otherwise for a company with one head office in Hamburg. In this area we assist our clients in their business activities. Be it in such sub-sectors as Oil and Gas, Steel, Chemicals, Textiles, Automotive or in areas of Retail.

Our financing volume in this area totals €3.2 billion and is thus €500 million up on the previous year. Trade financing is transacted mostly in foreign currency. Of course, we offer our clients the necessary currency transactions and currency hedging. The same goes for risk hedging in import and export business. Our clients today face a wide range of different challenges: currency volatility, international procurement, collection cycles, internationalisation and verticalisation. The development of own brands is another important and challenging topic.

We assist our clients in finding solutions to these challenges – in the face of intense competitive pressure on global markets undergoing profound changes as a result of the shift in sales from bricks-and-mortar to online trading. Moreover, the pressure to adapt will increase further with the progress of digitalisation. This makes our specialists with their market expertise not only perfect contact persons for our clients – but also forward-looking partners.

## Strong for entrepreneurs TRADE

**UNDERSTAND** A profound knowledge of goods and value chains allowing accurate identification of opportunities and risks is a constituent component of our Hanseatic DNA.

**RECOGNISE** From financing through to documentary business – with our specialists we are your forward-looking partner for anything you require in the markets that matters to you.

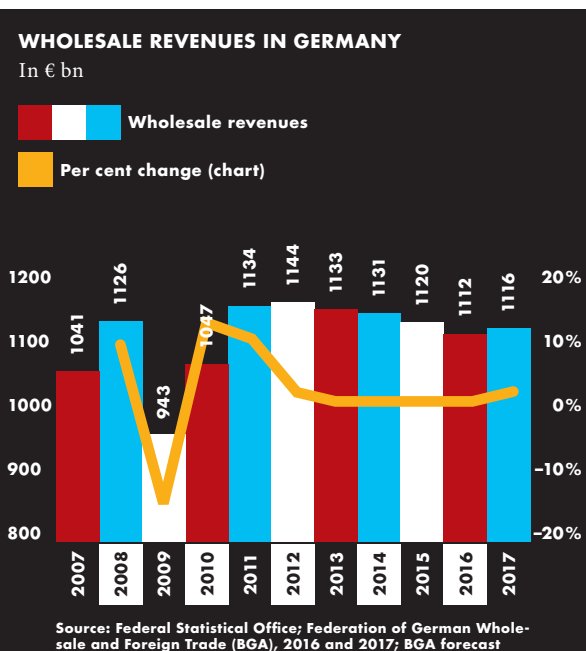
**SHAPE** Our competence bred from extensive experience offers rapid and sure decisions, leaving you the freedom to do what you need.

**THE MARKET IN A NUTSHELL.** Trade companies have played a major role in ensuring that Germany is a winner of the international division of labour and that it generated new record levels of exports and imports in 2016, as it had done in the previous year. In 2016, goods worth €1,207.5 billion were exported along with imports totalling €954.6 billion. This is equivalent to an increase of 1.2 per cent and 0.6 per cent, respectively, over 2015. Germany's most important trading partner is China (just under €170 billion in imports and exports) followed by France (about €167 billion) and the USA (almost €165 billion). Given the encouraging economic setting, exports and imports are likely to continue their growth in 2017.

At the same time, according to the German Federation of Wholesale, Foreign Trade and Services (Bundesverband Großhandel, Außenhandel, Dienstleistungen e. V., BGA for short) wholesale sales recorded a minor decline from €1,120 billion to €1,112 billion in 2016. This decline is an expression of a trend observed over the past three years, that as prices are down slightly companies have to sell more products in order to maintain their high sales levels. The BGA is slightly more optimistic for 2017 and projects marginal sales growth of around 0.5 per cent.

In Hamburg and the northern German coastal cities, wholesale and foreign trade are traditionally an important economic factor. At present, around 18,650 companies operate in this sector. They generated sales of more than €292 billion with a total staff of 248,500. In the fourth quarter of 2016 alone, sales according to the Confederation of northern German Wholesale, Foreign Trade and Service Businesses (Norddeutscher Unternehmensverband Großhandel, Außenhandel, Dienstleistung e. V., AGA for short) rose by 1.1 per cent. The trade companies also project a positive trend for 2017. Thus many northern German companies stated their intention in the AGA Economic Test at the end of 2016 to invest and recruit new employees in 2017 – making a further rise in sales appear likely.

Source: Research HSH Nordbank



# TRADE? DOING DEALS!



*Hans Redlefsen,  
Owner of Closed*



*Markus Prante,  
Trade, Client  
Relationship Manager*



OUR TOTAL FINANCING VOLUME?

**€3.2 BILLION;**

€500 MILLION MORE THAN IN THE PREVIOUS YEAR





**EXPERTISE BEATS COMPLEXITY.** The food industry is multifaceted and diverse. It therefore requires a high level of know-how: among producers, traders and banks. Thanks to the expertise we have built up over the past decades, our advisors are not only very familiar with the challenges and specific characteristics of the individual markets – they are also very well connected in these markets. Thus our Food team currently assists more than 170 clients with a total loan volume of €2.2 billion, equivalent to a ten per cent increase over the previous year. Among other things, we are active in the coffee and tea industries, in agriculture and the meat industry. Here, we work together with companies that represent enjoyment and life's pleasures for consumers and are well-managed on a hotly contested market – assisted accordingly by the bank partner. The entire industry is marked by such trends as ultra-fresh food, increasing nutritional awareness and product sustainability. At the same time, companies' operations are becoming increasingly international: even now they sell around one-third of their products abroad.

Our service portfolio includes not only company finance but also the processing of domestic and foreign payments and the reliable execution of international documentary transactions. Of course, we also provide the right hedging instruments when it comes to forex transactions in international trade and in imports and exports in foreign currency.

### Strong for entrepreneurs **FOOD INDUSTRY**

**UNDERSTAND** The market for food products is constantly on the move because of changing consumer behaviour, vigorous innovation and fierce competition.

**RECOGNISE** Whether brands, white labels, production or trading: we know the challenges and opportunities of the business models and will do our bit to help you achieve your objectives.

**SHAPE** No matter where the market is heading: our sector experts feed you with fresh ideas so that you can realise yours.

**COFFEE.** Germans drink more coffee than mineral water. The annual per-capita consumption totals around 162 litres. This makes Germany the world's third-biggest market for coffee after the USA and Brazil as well as the main trans-shipment centre for green coffee in Europe. Annual sales of the German coffee industry total around €6.1 billion. Demand in Germany for higher-quality coffee varieties has been growing for some years. At the same time, the proportion of the "full bean" segment and of single-cup coffee is rising sharply. Pods currently account for around 5.5 per cent of the overall market.

Consequently, the markets are anything but steady. This volatility makes increasingly efficient risk management necessary. Green coffee traders, in particular, require considerable scope with their liquidity to hedge the sharply fluctuating coffee prices on the commodities exchanges. We offer our clients hedging of currencies, commodity prices and interest rates.

In summary, it can be said that the complexity of coffee trading is increasing and thus the financing requirements of our clients are as well. Climate change, population growth and ever scarcer cultivation areas mean considerable uncertainty for the future of the coffee industry. At the same time, coffee trade provides good opportunities for opening up new markets outside Europe. We help our clients master all these challenges.

**OUR FOOD TEAM CURRENTLY ASSISTS MORE THAN**

# 170

**CLIENTS WITH A TOTAL LOAN VOLUME OF**

# €2.2 BILLION

**+10%**  
YEAR-ON-YEAR





*Ute Brettschneider,  
Food Industry, Client Relationship Manager*

# HOW DO YOU WITHSTAND PRESSURE? WITH QUALITY.



**THE MARKET IN A NUTSHELL.** The food industry is the third-largest sector of the German economy – offering consumers a broad range of 170,000 high-quality products. In 2015, around 570,000 employees in approx. 5,800 companies generated sales in excess of €169 billion. The most important segments are the meat and meat products industry, dairy processing, confectionery and baked goods, drinks production and the processing of fruit and vegetables. The food industry is marked by SMEs to a particularly high extent: 95 per cent of companies have fewer than 250 employees. Business in the food industry is virtually unaffected by economic fluctuation and has been showing a relatively stable performance. Nevertheless, the sector is marked by huge margin pressure due to overcapacity and the heavy consolidation within the German food

retail industry. Strict cost management, the opening up of new markets and product innovations are therefore at the top of the agenda for the companies. The most promising strategy for outperforming the competition is thus for a company to position itself as an innovative brand and quality producer. Many companies are focusing on current trends such as freshness, convenience, regionality, increased nutritional awareness and sustainability. According to the Confederation of the German Food Industry (Bundevereinigung der Deutschen Ernährungsindustrie, BVE), sales in 2016 were up following a decline in the previous year: forecasts anticipate a gain of around 1 per cent in 2016. The growth was attributable not least to the export business, which the companies hope will lead to a strong surge in 2017 as well.





**STRENGTH  
THE B  
OF THE E**



Strong for entrepreneurs  
**INDUSTRY & SERVICES**

**UNDERSTAND** Companies in the industrial and services sectors form the backbone of the German economy.

**RECOGNISE** We are familiar with the specific challenges of your market – from automotive to steel, from R&D through to the travel business.

**SHAPE** Cooperating with you, we develop distinct ideas and inch-perfect solutions so you can take profitable advantage of the opportunities your business presents.



*Christian Alpert,  
 Industry & Services,  
 Department Manager*



**HOW WE ARE  
 STRENGTHENING  
 THE BACKBONE  
 OF THE ECONOMY.**



Factory Clyde Bergemann GmbH, Wesel



**WE CREATE  
STRUCTURE  
FOR  
PROGRESS**



**WHETHER EXPANSION,** strategic partnership, capital market financing or arranging promissory notes – we assist our clients as expert advisors even in complex projects. For us, sustainable cooperation in a spirit of partnership is the top priority. For this reason, we stand by them over the long term through all economic cycles and are thus able to develop tailored structures. And it is precisely with these individual solutions that we guarantee that our clients remain successful in the complex interplay between globalisation, structural change and technological progress. And this not only in our northern German core region, but also nationwide: whether in Hanover, Berlin or Düsseldorf, in Munich or Stuttgart, where we have now been active for more than ten years. In Bavaria and Baden-Württemberg alone we currently assist more than 100 selected SME clients with a loan volume of around one billion euros. And we also have exposure to Germany’s most important sector, the automotive industry, with a financing volume of one billion euros.

**IN BAVARIA AND BADEN-WÜRTTEMBERG WE ASSIST MORE THAN 100 SME CLIENTS – WITH A LOAN VOLUME OF AROUND €1 BILLION**

EE

S.



*Frank Kraemer,  
Industry & Services,  
Client Relationship Manager*

**LOAN PORTFOLIO  
AROUND €1.2 BILLION**



*Sandro von Korff,  
Healthcare, Team Leader*

**ACROSS GERMANY, WE FINANCE  
130 IN-PATIENT CARE FACILITIES  
WITH 12,000 BEDS**



**HEALTH COME  
FIRST. WE'RE  
THERE EVERY  
STEP OF THE V**





**VIRTUALLY NO OTHER SECTOR** is reporting steady growth comparable to that of the healthcare industry. Around 230,000 mostly SMEs now account for some twelve per cent of Germany's gross domestic product (GDP).

While the medical sector and technology continue to develop, cost pressure for businesses is mounting at the same time. The main challenges are thus: increasing industrialisation, digitalisation and networking. And what does the client expect from us? Competence, expertise and reliability – characteristics we are able to offer. Our clients include companies from the medical technology and pharmaceuticals sectors, specialised service providers, associations of accredited physicians and dental healthcare providers, healthcare insurance funds and associations. We are also one of the main providers of finance for clinics and care facilities in Germany. Across the country, we have financed around 130 in-patient care facilities with a total of 12,000 beds.

Our long-standing activity in the healthcare sector has made us genuine sector specialists: client relationship managers, risk specialists, product experts and researchers are thus not only experts in a highly complex area of work – but also competent contact partners who always work out a suitable solution for their clients.

**THE MARKET IN A NUTSHELL.** The German population is ageing. And thus the issue of healthcare is becoming increasingly important not only for our society – but also for the economy. After all, total German healthcare spending in 2015 already came to €344 billion or €4,213 per capita. This is equivalent to 11.3 per cent of Germany's gross domestic product – one in every nine euros in Germany is thus spent on health.

The issue of health will continue to ensure strong growth and employment stimuli in the healthcare industry: over the past ten years, gross added value has grown by 3.3 per cent annually while growth of the German economy as a whole was only 1.6 per cent.

Between 2004 and 2015, the number of those in gainful employment in the healthcare industry rose from 4.4 million to more than five million.

And the demographic trends show that the momentum of the healthcare industry will not wane. We are increasingly faced with the exciting challenge of not only maintaining the quality of healthcare, but of improving it: by always striking an intelligent balance between humanitarian and economic aspects.

Source: HSH Nordbank Research

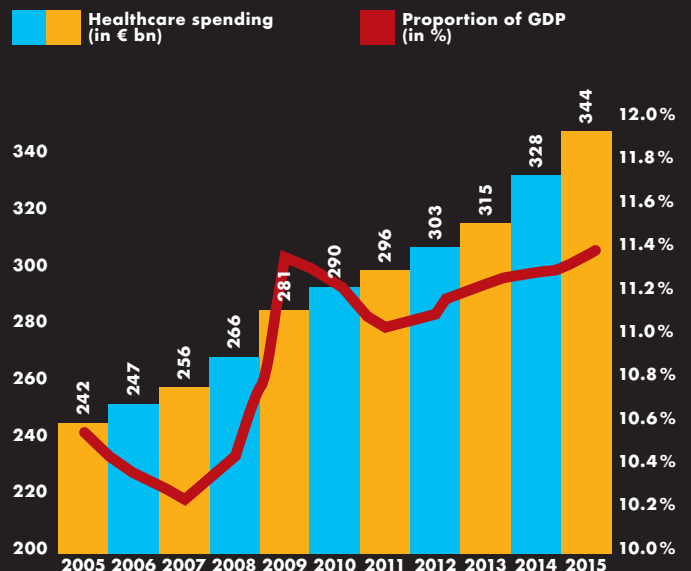
**Strong for entrepreneurs  
HEALTHCARE**

**UNDERSTAND** The healthcare sector is a growth market of steadily increasing importance to society as a whole.

**RECOGNISE** While the medical sector and technology continue to develop, systemic cost pressure is also mounting. We help you navigate the conflicting priorities involving investment, acquisitions and other complex plans.

**SHAPE** Medical technology, hospitals or care, specialised service providers or pharmaceuticals, together we ensure that you are fit for your future.

**HEALTHCARE SECTOR  
A GROWING ECONOMIC FACTOR**



Source: Federal Statistical Office

# MANA ESTABLIS

**IN SUPPORTING** high-net-worth private clients and foundations with our wealth management we are one of the leading banks in our northern German core region. As a bank for entrepreneurs we assist our clients not only in all business-related matters, but also at a private level. Relations with private clients or foundations often stretch back over many decades and there is a reason for this: dependability, transparency and solidity are principles we have always upheld.

Our relationship managers and specialists in wealth management offer a wide range of services. In the interest of our clients, the advice we give is independent of both products and providers. Our work focuses on individual investment advice and asset management. Our clients have confidence in our expertise: overall, we have around four billion euros in assets under management. This says something not only about our size, but also about the confidence our clients have in us.

We are also one of the leading banks in Germany when it comes to the area of philanthropy and foundations. Our specialists are trained foundation managers or consultants and support our clients on all relevant topics from strategic advice and setting up foundations down to fundraising or donation optimisation.

This profound knowledge is appreciated by our clients. And this is why we advise 700 foundations and non-profit partnerships across Germany.

## Strong for entrepreneurs **WEALTH MANAGEMENT**

**UNDERSTAND** Every asset is unique.

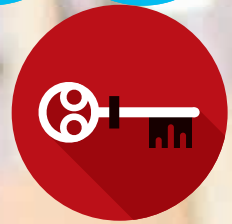
**RECOGNISE** It is our responsibility to find the right solution for your personal requirement.

**SHAPE** When you feel confident that your assets are in good hands, today and tomorrow, then we feel we have done our job.

**WE ADVISE 700 FOUNDATIONS  
AND NON-PROFIT  
PARTNERSHIPS ACROSS GERMANY**

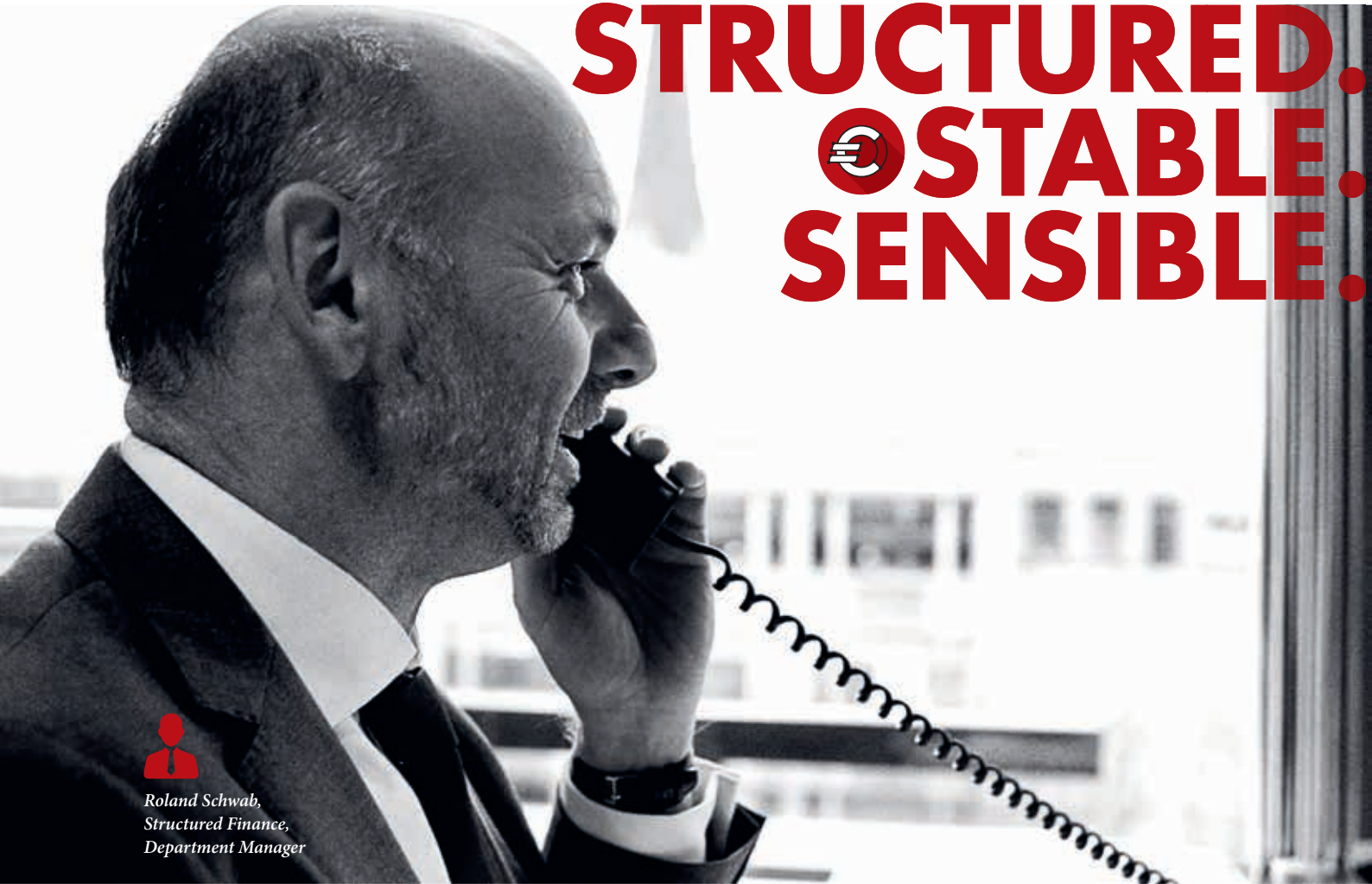


# AGING ASSETS. SHINING TRUST.



*Nico Hamm,  
Wealth Management, Department Manager*

# STRUCTURED. STABLE. SENSIBLE.



*Roland Schwab,  
Structured Finance,  
Department Manager*

**OUR REORGANISED STRUCTURED FINANCE DEPARTMENT** combines the Leveraged Finance (LBO) team for private equity investors with the Capital Structuring unit, which has supported the corporate client advisors on more complex financing structures in the past. Our range of services is complemented by our Smart Fact colleagues, formerly in the Capital Markets unit, who offer factoring solutions. This unit therefore covers all the main forms of financing required by corporate clients.

We structure financing solutions for leveraged buy-outs (LBOs) for German SMEs with annual revenues in excess of €50 million as well as for private equity companies. Unlike conventional corporate finance, for such transactions extensive due diligences – these are intensive checks conducted prior to the sale of a company – are drawn up and detailed legal documentation created, tailor-made for the financing. We also help clients improve their balance sheet structure. Sometimes there are a large number of individual agreements on the liabilities side – which we tackle together, for example by improving the maturity structure or setting up a new syndicate structure to ensure that the client is stably financed over the long term. The usual size of the financing tranche we take on stands at around €20 to 40 million and in individual cases up to €75 million. Our principal product in Capital Structuring is

the syndicated loan in the form of term loans, guarantees or working capital facilities. Here we structure the financing, i. e. the content, depending on the client's situation and the respective reason for the financing – for example, investment in material goods, financing working capital or a takeover.

## Strong for entrepreneurs STRUCTURED FINANCE

**UNDERSTAND** The financing of any project depends on the sector, the business model, the market situation and the right timing.

**RECOGNISE** At the interface between conventional corporate banking and investment banking we support you with our expertise in the (re-)structuring of debt and equity capital, financing your current assets and funding your acquisition.

**SHAPE** We solve these complex tasks in an all-round, tailor-made, efficient manner. In this way we create a stable financing structure for your project.





Karsten Maschler,  
M&A, Department Manager



# FIRST LEADING TOGETHER. THEN BRINGING TOGETHER.

**SALE OF THE COMPANY**, joint ventures, buying a business, acquiring a stake, raising growth capital or arranging succession – no matter which entrepreneurial project is planned: our specialists in mergers & acquisitions (M&A) help clients implement it successfully. With more than 120 transactions successfully completed in the past 15 years, we are among the established M&A consultants in the German market. In 2016 too, we were entrusted with numerous interesting mandates. Here we are able to draw not only on our profound knowledge of the market, but also on our excellent national and international network – consisting of strategic investors, private equity funds, family offices and external advisors. This is because in order to find a buyer, a co-investor or a suitable target company for clients, a thoroughgoing knowledge of the market with all its opportunities and risks is required – as well as an excellent and skilful command of all the financing options. A successful M&A project is therefore always a demonstration of a job well and properly done.

Since 2002, we have worked mainly for SMEs, where we serve a multi-faceted client portfolio – from owner-managed companies to international conglomerates. The core industries for our M&A consulting are retail and food, industry and services, healthcare, shipping and energy & utilities as well as logistics & infrastructure.

No matter what challenges our clients are facing: thanks to our sector expertise we offer realistic options and a perfect strategy for long-term profitable action.

## Strong for entrepreneurs M&A CONSULTING

**UNDERSTAND** We offer the network and the detailed expertise to promote your entrepreneurial interests and create strategic added value.

**RECOGNISE** In a close dialogue we provide you with ideas on how you can better position yourself given the current market and competitive situation in your sector.


**SHAPE** Whether for a sale or a takeover, a merger or a shareholding – we help you successfully prepare your company for the future.

**WITH MORE THAN 120 TRANSACTIONS SUCCESSFULLY COMPLETED IN THE PAST 15 YEARS, WE ARE AMONG THE ESTABLISHED M&A CONSULTANTS IN THE GERMAN MARKET**



**DEMANDING  
DEMANDING  
MARKETS.**



Christian Nieswandt,  
Head of Shipping 

Strong for entrepreneurs  
**SHIPPING**

**UNDERSTAND** To achieve lasting success for your business in the maritime industry you need a business model that has a future.

**RECOGNISE** In us you will find a team that stays the course. Even when those storms come.

**SHAPE** Our promise is that we will scrutinise deals down to the fine details; we will weigh up opportunities and we will offer you the kind of support you need.

**THE CONSOLIDATION PROCESS IS ON-GOING.**

The shipping industry is going through one of the severest and longest crises in its history. What role does shipping play at HSH Nordbank?

**Christian Nieswandt:** Shipping is still one of HSH Nordbank’s core business areas. However, in the current extremely challenging market setting we only engage selectively in new business. At the same time, we are resolutely reducing our legacy assets. Almost all of these relate to exposures from before 2009. Overall, our holdings in the shipping business area will continue to decline.

**What do you pay particular attention to in shipping transactions?**

**Christian Nieswandt:** We focus on developing and diversifying our portfolio by means of German and foreign exposures with good credit ratings, sufficient equity capital and a successful business model. Among other things, this means that the borrower constantly has good access to the cargo and that his fleet is reliable and engaged on attractive terms. At the moment, we see greater opportunities in the tanker and bulker market than in the container market. However, we are not only active in the market as a lender, but also as an arranger and offer our clients other products from our Bank that are useful to them. We are becoming increasingly successful at this.

**Do you expect the markets to pick up significantly?**

**Christian Nieswandt:** Probably not in the short term because a considerable number of new ships are due for delivery in the coming twelve months. This is likely to make a recovery of the markets more difficult. However, noticeably fewer orders were placed in 2016 – that is a positive sign. In spite of all these problems, there is one thing we should not forget: the demand for transport capacity is increasing in line with the growth of global trade. And well over 90 per cent of these international transports make use of ships – this type of goods transfer cannot be replaced. This points to sound business prospects in this area over the long term.

**What changes do you anticipate in the shipping market as a whole?**

**Christian Nieswandt:** The process of consolidation is ongoing and has advanced particularly far among the shipping lines. A similar process is now necessary for the tramp shipping companies to restore balance in the market. We are therefore supporting alliances and utilisation pools.

IN





*Mark Bussmann,  
Head of Treasury & Markets*

**NEW  
STRUCTURE,  
NEW   
EFFICIENCY.**



**ACTING EFFICIENTLY. FINANCING CO-OPERATIVELY.**

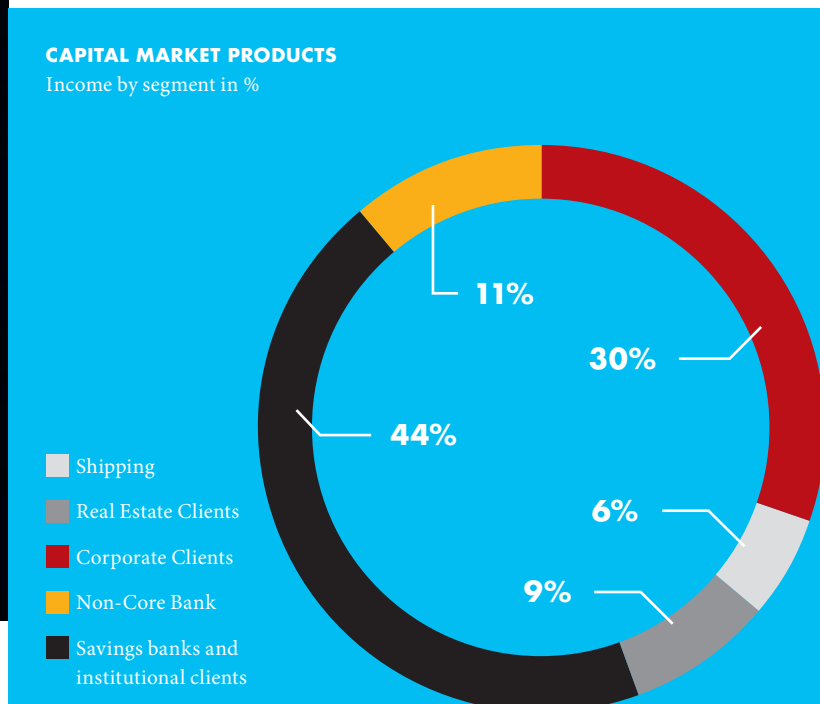
The Bank restructured the Treasury & Markets unit in 2016 – and in doing so further increased its efficiency. This involves a wide range of tasks. In the so-called ‘Markets’ function, for example, we develop and sell products for risk and investment management as well as capital market finance. In other words, we offer savings banks, institutional investors and companies instruments for hedging interest and exchange rate risks as well as structured bonds, certificates and products for investing in the money and capital market. Furthermore, corporate clients receive suitable solutions for actively managing their own equity capital and liquidity position. In addition to this, we arrange large-volume promissory notes for the public sector, thus contributing to the financing of the federal states and municipalities.

Another important task of this unit is the Bank’s entire operational treasury function. Here we not only play a leading role in funding the Bank across the entire liabilities side – but also in the management of the Bank’s daily liquidity.

In doing so, at Treasury & Markets we always see ourselves as service providers and partners for all HSH Nordbank business units – and work with them hand in hand.

**HIGHLIGHTS FROM OUR RANGE OF SERVICES:**

- Collaboration with more than 300 savings banks in Germany
- Placement of bonds and Landesschatzanweisungen with a total volume of more than €6 billion for the public sector
- Issue of promissory notes from 2013 until today more than sextupled at €1.6 billion
- Placement of several benchmark bonds
- Funding support for nine federal states
- Assistance for several solar and wind energy companies with combined interest and exchange rate hedges in non-euro countries
- Risk calculation for companies in our Enterprise Risk Management concept (ERM)
- Creation and implementation of dynamic hedging concepts with our clients in the food industry
- Successful support for real estate companies in sector-specific interest rate risk strategy



## THE WORK IN A COMPANY'S ENGINE ROOM HAS TO RUN SMOOTHLY:

the daily management of liquidity, continuous cash flow optimisation and the comprehensive hedging of risks are some of the main tasks in this respect. Our Transaction Banking unit takes care of these tasks, meeting our clients' demands with a number of products: these may relate to a range of possibilities for global payments, the financing and hedging of international delivery transactions or interest and exchange rate risks. In addition, we offer various digital solutions, which we have developed with the "Initiative Digital Business".

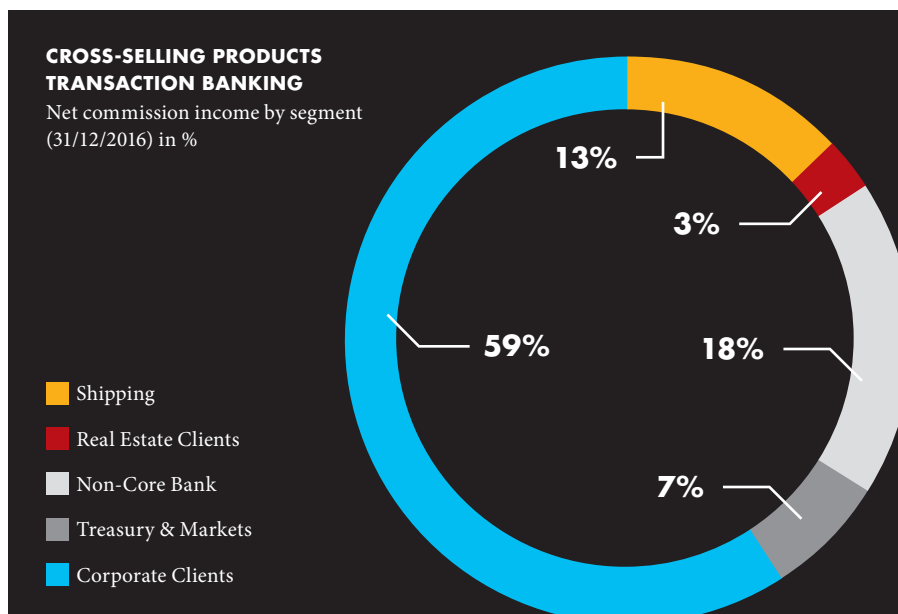
For example, in PAYONE we work with a company in the Savings Banks Finance Group, which offers internet shop operators an optimum solution for their payment transactions. The range of services offered by the leading payment service provider covers the assumption of risk management as well as debtor and receivables management and billing. With the support of the paydirect internet payment procedure, we also offer our clients the possibility of electronic payment – with secure payment ensured.

The range of services we offer is always tailor-made for our clients, with clearly defined sector focuses. For instance, in the real estate business we see ourselves as providers of not only property finance, but also all-round solutions. Together with PROMOS consult Projektmanagement, Organisation und Service GmbH we have developed a service for optimising the recording of rent payments. The HSH PROMOS Cash Connection offers significant savings in time and costs for housing companies. "HSH Nordbank has been one of our company's banks for many years. With the HSH PROMOS Cash Connection it has added an important tool to its service that helps us efficiently allocate and book our rental receipts," says Ulrike Bondkirch, Head of Group Finance and Treasury at Hamburger TAG Immobilien AG, which manages some 80,000 properties.

Furthermore, we offer our clients international trade financing. Here, among other things, we support project planners from the renewables sector by providing suitable solutions for procurement. The classic hedging function of import L/Cs and the financing function give our clients the opportunity to conclude contracts with suppliers ahead of long-term project financing. This makes it possible to bridge the construction phase until the project financing is paid. At the same time, we deal with issues of the future, e.g. Blockchain, a technology that some people think is going to change the world. However, as yet there are not many practical applications. Yet we have already developed a proof of concept for promissory note loans on a Blockchain. At the moment, we are looking into how individual solution platforms can be developed from this together with institutional investors and banking partners.



# INV FOR TION







*Yoram Matalon,  
Head of Transaction Banking*

# ESTMENT INNOVA- N.

Strong for entrepreneurs  
**TRANSACTION BANKING**

**UNDERSTAND** The importance of reliable cash management and global trade finance is growing in an accelerating and digital economy.

**RECOGNISE** With certified processes, we offer total care for all your national and international payments and hedge risks in import and export trading.

**SHAPE** Our dedicated, scalable solutions allow you to have an overview of your liquidity and payments at all times, leaving you free to focus fully on your core business.



The organisational units Documentary Business, Cash Management Operations and Customer Service Centre have been certified as meeting the requirements of ISO 9001:2008 for a quality management system.



Dr Cyrus de la Rubia,  
Chief Economist







# RESEARCH MEETS PRACTICE.

## THE OPPOSITE OF SCIENCE IN AN IVORY TOWER?

We are confident and assertive and say: HSH Nordbank's sector and macroeconomic Research unit. Close to the client, close to the market – and with sufficient distance to form a balanced judgement. In our Research unit our clients find sparring partners, who, with their knowledge, experience and flexibility, rapidly understand complex economic correlations, enabling them to assess the opportunities and risks of business models. In their studies on the subject of wind energy, real estate, infrastructure, healthcare, trade and the food sector our experts analyse not just individual markets, but also look forward and plot future developments.

In close cooperation with the market units, Research provides support for loan arrangements and, for example, for promissory notes. A further offer for our clients: generating a rating indication. Companies without a rating can thereby find out without obligation what rating they would be given if they were to contact one of the major rating agencies.

In addition to these services clearly geared to companies, our Chief Economist Dr Cyrus de la Rubia and his team deal with current economic and political trends, which they assess and classify. They develop scenarios showing possible trends. Thus they provide decision-making aids, which are used by our market units – be it corporate clients, real estate, shipping, energy or others. And of course they are used by our clients. Whether the questions relate to interest rates, currencies, the performance of the German economy or Bitcoin: our team of macro and micro-economists provides expert advice – and in conjunction with our relationship managers create real added value for our clients.





**UP°**  
UNTERNEHMER  
POSITIONEN NORD

**SUPPORTING SMES.** We are strong partners for SMEs with expertise and commitment for all matters relating to finance – and beyond. With our initiative “Unternehmer Positionen Nord”, or UP° for short, we support our SME clients with comprehensive, up-to-the-minute information at [www.unternehmerpositionen.de](http://www.unternehmerpositionen.de) and regularly at events – always with a clear focus on entrepreneurs and their view of things.

Whether it's interest rate increases in the US, higher oil prices or the failure of TTIP, the energy turnaround in Germany or discussions on inheritance tax – on our website readers will find the latest data, analyses and assessments by our Research team under Dr Cyrus de la Rubia. In addition, we offer articles by experts, comments by well-known journalists and regular interviews with such opinion leaders as Professor Thomas Straubhaar. Our website furthermore offers studies by leading economic institutes on sectors, markets and economic trends – always from the point of view of SMEs and tailor-made for our clients.

Another pillar of UP°: our events, where in 2016 we once again discussed a wide range of issues. We talked to experts about Big Data and the question as to the opportunities these huge quantities of data have for companies. We debated such controversial issues as “Global climate protection – motor or economic killer?” And we discussed Europe – following Brexit and the election of Donald Trump as the new US President – in times of uncertainty and how entrepreneurs can react to the current crisis. Always involved: incisive experts from economy, politics and society.

For example, our list of prominent guests includes the former IBM Chief Technologist Officer and best-seller author Professor Gunter Dueck, Regine Günther, Director General for Politics and Climate at the IMF, former Federal Minister Professor Peer Steinbrück and the Head of the Munich Security Conference, Professor Wolfgang Ischinger. Just as important as the meaningful presentations and discussions: face-to-face meetings – with the guest speakers and the senior management of HSH Nordbank.

And closing the circle: detailed reports on these events can be found at [www.unternehmerpositionen.de](http://www.unternehmerpositionen.de), together with background information and interviews with experts. But you can also follow us on Twitter and Facebook – with these social media channels we have significantly increased the range of our content once again.







*Professor Peer Steinbrück,  
German Federal Minister, retired*



# REJECTION

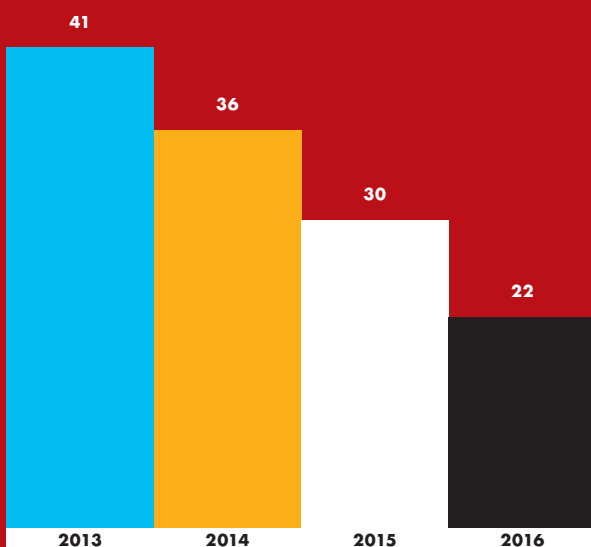
# R ES: UP.

# PROBLEM LOANS REDUCED.

## MAJOR LEGACY ASSETS – GOOD WIND-DOWN SUCCESS.

We have combined all loan portfolios that no longer form part of our core business and are in large part non-performing in our Non-Core Bank. These holdings, most of which originate from before 2009, are largely covered by the guarantee provided by our federal state owners. We are resolutely winding down these problematic legacy portfolios – many of which stem from the Shipping business – in a manner that minimises losses as far as possible. Just in 2016 we reduced our legacy assets by about €10 billion (EAD): we transferred five billion euros' worth to the federal states' public-law institution (AöR) and wound down a further sum of about five billion euros in day-to-day business.

SEGMENT ASSETS OF THE NON-CORE BANK  
in € bn



Overall, our team of restructuring experts has succeeded in cutting the Non-Core Bank's holdings from more than €80 billion in 2009 to slightly over €20 billion in 2016. This corresponds to a **REDUCTION OF WELL OVER 70 PER CENT.** This reduction came about by way of both early and regular repayments as well as loan disposals and structured solutions. The Non-Core Bank's intention for the planning period through to 2019 is to further reduce its non-strategic and capital market holdings significantly while safeguarding value. The Non-Core Bank holds loans from the real estate and aviation sectors, among others, but portfolios related to shipping account for by far the largest proportion. For nine years now, this sector has been in a worldwide crisis of historic proportions with the corresponding fallout on shipping companies.

We reallocated our portfolios in 2016 to provide the clearest possible view of our operational strength and healthy Core Bank. This transaction involved the transfer of primarily non-performing loans to the amount of €6.6 billion to the Non-Core Bank, where they are now being processed and further reduced. At the same time, we transferred good portfolios to the amount of €4.6 billion from the Non-Core Bank to the Core Bank. By resolutely winding down the portfolio, the Non-Core Bank is reducing the Bank's risk-weighted assets and therefore also easing the pressure on the Bank's equity capital. As a result, we are improving our Bank's overall risk-bearing capacity and establishing the conditions for profitable new business.



**EMPLOYEES.** Well trained, motivated and with individual strengths: when it comes to our staff, we know what we can count on. Accordingly, modern HR work has high priority at HSH Nordbank. We provide specific support as well as individual basic and advanced training. We make use of our internal seminar programme to teach specific, specialist content and offer training courses, among other things on communication, methodology and leadership skills. And we are not the only ones who think our HR work is exemplary: in 2015 we were awarded the “Fair Company” label by the *karriere.de* initiative for our promotion of the next generation of employees and the fair treatment of trainees and university graduates. The Absolventa job exchange calls our trainee programme career-enhancing and fair. We were among the finalists in the German national Corporate Health Award with our comprehensive healthcare services, which are tailor-made for the needs of our workforce. We see this as confirmation and, at the same time, as an incentive to carry on precisely at this point.

**COMPLIANCE.** The Compliance division works centrally and across divisions to ensure compliance with the main legal provisions and parameters within HSH Nordbank. It monitors compliance with the legal requirements governing the Bank’s capital market activities, the prevention of money laundering, the financing of terrorism and other criminal acts punishable under the German Banking Act, as well as monitoring compliance with financial sanctions and embargoes. The basic rules of behaviour for the Bank’s employees are summarised in a Code of Conduct. In conjunction with regular training events, employees are provided with a reliable guide regarding legal requirements as well as ethical and societal principles. In addition, HSH Nordbank has established an external office for whistleblowers. It follows up internal tip-offs, including those received anonymously, and passes suspected cases on to the Compliance division.



Judith Steinhoff,  
Head of Human Resources

**INTERNAL AUDITING.** The Internal Audit department provides objective, risk-focused auditing and consulting services that extend across all of the HSH Nordbank’s business activities and processes. It evaluates the effectiveness, efficiency and regularity of risk management, the internal control system and of management and oversight processes. Internal Auditing is involved in all material projects and in all changes to operational processes and structures. It has an unlimited right of information in order to fulfil its mandate. It acts independently and on its own initiative at all times.



WHY DO WE  
ENGAGE IN  
SOCIETY?  
BECAUSE WE  
ENJOY  
DOING SO.



**SUCCESS CANNOT BE MEASURED JUST BY NUMBERS** – of that we are firmly convinced. That

is why we as a bank also live up to our social responsibility. We promote important social activities where we bring different people together – be it during the Kieler Woche international sailing event, the Schleswig-Holstein Music Festival, with the Elbphilharmonie Hamburg foundation or with the HSB Nordbank Run in Hamburg’s HafenCity. At the same time, we support the Herz As (Ace of Hearts) initiative in Hamburg and the Hempels association in Kiel, both of which work with the homeless and socially disadvantaged. Furthermore, since 2015 we have collaborated with the Hamburg branch of the German Child Protection Association in the integration of refugee families. We do all this not only because we consider it our duty or because we think it is the right thing to do, but also because we enjoy doing so.

We support the programme diversity of the Schleswig-Holstein Music Festival (SHMF) as one of its principal sponsors. This sponsorship also includes the **€10,000** Leonard Bernstein Award, which the Savings Bank Finance Group presents each year in collaboration with the SHMF.

With our HSB Nordbank Run we have raised more than **€1.5 MILLION** in donations for the ‘Kids into Clubs’ initiative since 2004. By doing so we have enabled more than **100,000** children and young people to enjoy sports as part of a club.

We are a premium partner of the world’s biggest sailing event, Kieler Woche. Here we have generated more than **€150,000** since 2011 with the ‘Good for Kids’ charity campaign, which helps children and young people to be active in sports.

We are a founding member of the Elbphilharmonie foundation and have thus been contributing to outstanding concerts in Hamburg since 2005. As a ‘Classic Sponsor’, we furthermore support the Elbphilharmonie’s programme of events. As a season opening sponsor, we enabled the Ensemble Resonanz to perform its vibrant classical music in the Elbphilharmonie.

With an independent, business-related arts foundation, we support contemporary art and culture in Schleswig-Holstein.

**HSB  
NORDBANK  
RUN 2016**

in der HafenCity



**ELBPHILHARMONIE  
HAMBURG**



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## REPORT OF THE SUPERVISORY BOARD ON THE 2016 FINANCIAL YEAR.

In the 2016 financial year, the Supervisory Board performed the tasks incumbent on it by law and in accordance with the articles of association. In particular, it monitored the management of the company and provided advice to the Management

# THE SUPERVISORY BOARD

Board in matters relating to corporate governance. In addition to strategic matters relating to the Bank's focus, the Supervisory Board continually obtained information on the Bank's economic and financial development, as well as on the development of individual business segments. The Supervisory Board was provided with explanatory information on any deviations from the plan in the course of business.

In the 2016 reporting year, the Management Board provided the Supervisory Board with regular, timely and comprehensive information on the Bank's business policy and other fundamental issues relating to corporate governance and planning, financial development, operating performance and the Bank's risk, liquidity and capital management, as well as on major legal disputes and transactions and on events of fundamental significance to the Bank. The Supervisory Board was involved in any decisions that were of key significance to the Bank. The Management Board also provided the Chairperson of the Supervisory Board and the Chairpersons of both the Risk and Audit Committees with information on key issues and upcoming decisions between the planned meetings. Where resolutions had to be passed between meetings, the Supervisory Board passed these resolutions using written proceedings.

In the 2016 financial year, the Bank's focus was shaped – in an environment characterised by continued difficult market conditions, the ongoing crisis on the shipping markets and the development of the US dollar – by the final EU decision of May 2016. The EU decision approving the replenishment of the guarantee from €7 billion to €10 billion in 2013 allows the Bank to transfer part of its troubled assets to the sphere of the majority shareholders, the federal states of Hamburg and Schleswig-Holstein, and to sell further non-performing loans itself on the market. At the same time, the Bank was relieved of part of the guarantee fees. These relief measures are tied to the condition that the federal states give up the majority of their shares in the Bank by 28 February 2018. The Supervisory Board was closely involved in both issues. It sought ongoing information on the status of the key milestones on the path towards privatisation and on the sale of loan portfolios and – where necessary – passed corresponding resolutions. The Supervisory Board sought legal advice within this context where necessary.



# REPORT OF SUPERVISORY BOARD FOR THE 2016 FINANCIAL YEAR.

**MEETINGS OF THE SUPERVISORY BOARD.** The Supervisory Board held eleven meetings in the 2016 financial year, six of which were convened as extraordinary meetings.

At all ordinary meetings, the Management Board provided the Supervisory Board with information, based on the figures for each quarter, on the Bank's current financial situation, business developments on the whole and in the individual business segments, as well as in relation to the current business plan, on the risk situation, capital

development and on the liquidity and funding situation. The Management Board also provided the Supervisory Board with regular information on the current status of the EU proceedings and their implementation. The Supervisory Board subjected the reports to critical analysis and, in some cases, requested additional information and documents. The Supervisory Board also addressed various Management Board matters. The auditor of the annual financial statements took part in the Supervisory Board meetings on a regular basis and was available to provide the Supervisory Board with supplementary information.

In addition, two further training events were held for the Supervisory Board in the 2016 financial year. These were used to explain and discuss not only practical issues relating specifically to the Bank, but also new supervisory law developments as well as rights and obligations in connection with the privatisation process.

The meeting held on 11 February 2016 focused on an intensive assessment of the financial, investment and workforce plan for 2016-2018 submitted by the Management Board. The Supervisory Board also addressed its Corporate Governance Report and Declaration of Conformity, as well as the Report of the Supervisory Board for the 2015 financial year. The current challenges facing the corporate business were the subject of an intensive discussion on the basis of a presentation on the Corporate and Wealth Management business segments. A report on the Asset Management implementation project, with the aim of achieving more favourable refinancing for infrastructure projects, was another issue that was addressed. Finally, the Supervisory Board approved the conclusion of an assumption of contract agreement on a partial profit and loss transfer agreement (silent participation) at this meeting.

At its extraordinary meeting held on 16 March 2016, the Supervisory Board looked exclusively at the current status of the EU proceedings and the consequences for the 2015 annual financial statements, whose preparation and adoption were delayed.

At the meeting held on 23 March 2016, the Supervisory Board appointed Mr Temp as a member of the Management Board for a further period of office leading up to 30 April 2019. The Supervisory Board also approved the conclusion of an assumption of contract agreement on four partial profit and loss transfer agreements (silent participations). The Supervisory Board's agenda also included the discussions on the "Report on equity investments", "Overview of secondary employment relationships of Management Board members" and the "Report on donations" of HSH Nordbank, which are conducted once a year.

On 9 May 2016, the Supervisory Board passed a resolution approving the resignation of Mr von Oesterreich as member and Chairman of the Management Board, and the resignation of Mr Wittenburg as member of the Management Board, both with effect from 10th June 2016. The Supervisory Board also appointed Mr Ermisch as Chairman of the Management Board with effect from 10 June and Mr Gatzke as member of the Management Board with effect from 1 July 2016. The Supervisory Board also passed a resolution on an update to the Declaration of Conformity with the German Corporate Governance Code, which was necessary due to the delay in the annual financial statements.

The meeting held on 24 May 2016 focused on the imminent portfolio transfer to the federal states. The Supervisory Board analysed the relevant content and contracts in detail and made corresponding resolution proposals to the Annual General Meeting. One day before

the relevant extraordinary general meeting on 29 June 2016, the Supervisory Board addressed the documents, which were now final, once again and approved the execution of the portfolio transaction on the basis of these final documents. The resolution proposals of the Supervisory Board for the Annual General Meeting were also set out in greater detail accordingly.

The meeting on the annual financial statements, which had been postponed, was held on 8 June 2016. As a result, the main issue covered at this meeting was the approval, based on the recommendation made by the Audit Committee, of the annual financial statements and consolidated financial statements for 2015 following the Supervisory Board's own assessment and prior discussion with the auditor of the annual financial statements. The other standard resolutions to be passed within this context regarding the recommendations to be made to the ordinary Annual General Meeting were also passed. The Supervisory Board also used this meeting to discuss the target achievement level of the Management Board for the 2015 financial year and to pass a resolution on the Management Board targets for 2016. In addition, the Supervisory Board was consulted on the appointment of a new deputy remuneration officer for the Bank.

At its meeting held on 25 August 2016, the Supervisory Board passed a resolution on an amendment to the guidelines in the lending business, which was necessary, in particular, as a result of organisational changes within the Bank. It also approved, in line with the articles of association, the sale of two Airbus A320-200 passenger aircraft owned by a group subsidiary of the Bank as a result of a bailout acquisition. It also received, among other things, a report on the conclusion of a new D&O insurance policy. As Management Board members of the Bank can also be classed as officials, the Supervisory Board had to review the procedure governing the acceptance of gifts or other advantages by Management Board members. This procedure was amended accordingly at the following meeting.

The extraordinary meeting held on 13 October 2016 focused on the report on the Bank's position and, in particular, the status of the implementation of the EU decision.

On 8 December 2016, the Supervisory Board held its last ordinary meeting of the year, addressing issues including the outcome of its efficiency review pursuant to Section 25d of the German Banking Act (KWG) and the evaluation of the Management Board. The history and role of the Advisory Board were the subject matter of a Management Board report for topical reasons. The fact that Dr Morgan had left the Risk Committee at the end of the year meant that a new member had to be elected. This resulted in



Dr Nimmermann being elected to the Risk Committee with effect from 1 January 2017. The Supervisory Board also passed a resolution on an amendment, of a more editorial nature, to the rules of procedure of the Management Board. Finally, the Supervisory Board acknowledged the annual report of the Management Board on the structure of the remuneration systems of HSH Nordbank.

The planned market portfolio transaction prompted another extraordinary meeting of the Supervisory Board in the reporting year, namely on 22 December 2016. The Supervisory Board was provided with detailed information on the current status of the procedure.

Where individual members of the Supervisory Board were affected by resolutions passed by the Supervisory Board or its committees, either in person or on account of their function, or if other potential conflicts of interest arose, then these members did not participate in the deliberations and resolutions in the executive body concerned. The number of other significant mandates held by the Supervisory Board members can be found in the Corporate Governance Report in this Annual Report.

All members of the Supervisory Board took part in at least half of the meetings of the Supervisory Board and the committees of which they are members. The participation rate in all meetings among all members came to around 91 per cent in 2016.

**COMMITTEES OF THE SUPERVISORY BOARD.** The Supervisory Board has formed five committees from among its members that support it in its work.

Last year, the General/Nominating Committee held eleven meetings, six of which were extraordinary meetings. In accordance with the rules of procedure for the Supervisory Board, the General Committee prepared the resolutions of the Supervisory Board and, within this context, addressed the current status of the negotiations with the European Commission, particularly at the beginning of the year, as well as addressing Management Board matters, in particular the timing of, and procedure for, changes at the top of the Management Board and the reduction of the size of the Management Board. Where necessary, resolutions were passed or the Supervisory Board was provided with recommendations on the passing of resolutions.

The Risk Committee met four times during the last financial year and passed one written resolution in writing. Following the cancellation of a meeting that had originally been planned, the Committee was also provided with relevant documents outside of a meeting. Representatives of the auditor of the annual financial statements also took part in the meetings on a regular basis. The Risk Committee

took an intensive look at the Bank's risk position and risk management system. Within this context, it addressed the Strategic Risk Framework, which provides the risk framework for business strategy and planning. In addition to the risk strategy principles, the Strategic Risk Framework (SRF) contains the Risk Appetite Statement (RAS) that is drawn up in line with the requirements set out by the Financial Stability Board (FSB). The SRF also consolidates the risk strategies, the methods for arriving at the RAS, the risk limits and risk guidelines, as well as SRF governance, i. e. the processes, roles and responsibilities within the context of the SRF. Individual commitments that are significant to the Bank were also discussed, such as the portfolio reports on the individual asset classes, which are submitted on a regular basis. The Risk Committee sought information on all commitments subject to a submission requirement and granted its approval for those business transactions requiring approval by law. In particular, reports on current events and developments, and their impact on the risk situation, were made to the Committee at all of its meetings. The extent to which the incentives set by the Bank's remuneration systems take the Bank's risk, capital and liquidity structure into account was assessed at a joint meeting of the Risk Committee and the Remuneration Control Committee.

The Audit Committee met three times in 2016 and also received additional relevant information outside of its meetings. Representatives of the auditor of the annual financial statements took part in all of the meetings. At its first meeting held on 7 June 2016, the members of the Audit Committee discussed the Bank's annual and consolidated financial statements for 2015, as well as the corresponding audit reports, together with the auditor of the annual financial statements. Within this context, the Audit Committee also addressed the Dependent Company Report. The Committee reviewed the independence of the auditor of the annual financial statements in accordance with the requirements set out in the German Corporate Governance Code based on the declaration of independence issued by the auditing firm, and prepared the appointment of KPMG AG Wirtschaftsprüfungsgesellschaft as the auditor of the annual financial statements for 2016. At the meeting of the Audit Committee held on 24 August 2016, the auditor of the annual financial statements presented its results of the review of the half-year financial report and discussed them with the Committee before the report was published.

This meeting was also used to discuss the initial results of the audit of the annual financial statements with the Committee. The Audit Committee also acknowledged the new requirements to be met by the Audit Committee and the Supervisory Board as a result of the EU audit reform. At the meeting held on 7 December 2016, the Audit Committee addressed the project to implement the requirements resulting from the EU audit reform in detail.

The Committee discussed the corresponding reports to satisfy itself as to the effectiveness of the risk management system – in particular the internal audit and internal control system. Furthermore, the Committee discussed the results of the securities account audit and the audit of investment services pursuant to the German Securities Trading Act (WpHG). Finally, the topics covered by the meeting also included current reports on IT restructuring and IT strategy.

The Remuneration Control Committee met three times in the reporting year and also held an additional joint meeting with the Risk Committee. It took an in-depth look at the Bank's remuneration systems and received regular reports on the status of the implementation of the requirements resulting from the German Ordinance on the Remuneration of Financial Institutions (Institutsvergütungsverordnung), and on the current status of statutory developments relating to remuneration in the banking sector. The remuneration officer also reported on the Remuneration Control Committee on the results of his control activities and presented his remuneration control report, which has to be prepared once a year, to the Committee. The Chairperson of the Remuneration Control Committee consulted the remuneration officer on relevant issues on a regular basis even outside of the meetings.

There was no need for any meeting of the Mediation Committee, which is to be set up in accordance with the provisions of the German Co-Determination Act (Mitbestimmungsgesetz), in 2016.

The Chairpersons of the Committees regularly reported to the Supervisory Board during the subsequent plenary sessions about the work and results of the Committees' deliberations.

## **AUDIT AND ADOPTION OF THE FINANCIAL STATEMENTS AND CONSOLIDATED FINANCIAL STATEMENTS FOR 2016**

The accounts, annual financial statements including the status report and the consolidated financial statements including the Group status report for 2016 were audited by KPMG AG Wirtschaftsprüfungsgesellschaft. KPMG were elected as auditors and Group auditors by the shareholders for the 2016 financial year at the Annual General Meeting on 19 July 2016. All audits resulted in an unqualified auditor's certificate with an explanatory note saying that, without limiting this assessment, the going concern assumption for accounting and valuation as well as the continued existence of HSH Nordbank AG and key group companies is based, in particular, on:

(i) full and on-time conclusion of the agreements required for implementation of the EU Commission's formal decision in the EU state aid proceedings on replenishment of the second-loss guarantee as well as HSH Nordbank AG and its shareholders implementing the formal decision fully and on time.

(ii) a sale of the operational HSH Nordbank AG having taken place by 28 February 2018 by way of an open, discrimination-free, competitive and transparent process at a favourable selling price free of state aid and the EU having approved the new corporate structure following a viability review. Should the selling process not, by the disposal deadline, lead to favourable bids free of state aid or the EU Commission conclude the viability review with the finding that integrating the operating company in the new corporate structure would not result in a business model that is viable in the long term, the operating company would discontinue its new business and manage its assets within the scope of what is legally permissible with the objective of an orderly wind-down. Should the Bank, for this or another reason, enter a wind-down or there were to be a rating downgrade or another adverse development during the privatisation period, this could trigger significant outflows of short-term funds and fundamentally restrict HSH Nordbank's funding options. In the event of material, unexpected outflows, additional measures by the owners and/or third parties to strengthen the liquidity situation would be required.

(iii) a complete disposal, within the framework of the process to privatise HSH Nordbank AG that is under way, of HSH Nordbank AG as an entire Bank, i. e. the sale of the shares in the Bank held by the vendor including all assets and liabilities without material, advance disposals of assets or sub-segments below the carrying amounts in the case of outstanding bids for a complete sale. Should extensive disposals of loan portfolios especially in the Non-Core Bank be necessary, this could require substantial, additional loan loss provisions that would not be offset by the guarantee as well as major write-downs of deferred taxes.

(iv) the minimum capital requirements on all regulatory assessment levels according to the corresponding SREP decisions of the European Central Bank as well as the legal requirements being adhered to during the forecast period. Should substantial, additional loan loss provisioning expenses as well as write-downs of deferred taxes be required (e. g. in the scenario described above) or the recovery of the shipping market assumed in the Bank's planning does not occur, or the material transfer of risk for the second loss guarantee is no longer given from the perspective of the banking supervisory authority, this could result in major strain on the capital ratios. This could in turn require additional measures by the owners and/or third parties to strengthen the capital ratios to be able to adhere to the minimum capital requirements, especially at the level of the financial holding group. A wind-down of HSH Nordbank could ensue if corresponding measures cannot be applied.



Furthermore, it is necessary that the acceptance of market participants and other relevant stakeholders required for the successful implementation of HSH Nordbank's business model and the stipulations arising from the EU Commission's formal decision is maintained or gained.

The documentation relating to the financial statements and the audit reports together with all attachments were sent out to the members of the Supervisory Board. The auditor initially reported on the implementation and material results of his audit at the meeting of the Audit Committee on 28 March 2017. The Audit Committee discussed the results in detail with the auditor on this basis and on the basis of its own audit. At the Supervisory Board meeting on 29 March 2017, the Chairman of the Audit Committee reported to the Supervisory Board on the result of the deliberations on the Audit Committee. The auditors took part in the meeting of the Supervisory Board and also reported on the material results of their audit there. On the recommendation of the Audit Committee, the Supervisory Board finally agreed with the findings of the audits following its own examination of the reports of the auditors and in-depth discussion and established that following the final result of its own inspections there were no objections to be raised. The Supervisory Board adopted the 2016 annual financial statements prepared by the Management Board and approved the 2016 consolidated financial statements. Furthermore, it adopted the report of the Supervisory Board for the 2016 financial year.

The Management Board also presented its own report on relations with associated companies (dependence report) in fiscal year 2016 to the Supervisory Board and the statutory auditor on time. The statutory auditor has reviewed the dependence report and issued the following unqualified auditor's certificate: "Following our obligatory examination and evaluation performed in accordance with professional standards, we hereby confirm that 1) the factual statements of the report are correct; and 2) the Company's services with respect to the transactions listed in the report were not disproportionately high."

The Audit Committee and the Supervisory Board have reviewed the Management Board's dependence report and the statutory auditor's audit report and have held discussions with the Management Board and the statutory auditor in the context of the annual financial statements. The Supervisory Board agreed with the results of the statutory auditor's report because, in its assessment, no objections could be raised to the Management Board's statement on the dependence report.

**CHANGES IN PERSONNEL.** Ms Auerbach resigned as trade union representative on the Supervisory Board with effect from 31 March 2016. Ms Cornelia Hintz was appointed by the court as her successor with effect from 18 May 2016. The Supervisory Board would like to thank Ms Auerbach for her many years of commitment.

There were several changes within the Management Board in the 2016 reporting year. Constantin von Oesterreich and Matthias Wittenburg left the Bank's Management Board with effect from 10 June 2016. Mr Stefan Ermisch was appointed to succeed Mr von Oesterreich as Chairman of the Management Board with effect from 10 June 2016. Mr Oliver Gatzke was appointed member of the Board of Management with effect from 1 July 2016.

The Supervisory Board would like to thank the Management Board and all of the Bank's employees for their considerable commitment and performance in an environment that has been difficult for the Bank.

Hamburg/Kiel, 29 March 2017

The Supervisory Board

Dr Thomas Mirow

*Chairman of the Supervisory Board of HSH Nordbank AG*



# CORPORATE GOVERNANCE

## **ALL STATEMENTS IN THIS CORPORATE GOVERNANCE REPORT REFLECT THE SITUATION THAT PREVAILED ON 16 FEBRUARY 2017.**

As an unlisted company, HSH Nordbank has been recognising the German Corporate Governance Code (GCGC) voluntarily since 2005. The Management Board and the Supervisory Board of HSH Nordbank expressly support the recommendations and objectives of the GCGC. Corporate governance at HSH Nordbank is also principally based on the provisions of the German Stock Corporation Act, the German Banking Act and internal rules such as the Articles of Association and the rules of procedure that apply to the Management Board and the Supervisory Board, as well as the Code of Conduct of HSH Nordbank. By presenting our system of corporate governance and control and transparent reporting on conformity to the recommendations of the Code, we aim to strengthen the confidence that investors, clients and employees, as well as the general public, have in HSH Nordbank.

## **DECLARATION IN ACCORDANCE WITH SECTION 161 OF THE GERMAN STOCK CORPORATION ACT.**

In accordance with Section 161 of the German Stock Corporations Act, the Management Board and Supervisory Board of listed companies must publish an annual declaration of how their management and supervision systems conform to the recommendations of the German Corporate Governance Code or deviate from them. Our aim is to conform to the GCGC as fully as possible even as a non-listed company. In February 2017, the Management Board and the Supervisory Board of HSH Nordbank therefore voluntarily issued the Declaration of Conformity set out below, in which the deviations from the GCGC recommendations are disclosed.

**DECLARATION OF CONFORMITY.** The Management Board and the Supervisory Board of HSH Nordbank declare that since publishing their last Declaration of Conformity on 9 June 2016, HSH Nordbank has conformed to the recommendations of the German Corporate Governance Code in the version dated 5 May 2015 respectively in every respect save for the exceptions stated below. Until the date on which the next Declaration of Conformity is published, HSH Nordbank will be conforming to all the recommendations of the Code in the version dated 5 May 2015 save for the exceptions stated below.

Pursuant to Section 4.2.3, Management Board remuneration is to contain fixed and variable elements.

*In line with the requirements set out in the EU state aid decision and the Bank's obligation within the framework of the guarantee provided by the federal states of Hamburg and*



# ATE ANCE.

*Schleswig-Holstein, the current remuneration system for the Management Board does not involve any variable remuneration for the members of the Management Board.*

Pursuant to Section 4.2.3.3, the Supervisory Board is to establish, in respect of pension schemes, the level of provision aimed for in each case and take into account the resulting annual and long-term expense for the company. *A defined contribution plan is in place for the Management Board members of HSH Nordbank that does not aim at a certain level of provision.*

In accordance with Section 4.2.4, the total compensation of each one of the members of the Management Board is to be disclosed by name, divided into fixed and variable compensation components. *This is not a GCGC recommendation, but rather a mandatory statutory provision for listed companies, because the German Commercial Code (HGB) sets out a mandatory disclosure requirement for listed companies. As an unlisted company, however, HSH Nordbank is not subject to this obligation in principle. Furthermore, the parameters of Management Board remuneration have already been made sufficiently public in line with the requirements set out by the European Commission – set upper threshold for basic salary, no variable remuneration.*

In accordance with Section 4.2.5, model tables are to be used to provide certain pieces of information on remuneration and fringe benefits for each Management Board member. *As HSH Nordbank does not disclose the Management Board remuneration paid to individual members, this information is not published either. (See also Section 4.2.4)*

In accordance with Section 5.4.1.2, the Supervisory Board is to specify concrete objectives regarding its composition, including a limit of length of membership to be specified for the Supervisory Board.

*The Supervisory Board has decided not to set a limit of length of membership for the Supervisory Board, as the optimum length of membership is difficult to define and, given the Bank's current situation, the aim is to retain the existing expertise within the Supervisory Board.*

According to Sentence 4 of Section 7.1.2, the consolidated financial statements shall be publicly accessible within 90 days of the end of the financial year and interim reports shall be publicly accessible within 45 days of the end of the reporting period. *HSH Nordbank did not publish the consolidated financial statements for 2015 or the interim reports for 2016 by the specified deadlines. The Bank is likely to publish the consolidated financial statements for 2016 by the recommended deadline. The Bank is working on adhering to the recommended deadline for the publication of the interim reports in the future, too.*

HSH Nordbank has complied with the recommendations set out in the Code insofar as they make sense for an unlisted corporation.

Hamburg/Kiel, 16 February 2017

For the  
Management Board:



Stefan Ermisch

For the  
Supervisory Board:



Dr. Thomas Mirow

**SUPERVISORY BOARD. COMPOSITION:** HSH Nordbank's Supervisory Board consists of 16 members, of whom – in accordance with the provisions of the German Co-Determination Act (Mitbestimmungsgesetz) – half are representatives of the capital side and half are employee representatives. The capital side of the Supervisory Board predominantly comprises expert representatives of the business world who are independent of the shareholders and the Bank. Four Supervisory Board members have held management positions at German and international financial institutions in the past. One member is also a member of the Management Board of a credit insurance company. The Supervisory Board also includes a self-employed auditor, a managing director of an international private equity company and a managing director of an investment holding company.

Section 5.4.1 of the GCGC stipulates that the Supervisory Board shall specify concrete objectives regarding its composition which, whilst considering the specifics of the enterprise, take into account the international activities of the enterprise, potential conflicts of interest, the number of independent Supervisory Board members, an age limit to be specified for the members of the Supervisory Board and diversity. The latter objective shall, in particular, provide for an appropriate degree of female representation.

The objectives set by the Supervisory Board back in 2011 are as follows:

1. HSH Nordbank will seek to continue to have at least the same number of international members on its Supervisory Board as it currently has (minimum one member).
2. When nominating new members to the Supervisory Board, HSH Nordbank will seek to avoid potential conflicts of interest, while also taking the rules of procedure for the Supervisory Board into due consideration, in future as well.
3. HSH Nordbank will seek to adhere to the age limit of 68 years at the date of appointment stipulated in the Rules of Procedure for the Supervisory Board in future.
4. HSH Nordbank will seek to maintain the proportion of representation by women at least at the current level of 20% in future as well. The Supervisory Board considers representation by women of initially 30% to be an appropriate objective.
5. On the shareholder side, the Supervisory Board will aim to have independent members comprise at least half of its members in the future, too. (Objective added in 2012)

When nominating new members, care is taken to prevent potential conflicts of interest and ensure the impartiality of the members. New members have fallen below the age limit of 68 years at the time of appointment in each case. The Nomination Committee also takes the objective of ensuring appropriate gender diversity levels into account when nominating new Supervisory Board members, to be

elected by the Annual General Meeting, to the Supervisory Board. As a company subject to co-determination, HSH Nordbank also falls under the scope of the German Act on Equal Participation of Women and Men in Executive Positions in the Private and the Public Sector (Gesetz für die gleichberechtigte Teilhabe von Frauen und Männern in Führungspositionen in der Privatwirtschaft und im öffentlichen Dienst), also known as the "Quota Act". As a result, the Supervisory Board has once again confirmed its previous target for the proportion of women on the Supervisory Board. With 37.5% female members, the Supervisory Board has already reached the target it had set itself. On the shareholder side, the proportion of women comes to 25% while on the employee side, it comes to 50%.

As part of its annual efficiency review, the Supervisory Board looked at the skills, competencies and experience within the Supervisory Board and updated its competence profile, which was prepared for the first time in 2014. The competence profile gives the Supervisory Board an overview of the competencies represented within the Supervisory Board. This means that, when members have to be appointed to the Supervisory Board or when the Supervisory Board is looking for suitable candidates in the future, it can draw up corresponding objectives directly to make sure that competencies are replaced/additional competencies added.

**PROCEDURE:** The Supervisory Board appoints, monitors and advises the Management Board and is involved in fundamental decisions made by the Bank. The Management Board informs the Supervisory Board regularly and in good time of the proposed business policy and other fundamental matters during the meetings and also orally, particularly in conversations between the Chairman of the Management Board and the Chairman of the Supervisory Board.

Section 25d (11) sentence 2 No. 3 of the German Banking Act (KWG) requires the Supervisory Board to evaluate the structure, size, composition and performance of the management and supervisory body on a regular basis, at least once a year. For this purpose, the Supervisory Board used questionnaires, as in the previous year, not only to evaluate various aspects of its own work, but also to evaluate the work of the Management Board. The efficiency review conducted in the autumn of 2016 revealed that the Supervisory Board is satisfied with the efficiency of its activities on the whole. In order to further improve its efficiency, the Supervisory Board used the answers to the questionnaires to pass isolated measures and identify topics for further training. The implementation of these measures shall be followed up on on a regular basis.

# SUPERVISORY B SHAREHOLDERS,



In order to ensure that the Supervisory Board has up-to-date specialist and expert knowledge at all times, two further training events were held for the Supervisory Board last year. The topics covered by the events resulted partly from the 2015 efficiency review, in which Supervisory Board members had proposed further training topics, but also from current developments. At these events, the Supervisory Board underwent further training on new supervisory law developments and bank-specific matters with internal and external speakers, and took an intensive look at the rights and obligations of the Management Board and the Supervisory Board during a privatisation process.

**OTHER MANDATES:** In order to be able to perform their Supervisory Board duties properly, the Supervisory Board members have to devote sufficient time to these activities. This means that the individual Supervisory Board members can only have a limited number of other duties over and above their Supervisory Board activities. The Supervisory Board members of HSH Nordbank have the following number of other Supervisory Board mandates at other companies:

Supervisory Board member	No. of other mandates (as of 31/12/2016)
Dr Thomas Mirow	2
Peter Axmann	2
Stefan Jütte	1
Dr Rainer Klemmt-Nissen	4
Dr David Morgan	4
Dr Philipp Nimmermann	4
Elke Weber-Braun	2

Detailed information on the Supervisory Board’s activities in 2016 can be found in the Report of the Supervisory Board.

**REMUNERATION:** The remuneration paid to the Supervisory Board is disclosed for each individual member in the notes to the annual financial statements.

**MANAGEMENT BOARD. COMPOSITION:**

The Management Board of HSH Nordbank has consisted of four members since June 2016 and is split into the following areas of Board responsibility: CEO, CFO, CRO and front office. When selecting new Management Board members, the Supervisory Board must adhere to the relevant legal requirements. The issue of diversity plays a key role in this regard. Pursuant to the German Quota Act, the Supervisory Board has set a target of 20% female members for the Management Board of HSH Nordbank that is to be

met, if possible, by 30 June 2017. The German Corporate Governance Code also requires, in particular, the appropriate representation of women, while the German Banking Act states that consideration should be given to ensuring balanced and varied knowledge, skills and experience for all Management Board members. The rules of procedure for the Supervisory Board also contain requirements that the Supervisory Board and/or the General/Nominating Committee has to take into account when identifying applicants to fill a Management Board position. This means that the Supervisory Board looks at the Management Board position to be filled on a case-by-case basis and selects Management Board members taking into account the requirements of the position in question and the competencies already represented on the Management Board based on an individual job profile.

**PROCEDURE:** The Management Board is responsible for the management of the Bank and works with HSH Nordbank’s other corporate bodies and with the employees’ representatives on a basis of mutual trust in the Bank’s best interests. It defines the Bank’s strategic alignment in consultation with the Supervisory Board. The Chairman of the Management Board represents the Management Board as a collegial body, presides over its meetings and coordinates its work. The Management Board largely met once a week during the period under review. The members of the Management Board are jointly responsible for running the Bank’s business. Their duties and responsibilities are laid down in the Rules of Procedure for the Management Board, as supplemented by the business allocation plan.

**OTHER MANDATES:** One Management Board member has a mandate on the Administrative Board of one of the Bank’s subsidiaries. Other than this, the Management Board members do not perform any management or supervisory functions at other companies.

**REMUNERATION:** Details of the compensation system for the Bank’s Management Board can be found in the management report and the notes to the annual financial statements.

**SHAREHOLDERS, ANNUAL GENERAL MEETING.** HSH Nordbank’s shareholders exercise their rights at the Annual General Meeting. The Management Board convenes the Annual General Meeting once a year, stating the agenda and including the requisite reports and documents.

One extraordinary general meeting was held in June 2016 to look at the portfolio transaction. In addition to the agenda items that an Annual General Meeting has to cover by law, the ordinary Annual General Meeting held in July 2016 also passed necessary resolutions on three silent participation agreements.

# BOARD, MANAGEMENT BOARD, ANNUAL GENERAL MEETING.

# CONTACT

HSH Nordbank AG  
Gerhart-Hauptmann-Platz 50  
20095 Hamburg, Germany  
Phone +49 40 3333-0  
Fax +49 40 3333-34001

Martensdamm 6  
24103 Kiel, Germany  
Phone +49 431 900-01  
Fax +49 431 900-34002

info@hsh-nordbank.com  
www.hsh-nordbank.de

## INVESTOR RELATIONS

Phone +49 40 3333-11500  
investor-relations@hsh-nordbank.com

## MEDIA RELATIONS

Phone +49 40 3333-12973  
Fax +49 40 3333-34224  
presse@hsh-nordbank.com

## MARKETING & DIGITAL MEDIA

Phone +49 40 3333-14136  
Fax +49 40 3333-34224  
marketing@hsh-nordbank.com

# IMPRINT

## CONCEPT AND BASIC DESIGN

Philipp und Keuntje GmbH, Hamburg

## PRODUCTION

HSH Nordbank/Philipp und Keuntje GmbH

## PHOTOS

Kotte, Anatol  
Rätzke, Thies  
Wied, Sven

## PRINTED BY

HSH Nordbank AG

## NOTE:

If at times only the masculine form is used for certain terms relating to groups of people, this is not meant in a gender-specific manner, but occurs exclusively for the sake of better readability.

This Annual Report was published on 30 March 2017 and is available at [www.annualreport2016.hsh-nordbank.com](http://www.annualreport2016.hsh-nordbank.com). This is an English translation of the original German version of the Annual Report.

## FORWARD-LOOKING STATEMENTS:

This Annual Report includes certain forward-looking statements. These statements are based on our beliefs and assumptions as well as conclusions drawn from information currently available to us from sources that we consider to be reliable. A forward-looking statement involves information that does not simply reflect historical facts, including information relating to possible or anticipated future growth and future economic developments.

Such forward-looking statements are based on a number of assumptions concerning future events and are subject to uncertainties, risks and other factors, many of which are beyond our control. Therefore, actual events may differ considerably from those forecast in the forward-looking statements. In view of this, you are advised never to rely to an inappropriate degree on forward-looking statements. We cannot accept any liability for the accuracy or completeness of these statements or for the actual realisation of forecasts made in this Annual Report. Furthermore, we are not obliged to update the forward-looking statements following the publication of this information. In addition, information contained in this Annual Report does not represent any kind of offer for the acquisition or sale of any type of securities of HSH Nordbank AG.



**FIGURES  
THAT  
WORK.**

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# AGEMENT

## BASIS OF THE GROUP

### BUSINESS ACTIVITIES

#### Headquarters, regional focus, clients and products

HSH Nordbank AG was established in June 2003 by the merger of Hamburgische Landesbank – Girozentrale – with Landesbank Schleswig-Holstein Girozentrale (LB Kiel) and is managed in the form of a German public limited company (Aktiengesellschaft – AG). The headquarters of the Bank are located in Hamburg and Kiel.

HSH Nordbank is one of the leading banking partners for upper medium-sized enterprises in the core region of Northern Germany. HSH Nordbank is also active throughout Germany primarily in the corporate and real estate clients business. The focus of the project financing business in the Corporate Clients division (Energy & Utilities and Logistics & Infrastructure business areas) additionally is on the rest of Europe. The Bank conducts business with shipping clients throughout the world. Based on classical loan financing HSH Nordbank offers a wide range of appropriate financing solutions tailored to the needs of corporate clients, wealthy private clients, savings banks and institutional clients.

#### Segments, divisions and locations

The business activities of HSH Nordbank are split between the Core Bank, which includes the strategic business divisions, and the Non-Core Bank, in which predominantly non-performing legacy portfolios from the years prior to 2009 are held. The administrative divisions and overall bank positions are disclosed as segments not subject to reporting requirements in the “Other and Consolidation“ division.

The Bank adjusted its internal reporting, and therefore segment reporting as well, in the second half of 2016 on the basis of the organisational changes implemented. The focus was on mapping the value creation structures of the individual segments in a more transparent manner based on causation. In conjunction with combining the market divisions under the responsibility of a single Management Board member the previous segments – Shipping, Project & Real Estate Financing and Corporates & Markets – were dissolved and transferred to the Real Estate, Shipping, Corporate Clients and Treasury & Markets segments. At the same time, the Bank made a portfolio reallocation between the Core Bank and Non-Core Bank (formerly: Restructuring Unit), which resulted in the optimisation of the Core Bank portfolio and consistent allocation of non-performing legacy portfolios earmarked for winding down to the Non-Core Bank. The complexity of the Group structure was thereby markedly reduced and the transparency of internal reporting and therefore segment reporting further increased.

The streamlining of the organisational structure was driven forward in addition to the changes made to the internal reporting, including segment reporting, as part of the cost reduction programme. In this regard, the Management Board was reduced from 5 to 4 members, the number of chief representatives from 2 to 1 and the divisions from 25 to 18. The lending processes of the Non-Core Bank were also integrated into the area of responsibility of the CRO as at 1 November 2016, whereby cross-divisional efficiency potential will be exploited to a greater degree in the future, expertise pooled in risk management and lending standards harmonised. Furthermore, methods for integrated bank steering were refined based on a close interaction between the CFO and CRO areas of responsibility in line with the statutory requirements (SREP, BCBS 239, among other things).

As part of the focussing of its business activities HSH Nordbank has significantly reduced its international network of locations over the past years and closed a number of branches abroad. HSH Nordbank continues to maintain branches in Singapore, Athens and Luxembourg as well as representative offices in Hong Kong and New York in line with its strategic direction. The branch in Luxembourg primarily provides services for the Non-Core Bank. In Germany, HSH Nordbank is represented in Berlin, Hanover, Düsseldorf, Munich, Stuttgart and Frankfurt am Main. The branches listed above are of secondary importance for understanding the Group situation of HSH Nordbank.

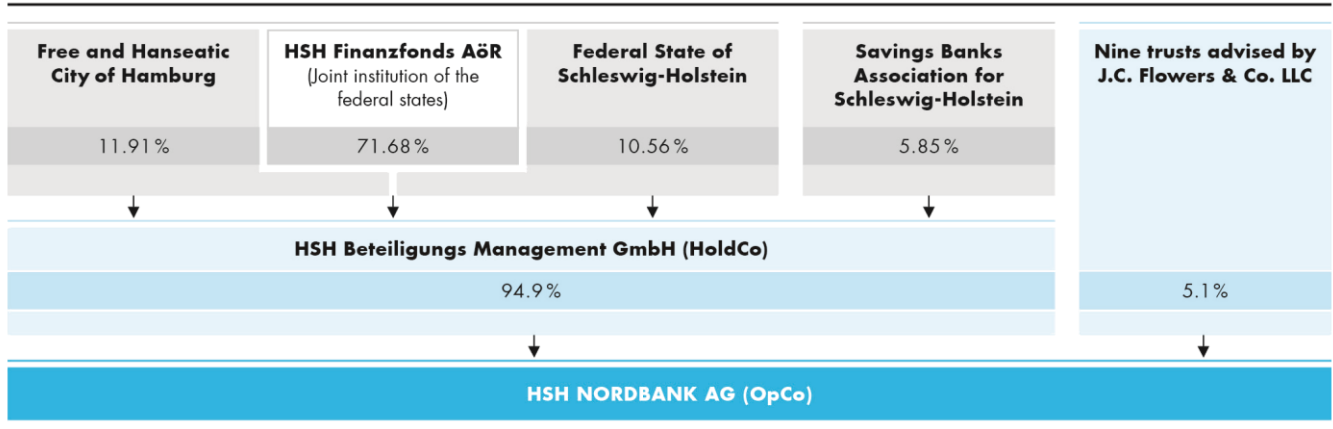
#### Equity holdings and scope of consolidation

The Bank has also sharply reduced its equity holding portfolio over the past years. At the 2016 year end the scope of consolidation for the Group financial statements included, in addition to the parent company, HSH Nordbank AG, 57 fully consolidated subsidiaries compared to 61 fully consolidated subsidiaries as at 31 December 2015. Significant additions to the scope of consolidation comprise, inter alia, the FSL Group, Singapore, included for the first time in the scope of consolidation (three fully-consolidated companies, one company accounted for under the equity method) and Amentum Aircraft Leasing No. Seven Ltd., Dublin. Disposals relate to Amentum Aircraft Leasing No. Three Ltd., Dublin, and SPE II Pissarro, SAS, Paris, companies no longer in the scope of consolidation as well as further changes primarily resulting from internal corporate reorganisations within the Group (integration, mergers). Subsidiaries of HSH Nordbank AG do not have branches that would be relevant for an understanding of the Bank's situation.

The impact of these changes to the scope of consolidation on the income statement is outlined in the Earnings section of this Group management report. Further details on the scope of consolidation are set out in Note 6 (Consolidation Principles) in the Group explanatory notes.



## OWNERSHIP STRUCTURE

**Ownership structure, guarantee and EU proceedings**

The principal owner of HSH Nordbank AG as at the 2016 year end is HSH Beteiligungs Management GmbH with a shareholding of 94.9%. Private investors advised by J.C. Flowers & Co. LLC also have a shareholding of 5.1%. The Free and Hanseatic City of Hamburg and the federal state of Schleswig-Holstein indirectly hold a combined shareholding of 89.35% via HSH Beteiligungs Management GmbH and 5.55% is held by the Savings Bank Association (Sparkassen- und Giroverband) for Schleswig-Holstein.

The federal states of Hamburg and Schleswig-Holstein issued via HSH Finanzfonds AöR a guarantee in favour of HSH Nordbank that provided capital relief (second loss guarantee), but which did not affect liquidity at that time, under which payment defaults in a specified portfolio are hedged (mainly in the Non-Core Bank). First piece losses incurred in this portfolio are to be borne by HSH Nordbank itself up to an amount of €3.2 billion. Further details are set out in Note 3 in the Group financial statements. Details regarding the impact of the guarantee on the net assets, financial position and earnings in 2016 are set out in the Economic report section.

In 2013, the guarantee facility provided by Hamburg and Schleswig-Holstein was replenished after a reduction in 2011 from €7 billion to the original facility of €10 billion in view of the changed underlying conditions. This measure was initially provisionally approved by the EU Commission in 2013. At the same time, the EU Commission instituted state aid proceedings to investigate whether the replenishment of the guarantee is consistent with state aid rules. In these EU state aid proceedings the owners, Hamburg and Schleswig-Holstein, the Federal Republic of Germany and the EU Commission, reached an informal agreement on 19 October 2015 to provide significant

relief to the Bank from the adverse impact of legacy assets and guarantee fees. It is also envisaged that HSH Nordbank be privatised by 28 February 2018. Based on the informal agreement the EU Commission reached a formal decision in the state aid proceedings on 2 May 2016 (hereinafter referred to as the EU decision) and thereby finally approved the replenishment of the second loss guarantee issued by the federal states. The decision of the EU Commission confirms the informal agreement in principle and defines it in concrete terms and is based on a list of conditions and commitments, which contains the foundations of the agreement, provided to the EU Commission by the Federal Republic of Germany as the representative of the federal state owners of HSH Nordbank.

The purpose of the structural measures envisaged in the list of conditions and commitments is to improve the financial and risk situation and create the basis for a sustainable structure and viable business model.

However, from today's perspective, the originally intended improvements are due to the existing capital structures only partially suited to reduce the high proportion of NPE significantly. The second loss guarantee granted in 2009 had no direct liquidity effect at that time, on the basis of which the necessary, accelerated winding down of non-performing loans could have been carried out. Instead, complex settlement conditions under the guarantee agreement mean that economically sound wind-down measures can only be taken to a limited extent. Furthermore, total guarantee premiums of €3.2 billion paid to date have also put considerable strain on the capital base

available for the absorption of potential losses. From today's perspective, the recapitalisation of HSH Nordbank at the time of the financial crisis in the form of a second loss guarantee of € 10 billion has proved to be disadvantageous from an economic point of view when compared to a strengthening of capital at that time that would have had an effect on liquidity.

The formation of a holding structure under the EU decision should have mainly relieved HSH Nordbank of a proportion of the high guarantee fees, which have adversely impacted the business model and restructuring efforts. HSH Nordbank as the parent institution of the financial holding company (HoldCo) for prudential purposes is, however, required to comply with the regulatory requirements at the financial holding level. In this regard, the intended relief for HSH Nordbank only has a limited effect on the financial holding group due to the regulatory requirements. This results in restrictions, particularly with respect to the requirements for compliance with capital ratios, large exposure limits, regulatory reporting and the recovery plan. HSH Nordbank's Management Board has no influence over the decisions made by the HoldCo.

Further information on the EU decision can be found in the Business developments section under Major developments and events as well as in the Forecast, opportunities and risks report.

### Membership in the German Savings Banks Finance Group

HSH Nordbank is a member institution of the German Savings Banks Finance Group, which has an institutional protection scheme. This scheme protects deposits held at a savings bank, Landesbank or a Landesbausparkasse. The objective of the protection scheme is to protect the member institutions and avert emerging or existing financial difficulties at these institutions.

The Deposit Guarantee Act (EinSiG) entered into force in Germany on 3 July 2015. The Act implements the relevant EU Directive. The German Savings Banks Finance Group has modified its proven protection scheme to meet these statutory requirements, and the scheme has been recognised as a deposit guarantee fund under the EinSiG.

### External influencing factors and processes

Besides the EU decision and the underlying list of conditions and commitments, other material external factors influencing HSH Nordbank's business include economic and financial market developments (movements in the EUR/USD exchange rate, interest rate level inter alia), developments in the relevant industry sectors such as the shipping industry (particularly charter rates and ship values), regulatory requirements and discretionary decisions of the supervisory authorities, external ratings, assessments of capital market participants and other stakeholders as well as the further course of the privatisation process

HSH Nordbank has defined processes within its business organisation that form the basis for operating and managing the Bank as well as for its internal control system. The main processes include strategy and planning, corporate management, customer management, financing, capital market as well as support processes.

## OBJECTIVES AND STRATEGY

HSH Nordbank's vision is to be a Bank for Entrepreneurs from the metropolitan regional base of Hamburg. Central to this perceived role is a focussed and entrepreneurial approach that creates added value for clients, shareholders and the Bank. The overall objective of HSH Nordbank is to support the Northern German economy in particular and to provide larger medium-sized enterprises with an appropriate services and product portfolio with regard to all aspects of loan financing. The Bank is a competent partner for both business and private matters particularly for medium-sized enterprises in their home region of Northern Germany and also throughout Germany and abroad on an industry-specific basis.

The Bank is developing strategies that are embedded in HSH Nordbank's strategy architecture to achieve its objectives.

Based on the Bank's mission statement, in which the objectives, strategy, purpose and values are combined in an appropriate framework, HSH Nordbank's strategy architecture includes the following central components:

### STRATEGY ARCHITECTURE





The strategic risk framework, which, as a framework document, describes the direction of the Bank's risk management and establishes the foundation for the risk culture, provides consistent guidelines for effectively aligning the organisation and business operations to the basic risk-strategy principles. The strategic risk framework includes the risk coverage potential (risk capacity), which is determined on the basis of the capital and liquidity resources available as well as key guidelines for risk-conscious actions on part of the Bank. Furthermore, tolerance ranges for the utilisation of risk capacity are determined for all material risks on the basis of various scenarios and the risk appetite. Details on the bank-specific risk types are explained in the Risk report section.

The business strategy, which is to be defined by management, describes the overriding strategic direction with regard to the business model and business area portfolio of the Bank. This transposes the overall strategic model into a specific strategic direction and plan. It describes the Bank's objectives for each key business activity and the measures to be taken to achieve these objectives. In this context, long-term objectives are to ensure sustained profitability and a manageable risk profile, to establish long-standing and solid customer relationships and follow a cross-selling approach. HSH Nordbank's operating business model comprises the Core Bank, in which the Bank's strategic divisions are consolidated, and the Non-Core Bank, which is responsible for ensuring that the portfolios bundled there are wound down in a swift and risk-commensurate manner. The business strategy also includes the definition of the strategic business areas and formulates a business area strategy for each business area. The business area strategies describe the strategic targets in the Bank's business divisions and define concrete implementation measures for each business area. An essential component for defining strategic goals and monitoring implementation are quantitative performance indicators, which are defined by a bank-wide target system as the basis for measuring performance and the effectiveness of the business strategy.

A consistent risk strategy is determined on the basis of the business strategy and the strategic risk framework. This includes developments in the key business activities planned in the business strategy taking due account of risk strategy factors and liquidity aspects as well as the measures required to achieve these goals.

The funding strategy establishes the framework for the active and sustainable management of funding and liquidity. It is a core component of HSH Nordbank's overall bank management processes.

Functional strategies, which are not formally part of the strategy process, are defined on the basis of the Bank's core business strategies. The long-term IT objectives are set in the IT strategy. Developments in the key business activities planned for the business areas are also taken into account. The personnel management tools required for the monitoring and support of HSH Nordbank are anchored in the human resources strategy.

Taking account of the business and risk strategy the lending standards define a binding and comprehensive framework for all parties concerned under which the lending business may be conducted.

HSH Nordbank's stated objectives and strategies are basically aimed at ensuring the sustainable development of the institution. This is also the subject of the ECB's integrated analysis conducted as part of the supervisory review and evaluation process (SREP), based on which banks are monitored taking into account the business model, capital and liquidity position and governance structures.

#### **Strengthening of the Bank for Entrepreneurs and systematic winding down of the legacy portfolios within the limits set by the guarantee agreement**

In order to implement the business model with a sustainable focus HSH Nordbank is continuing to concentrate on strengthening the strategic business areas of the Core Bank and, at the same time, on winding down the risky legacy portfolios which are bundled in the Non-Core Bank.

The aim of HSH Nordbank in the planning period up to 2019 is to increase new business with risk-commensurate margins in accordance with the business and risk strategy. On the one hand, business is to be promoted further in the core region of Northern Germany, where the Bank already has long-standing client relationships and a high level of market penetration, and, on the other hand, business activities outside Northern Germany are to be expanded further in order to achieve the planned new business objectives and to ensure a balanced portfolio structure.

Furthermore, the product sales of the entire range of services over and above traditional lending transactions will continue to be driven forward to strengthen sustainable client relationships and exploit the business potential in the product divisions.

### Strategic targets of the Core Bank's business areas

The strategic divisions are continually evolving and their business portfolios and positioning adjusted to the changing underlying conditions in the market and competitive environment.

The intention is to intensify new business in the Corporate Clients division. The approach of expanding business throughout Germany in the existing locations will be consistently continued in order to achieve this in a highly competitive market environment. At the same time, the potential in the core region of Northern Germany as well as in the project financing business in the Energy & Utilities and Logistics & Infrastructure business areas will be further exploited in the rest of Europe. In the past financial year, parts of the former Corporate Finance division were integrated into the Corporate Clients division. Specialists, who are an integral part of the division, will continue to support the client teams with special advisory and financing solutions and thereby contribute to the strengthening of client relationships.

The Real Estate Clients division will continue to make a risk-conscious contribution to the Bank's balanced portfolio mix taking account of the development in the German real estate markets. The profitability of transactions is the major driver for the sustained improvement in the Bank's risk/return profile.

In the Shipping division, the Bank continues to aim to selectively conclude additional new business based on its long-standing expertise and in accordance with strict margin and risk requirements. The focus is on a diversification of the portfolio through domestic and international commitments with counterparties with a good credit standing.

The new Treasury & Markets division bundles together trading with capital market and investment products as well as the servicing of savings banks, banks and insurance companies. The responsibility for the central management of the liquidity and market price risks of the bank positions as well as the Bank's issuance activities are also anchored in this division.

The client divisions will be generally supported by products and services provided by the Treasury & Markets, Transaction Banking and Structured Finance divisions in order to ensure an integrated product range and exploit cross-selling potential.

### Consistent winding down of non-performing loans

The Non-Core Bank is still aiming to achieve a significant reduction in the non-strategic loan and capital markets portfolios in the planning period up to 2019 while minimising losses by means of scheduled and early principal repayments, sales of loans as well as structured solutions, provided these are permitted under the guarantee

agreement (see also statements made in the "Ownership structure, guarantee and EU proceedings" sub-section in the "Basis of the Group" section regarding this). The winding down targets are derived from the risk strategy and reflected accordingly in the Bank's plan.

### SUSTAINABLE COST REDUCTIONS AND EFFICIENCY INCREASES

The continuous improvement in the Bank's efficiency remains a high priority for HSH Nordbank. It has revised its cost and efficiency targets for the period to 2019 in view of the challenging environment of a sustained shipping crisis, intensive competition in the German corporates business and constantly increasing regulatory requirements. The objective is to achieve a sustainable, competitive cost-income ratio. HSH Nordbank is therefore continuing to aim to achieve a cost-income ratio of in principal less than 50%.

A comprehensive cost reduction programme was implemented to reduce administrative expenses. This is reviewed on an ongoing basis in light of the imposed privatisation and continuously adjusted to the extent necessary. The organisational structure and key bank processes were streamlined, and operating expenses as well as the number of employees, and therefore personnel expenses, were further reduced as part of the 2018PLUS programme. Overarching initiatives are a further focus of the programme and include the simplification and standardisation of key processes as well as adjustments to the Bank's IT systems. Details regarding the programme measures currently being implemented are set out in the Business developments section.

### IT STRATEGY

Key elements of the IT strategy developed in 2014 were successfully implemented by the end of 2016 in line with the plan. These include, for example, the implementation of elements of the gradual upgrading of the IT system landscape, a significant reduction in IT costs and the expansion of IT control functions. In 2016 the Bank adjusted the strategic alignment of its IT, reorganised IT security and implemented an IT security strategy. This takes account of the requirements of the privatisation process and general technological changes. The most important objective of IT is to guarantee continuing stable production operations under more stringent regulatory requirements while further reducing IT costs. The conversion under way of the IT system landscape is to be continued with the objective of providing the Bank with an appropriate, cost-efficient IT system landscape that is capable of integration. The selective use of new technologies ("digitalisation") will also be driven forward.



## FINAL EU DECISION

The basis for a viable business model of HSH Nordbank was improved by the EU decision reached on 2 May 2016 and the structural measures implemented to date in 2016. Together with further strategic and operating optimisation measures the starting basis for the successful privatisation of HSH Nordbank has thus been established.

Further details on the EU proceedings and the implementation of the agreed structural measures can be found in the Business performance – significant developments and events in the 2016 reporting year section.

## MANAGEMENT SYSTEM

### Key value drivers and key indicator and ratio system

The Bank's integrated management system is aimed at the targeted management of key value drivers – income, efficiency/costs and profitability, risk, capital and liquidity. The Bank uses a risk-adjusted key indicator and ratio system for this purpose that ensures that the Overall Bank, Core Bank and Non-Core Bank are managed in a uniform and effective manner. The HSH Nordbank Group is managed mainly on the basis of figures for the Group prepared in accordance with the International Financial Reporting Standards (IFRS) and the relevant prudential rules, respectively.

In addition, a multi-level contribution margin accounting system is also used to manage the individual business areas. Other components of the Overall Bank management system are the annual strategy and planning process, plan/actual comparisons and targets agreement and assessment process. The key value drivers are managed by three management committees composed of representatives of the top management level. Further information regarding this is included in the Risk Report under "Risk management by central committee structure" and "Risk reporting and measurement systems".

In the 2016 reporting year, HSH Nordbank focussed on the internal management system and refined it in accordance with statutory requirements (SREP, BCBS 239). A focal point of this refinement process was the creation of an integrated view based on financial and risk key figures and ratios in a standardised and integrated management reporting system. This will be used by the Overall Bank Management committee to manage and allocate financial resources and to manage the business areas.

### Revised management indicators of the IFRS Group

HSH Nordbank's most important management indicators were also revised based on the integrated and comprehensive management report. The Bank is thereby pursuing the aim of increasing reporting transparency and efficiency, also with regard to external communication, and therefore focussing on the key management indicators of each of the value drivers of the IFRS Group relevant for the Bank. The trend of these indicators will continue to be reviewed in relation to the previous year and the previous year's forecast ("Economic report" section) and their expected change in 2017 is also described ("Forecast, opportunities and risks report" section).

Compared to the previous year, the following indicators are no longer defined as important management indicators: total income and the liquidity ratio under LiqV. The change in total income is included in net income before taxes and is therefore no longer separately defined as a management indicator. Furthermore, new business concluded solely in the Core Bank in accordance with HSH Nordbank's lending standards will only be reported in the future at the Core Bank level and no longer at the Group level as well. Risk-weighted assets are already adequately covered by the CET1 ratio and, accordingly, are no longer explicitly defined as an important management indicator. In order to highlight the particular importance of the key management indicators – administrative expenses, loan loss provisions and the management indicators generated by the stressed view of the liquidity transformation balance sheet –, the cost/income ratio was defined on the cost side, the NPE ratio and coverage ratio were defined on the risk side and the minimum survival period in the combined stress scenario on the liquidity side. Furthermore, the regulatory ratios – liquidity coverage ratio and net stable funding ratio – are applied instead of the LiqV management indicator to manage liquidity risk, whereby the liquidity position is extensively incorporated within the management indicators.

A comprehensive view of the key value drivers (income, efficiency/costs and profitability, capital and liquidity) is sufficiently ensured by HSH Nordbank's enhanced, integrated management system. The important management indicators used by HSH Nordbank are defined as follows:

**DEFINITION OF THE IMPORTANT MANAGEMENT INDICATORS**

<b>Important management indicators</b>	Definitions
<b>Net income before taxes</b>	Net income before taxes is equivalent to the IFRS result generated before deducting tax expense.
<b>CIR</b> = Cost/income ratio	The CIR is a cost efficiency ratio that measures administrative expenses as a percentage of total income plus other operating income.
<b>RoE</b> = Return on equity	RoE is calculated as the ratio of income before taxes to average equity capital disclosed on the balance sheet and shows the return on capital. The risk-adjusted allocation of the average equity capital disclosed on the balance sheet is determined on the basis of the regulatory capital committed.
<b>NPE ratio</b> = Non-performing exposure	The NPE ratio measures the sum of the risk positions (EaD, exposure at default) of borrowers in default as a percentage of the sum of the Bank's risk positions.
<b>Coverage ratio</b>	The coverage ratio is calculated as the quotient of the loan loss provisions (specific and general) recognised on risk positions and the sum of the risk positions in default.
<b>CET1 ratio</b> (phase-in, same period) = Common Equity Tier 1	The CET1 ratio is defined as the quotient of the core Tier 1 capital excluding hybrid instruments and the sum of the risk-weighted assets, expressed as a percentage. The CET1 ratio is determined in the same period calculation (i.e. taking the Group financial statements into account) in accordance with the transitional rules (phase-in) of the Capital Requirements Regulation (CRR).
<b>Minimum survival period in the combined stress scenario</b>	The minimum survival period according to the liquidity development report describes the period, during which the net liquidity position (NLP) must be adhered to in the base and stress cases. A minimum survival period of 1 month is set for the combined stress scenario in accordance with MaRisk. Furthermore, additional internal risk limits and ambition levels are defined for the base and stress cases according to the Management Board's risk appetite. The internal ambition levels represent targets and are more conservative or longer than the MaRisk requirements. The liquidity development report maps expected cash flows over a specific time period in a structured manner.
<b>LCR</b> = Liquidity coverage ratio	The LCR represents the security provided to the Bank in the event of a short-term acute liquidity stress scenario of more than 30 days by maintaining a liquidity buffer (short-term stress test ratio). The LCR is calculated as the ratio of highly liquid assets to net cash outflows over the next 30 days.
<b>NSFR</b> = Net stable funding ratio	The NSFR shows that stable long-term funding is secured by the Bank under stress conditions. The amount of stable funding available over one year must be sufficient to cover the existing long-term funding required. The NSFR is calculated as the quotient of the amount of available and required stable funding ( $\geq 1$ year).

Based on key value drivers and their important management indicators the following matrix of management indicators shows the key performance indicators relevant for the Core Bank and Non-Core Bank.

**MATRIX OF MANAGEMENT INDICATORS**

		<b>Group</b>	<b>Core Bank</b>	<b>Non-Core Bank</b>
<b>Income</b>	Net income before taxes	x	x	x
<b>Efficiency and profitability</b>	CIR	x	x	
	RoE	x	x	
<b>Risk</b>	NPE ratio	x	x	x
	Coverage ratio	x		x
<b>Capital</b>	CET1 ratio	x		
<b>Liquidity</b>	Survival Period	x		
	LCR	x		
	NSFR	x		



HSH Nordbank also uses the following two additional important management indicators for the specific management of the Core Bank and Non-Core Bank.

#### ADDITIONAL, IMPORTANT MANAGEMENT INDICATORS OF THE CORE BANK AND NON-CORE BANK

<b>Core Bank</b>	New business	New business includes, on the one hand, completely new credit risk incurred by the Bank designated as "acquisition of new loan" under the client responsibility of a Market division and, on the other, increases in the existing credit risk designated as a "loan increase" under the client responsibility of a Market division (also where the loan term is prolonged concurrently). Restructuring commitments – also in the case of increases in existing credit risks – are not taken into account in determining new business.
<b>Non-Core Bank</b>	Total assets	Total assets is the sum of the assets on the asset side or the sum of the total capital on the liability side of a balance sheet as at the balance sheet reporting date.

The extent of the indicators used at HSH Nordbank for managing the overall bank goes far beyond the important management indicators listed in this section and includes many other supporting key performance indicators, which are used by management for the purposes of managing and allocating financial resources in an effective and integrated manner. Further details regarding the key figures and ratios used for risk management are set out in the Risk Report.

HSH Nordbank also updated and refined its recovery/resolution plans in accordance with the statutory requirements. The recovery and early warning indicators defined in the German Recovery and Resolution Act (Sanierungs- und Abwicklungsgesetz, SAG) and by the EBA (European Banking Authority) are regularly monitored and assessed in order to be able, where necessary, to implement targeted measures on a timely basis.

#### Management Board remuneration

The remuneration system for the Management Board of HSH Nordbank meets all relevant, regulatory requirements. In addition, particular attention was paid to ensure that the remuneration system complies with the guarantee agreement of the federal states as well as the conditions imposed by the EU in the initial EU proceedings for the approval of the granting of the second loss guarantee. The limit on the fixed monetary remuneration of each board member of a maximum of 500,000 euros per year as long as HSH Nordbank AG is not capable of making dividend distributions is therefore implemented in the remuneration system. The Management Board has unilaterally waived until further notice the option of granting a success bonus following a successful privatisation, which was granted to the Supervisory Board under the EU decision of May 2016.

General agreements have not been concluded for the early termination of a Management Board member's contract without good cause. However, it is contractually agreed that – in accordance with Section 4.2.3 of the German Corporate Governance Code – any agreed payments to a departing member of the Management Board may not exceed the value of two years' fixed annual salary (including fringe benefits) and the total of the fixed salary for the remaining term of the employment period.

In the year under review no member of the Management Board received payments or promises of payment from a third party in respect of their activities as a Management Board member. The same also applies to payments or promises of payment from companies, with which HSH Nordbank maintains significant business relationships.

Further information on the Management Board's remuneration is set out in Note 66 (Related parties).

## ECONOMIC REPORT

### UNDERLYING MACROECONOMIC AND INDUSTRY SECTOR CONDITIONS

#### 2016 CHARACTERISED BY GEOPOLITICAL UNCERTAINTY AND VOLATILE FINANCIAL MARKETS

The global economy grew at a rate of 3.1% in 2016, which represents a slight slowdown compared to the previous year. Economic growth in the USA was particularly disappointing, whilst the rate of expansion declined less sharply in the eurozone. China's economy held up well despite a difficult start so that growth was only slightly lower than in 2015. The easing of the recession in Russia also had a stabilising effect, whereas the situation in Brazil remains difficult. The past year was characterised by a turbulent start in the form of sharp falls in prices on Chinese stock exchanges, the unexpected vote in Great Britain in the middle of the year to leave the EU (Brexit) and the outcome of the US presidential elections in November. Furthermore, concerns regarding inadequately capitalised banks, particularly in Italy, were one of the key issues that shifted markets. Interest rates also remained for the most part at an extremely low level in 2016. However, long-term yields increased significantly at the year end, as the US Federal Reserve raised its key interest rate, commodity prices rose and expectations of a future more expansive fiscal policy took hold. It was noticeable how quickly the financial markets processed unexpected events such as the so-called Brexit and the outcome of the US presidential elections without there being sustained turbulence.

#### MODERATE GLOBAL ECONOMIC GROWTH

Gross domestic product in the USA only increased slightly by 1.6% in 2016 (previous year: 2.6%). Private consumption was the most dynamic component, while investment activity except in the housing sector contracted. Exports again recorded only a below-average increase. According to the most recent economic indicators economic growth picked up somewhat at the end of the year. Employment increased steadily, the unemployment rate fell to below 5% and hourly wages recently rose sharply. In this environment, the inflation rate has moved closer to the inflation target of 2%. China's gross domestic product in 2016 was about 6.7% higher than in the previous year, driven not least by government investment programmes. India's economy grew at a similar rate, whereby growth in the final quarter may have suffered under the comprehensive currency reform. Brazil and Russia, whose national economies fell into a deep recession in 2015 as a result of political uncertainty and low commodity prices, showed signs of stabilisation, but to a lesser extent in the case of Brazil.

Gross domestic product in the euro area grew by 1.6% in 2016, thereby continuing the moderate recovery from 2014 and 2015. Growth was broad-based with both capital expenditure and exports increasing at an above-average rate. Government spending also made a significant contribution to the growth. All countries in the eurozone are likely to record positive growth for the first time since the financial market crisis of 2008/2009. Whereas Italy's and France's growth was 1%, the Spanish economy grew by around 3% at a dynamic rate similar to the previous year, Germany's growth of 1.8% (adjusted for calendar effects) was also above average. Unemployment rates in the currency union decreased slightly to 9.7%, while the inflation rate jumped to 1.1% at the end of the year, which was mainly attributable to higher energy prices. Although corporate lending increased in Germany and France, it decreased significantly in Italy and Spain. Even though the outcome of the EU referendum in Great Britain triggered much discussion, this has not visibly fed through to the eurozone economic indicators.

The comparatively high growth of the German national economy was mainly driven by private consumption, whereas investment activity hardly increased at all and exports grew at a considerably slower rate than in the previous year. Loans granted to non-financial enterprises increased in the final quarter by about 3% above the previous year.

#### SURPRISINGLY RESILIENT FINANCIAL MARKETS AND TO SOME EXTENT INCREASING INTEREST RATES

2016 started with increased nervousness due to the sharp fall in prices on Chinese equity markets. However, during the remainder of the year, the financial markets proved surprisingly resilient in the face of various unexpected events such as Brexit, news about the weak capitalisation of Italian credit institutions and the election of Donald Trump as US president. Their – temporary – impact was felt most strongly by German and US government bonds, whose yields declined sharply in the middle of the year. All German government bonds with a maturity of up to 15 years were trading at a negative yield at times at the end of June.

In this environment, the US Federal Reserve increased the key interest rate to a range of 0.25% to 0.5% in December 2016 and therefore only tightened its monetary policy once in the entire year, whereas the ECB had increased its monthly bond purchase programme from € 60 billion to € 80 billion in the first half of the year and included bonds of non-financial enterprises in its programme.

Risk premiums for corporate and governments fell following the announcement of these measures. The ECB also introduced a new long-term refinancing programme, under which commercial banks can borrow liquidity from the ECB for a period of four years at an interest rate of up to -0.4%. In December the ECB announced the extension of the purchase programme to December 2017, whereby the purchase programme will again be adjusted back to the original monthly amount of € 60 billion from March 2017.

The DAX fluctuated within a range of 8,753 and 11,481 points in 2016. At the year end it was 6.9% higher compared to the 2015 year end, which was mainly attributable to the year-end rally in the wake of the outcome of the US presidential elections.

In the currency markets the euro depreciated against the US dollar by about 3.2% compared to the 2015 year end. The EUR/USD exchange rate was 1.054 at the end of December (2015 year end: EUR/USD 1.089). The currency pair reached an interim high of 1.153 EUR/USD in May after the Fed indicated a more cautious approach towards hikes in the key interest rate. The oil price (Brent) increased in 2016 by 51% to USD 56.8 per barrel. The agreement reached between the major oil exporting countries to cut production was mainly responsible for this.

### UNEVEN TRENDS IN RELEVANT MARKETS

The shipping markets were still in a poor condition in 2016. The demand for container ships above all again disappointed the expectations of market participants. The market was somewhat friendlier for bulkers. The oil tanker market was unable to maintain its relatively high level and came under greater pressure in the third quarter 2016 than had been originally expected.

There was a further slump in the container ship market in 2016. Both charter rates and ship values declined significantly. The widening of the Panama Canal resulted in a concentration of overcapacity in the medium-sized segments and put particular pressure on their rates. Furthermore, the other, smaller sub-segments were adversely impacted by the capacity added by Neo-Post-Panamax ships. As the scrapping of ships increased sharply and deliveries fell significantly as a result of deferring delivery dates, fleet growth was pleasingly weak on the whole. Container demand improved slightly in 2016 compared to the previous year but could not yet achieve the desired momentum. The ongoing weak market situation is also reflected in the high number of laid-up ships. One positive aspect is that there were virtually no new orders for ships in 2016.

Rates and prices continued to stabilise for bulkers, with rates recording a seasonal upswing at the 2016 year end. Demand was surprisingly positive, but expectations were very low.

This was driven by positive impulses coming from China in particular, which again increased its imports of iron ore and coal. On the supply side, shipping lines were able to successfully lower fleet growth through scrapping and deferral or cancellation of orders for ships. Charter rates in all sub-segments were also recently slightly above the operating cost level, but were still below the level required to service debt. New orders for ships again decreased so that hardly any orders were observed in the recent past.

Trends in the oil tanker market were weak in the second half of 2016. On the demand side, the increase in the oil price slowed growth in transportation and storage needs. On the other hand, fleet growth accelerated significantly as a result of delivery lags on new orders. On the positive side, new orders for oil tankers have also been very low over a period of more than twelve months.

### TREND OF TIME CHARTER RATES IN THE SHIPPING INDUSTRY

(Market average, USD/day)

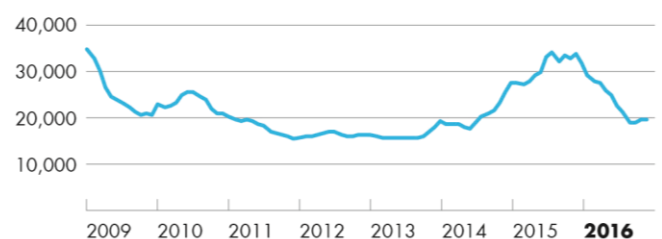
#### Container ships



#### Bulk carriers



#### Oil tankers





Developments in the real estate markets in Germany were mostly very positive in 2016. Rents and property prices continued to increase sharply, especially in the housing markets of large cities. The increase in property prices exceeded that of rents by a very clear margin. The restrictions imposed on rent increases have hardly had any effect to date on new rentals.

In fact, the persistent very high demand for housing exceeded the increase in completions causing the vacancy rates to decrease further. Weaker regions also benefited from this trend, as the accommodation of refugees generated here as well a higher demand for residential properties. Rental growth in the office real estate markets remained high in 2016. The marked rise in the number of office staff generated a stable demand for office space compared to the previous year. At the same time, the available space only increased moderately, because the increased number of completions was partially offset by many changes in usage. Nevertheless, the vacancy rate continued to decrease. On the other hand, rental growth in retail real estate markets decreased noticeably. Only prime rents in central prime locations managed to increase moderately. Although retail stores benefited from very strong levels of private consumption, the sales growth generated was significantly less than the sustained above-average growth in e-commerce. On the investment markets, there was a noticeable shortage of supply on a high level of investor interest. Whilst market values of office properties increased very sharply, commercial properties recorded somewhat lower increases in value.

Trends in European office real estate markets in foreign markets were very mixed in 2016. Whilst some markets such as Stockholm and Madrid continued to recover, rent levels stagnated in many other regions due to the persistent high level of vacancies. Demand for space weakened markedly in the office real estate markets in London, especially after the Brexit vote. At the same time, completions increased sharply causing vacancy rates to rise appreciably. Whereas rents have so far hardly fallen, market values have already decreased noticeably. However, market values increased significantly in the rest of Europe due to the very high investor demand. The upwards trend continued in the USA in both the office and residential real estate markets on a slight fall in office vacancies and hardly any increase in housing vacancy rates as well as increased rents and market values.

Further progress has been made in the first ten months of 2016 in the expansion of renewable energy, but at an uneven pace. In Germany, new installations of onshore wind energy turbine generators were nearly a quarter above the previous year but did not quite achieve the level in the record year of 2014, whilst there was a return to normal levels in the offshore sector.

The negative trend in the photovoltaic segment continued in Germany: Capacity added from January to October again declined significantly compared to the same period in the previous year. This is partly the result of the changeover to a competitive bidding process that has already been implemented in this sector.

According to preliminary figures, the project financing volume for transport infrastructure in Europe fell sharply in the first half of 2016. The proportion of public-private partnerships projects to the overall volume has fallen. The largest proportion of the financing was arranged for road projects. Transactions relating to airports and ports were also implemented. The regional focus of the activities was France, Spain, Great Britain and the Netherlands. The major institutional investors include pension funds and insurance companies, which regard infrastructure investments as an investment alternative in the low interest rate environment. Revenues in the logistics sector were weaker in the first nine months of 2016 than in the same period of the previous year.

Production growth in the manufacturing industry in the period from January to September 2016 was significantly higher than in the same period of the previous year. Trends were uneven in the individual sectors. Whilst production volume decreased in the chemical and engineering sectors, electrical engineering, the metal industry and companies in the pharmaceuticals and automobile industries reported growth. Production in the food industry also increased again following a decline in the previous year.

Wholesalers recorded lower sales in the first nine months of 2016 compared to the same period of the previous year, which is primarily attributable to the reduction in sales of production-related wholesalers. In contrast, wholesalers for consumer-related goods recorded slight growth. Compared to the wholesale sector the sales performance of the retail sector was positive. Both the food retail industry and other key segments of the retail sector were able to increase sales. However, the clothing retail sector recorded a significant drop in sales.

The health market is growing constantly, as is the hospital market as well, as a result of demographic trends and medical advances. The financial situation of many hospitals remains strained despite increasing revenues. It is expected that the profitability of hospitals will increase in the future with the entry into force of the Hospital Structure Act (*Krankenhausstrukturgesetz*) at the beginning of 2016.

## UNSETTLED AND CHALLENGING ENVIRONMENT FOR BANKS

### VOLATILE MARKET ENVIRONMENT CHARACTERISED BY UNCERTAINTY

Against the backdrop of uncertainty regarding the future policy of large central banks, growth prospects of important emerging markets, namely China, Brazil and Russia, and not least growing concerns about increasing protectionism following the US presidential elections, the market environment for banks in 2016 was also characterised by considerable volatility. Whereas global issues caused a sharp decline in share prices of banks especially at the beginning of the year, the vote of the British electorate regarding remaining in the EU (Brexit) was – following a temporary recovery – an additional factor that created turbulence. The fears of market participants regarding the impact of Brexit are not restricted to British banks but, due to the central role of the London financial centre for the European banking market, apply to other large European financial institutions. This resulted in the worsening of the negative market mood, particularly the already simmering concerns regarding the stability of the Italian banking system. There were renewed discussions at the year end regarding the need to recapitalise individual institutions and the application of BRRD. In Germany, the focus was on the high level of loan loss provisions recognised by ship financing banks.

An issue resolved during 2016 was the debt moratorium announced at the beginning of March 2015 for the Austrian Heta Asset Resolution AG (HETA). Following the rejection of an initial buyback offer from the province of Carinthia to the creditor banks, an agreement was signed in May, which became legally binding in October. Carinthia reached a compromise with the overwhelming majority of the creditors, which provides for the exchange of Heta bonds for zero coupon bonds issued by the Carinthia settlement fund (Ausgleichszahlungsfonds) with a net present value of 90% of the claims or, alternatively, a cash payment of 75% of the claims.

In view of the significant economic and political uncertainty the ECB maintained its expansionary monetary policy, which now also provides for the purchase of corporate bonds, thereby extending the outlook for market participants to a continuing low interest rate environment that adversely impacts bank earnings. An upward trend set in at the year end, triggered not least by the expectations of a rising budget deficit in the USA. The continuing flat yield curve resulted in sustained pressure on net interest income of banks due to lower earnings generated from the maturity transformation and lower interest earned on equity items.

Against this difficult backdrop, the banks feel challenged to constantly review their strategic direction, as the substantial pressure on earnings

entails, in conjunction with the weak loan demand of German companies, the increasing risk that loan financing is not priced on a risk-commensurate basis. At the same time, higher expenses for the European bank levy and costs for the increasing regulatory requirements were clearly reflected on the cost side. Against this backdrop many banks in addition to focusing their business models initiated comprehensive cost and efficiency programmes in order to be able to generate adequate returns on a sustained basis.

### BANKING SUPERVISION IN LIGHT OF SREP

Besides the difficult market environment, the banking market in 2016 was also characterised by regulatory changes as part of the further implementation of the European Banking Union and Basel III. The Bank Recovery and Resolution Directive (BRRD) entered into force as at 1 January 2016. The corresponding German Act on the Recovery and Resolution of Credit Institutions (SAG) had already come into force a year earlier than at the European level. In this connection, the ultimate responsibility for resolution plans was transferred from the national resolution authority (Federal Agency for Financial Market Stabilisation – FMSA) to the European Single Resolution Board (SRB) as at 1 January 2016.

Monitoring of banks by the banking supervisory authority has also been further intensified by the expansion of the Banking Union and protection schemes. Regulatory monitoring was substantially increased for banks directly supervised by the ECB through the supervisory review and evaluation process (SREP). The ECB has already set out its priorities at the beginning of 2016 for the topics to be examined in detail in the SREP process. The five priorities identified by the supervisory authorities are a review of the business models of banks, credit risk, appropriateness of capital and liquidity resources as well as governance and data quality. The main focus will be on risks associated with the business models and earnings weakness in the low interest rate environment. The review of credit risk focuses on the treatment of and reduction in non-performing loans.

The SREP process includes in particular large-scale data analyses, so-called “short-term exercises”. This also affected not least the German ship financing banks, which had to deliver extensive data to the banking supervisory authorities. The ECB as well as national supervisory authorities review the business models, funding plans and internal risk models of the banks more closely than under the previous supervisory practice and draw on EU-wide benchmark analyses for their assessment, for example, as part of the transparency exercise carried out again in autumn 2016. The objective of the more comprehensive regulatory monitoring approach is to identify failings at banks at an early stage and to take appropriate countermeasures. At the same time, market transparency is to be strengthened by the increase in disclosure obligations.

The European banks were also occupied in working on the stress test published on 29 July 2016. This was started in the first quarter of 2016 with the publication of the methodology and scenarios. Whilst in 2016 only a selection of European banks with total assets in excess of € 100 billion participated in the EBA stress test, other banks directly supervised by the ECB went through a so-called SREP stress test, the contents of which essentially corresponded to those defined in the EBA stress test, which will not be published for the institutions that did not take part in the EBA stress test. HSH Nordbank participated in the ECB stress test as part of the SREP process.

The key substantive areas of focus in the stress test were directly linked to the current challenges in the banking environment. The stress test provided in particular for the modelling of the effects of the low interest rate environment, currency fluctuations and exposure to legal risk. The stress test results were incorporated by the supervisors into the assessment of the banks' business models as part of the SREP process. In December 2016, the regulator notified the banks supervised by it in the SREP process of the individual capital requirements. These now include a regulatory early warning threshold (Pillar 2 Guidance "P2G") as well as a binding minimum requirement (Pillar 2 Requirement "P2R"). In total, the capital requirements for large European banks increased slightly.

The comprehensive and stricter regulatory requirements have made a significant contribution in their entirety to strengthening the stability of the European banking system. Against the backdrop of stricter capital requirements through the gradual implementation of Basel III and the planned introduction of additional regulatory capital buffers German banks on average are likely to have further strengthened their capital base in 2016. However, it is becoming increasingly clear at the same time that low market shares compared with international benchmarks and the weak earnings situation of German banks in particular is placing tight constraints on the ability to retain profits and the focus will therefore remain on strict cost management and the consistent winding down of risk positions.

#### **HSH NORDBANK'S BUSINESS IMPACTED BY UNDERLYING CONDITIONS**

The volatile and highly competitive environment was also reflected in the Bank's business performance. Trends in markets relevant for the Bank were uneven in 2016. Whilst the real estate environment in Germany was largely positive, the situation in the shipping markets remained very challenging. In the Corporate Clients division the solid liquidity base of clients and persistent low level of interest rates had a tangible impact in the increasingly competitive environment. In the context of these market developments, the Bank was able to maintain

its good position in its target markets while taking account of the strict risk requirements. New business concluded was slightly above that of the previous year. Nevertheless, lending margins declined further given the highly competitive environment and is appreciably below the defined ambition level. The Real Estate division again maintained its good market position with a new business volume at the previous year's level; the Corporate Clients division was able to clearly exceed the previous year's volume. Transactions were concluded on an extremely selective basis in the Shipping division against the backdrop of the difficult market situation.

The Bank's earnings and financial position and net trading income in particular were affected by the uncertainty prevailing in the financial markets, not least in the period around the Brexit decision. The slight appreciation in and marked volatility of the US dollar against the euro also had an impact on earnings, net assets and the financial position, even though the Bank's dependence on movements in the EUR/USD exchange rate has decreased significantly following the sale of non-performing loans of a nominal amount of € 5 billion, primarily denominated in US dollars, to hsh portfoliomanagement AöR. This also tangibly relieved the pressure on the Bank's refinancing requirements and liquidity position.

The uneven trends in the relevant markets were also reflected not least in loan loss provisions. The Bank again recognised high loan loss provisions in 2016 for the legacy portfolios concerned, which are predominantly covered by the federal state guarantee, due to the ongoing difficult sector trends in the shipping industry. On the other hand, the strong earnings, particularly of German corporate clients, enabled the Bank to reverse loan loss provisions in this division.

The Bank also responded to the continuing challenge regarding a cost base appropriate for the market environment. Controllable personnel and operating expenses were further reduced compared to the previous year as part of the implementation of cost savings measures. The Bank is also using these measures to counteract cost increases caused by the large number of new regulatory requirements and charges incurred in 2016 for the European bank levy and HSH Nordbank's contribution to the deposit guarantee fund.

The EU proceedings, the Bank's business performance and position are explained in detail in the following sections.



## BUSINESS PERFORMANCE — SIGNIFICANT DEVELOPMENTS AND EVENTS IN THE 2016 REPORTING YEAR

Developments in the 2016 financial year were mainly characterised by the preparations for and implementation of the decision reached by the EU Commission on 2 May 2016 in the EU state aid proceedings which concerned the replenishment of the second loss guarantee issued by the federal states from €7 billion to €10 billion and the focusing on the Bank's operating activities.

According to the list of conditions and commitments provided to the EU Commission by the Federal Republic of Germany, on which the decision in the EU state aid proceedings is based, HSH Nordbank AG is to be sold by its current strategic owners by 28 February 2018. Against the backdrop of this privatisation significant measures were initiated in the 2016 financial year to prepare for the upcoming change in ownership. These include, on the one hand, the implementation, largely in line with the plan, of the structural measures provided for in the EU decision and, on the other, organisational and personnel changes within the Bank. Concurrently with the preparations for the change in ownership the Bank vigorously drove forward its operating business in the past year. The focus was on generating new business with reasonable income and risk profiles in a partially very challenging market environment. Furthermore, restructuring activities in the Shipping division were rigorously stepped up to further reduce the volume of non-performing loans. The Bank also made progress in line with the plan in optimising the organisation and processes as part of the intensified cost reduction programme.

Overall, the Bank achieved its key stated objectives for 2016 and closed the financial year with positive earnings before taxes, which were characterised by a good operating performance on the part of the Core Bank and structural charges in the Non-Core Bank.

### FORMAL DECISION IN THE CURRENT EU STATE AID PROCEEDINGS

The EU decision reached on 2 May 2016 regarding the replenishment of the second loss guarantee issued by the federal states from €7.0 billion to €10.0 billion confirms the informal agreement made on 19 October 2015 and, in principle, defines it in concrete terms and is based on a list of conditions and commitments provided to the EU Commission by the Federal Republic of Germany (EU decision). The structural measures agreed should result in an improved financial and risk situation following implementation and create the basis for a sustainable structure and viable business model for HSH Nordbank.

The structural measures include the sale of non-performing loans of €5.0 billion to the federal state owners at market values determined by the EU Commission under state aid aspects and the sale of a legacy portfolio of up to €3.2 billion in the market, which was mainly covered by the guarantee. A further point in the EU decision is the change relating to the future fee structure for the second loss guarantee, which is linked to the formation of a holding company and a subsidiary, which comprises HSH Nordbank's operating business and is to be privatised. Furthermore, it is intended to sell the operating company by 28 February 2018. This divestment deadline is met upon the signing of a purchase agreement and may be extended by up to six months with the consent of the EU Commission where there are delays in the technical implementation of the model for reasons outside the control of the federal states.

### Rigorous implementation of the EU structural measures

Following the EU decision the Bank immediately started making preparations and implementing the structural measures. Important structural measures were completed as far as possible in line with the plan.

In this connection, a portfolio of non-performing shipping loans of €5 billion had already been sold to the federal state-owned hsh portfoliomanagement AöR as at 30 June 2016 (reporting date: 31 December 2015), under which the Bank was relieved to an appreciable extent of the burden of legacy loans in the Shipping division, which were entered into as part of the significant business expansion in the years up to 2009. The purchase price (€2.4 billion) determined by the EU Commission for this portfolio was paid to the Bank in the third quarter of 2016, thereby further improving the Bank's liquidity position. Losses (€2.6 billion) incurred on the sale were invoiced under the guarantee as part of the settlement of losses, of which €1.3 billion was attributable to the first loss piece and €1.3 billion to the second loss piece of the guarantee. The second loss piece was drawn down by a total amount of €1.9 billion as at 31 December 2016. Nevertheless, the Bank has a very large portfolio of legacy assets from the years prior to 2009 due to the complex settlement conditions under the guarantee agreement and the only low level of relief relative to the total NPE volume provided under the EU decision, which is making the privatisation process more difficult and continues to be systematically wound down.

Furthermore, the holding structure was established in the second quarter of 2016 which provided the operating HSH Nordbank with considerable relief from guarantee fees. Under this the operating company pays from 1 January 2016 a base premium of 2.2% (previously 4%) for the provision of the second loss guarantee, which is calculated solely on the unutilised, i.e. undrawn, portion of the guarantee (previously calculated on the nominal amount of the guarantee facility).

The implementation of the holding structure also entailed a change in the ownership structure of HSH Nordbank. The principal owner of the operating HSH Nordbank is HSH Beteiligungs Management GmbH with a shareholding of 94.9%. Private investors advised by J.C. Flowers & Co. LLC. also have a shareholding of 5.1%.

The Bank also started making intensive preparations in the second half of 2016 for the planned portfolio sales in the market. The sale of non-performing loans of up to €3.2 billion was approved as part of the implementation of the EU decision. In this regard, the Bank selected important legacy portfolios with a clear focus on further reducing risk on the Bank's balance sheet (market portfolio) and conducted a sales process in various phases. As a result of this process, a contractual agreement for the sale of a loan portfolio of around €1.6 billion was signed on 27 January 2017. This represents a slight delay in the planned implementation by the 2016 year end. The impact on earnings was nevertheless recognised in the financial statements as at 31 December 2016. This portfolio mainly consists of around €0.8 billion of aircraft financing transactions and around €0.5 billion of Continental European commercial real estate loans from the years prior to 2009. Additional relief of around €0.3 billion was also achieved by HSH Nordbank by individual sales to other investors and principal repayments within the portfolio originally held for sale. The parties have agreed not to disclose details of the purchase price. In addition to meeting further conditions the purchase agreements still require approval from the cartel authorities, which is expected to be received in the second quarter of 2017. Further details on the sale of the market portfolio are set out in the Forecast, opportunities and risks report and Note 34 in the Group explanatory notes.

### Privatisation process has started

The privatisation process is proceeding at a rapid pace. The official part of the privatisation of HSH Nordbank started with the announcement of the sale by the federal state owners, which was published on 23 January 2017. The Bank has strongly supported its owners in making preparations for the sales process since the third quarter of 2016. Special sales documentation is being prepared, discussions are being held with potential interested parties and organisational changes initiated. In particular, the reporting structures of the Core Bank and Non-Core Bank (formerly the Restructuring Unit), and therefore the segment structure, were adjusted. A portfolio reallocation was made between the Core Bank and Non-Core Bank in order to present each value creation structure in a transparent manner. This optimised the Core Bank portfolio and resulted in a more appropriate

and uniform allocation of non-performing legacy loans in the Non-Core Bank, thereby further reducing the complexity of the Group structure.

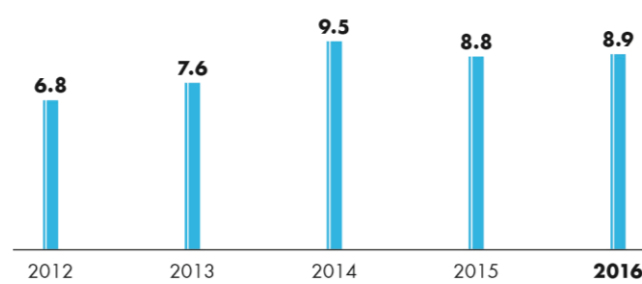
Further details regarding the portfolio reallocation and changes in the segments are provided below in the "Segment reporting" section.

### POSITIVE NEW BUSINESS DEVELOPMENTS

New business of the Core Bank performed well, especially in the second half of 2016. In total, the Core Bank of HSH Nordbank generated new business of €8.9 billion in the past year. The Bank has therefore succeeded in slightly exceeding the previous year's volume of €8.8 billion as well as the forecast made at the end of the first half of 2016 despite the partially very difficult market environment. The Corporate Clients and Real Estate divisions made a significant contribution to these positive developments. The very good previous year's level was substantially exceeded in the Corporate Clients division in particular, whilst it was achieved in the Real Estate division and thus the new business plan was clearly exceeded in this segment. As expected, new business in the Shipping division was unsatisfactory due to the extremely challenging market conditions and the targeted management of the risk profile in this division. It is therefore both significantly below the plan amount and the previous year's level. This was the main reason for the original new business plan not being met.

### NEW BUSINESS OF THE CORE BANK

(€ bn)



The ratio of new loans disbursed to new business concluded (disbursement ratio) increased during the 2016 financial year and was above the planned level as at 31 December 2016. Interest margins achieved in the highly competitive environment stabilised in the fourth quarter of 2016 but are still below the previous year and, overall, also failed to meet the targeted ambition level. However, cross-selling income generated by banking services over and above loan financing was in line with the plan. As expected, lower loan commissions were received for restructuring activities, particularly in the Non-Core Bank, as a result of the progress made in reducing risk, which was the main contributory factor in cross-selling income being

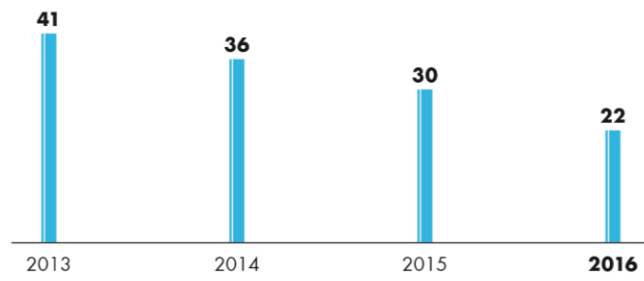
overall moderately below that for the previous year. Investment products were still the services most in demand with Core Bank clients. Cross-selling income in the derivatives area was at the previous year's level but was nevertheless moderately below the planned amount.

### ACCELERATED WINDING DOWN OF LEGACY PORTFOLIOS

The winding down of the legacy portfolios held in the Non-Core Bank was also continued in 2016 according to plan taking account of the complex settlement conditions under the guarantee agreement. The portfolios have been reduced by €8 billion in total since 31 December 2015. The change is composed of the reduction in connection with the federal state transaction of €5 billion and, over and above this, the regular winding down of legacy assets of €3 billion (including currency translation effects).

#### NON-CORE BANK: SEGMENT ASSETS

(€ bn)



In the second half of 2016 the Bank made a portfolio reallocation between the Core Bank and Non-Core Bank to ensure that there is a clear separation between troubled legacy loans on the one hand and the strategic existing and new business portfolio on the other and that the structure is presented in a more transparent manner based on causation on the basis of the internal reporting. Non-performing legacy loans in the amount of €6.2 billion were mainly transferred from the Core Bank's Shipping division to the Non-Core Bank. At the same time portfolios in the amount of €4.5 billion consisting mainly of the public sector financing portfolio, which is used as the cover pool for public sector Pfandbriefe, were transferred from the Non-Core Bank's Divestment division to the Core Bank. The Non-Core Bank's portfolio increased in total by €1.7 billion as a result of this reallocation, while the Core Bank's portfolio decreased by the same amount. All previous year and plan figures have been adjusted accordingly for comparative purposes.

Following the portfolio reallocation the Core Bank accounts for 38% of the volume covered by the guarantee, the Non-core Bank 61% and segments not subject to reporting requirements 1%. The guarantee

fees are allocated to the segments based on the regulatory capital of the guaranteed portfolio. The Core Bank and Non-Core Bank accounted for 12% and 88% of these guarantee fees, respectively.

Despite the continuing very difficult market conditions in the shipping industry, the winding down of non-performing ship financing transactions was continued in the first half of 2016 through restructuring shipping loans. Under the restructuring, shipping loan tranches are transferred to investors thus reducing the Bank's risks in the portfolio. At the same time, the Bank secures as part of the transaction the option to benefit from a recovery in the shipping industry. Five new transactions of this type totalling around US dollar 0.5 billion were concluded in the first half of 2016. No further transactions of this type were entered into in the second half of 2016.

### STRINGENT IMPLEMENTATION OF COST PROGRAMME

The reduction in costs achieved since 2014 is countering the increasing pressure on earnings in the highly competitive banking market and increasing costs incurred for regulatory requirements. The Management Board on 15 June 2016 agreed a further reduction in administrative expenses in the years 2016 to 2018 as part of the 2018PLUS cost reduction programme with the objective of achieving a sustainable, appropriate cost/income ratio of in principle under 50% for the Bank. The planned measures provide for an additional reduction in headcount by 317 full-time employees (FTE) and further savings in operating expenses, especially for land and buildings as well as consultancy. Details regarding the implementation of the reduction in staff are governed by a reconciliation of interests, on which the Management Board and Group Works Council agreed in the third quarter of 2016. The social plan in place since 2011 was modified slightly and contains the tools to be used for a socially acceptable reduction in staff. In the 2016 financial year further savings in the area of operating expenses were identified, agreed and have already been partially implemented.

The Bank made progress in 2016 in line with the plan in implementing measures for controllable operating expenses. The organisational structure in particular was streamlined as the basis for the planned reduction in staff. Furthermore, the Special Loans division, which is responsible in particular for loan restructuring in the legacy portfolios of the Non-Core Bank, was integrated under the responsibility of the CRO in the fourth quarter of 2016. In addition, the reduction in legal fees, building costs and other personnel-related operating expenses particularly contributed to the targeted management of operating expenses. In the case of personnel expenses around two thirds of the planned reduction had been contractually agreed with the employees by the year end.



Over and above the cost reduction programme the so-called lean management programme is contributing to the targeted improvements in processes and quality. The lean management philosophy and method has been gradually introduced since 2011 into the divisions with the help of the managers and with extensive employee participation. The bank-wide implementation had already been completed by the end of 2015. Further measures for improving efficiency were continually identified and implemented by the divisions as part of the so-called continuing improvement process. Since the beginning of the lean management programme a considerable amount of efficiency improvements has been identified and already implemented.

Already in 2015, the Bank launched a “Digital Business” initiative to benefit even more from the opportunities offered by digitisation. Key objectives are the development of tailored, innovative solutions to strengthen client relationships as well as the further improvement in internal processes. Focussed digitisation measures with a tangible value added for HSH Nordbank and its clients are being developed and already existing activities consolidated across the Bank. The first significant measures have already been implemented. For example, the introduction of the HSH banking app enables business clients to monitor and manage their accounts and payment transactions using mobile devices.

#### **CHANGE IN COMPOSITION OF HSH NORDBANK'S MANAGEMENT BOARD IN 2016**

In its meeting held on 9 May 2016, the Supervisory Board adopted changes to the Management Board: Stefan Ermisch, formerly Chief Financial Officer and Deputy Chairman of the Bank, moved to the head of HSH Nordbank AG on 10 June 2016 and, as Chairman of the Bank, will manage the Bank in the crucial phase of the planned change in ownership. Constantin von Oesterreich stepped down as Chairman following the annual results press conference on 9 June 2016, thereby initiating the change in leadership at the beginning of the privatisation process. Matthias Wittenburg, the Management Board member responsible for Market divisions, left the Bank with effect from 10 June 2016 by mutual agreement. On the same day Torsten Temp as sole Management Board member responsible for the Market divisions assumed this responsibility. Oliver Gatzke, who was previously head of the Finance division, was appointed Chief Financial Officer from 1 July 2016. Ulrik Lackschewitz was appointed Chief Risk Officer (CRO) of HSH Nordbank on 29 May 2015.

## EARNINGS, NET ASSETS AND FINANCIAL POSITION

### CORE BANK RESULTS ABOVE EXPECTATIONS

The Core Bank, which includes the Real Estate, Shipping, Corporate Clients and Treasury & Markets segments following the change to the internal reporting and therefore the segment structure as well, generated net income before taxes of € 639 million (previous year: € 204 million) in the past financial year, which was significantly above the previous year (all previous year and plan figures have been adjusted in line with the changes in the segment structure for comparative purposes).

Total income of € 1,003 million (previous year: € 850 million), which exceeded the previous year by € 153 million and includes the recognition of unrealised gains on the sales of promissory note loans and securities, had a positive impact on this result. On the one hand, increased net income, which particularly reflects the development in interest income from operating activities, contributed € 649 million to this. On the other, net trading income, which includes earnings contributions from the client operating business, the management of key liquidity and market price risks and measurement effects arising on client derivatives and assets measured at fair value, made a significant contribution of € 186 million. Following the portfolio reallocation made in the reporting year, the objective of which was to bundle together the strategic portfolios in the Core Bank and the non-performing legacy portfolios earmarked for winding down in the Non-Core Bank, the Core Bank results benefited from structurally lower loan loss provisions totalling € 12 million (previous year: € -150 million). This provided total relief of € 47 million (previous year: € -168 million) after taking account of the compensation under the second loss guarantee disclosed within loan loss provisions.

The ongoing cost reduction programme was also implemented in the Core Bank in line with the plan. Administrative expenses amounted to € -357 million and were noticeably lower than in the previous year (€ -395 million) and moderately below the planned amount. The Core Bank results were adversely impacted by expenses for the bank levy and deposit guarantee fund as well as for government guarantees amounting to € -56 million (previous year: € -64 million). The Core Bank accounted for € -25 million, representing about 12% of total guarantee expense, as the Core Bank's portfolios hedged by the second loss guarantee only tie up a small amount of capital.

All segments contributed to the overall good earnings performance. Real estate with € 148 million, Shipping with € 104 million, Corporate Clients with € 89 million and Treasury & Markets with € 298 million made positive contributions. The low level of interest rates and intense competition, which adversely impacted the new business margin trend in particular, had a negative effect on earnings.

### VERY HIGH LOAN LOSS PROVISIONS IN THE NON-CORE BANK

As expected, the Non-Core Bank, in which predominantly legacy loans earmarked for winding down and non-performing legacy loans are bundled following the portfolio reallocation, disclosed a substantial net loss of € -299 million as at 31 December 2016 (previous year: € 173 million). This result mainly includes administrative expenses of € -299 million (previous year: € -253 million) and expenses for the second loss guarantee of € -189 million (previous year: € -433 million), as the Non-Core Bank accounts for most of the risk coverage. The loss is mainly attributable to the continued winding down of the portfolio and setting of loans to a non-accrual basis as part of the recognition of loan loss provisions. This resulted in a further reduction in the interest-bearing loan volume and a corresponding sharp fall in net interest income. Total income of the Non-Core Bank amounted to € 36 million (previous year: € 407 million). Net interest income of € 15 million (previous year: € 285 million) and net income from financial investments of € 54 million (previous year: € 40 million) made a positive contribution, and net trading income of € -53 million (previous year: € 53 million) a negative contribution to this.

Net income before taxes was also adversely impacted by high loan loss provision expense of € -1,594 million (previous year: € -2,869 million). This expense was recognised for shipping loans and compensated for in the guaranteed portfolio by the guarantee. Taking account of the compensation, which also includes positive effects of € 430 million mainly arising from the settlement of losses in connection with the sale of a loan portfolio to hsh portfoliomangement AöR, income of € 581 million was recognised for loan loss provisions (previous year: € -222 million). Together with the income effect of the change in the hedging effect of the credit derivative, loan loss provision income for the Non-Core Bank would amount to € 106 million (previous year: € 436 million) after the guarantee effect.

### OVERALL SATISFACTORY GROUP PERFORMANCE

Group net result, which comprises the results of the Core Bank, Non-Core Bank, segments not subject to reporting requirements as well as reconciliation and consolidation effects, was a generally satisfactory performance in a challenging environment. Group net income before taxes amounted to € 121 million as at 31 December 2016, which was markedly above expectations but below the previous year (€ 450 million) due to the exceptional items recognised in the previous year's results (including the revaluation of hybrid instruments in the previous year as a result of the elimination of future coupon payments and reversal of guarantee premiums in connection with the EU decision). Group net result after taxes amounted to € 69 million (previous year: € 98 million).

The Core Bank's strategic business divisions and the effect of the recognition of unrealised gains on the sales of promissory note loans and securities made a significant positive contribution to these results. It was therefore possible to more than offset the recognition of signifi-

cant charges in the Non-Core Bank relating to legacy assets and the high level of guarantee, restructuring and privatisation expenses.

Total income of € 921 million exceeded the plan and, as expected, was below the previous year (€ 1,296 million). Net interest income amounted to € 607 million as at the reporting date compared to € 1,032 million in the previous year. Interest income from operating activities was offset by negative effects resulting from a noticeable decrease in the interest-bearing loan volume compared to the previous year, which the Bank assumed accordingly in its planning. The reduction in the interest-bearing loan volume is mainly attributable to restructuring measures and the recognition of loan loss provisions, which mainly relate to the Non-Core Bank's shipping portfolio. The low level of interest rates and intense competition also continued to have an adverse impact on the Group's earnings situation. This was partially offset by the effects of the recognition of unrealised gains on the sales of promissory note loans and securities, included in total income.

A high amount of impairment losses had to be recognised again in the reporting year for shipping loans held in the Non-Core Bank to take account of the continuing very difficult market conditions in the shipping industry, which are reflected in charter rates not covering costs and very low ship values. After taking account of the compensation under the second loss guarantee disclosed in loan loss provisions and including the hedging effect of the credit derivative (as a component of the second loss guarantee) total relief provided to the Group amounted to € 156 million (previous year: € 304 million). The loan loss provision results were positively impacted by the result of the settlement of losses via the compensation under the second loss guarantee. The Bank was also able to essentially charge interest payments not received in the past in the settlement of losses under the guarantee with HSH Finanzfonds AöR in addition to loan losses incurred.

A further significant reduction in controllable operating and personnel expenses was achieved against the backdrop of the ongoing cost reduction programme. Nevertheless, administrative expenses amounted to € 634 million and were therefore the same as last year (€ 634 million) due to unplanned impairment losses recognised in connection with the revaluation of property, plant and equipment of subsidiaries. Earnings were also adversely impacted by increased restructuring and privatisation expenses (totalling € -110 million, previous year: € -31 million) incurred in connection with planned personnel measures and preparations for the privatisation process.

The return on equity for the Group calculated on the basis of net income before taxes is an above-plan 2.5% (previous year: 9.4%). The Bank had included a lower net income before taxes and return on equity than in the previous year in its planning due to the exceptional

items recognised in the previous year's results. The cost income ratio of 64.8% was weaker than planned due to unplanned impairment losses (previous year: 47.5%) and is therefore significantly above the previous year.

The NPE ratio declined only slightly from 18.8% to 17.5%, as the positive effect resulting from the sale of non-performing loans to hsh portfoliomanagement AöR and other reductions in the portfolio were for the most part offset by the further deterioration in the shipping markets. Furthermore, the complex settlement conditions under the guarantee agreement have a detrimental effect on the rapid winding down of non-performing legacy loans. Overall, the NPE volume and NPE ratio were more unfavourable than expected. It has reached a level that still requires considerable improvement. The coverage ratio of 48.8% reflects solid coverage of the entire NPE portfolio.

The core Tier 1 capital ratio (CET 1 ratio) amounted to 14.1% as at 31 December 2016 (31 December 2015: 12.3%) and is therefore at a good level from the Bank's perspective. The reasons underlying these trends include the overall good annual results, significant reduction in RWA due to the sale of non-performing loans to hsh portfoliomanagement AöR, the synthetic transaction entered into and changes made with regard to the recognition of the senior tranche of the second loss guarantee. The leverage ratio improved to a very solid 7% (31 December 2015: 6.3%) and the liquidity ratios (survival period: 10 months, LCR: 229% and NSFR: 111%) exceeded the Bank's plan and reached also a very good level.

#### KEY GROUP MANAGEMENT INDICATORS

	31.12.2016	31.12.2015
Net income before taxes (€ m)	121	450
CIR	64.8 %	47.5 %
RoE	2.5 %	9.4 %
NPE ratio	17.5 %	18.8 %
Coverage ratio	48.4 %	46.5 %
CET1 ratio	14.1 %	12.3 %
Survival period	10 months	4 months
LCR	229.0 %	112.0 %
NSFR	111.0 %	95.0 %

Further details underlying the business performance are given below in the "Earnings, net assets and financial position" and "Segment reporting" sections.



## EARNINGS SITUATION

## INCOME STATEMENT

(€ m)	2016	2015	Change in %
Interest income	3,466	4,397	-21
Negative interest on investments and derivatives	-191	-55	> 100
Interest expense	-2,733	-3,443	-21
Positive interest on borrowings and derivatives	183	29	> 100
Net income from hybrid financial instruments	-118	104	> -100
<b>Net interest income</b>	<b>607</b>	<b>1,032</b>	<b>-41</b>
Net commission income	87	114	-24
Result from hedging	-4	12	> -100
Net trading income	88	84	5
Net income from financial investments	140	54	> 100
Net income from financial investments accounted for under the equity method	3	-	> 100
<b>Total income</b>	<b>921</b>	<b>1,296</b>	<b>-29</b>
Loan loss provisions in the lending business	631	-354	> -100
Hedging effect of credit derivative under the second loss guarantee	-475	658	> -100
Administrative expenses	-634	-634	-
Other operating income	58	38	53
Expenses for bank levy and deposit guarantee fund	-56	-50	12
<b>Net income before restructuring and privatisation</b>	<b>445</b>	<b>954</b>	<b>-53</b>
Net income from restructuring and privatisation	-110	-31	> -100
Expenses for government guarantees	-214	-473	-55
<b>Net income before taxes</b>	<b>121</b>	<b>450</b>	<b>-73</b>
Income tax expenses	-52	-352	-85
<b>Group net result</b>	<b>69</b>	<b>98</b>	<b>-30</b>
Group net result attributable to non-controlling interests	2	-1	> 100
Group net result attributable to HSH Nordbank shareholders	67	99	-32

### Total income for the Group higher than planned

Total income decreased in the past year to € 921 million compared to € 1,296 million in the previous year. The Bank assumed a decrease in total income in its planning due to the expected reduction in the interest-bearing volume.

Net interest income of € 607 million (previous year: € 1,032 million including the effect of € 214 million from the revaluation of hybrid capital instruments as a result of the impact of the EU decision), made significant contribution to total income in the reporting period. It includes, on the one hand, interest income from operating activities and, on the other, the sale of promissory note loans of € 142 million. The overall positive earnings generated by the client business were partly offset by the more rapid portfolio reduction and the decrease in the interest-bearing loan volume. This was attributable to restructuring measures and the recognition of loan loss provisions in the Non-Core Bank and generally higher loan repayments, which are reflected in the sharp decrease in net interest income.

Net commission income amounted to € 87 million in the reporting year compared to € 114 million as at the previous year end. The decrease is attributable to lower cross-selling income as a result of lower loan restructuring fees in the Non-Core Bank in the wake of the significant reduction in the portfolio.

Net trading income contributed € 88 million to total income in the past year (previous year: € 84 million). In accordance with the list of conditions and commitments of the first EU decision of 20 September 2011 the Bank does not engage in proprietary trading. Operating successes in the client business (€ 128 million including hedging effects) and positive effects arising from assets measured at fair value (€ 22 million) in particular had a positive impact on performance. Net trading income was adversely impacted by € -23 million relating to measurement effects in the derivatives area. Measurement losses in the credit investment portfolio, which were mainly attributable to a substantial widening of CDS spreads, also had a negative effect.

Net income from financial investments amounted to € 140 million and was driven mainly by gains on the sale of financial investments (€ 109 million) and write-ups of securities of Heta Asset Resolution AG (HETA) (€ 48 million). It was adversely impacted by impairment losses recognised on equity holdings and profit participation certificates (€ -39 million). Overall, net income was significantly above that of the previous year (€ 54 million).

In accordance with the announcement made under the Financial Market Stability Act HSH Nordbank exchanged its HETA portfolio (€ 223 million) of securities and promissory note loans in the fourth quarter of 2016 for zero coupon bonds of the Carinthia Settlement Fund (Ausgleichzahlungs-Fonds). This resulted in the above-

mentioned write-up as at the reporting date. This write-up was offset by the recognition of an expense in the equivalent amount resulting from a corresponding reduction in the hedging effect of the second loss guarantee in loan loss provisions due to the hedging of transactions under the second loss guarantee.

### Continuing high level of loan loss provisions

Loan loss provisions continued to be dominated in the reporting year by a high level of additions in the shipping portfolio. Additional loan loss provision expense was recognised for legacy portfolios in the shipping portfolio to take account of the very difficult market developments, which were reflected in a significant reduction in charter rates and ship values. This expense was mainly accounted for loans for bulkers and container ships. The risk trend in the other segments (Real Estate, Corporate Clients) was unremarkable.

In total, loan loss provision expense amounted to € -1,577 million (previous: € -3,020 million) before taking account of the compensation under the guarantee as at 31 December 2016. Although it was significantly below the previous year, it exceeded the plan amount. In the previous year, loan loss provisions were mainly shaped by the changed commitment strategies that took account of market values as at the planned disposal date for the portfolios to be sold in accordance with the findings of the EU state aid investigation. In this regard, additional loan loss provisions of € 1,584 million were recognised for the transaction portfolios. Loan loss provisions recognised in the reporting year, particularly for legacy portfolios, continued to be compensated for by the guarantee if they related to portfolios covered by the guarantee. Compensation under the second loss guarantee for the guaranteed portfolio, which is disclosed within loan loss provisions, amounted to € 2,208 million (previous year: € 2,666 million) after taking account of currency translation gains/losses. After the compensation effect of the second loss guarantee loan loss provision income including current loan loss provision expense amounted to € 631 million (previous year: expense of € -354 million). Taking account of the expense of € -475 million arising from changes in the hedging effect of the credit derivative (previous year: € 658 million) loan loss provision income would amount in total to € 156 million (previous year: € 304 million).

The loan loss provision results were positively affected by the settlement of the losses incurred by the Bank on the sale of the loan portfolio of € 5 billion to hsh portfoliomanagement AöR via the compensation under the second loss guarantee. In connection with the settlement of losses arising on this federal state transaction and further losses under the guarantee with HSH Finanzfonds AöR primarily interest payments not received in the past of € 430 million could also be charged by the Bank in addition to loan losses incurred.

The hedging effect of the guarantee also gave rise for the first time to a cash drawdown of the guarantee after taking account of the transfer of non-performing loans to the federal state owners in the financial year. The Bank's first loss piece (€3.2 billion) was exceeded by €2.3 billion by losses incurred in particular in connection with the settlement of losses relating to the federal state transaction as of the reporting date. The balance sheet utilisation of the second loss guarantee amounted to €9.9 billion (including guarantee payments of €1.9 billion already received) as at 31 December 2016 (31 December 2015: €8.1 billion).

The actual payments made under the guarantee are offset by significant fees already paid for the guarantee. The premiums paid to the guarantors and recognised through profit or loss by HSH Nordbank amounted to €3.2 billion as at the reporting date (including one-off payments of around €0.3 billion made to HSH Beteiligungs Management GmbH). Furthermore, a further one-off payment of €0.5 billion was made to the federal state owners in 2011, which was reintroduced into the Bank in the form of a mixed contribution of cash and in kind in 2012. The total payments made represented a significant burden in the restructuring period.

#### **Administrative expenses adversely impacted by special factors**

Administrative expenses amounted to €-634 million in the reporting period (previous year: €-634 million). Savings realised in line with the plan under the ongoing cost reduction programme for controllable personnel and operating expenses were offset by unplanned special depreciation of €-66 million recognised in connection with the revaluation of property, plant and equipment of subsidiaries. Administrative expenses consequently exceeded the plan amount by a considerable extent. Excluding this unplanned effect, administrative expenses would have decreased by 10% compared to the same period in the previous year despite increasing costs for regulatory requirements.

Personnel expenses, which decreased significantly from €-277 million to €-256 million, were mainly affected by the number of employees that was reduced even further, according to plan. Compared to the end of 2015, the number of employees within the Group declined by 220 to 2,164 (computed on a full-time equivalent (FTE) basis).

Operating expenses (excluding depreciation/amortisation) decreased noticeably to €-278 million compared to €-302 million in the previous year. Savings were mainly achieved by reducing building costs. Higher costs incurred for restructuring commitments also had an adverse impact in the previous year. These savings continue to be offset by high costs incurred in implementing regulatory and accounting requirements.

Depreciation of property, plant and equipment and amortisation of intangible assets increased above plan to €-100 million compared to €-55 million in the previous year. This increase was mainly attributable to unscheduled depreciation of €-66 million, which was recognised as part of the revaluation of property, plant and equipment (particularly aircraft in consolidated companies) that mainly relates to the market portfolio sold in January 2017.

Other operating income amounted to €58 million (previous year: €38 million) and mainly includes income from cost reimbursements and reversals of provisions.

#### **High restructuring and privatisation expenses**

Earnings were adversely impacted to a significant extent by increased restructuring and privatisation expenses of €-110 million (previous year: €-31 million) incurred in connection with planned personnel measures and preparations for the privatisation process.

#### **Reduction in base premium expense**

The base premium expense for the second loss guarantee amounted to €-214 million in the reporting year (previous year: €-473 million). The sharp decrease in premium expense is mainly attributable to the reduction approved under the EU decision in the base premium from 4% (calculated on the guarantee facility) to 2.2% (calculated on the undrawn, i.e. unutilised, portion of the guarantee) from 1 January 2016.

#### **Overall satisfactory Group net income**

After taking account of the operating performance and against the backdrop of the implementation of structural measures HSH Nordbank generated overall net income before taxes of €121 million as at 31 December 2016 (previous year: €450 million). After deducting income tax expense there remained Group net income of €69 million (previous year: €98 million).

The income taxes line item comprised current tax expense of €-45 million and deferred tax expense of €-7 million.



## NET ASSETS AND FINANCIAL POSITION

## MATERIAL ITEMS ON THE STATEMENT OF FINANCIAL POSITION

(€ m)	2016	2015	Change in %
<b>Assets</b>			
Cash reserve	3,491	3,394	3
Loans and advances to banks	4,192	5,595	-25
Loans and advances to customers	50,910	56,575	-10
Loan loss provisions	1,142	-1,065	> -100
Credit derivative under the second loss guarantee	199	663	-70
Trading assets	5,433	7,356	-26
Financial investments	15,493	16,636	-7
Non-current assets held for sale and disposal groups	1,382	5,082	-73
Other assets	2,123	2,737	-22
<b>Total assets</b>	<b>84,365</b>	<b>96,973</b>	<b>-13</b>
<b>Liabilities</b>			
Liabilities to banks	9,501	14,398	-34
Liabilities to customers	40,172	44,567	-10
Securitised liabilities	16,624	18,616	-11
Trading liabilities	5,981	6,758	-11
Liabilities relating to disposal groups	65	1	> 100
Subordinated capital	3,536	3,452	2
Equity	4,950	4,885	1
Other liabilities	3,536	4,296	-18
<b>Total equity and liabilities</b>	<b>84,365</b>	<b>96,973</b>	<b>-13</b>

### Total assets reduced by portfolio transfer

Total assets decreased in the 2016 financial year to €84,365 million (31 December 2015: €96,973 million). This was mainly attributable to the transfer of a portfolio of non-performing shipping loans of €5 billion to federal state-owned hsh portfoliomanagement AöR in the second quarter of 2016. The continued winding down of risk positions in the Non-Core Bank as well as principal loan repayments also contributed to the decrease.

All material line items on the asset side of the balance sheet decreased. Loans and advances to banks of €4,192 million were significantly lower than as at the previous year end (31 December 2015: €5,595 million). This was due to lower demand and time deposits held at other banks and a decrease in repurchase agreements. Loans and advances to customers amounted to €50,910 million (31 December 2015: €56,575 million). A portion of this decrease relates to the reclassification of the portfolio of customer loans to be sold in the market to the “Non-current assets held for sale and disposal groups” line item. Loan principal repayments in the client divisions also played a significant role, which more than offset new business generated in the Core Bank.

Loan loss provisions disclosed on the balance sheet (after compensation effects) is positive and amounted to €1,142 million as at 31 December 2016 (31 December 2015: €-1,065 million). The transfer of the portfolio to hsh portfoliomanagement AöR in the second quarter 2016 resulted in a decrease in loan loss provisions before taking account of the compensation. Excluding compensation, total loan loss provisions decreased to €-6,713 million (31 December 2015: €-8,227 million). The hedging effect of partial guarantee Two is presented by recognising a credit derivative under the “Credit derivative under the second loss guarantee” line item in the statement of financial position with a positive fair value of €199 million (previous year: €663 million). The reduction in the market value of the credit derivative as at 31 December 2016 is also caused by the sale of the portfolio of loans covered by partial guarantee Two to hsh portfoliomanagement AöR and losses incurred that have been settled under the second loss guarantee.

Trading assets decreased to €5,433 million (31 December 2015: €7,356 million). Securities positions held in trading assets decreased in particular, while market values of derivatives declined only slightly. Financial investments recorded a slight decrease to €15,493 million (31 December 2015: €16,636 million). This was mainly attributable to a lower securities portfolio.

On the liabilities side, liabilities to banks in particular decreased to €9,501 million (31 December 2015: €14,398 million). This was mainly due to a decrease in liabilities to central banks and repurchase agreements. Liabilities to customers also fell to €40,172 million (31 December 2015: €44,567 million). Demand deposits and repurchase agreements with clients decreased. Securitised liabilities amounted to €16,624 million (31 December 2015: €18,616 million). The reduction was attributable to a higher volume of maturities than new issues. Similar to trading assets, trading liabilities consisting primarily of negative market values of derivatives decreased to €5,981 million (31 December 2015: €6,758 million).

Subordinated capital increased slightly to €3,536 million compared to the previous year end (31 December 2015: €3,452 million). Reported equity of €4,950 million (31 December 2015: €4,885 million) remained at around the same level as in the previous year. The capital position was adversely impacted by the measurement of pension provisions against the backdrop of the low level of interest rates, whilst the revaluation reserve had a positive effect particularly as the result of the higher measurement of financial instruments recognised at fair value.

Business volume decreased to €93,208 million (31 December 2015: €106,176 million) due to lower total assets. Contingent liabilities (sureties and guarantees) also decreased to €2,189 million (31 December 2015: €2,833 million), whilst irrevocable loan commitments increased slightly to €6,654 million (31 December 2015: €6,370 million).

**STRUCTURE OF LIABILITIES BY FINANCIAL INSTRUMENT**

(€ m)	31.12.2016		31.12.2015	
	Total	of which > 1 year	Total	of which > 1 year
Secured: Covered bonds and asset-based funding	16,031	13,208	17,161	14,415
of which: Covered bonds	10,076	8,616	10,653	8,887
of which: other secured funding	5,955	4,592	6,508	5,528
Unsecured liabilities	32,534	2,937	40,068	1,596
Unsecured (senior unsecured)	17,073	13,464	19,746	16,446
Profit participation certificates and other subordinated liabilities	2,123	1,085	2,122	2,105
Silent participations	2,072	2,072	1,936	1,936
<b>Total</b>	<b>69,833</b>	<b>32,766</b>	<b>81,033</b>	<b>36,498</b>

The above table breaks down HSH Nordbank's liabilities by financial instrument and thereby takes into account the requirements of capital markets participants. Liabilities with a maturity of more than one year are separately shown. The financial instruments can be reconciled to the "Liabilities to customers", "Liabilities to banks", "Securitised liabilities" and "Subordinated capital" balance sheet line items. The carrying amounts of financial instruments excluding principal repayments and accrued interest are assigned to maturity bands in the above table.

One focus within the framework of long-term liabilities are securitised debt instruments (covered bonds, asset-based funding). These mainly include debt instruments issued under Pfandbrief programmes (mortgage, public sector and ship Pfandbrief programmes) as well as other asset-based funding issues, repo transactions and deposits from development banks. The total amount of secured debt instruments outstanding was €16,031 million as at the year end (31 December 2015: €17,161 million).

Unsecured liabilities include call and time deposits comprising mainly client deposits, bearer and registered bonds and other unsecured financing instruments and amounted to €32,534 million as at the reporting date (31 December 2015: €40,068 million). Call and time deposits account for most of the client deposits. The volume of bearer and registered bonds (senior unsecured) amounted to €17,073 million as at the 2016 year end (31 December 2015: €19,746 million).

The total of the profit participation certificates and other subordinated liabilities line items of €2,123 million (31 December 2015: €2,122 million) and silent participations of €2,072 million (31 December 2015: €1,936 million) represent subordinated capital. €660 million of silent participations is disclosed as hybrid financial instruments (Resparc I and Resparc II) under the Securitised liabilities balance sheet line item as at the reporting date.



## Capital and funding

### REGULATORY CAPITAL RATIOS

(SAME PERIOD CALCULATION)

(%)	31.12.2016	31.12.2015
Total capital ratio	24.8	20.6
Tier 1 capital ratio	18.7	16.4
CET1 ratio	14.1	12.3
CET1 ratio (full implementation of Basel III)	13.4	11.6
Leverage ratio	7.0	6.3

### ELIGIBLE CAPITAL

(SAME PERIOD CALCULATION)

(€ bn)	31.12.2016	31.12.2015
Regulatory capital	7.1	7.7
of which: Tier 1 capital	5.4	6.1
of which: CET1 capital	4.0	4.6
of which: additional Tier 1 capital	1.3	1.5
of which: supplementary capital	1.7	1.6
Risk assets (RWA)	28.6	37.4
of which: risk assets counterparty default risk	23.4	26.8
Leverage exposure	77.0	97.6

### CET1 ratio of 14.1 % at good level

The core Tier 1 capital ratio (CET 1 ratio, under the Basel III transitional arrangements, phase-in) increased to 14.1% as at 31 December 2016 and is therefore above plan and still at a good level from the Bank's perspective. It significantly exceeded the previous year's ratio also in the fourth quarter 2016. The development since 31 December 2015 (12.3%) includes the net income for the year, a significant reduction in RWA and the change made to the recognition of the senior tranche of the second loss guarantee for regulatory purposes. This was partially offset by significantly higher items deducted from equity capital.

RWA have decreased compared to 31 December 2015 by around € 9 billion to € 28.6 billion and were therefore significantly below the plan level. The reduction in RWA is mainly attributable to the sale of shipping loans, mostly denominated in US dollar, to hsh portfolio-management AöR (federal states) as at 30 June 2016 and associated significant decrease in market risk RWA, securitisation of portfolio risks (synthetic securitisation transaction) and the continued active winding down of legacy portfolios. However, the trend in the Bank's key risk parameters was negative compared to the previous year, primarily because of developments in the shipping markets.

The calculated risk weight for the senior tranche of the second loss guarantee of the federal states amounted to around 24% and therefore slightly exceeded the regulatory minimum risk weight of 20%. There was no free guarantee buffer available at the 2016 year end (31 December 2015: around € 1.7 billion of free capacity for expected and unexpected losses/guarantee buffer). Besides the deterioration in risk parameters in the shipping portfolio, this is mainly attributable to the settlement of losses (particularly those arising from the federal state transaction) under the second loss guarantee. In a change in the approach adopted as from the fourth quarter 2016 as compared to the approach used until the third quarter of 2016 full settlement of losses is assumed for loan loss provisions derecognised but not yet invoiced to the guarantor under the federal state guarantee.

Furthermore, full implementation of the findings of the supervisory review of the second loss guarantee and charges for regulatory purposes was taken into account by the creation of a virtual so-called "sub-senior tranche" as part of the regulatory recognition of the federal state guarantee as at the reporting date. The senior tranche of the Sunrise guarantee was split into two (virtual) tranches of whom a sub-tranche, receiving a risk weight of 1,250%, is deducted from regulatory capital. The resulting deduction from capital amounted to € 0.6 billion as at 31 December 2016. The economic utilisation of the second loss guarantee increased in the reporting year.

The capital ratios disclosed assume that the material transfer of risk is allowed for the second loss guarantee despite a marked increase in the economic utilisation of the guarantee as at 31 December 2016.

Even under the assumption of full implementation of the Basel III rules (fully loaded) HSH Nordbank's CET1 ratio increased significantly to 13.4% compared to 31 December 2015 (11.6%).

As part of the supervisory process in the Banking Union, HSH Nordbank was assigned an individual minimum ratio by the ECB that is reviewed annually in the SREP process. This ratio was adhered to at all times during 2016. A CET1 capital ratio of 10.5% (phase-in) including a regulatory early warning threshold (Pillar 2 Guidance "P2G") applies to HSH Nordbank from 1 January 2017. This is composed of the SREP minimum requirement of around 8.9% (Pillar 2 Requirement "P2R") plus an early warning buffer of 1.6%.

As part of the supervisory process in the Banking Union, the financial holding group was assigned an individual minimum ratio by the ECB, which is in line with the statutory regulations and reviewed annually in the SREP process. In this regard, a core Tier 1 capital ratio of 4.5% plus capital buffer requirements of around 5.8% in total then applies to the financial holding group from 1 January 2017. The CET 1 capital ratio was 7.9% as at 31 December 2016.

HSH Nordbank's leverage ratio was a very solid 7% as at 31 December 2016 (31 December 2015: 6.3%). A statutory binding minimum leverage ratio value has not yet been defined. With the revision of the CRR the leverage ratio based on Tier 1 capital is to be determined as a binding minimum requirement for all institutions, probably at 3%. The increase in the leverage ratio is primarily attributable to the sharp reduction in the leverage exposure. The reasons for the reduction in the leverage exposure are the change in the methodology used to calculate leverage exposure incorporated in the Capital Requirements Regulation (CRR) on the basis of a EU decision and the reduction in total assets and off-balance sheet transactions, which is thus proof of the massive balance sheet restructuring undertaken by HSH Nordbank.

Detailed information regarding HSH Nordbank's capital and RWA forecast is set out in the Forecast, opportunities and risk report.

#### **Funding activities again expanded**

HSH Nordbank has successfully continued to implement its funding strategy as planned in 2016 by using different sources of funding.

Retail funding performed well in the challenging low interest rate environment. The raising of funding was significantly above plan in the reporting period due to placements with institutional clients.

The Bank had already successfully used the capital markets in the first half of 2016 to issue two large volume Pfandbriefe. A public sector Pfandbrief of € 500 million was followed in April 2016 by a seven year mortgage Pfandbrief in the same amount of € 500 million, which was increased to € 850 million in July 2016 due to the strong demand.

Asset-based funding (ABF) also remains an important refinancing instrument for the Bank, which strengthens the primary US dollar refinancing base in particular. Two further long-term transactions were concluded in the past year via the ABF platform. USD 200 million was raised via a transaction secured by infrastructure loans and USD 250 million via a transaction secured by corporate loans.

Besides the issuing activities, the level of deposits contributed to the implementation of the funding strategy. The deposit and depositor structure was further improved by the liquidity inflow from the sale of the shipping loan portfolio to hsh portfoliomanagement AöR. Total deposits amounted to € 29.7 billion as at 31 December 2016 (31 December 2015: € 35 billion). Furthermore, at the 2016 year end, the

Bank held liquidity reserves in the form of credit balances at central banks in the total amount of € 3.4 billion and collateral eligible for refinancing at central banks in the amount of € 12.0 billion, which the Bank can access at any time.

The sale of the shipping loan portfolio to hsh portfoliomanagement AöR resulted in a strengthening of the liquidity situation in the middle of 2016 following the receipt of the sales price of € 2.4 billion. The liquidity position was also improved by the receipt of payments of € 1.9 billion relating to the settlement of losses under the second loss guarantee. The regulatory requirements for the Bank's liquidity ratios were met during the reporting period. The liquidity ratio as defined in the German Liquidity Regulation (LiqV) was 1.92 as at 31 December 2016 (31 December 2015: 1.89) and remained significantly above the regulatory minimum requirements. The liquidity coverage ratio (LCR, short-term minimum liquidity ratio) reached a very good level of 229% as at 31 December 2016 (31 December 2015: 112%, in accordance with the Basel QIS framework) and was therefore also significantly above the minimum requirements.

The liquidity development report showed a minimum survival period of 10 months in the combined stress scenario as at 31 December 2016. This was 4 months as at the previous year's reporting date (31 December 2015) due to higher maturities of financial instruments covered by the guarantor liability. The regulatory requirement of 1 month was therefore clearly exceeded.

Opportunities and risks regarding funding, liquidity and ratings are set out in the Forecast, opportunities and risks report section.

#### **FINAL ASSESSMENT OF HSH NORDBANK'S POSITION**

The EU decision and structural measures implemented in the reporting period have made a significant contribution to the Bank's overall satisfactory performance in the past year. The CET1 ratio was substantially increased by the net income for the year and especially by the reduction in RWA due to the sale of non-performing loans to hsh portfoliomanagement AöR (federal state owners) as well the securitisation of portfolio risks (synthetic securitisation transaction). The NPE ratio also improved slightly despite the additional significant loan loss provision expense recognised on legacy loans in the Non-Core Bank. Funding requirements also decreased due to the ongoing reduction in total assets, particularly in the US dollar area. The Bank's overall liquidity situation has clearly improved as a result of this and the drawdown of the guarantee made as part of the settlement of losses. Furthermore, HSH Nordbank's operating performance was

also satisfactory under the current conditions. New business concluded and product sales in the Core Bank made a significant contribution to this, although the Bank deliberately placed restrictions on new shipping business due to developments in the shipping markets. The Bank's positive performance was also supported by the cost measures implemented and progress made in optimising processes and organisational structures.

The Core Bank results show that the market successes and efficiency improvements achieved in the segments in the past year under demanding underlying conditions (including deterioration in market conditions in the shipping industry, low level of interest rates, intense competition, EU proceedings) are having a noticeable effect in the segments. With the implementation of the Core Bank's further expandable business model HSH Nordbank is well-positioned overall and is on the right track with regard to its operating business.

The Non-Core Bank mainly holds legacy loans that originate from the years prior to 2009 and are covered by the second loss guarantee. Shipping loans account for most of the portfolios. On the one hand, the continuing very difficult market conditions in the shipping industry and the resulting high additions to loan loss provisions for legacy assets in the reporting period had a clearly negative effect on the Bank's performance. On the other, the required acceleration in the winding down of non-performing loans is only possible to a limited extent due to the complex settlement conditions under the guarantee agreement, thereby putting additional pressure on the Bank's performance.

In summary, HSH Nordbank assesses its performance as positive taking account of the EU decision and the operating progress achieved. Through the structural measures implemented by the Bank in 2016, in line with the plan to the greatest possible extent, key milestones were achieved on the road to meeting the divestment order. Overall, the improvements achieved in the Bank's financial and risk situation form a solid basis for the focussed driving forward of the sales process officially opened in January 2017.

Details regarding the continuing challenges as well as opportunities and risks can be found in the Forecast, opportunities and risks report.



## SEGMENTS

SEGMENT OVERVIEW<sup>1)2)</sup>

(€ m)		Corporate Clients	Real Estate	Shipping	Treasury & Markets	Core Bank <sup>3)</sup>	Non-Core Bank	Other and Consolidation <sup>5)</sup>	Group
<b>2016</b>									
<b>Total income</b>	<b>2016</b>	<b>251</b>	<b>218</b>	<b>127</b>	<b>407</b>	<b>1,003</b>	<b>36</b>	<b>- 118</b>	<b>921</b>
	2015	252	187	127	284	850	407	39	1,296
<b>Loan loss provisions (including credit derivative)</b>	<b>2016</b>	<b>- 5</b>	<b>-</b>	<b>52</b>	<b>-</b>	<b>47</b>	<b>106</b>	<b>3</b>	<b>156</b>
	2015	- 10	11	- 169	-	- 168	436	36	304
<b>Administrative expenses</b>	<b>2016</b>	<b>- 149</b>	<b>- 57</b>	<b>- 53</b>	<b>- 98</b>	<b>- 357</b>	<b>- 299</b>	<b>22</b>	<b>- 634</b>
	2015	- 160	- 56	- 63	- 116	- 395	- 253	14	- 634
<b>Net income before taxes</b>	<b>2016</b>	<b>89</b>	<b>148</b>	<b>104</b>	<b>298</b>	<b>639</b>	<b>- 299</b>	<b>- 219<sup>4)</sup></b>	<b>121</b>
	2015	77	131	- 166	162	204	173	73	450
<b>Segment assets (€ bn)</b>	<b>31.12. 2016</b>	<b>12</b>	<b>11</b>	<b>6</b>	<b>19</b>	<b>48</b>	<b>22</b>	<b>14</b>	<b>84</b>
	31.12. 2015	12	11	8	19	49	30	18	97

<sup>1)</sup> Following the change in the segment structure in the reporting year, previous year's figures adjusted accordingly.

<sup>2)</sup> Summary of the loan loss provisions and hedging effect of credit derivative under second loss guarantee line items.

<sup>3)</sup> The Core Bank is the sum of the four segments: Real Estate, Shipping, Corporate Clients and Treasury & Markets.

<sup>4)</sup> Net income before taxes including result from restructuring and privatisation.

<sup>5)</sup> Consolidation includes the effects of different accounting treatment.

## Change in segment structure

The Bank adjusted its segment structure in the second half of the year based on the organisational changes implemented. As a first step, a portfolio reallocation was made at the Bank in anticipation of these changes. Non-performing loan portfolios of €6.2 billion were transferred mainly from the Core Bank's shipping recovery unit to the Non-Core Bank. These mainly included legacy assets from years prior to 2009, which are covered by the second loss guarantee of the federal state owners. This structurally relieved the Core Bank portfolio of loans earmarked for winding down. In return, €4.5 billion of mainly covered pool portfolios was transferred from the Non-Core Bank to the Core Bank's Treasury & Markets segment. This resulted in the consistent allocation of loan portfolios to continuing operations in the Core Bank and the reduction in risk in certain non-performing portfolios in the Non-Core Bank.

In a second step, the Bank changed the segment structure on the basis of the portfolio reallocation and changes made to the internal reporting and management processes. This includes the structural adjustment of the segments and reallocation of the guarantee effects to the individual divisions. Segments not subject to reporting requirements (mainly overall bank positions) and reconciliation items reported under "Other and Consolidation" were also combined. These changes

are aimed specifically at increasing the external transparency of the Core Bank's strategic business divisions as well as the non-strategic wind-down portfolios and thereby also at establishing a rigorous and clear reporting process for each value creation structure.

The above-described changes in the internal management processes and organisational structure, which result in the described changes in segment reporting, also enables HSH Nordbank's value creation structures to be presented in a more transparent manner as the basis for the privatisation process.

## Adjustment of segments

In conjunction with combining the market divisions under the responsibility of a single Management Board member the Shipping, Project & Real Estate Financing and Corporates & Markets segments were dissolved and transferred in the reporting year to the Real Estate, Shipping, Corporate Clients and Treasury & Markets segments. Furthermore, the former Corporate Center segment as a segment not subject to reporting requirements is mapped under "Other and Consolidation". This presentation results from the organisational structure based on products and client groups and reflects the internal control and monitoring system.

### Reallocation of guarantee effects

The guarantee effects of the federal state guarantee, which had previously been reported in summary form in the respective consolidation columns of the Core Bank and Non-Core Bank (formerly Restructuring Unit) were allocated to the individual segments mainly based on causation and the two consolidation columns were thus merged into a single consolidation column for the Group. The hedging effect of the second loss guarantee on loan loss provisions recognised in each of the segments is also mapped in the appropriate segments, if the loan commitments concerned are hedged under the second loss guarantee. The guarantee fees are allocated to the segments based on the regulatory capital of the guaranteed portfolio. For reasons of simplification, other interest effects, which arise, inter alia, as part of the settlement of losses under the guarantee, are allocated in full on the basis of the losses already settled, which are incurred primarily in the Non-Core Bank following the portfolio reallocation. Other effects previously included in the former consolidation columns are disclosed in the Group's consolidation column.

### "Other and Consolidation"

Segments not subject to reporting requirements (including the Corporate Center) combined under "Other and Consolidation" include administrative divisions and overall bank positions. Reconciliation items, arising from the difference between internal reporting and the Group financial statements, are also disclosed under "Consolidation". In view of the of the above, the result from restructuring and privatisation is reported in the Group's now combined consolidation column. Expenses for the bank levy and deposit guarantee fund were also allocated to the segments as at the 2016 year end. The previous year's figures have been adjusted accordingly.

Most of the Bank's liquidity reserves are also reported in the segment assets of other segments not subject to reporting requirements. The former Corporate Center segment is also included under the "Other and Consolidation" as a segment not subject to reporting requirements.

### Earnings impact of segment changes

In light of the segment changes described above the results reported for the Core Bank have changed significantly. The Core Bank previously included the Shipping, Project & Real Estate Financing segments with the Shipping, Real Estate and Corporate Finance divisions, the Corporate & Markets segment with the Capital Markets and Corporate Clients divisions, the Corporate Center segment (for reporting overall bank positions as well as administrative and service divisions) and the Core Bank consolidation column (for reporting the guarantee effects and other charges such as the result from restructuring and expenses for the bank levy and deposit guarantee fund). Following the change in the segment structure the Core Bank comprises the sum of the four segments – Real Estate, Shipping, Corporate Clients and Treasury & Markets.

Following the changes to the segments the Non-Core Bank comprises the former Restructuring Unit segment and the guarantee effects previously reported in the Restructuring Unit's consolidation column.

All previous year's and plan figures have been adjusted accordingly for comparative purposes. The comparability of the segment results and the forecasts made are thus ensured in full.

### Core Bank results exceed expectations

The Core Bank, in which HSH Nordbank's strategic activities are combined, increased its new business in the past year in a partly very challenging environment and thus made further progress in implementing its client- and sector-based strategy.

In the 2016 financial year, the Core Bank generated net income before taxes of €639 million, which was significantly above plan and the previous year (€204 million). The overall satisfactory operating performance of all Core Bank segments contributed to this, although interest margins achieved decreased further in the highly competitive environment. The results continued to be adversely impacted by a decrease in the interest-bearing loan volume as a result of scheduled and early loan repayments made by clients and ongoing restructuring activities in the Shipping segment.

In addition to new business transacted, the Core Bank's above plan total income, which increased significantly by €153 million to €1,003 million compared to the previous year (€850 million), reflects the effect of the recognition of unrealised gains on the sales of promissory notes and securities as well as valuation effects in net trading income. The Core Bank results also benefited in comparison with the Non-Core Bank from lower loan loss provisions, which amounted in total to income €60 million including the compensation effects (previous year: expense of €-168 million). Loan loss provisions recognised in the previous year were also adversely impacted by the recognition of general loan loss provisions. Implementation of the ongoing cost reduction programme in line with the plan also contributed to the improved Core Bank results. Administrative expenses decreased markedly from €-395 million to €-357 million compared to the previous year. The Core Bank results include €-25 million, and therefore about 12%, of the total guarantee expense.

Based on these positive results, which also includes the recognition of unrealised gains on the sales of promissory note loans and securities, the Core Bank achieved a return on equity of 19.8% (previous year: 6.7%). The cost/income ratio is 35.5% (previous year: 47.5%). Total assets of the Core Bank decreased slightly despite the new business performance to €48 million as at 31 December 2016 (31. December 2015: €49 million). The NPE ratio decreased only slightly due to the further deterioration in the situation in the shipping markets. It was a low 1.9% (previous year: 2.1%), which still indicates a solid portfolio quality.

**KEY MANAGEMENT INDICATORS FOR THE CORE BANK<sup>1)</sup>**

	31.12.2016	31.12.2015
Net income before taxes (€ m)	639	204
CIR	35.5 %	47.5 %
RoE	19.8 %	6.7 %
NPE ratio	1.9 %	2.1 %
New business (€ bn)	8.9	8.8

<sup>1)</sup> Following the change in the segment structure in the reporting year, previous year's figures adjusted accordingly.

Further information can be found in the explanatory comments on the individual segments.

**SEGMENT RESULTS IN THE CORE BANK**

The Corporate Clients segment is organised on a sector-specific basis, in which the Logistics & Infrastructure, Energy & Utilities, Trade & Food, Healthcare, Industry & Services and Wealth Management business areas are combined. This segment generated net income before taxes of € 89 million in 2016 (previous year: € 77 million). This includes total income of € 251 million (previous year: € 252 million), which reflects the business performance across all industry sectors in a highly competitive environment. Compared to the previous year new business volume increased significantly by € 0.6 billion to € 3.8 billion, which also exceeded the forecast made in the middle of 2016 (€ 3.7 billion). However, the originally planned new business volume was not achieved. The performance was adversely impacted by the low level of interest rates and good liquidity situation of companies, which is reflected in the level of scheduled and early loan repayments. The loan volume was stabilised compared to the previous year by the marked year on year increase in new business. At the same time, the client base was broadened in all German locations. Structured project financing transactions were concluded in 2016 in the railway transport, district heating grid and data infrastructure sectors. Another focal point was wind energy (onshore projects) in Germany and Scandinavia.

The Real Estate segment made a significant contribution of € 148 million to the Bank's earnings (previous year: € 131 million). This performance was clearly positive compared to the previous year and reflects the Bank's good market position in this segment.

The Bank was successful in further increasing new business of € 4.6 billion in 2016 in an increasingly tough competitive environment compared both to the plan and the previous year. Business in the West German metropolitan regions and with international institutional investors was particularly successful. It was possible to maintain the high market penetration in the core region of North Germany.

Total income of the Shipping segment of € 127 million (previous year: € 127 million) was maintained at the previous year's level. As expected, the decrease in interest income was offset by positive measurement effects recognised in net trading income. The considerably improved

net income before taxes of € 104 million compared to the previous year (€ -166 million) was primarily driven by loan loss provisions after compensation, which resulted in an income effect of € 52 million, as well as effects arising from the reversal of general loan loss provisions. The shipping market was characterised in the financial year 2016 by an ongoing challenging environment. Selective new business transacted during the year with counterparties of good credit quality amounted to € 0.3 billion and, as expected, was significantly below plan.

The Treasury & Markets segment generated net income before taxes of € 298 million (previous year: € 162 million). The sale and distribution of capital markets products generated earnings at the previous year's level, which were in line with the sector trend, with positive trends in the derivatives business. Deposit business with savings banks and institutional investors continued to perform well. The increase in net income is also attributable to the recognition of unrealised gains on the sales of promissory note loans and securities on optimising cover pools in the public sector Pfandbrief business.

The Core Bank results include the significant earnings of the Transaction Banking product division. Product net income amounted in total to € 17 million (previous year: € 24 million), which mainly includes income from the use of products by clients in the area of payment transactions, from account management including investment products as well as foreign trade documentary business. The division was thus able to make a tangible contribution to the Bank's cross-selling income. Under the Bank's internal management system the whole of the net income of the Transaction Banking product division is disclosed in the client divisions and therefore in the results of the individual segments.

**Segment results of the Non-Core Bank**

As expected, the Non-Core Bank, in which predominantly legacy loans earmarked for winding down and non-performing legacy loans are bundled following the portfolio reallocation, disclosed a substantial net loss of € -299 million (previous year: net income of € 173 million). The loss is mainly attributable to the continued reduction in the portfolio and setting of loans to a non-accrual basis as part of the recognition of loan loss provisions. This resulted in a further reduction in the interest-bearing loan volume and a corresponding sharp fall in net interest income. In the previous year, the results were positively affected by recognition of exceptional items relating to the informal agreement reached with the EU Commission, which was defined in concrete terms in the EU decision. The Non-Core Bank benefited particularly from the reversal of guarantee premiums, which impacted the compensation item in loan loss provisions.



Total income of the Non-Core Bank amounted to € 36 million (previous year: € 407 million), to which net interest income of € 15 million (previous year: € 285 million) and net income from financial investments of € 54 million (previous year: € 40 million) made a positive contribution, and net trading income of € –53 million (previous year: € 53 million) a negative contribution. The sharp reduction in net interest income is primarily attributable to the continued winding down of the portfolio and the setting of loans to a non-accrual basis.

Net income before taxes was also adversely impacted by high loan loss provision expense of € –1,594 million (previous year: € –2,869 million). This expense was compensated for in the guaranteed portfolio by the guarantee. Loan loss provision income amounted to € 581 million after taking account of the compensation, which includes the positive effect of the loss settlement (previous year: expense of € –222 million). Together with the hedging effect of the credit derivative, loan loss provision income for the Non-Core Bank would amount to € 106 million after the guarantee effect (previous year: € 436 million).

Administrative expenses amounted to € –299 million (previous year: € –253 million), expenses for the second loss guarantee to € –189 million (previous year: € –433 million) and expenses for the bank levy and deposit guarantee fund to € –15 million (previous year: € –17 million). Furthermore, the Non-Core Bank accounted for € –189 million, and therefore about 88%, of the total guarantee expense.

Total assets of the Non-Core Bank declined to € 22 billion as at 31 December 2016 due to the reduction in the portfolio (31 December 2015: € 30 billion). Its NPE ratio is very high for structural reasons and increased sharply to 63.6% compared to the previous year (54.6%) due to the further deterioration in the situation in the shipping industry during the reporting year. The coverage ratio increased slightly compared to the previous year (45.3%) to 47.7% and reflects the further additions to loan loss provisions and overall solid risk coverage in the NPE portfolio. The coverage ratio increased markedly in the shipping portfolio from 52.7% to 59.2% as this portfolio was the focal point of the loan loss provisions recognised.

### Results: “Other and Consolidation”

Administrative functions and overall bank positions are disclosed in Other under “Other and Consolidation” as segments not subject to reporting requirements. Consolidation also comprises reconciliation items that reconcile the internal reporting results presented in the segment report to the Group financial statements prepared in accordance with IFRS. In addition to the measurement and disclosure differences the result from restructuring and privatisation is allocated in full to this division. Expenses for the bank levy and deposit guarantee fund have been allocated to the segments in the internal reporting since 31 December 2016 and therefore impacts the net income before taxes adversely under “Other and Consolidation” only on a pro rata basis.

Net income before taxes amounted to € –219 million as at 31 December 2016 (previous year: € 73 million), which was mainly attributable to charges recognised in total income and restructuring expenses of € –110 million (previous year: € –31 million) incurred in connection with the planned reduction in staff and the planned privatisation. Income from the management of liquidity and capital positions made a positive contribution to the results. The Transaction Banking product division generated product net income of € 17 million (previous year: € 24 million). Under the Bank’s business unit steering net income from the Transaction Banking product division is disclosed largely in the Core Bank’s segments and to a lesser extent in the Non-Core Bank in line with the internal reporting.

Liquidity reserves are disclosed in the segment assets of “Other and Consolidation”. They amounted to € 14 billion as at 31 December 2016 (31 December 2015: € 18 billion).

#### KEY MANAGEMENT INDICATORS FOR THE NON-CORE BANK<sup>1)</sup>

	31.12.2016	31.12.2015
Net income before taxes (€ m)	– 299	173
NPE ratio	63.6 %	54.6 %
Coverage ratio	47.7 %	45.3 %
Total assets (€ bn)	22	30

<sup>1)</sup> Following the change in the segment structure in the reporting year, previous year’s figures adjusted accordingly.

## EMPLOYEES OF HSH NORDBANK

### Human resource strategy of HSH Nordbank

The human resource strategy supports the overall bank strategy and provides the framework for operational human resource functions. It attaches great importance to ensuring that quantitative and qualitative staffing levels are in place and to managing and avoiding related personnel risks. This goes hand in hand with the ability to attract and retain motivated employees willing to perform.

The Human Resources division is responsible for its governance function, especially in managing personnel expenses and implementing, complying with and enhancing the legal and regulatory principles and guidelines, e.g. in respect of the German Ordinance on the Remuneration of Financial Institutions (InstitutsVergV). Modern and reliable operating processes form the basis for all topics relating to human resource functions.

### Effective resource management

The programmes initiated by the Management Board in 2015/2016 to permanently reduce administrative expenses were successfully implemented. It was possible to agree socially acceptable solutions for the reduction in staff with the Works Councils and achieve the targeted 2016 objectives in this regard.

The number of employees decreased in the course of the ongoing reduction in staff within HSH Nordbank Group to 2,164 based on full-time equivalents by the 2016 year end (31 December 2015: 2,384). Changes to the scope of consolidation also had an impact on headcount. The number of employees (FTE) at HSH Nordbank AG (single entity) decreased to 1,902 by the end of 2016 (31 December 2015: 2,117).

### FULL TIME EMPLOYEES IN THE GROUP

	31.12.2016	31.12.2015
<b>Full-time equivalents (FTE) in the Group<sup>1)</sup></b>	<b>2,164</b>	<b>2,384</b>
of which: Women	820	891
Men	1,344	1,493
Employees in Germany	2,068	2,264
Employees abroad	96	120
<b>Total number of employees in the Group<sup>2)</sup></b>	<b>2,613</b>	<b>2,838</b>
<b>Employee key ratios and figures</b>		
Part-time employment ratio (%)	27.2	26.1
Average age <sup>3)</sup> in years	45.3	44.3
Average length of employment in years	13.7	12.9

<sup>1)</sup> Total number of employees excluding trainees, temporary staff and interns (previous year adjusted).

<sup>2)</sup> Headcount (previous year's number adjusted).

<sup>3)</sup> Only headquarters, excluding branches and subsidiaries

### Focus on professional development

Staff development is the focal point of human resource functions for HSH Nordbank. To this end, the comprehensive range of programmes was tailored in 2016 to professional requirements in particular and focussed on the further development of sales expertise by offering a wide range of training sessions, coaching, seminars and linked in-house presentations by all client divisions. There are also programmes for the further development of managers with the focus on change and implementation skills. A wide range of continuing IT education as well as specialist and health-related seminars complete HSH Nordbank's multi-faceted personnel development programme.

### Young professionals programme expanded further

In addition to developing all employees, the recruitment and promotion of young professionals was further boosted in 2016 by increasing the number of trainee places and the possibility of being hired and promoted after the training period. HSH Nordbank thus offers qualitatively high-quality education for the Bachelor of Arts/Science degree in business management/information systems and for the office management specialist occupations. A total of 33 students/trainees were employed in 2016. In the past year, seven dual students and one trainee completed their dual studies or training at HSH Nordbank with a very good or good overall score and received an open-ended job offer. These young professionals now have further promotion possibilities following the training.

A 24 month individual trainee programme covering a wide range of topics is offered to new entrants to the profession. High-quality training is hereby ensured by comprehensive and in-depth insights into each of the Bank's fields of activity. A total of 21 trainees were employed in 2016.

Due to the expanded young professionals programme HSH Nordbank was also again honoured in 2016 by Absolventa GmbH as a provider of a career-enhancing and trainee programmes as well as by Initiative Karriere.de as a Fair Company for its good treatment of trainees and university graduates.

The young professionals programme is a key element for counteracting the demographic trend of the workforce and increasing age of HSH Nordbank's employees. In 2016 HSH Nordbank developed a target for a balanced demographic employee structure for 2020 for this purpose. Vacant positions are used to achieve this target and – to the extent possible – are filled by young professionals. HSH Nordbank adopted new approaches in 2016 for this purpose and successfully used social media to recruit.

### Further expansion of exemplary health care and social management services

Employees are offered extensive health care and social management services in an integrated approach. Besides in-house seminars, these also include individual counselling for employees, managers and whole teams. HSH Nordbank also supports the work-life balance of its employees by offering comprehensive counselling and information services on such topics as “maternity and parental leave”, “child care” and “caring for relatives”. The services offered are regularly reviewed and flexibly tailored to employee requirements.

HSH Nordbank was recognised in 2016 by the Hamburg Office for Occupational Safety for “exemplary occupational safety and health protection” due to its comprehensive health management tailored to employee needs. The award is also an incentive to ensure that there is no let-up in the activities to maintain and promote employee health.

### Clear communication strategy prerequisite for a successful privatisation process

The wide range of health care and social management services offered as well as the interesting work opportunities make HSH Nordbank an attractive employer in a challenging, competitive environment with a clear objective for the future, but which is still subject to uncertainty. Managers at HSH Nordbank are committed to communicating openly with all employees regarding the privatisation objective as well as the associated uncertainty, as clear communication creates trust and is essential for the Bank's success.

### Equal opportunities and women in management positions – Management Declaration pursuant to Section 289a of the German Commercial Code (Handelsgesetzbuch – HGB)

HSH Nordbank is continuing to actively address the issues of equal opportunity and the promotion of women with the assistance of its equal opportunities officer. In 2015 the Bank had set quotas in line with the law, which came into force in May 2015, regarding equal representation of women and men in management positions in the private sector and public services and the resulting introduction of Section 76 (4) of the German Stock Corporation Act (AktG).

In August 2015, the Supervisory Board approved a target of 20% for the proportion of women on HSH Nordbank AG's Management Board, which is to be achieved preferably by 30 June 2017. There is currently no female member of HSH Nordbank AG's Management Board.

Furthermore, a target of at least 15% was agreed for the proportion of women at the department head level as at 30 June 2017. The lower limit for the proportion of women in management positions reporting

directly to the Management Board is 16%. Whereas the department head ratio was clearly exceeded as at 31 December 2016 with females accounting for 21% of the department head positions, the target for direct reporting department heads, currently 15%, has not yet been fully achieved. However, the efforts made to promote young female professionals in particular allow the Human Resources division to fill vacant positions at the next higher level from the large group of female department heads. HSH Nordbank is confident that it will be able to achieve both quotas by the 30 June 2017 reporting date. To this end, the “Equal Opportunity Promotion Plan” has been expanded in 2016 to include further measures such as workshops on female promotion and the embedding of this topic in the overall bank objectives.

Topics such as equal opportunities, diversity and female promotion are also of importance for the composition of the Supervisory Board. Under the requirements of Section 111 (5) AktG, also newly introduced in 2015, HSH Nordbank is required to set targets for the proportion of women at the Supervisory Board level as well. Deadlines for achieving these targets are also to be agreed at the same time and reasons given if such targets are not met.

The Supervisory Board had already approved in 2011, based on the then new requirements of the German Corporate Governance Code (DCGC), the objective that the prevailing proportion of women should also not fall below 20% in the future. The Supervisory Board considers an initial target of 30% to be an appropriate proportion of women. With a current proportion of women of 37.5% the Supervisory Board has already met the target set by itself. The proportion of women employed by the shareholders is currently 25%, and 50% on the employer side.

### Employee remuneration

The remuneration system for employees below the Management Board level is based on a total remuneration approach, counteracts any significant dependence on variable remuneration and thereby prevents the employees from taking excessively high risks for the purposes of realising the variable remuneration potential. The amount of the total budget for the variable performance-related remuneration is determined on the basis of the Bank's performance, which is calculated using parameters that reflect the success of the Bank. In addition to achieving key financial ratios these parameters are also based on the Bank's strategic objectives amongst other things. They take account of the concept of sustainability and are always tailored to the business model as well as the Overall Bank strategy and risk strategy.

The budget for the Overall Bank for variable performance-related remuneration of the employees is distributed to the employees taking into account the performance of the divisions and based on the achievement of individual objectives. Fixed upper limits for the ratio



of variable to fixed remuneration were set for all employees of the Group in accordance with the German Ordinance on the Remuneration of Financial Institutions (Institutsvergütungsverordnung – InstitutsVergV) in order to avoid disproportionately high variable remuneration.

In accordance with the specific requirements of the InstitutsVergV HSH Nordbank defines a group of employees as so-called risk takers, who have a significant influence on the overall risk profile of the Bank by virtue of their function. In accordance with the InstitutsVergV parts of their variable remuneration are paid on a deferred basis and are dependent on the Bank's sustained performance.

The required adjustments identified on the basis of the amended InstitutsVergV that came into force on 1 January 2014 were implemented. Due to the fact that these regulations are dependent upon the relevant collective bargaining agreements, they have been adapted in 2015.

The Human Resources division is preparing for the changes in the InstitutsVergV and, together with the Mediation Committee, will probably make further adjustments to the remuneration systems in 2017. The objective is to ensure that remuneration is attractive and in line with the market.

In accordance with the ordinance further details are published in a separate remuneration report on HSH Nordbank's website.

## REPORT ON EVENTS AFTER THE REPORTING PERIOD

### **Sale of the first tranche of the market portfolio**

The sale of non-performing loans of up to €3.2 billion in the market was approved as part of the implementation of the decision reached by the EU Commission on 2 May 2016 in the EU state aid proceedings regarding the replenishment of the second loss guarantee. In this regard, the Bank has selected significant portfolios that are to be sold in the market by the middle of 2017 (market portfolio). By winding down the NPE portfolios the portfolio quality will be gradually improved and the Bank will be further relieved of high levels of legacy assets. The defined portfolio consists of four non-strategic portfolios – aviation, continental European real estate (Scandinavia, the Netherlands, Germany), energy and international real estate.

Sales agreements were signed on 27 January 2017 for the first tranche, which includes, inter alia, aircraft financing transactions (volume of around €0.8 billion EaD) and continental European real estate loans (volume of around €0.5 billion EaD). The purchaser of the aircraft portfolio is the Australian investment bank, Macquarie and the real estate loans were acquired by Bank of America Merrill Lynch. The parties have agreed not to disclose details of the sales price. The sales agreements still require approval from the cartel authorities in this context, which, if they have not already done so, is expected to be received in the second quarter of 2017.

There are further closing conditions with respect to the aircraft financing transactions, including technical inspections of the aircraft, which may give rise to other consequences (e.g. adjustments to the sales price or withdrawal from the contracts). Accordingly, the transfer in rem of the commitments, and therefore the de facto relief of the balance sheet, is expected to take place in the first half of 2017 (closing). The closing of the real estate loans transaction took place on 3 March 2017. The impact on the measurement of the receivables and aircraft concerned was recognised in the Group financial statements as at 31 December 2016.

Additional relief of around €0.3 billion was also achieved by HSH Nordbank as part of the market transaction with individual sales to other investors and principal repayments within the portfolio originally held for sale.

## FORECAST, OPPORTUNITIES AND RISKS REPORT

### FORECAST REPORT INCLUDING OPPORTUNITIES AND RISKS

The following section should be read in conjunction with the other sections in this Management Report. The forward-looking statements contained in this forecast report are based on assumptions and conclusions based on information currently available to the Bank. The statements are based on a series of assumptions that relate to future events and are incorporated in HSH Nordbank's corporate planning. The occurrence of future events is subject to uncertainty, risks and other factors, many of which are beyond HSH Nordbank's control. Actual events may therefore differ considerably from the following forward-looking statements below. Assumptions made by the Bank in the planning process are addressed in greater detail in this forecast report.

One key assumption used in corporate planning in view of the ongoing sale process of HSH Nordbank AG is the overall sale of HSH Nordbank AG as a whole, i.e. the sale of all shares in the Bank held by the seller, including all assets and liabilities, as a preferred solution without any early disposals of assets or sub-areas at amounts below the carrying amount in the event of outstanding bids for an overall sale. The owners are responsible for the sale of the shares, HSH Nordbank's Management Board supports the sale accordingly. In its forecasts and assumptions, the Bank has assumed the sale of the overall bank, as scheduled, adhering to the time schedule agreed in the agreed list of conditions and commitments, such that HSH Nordbank's business model is not negatively affected. The plan is thus based on the assumption that a potential acquirer will in principle continue the Bank's business model. Within this context, it is assumed that the viability assessment to be performed by the European Commission following a successful change of ownership will have a positive outcome, meaning that the Bank will comply with all of the agreements reached in the EU proceedings. As it is not possible to objectively predict the course and outcome of the privatisation process, the process involved in the sale of HSH Nordbank AG creates considerable uncertainty regarding the implementation of the corporate planning, the determination of the loan loss provisions and accounting and measurement.

Estimates regarding the long-term trend in loan loss provisions as well as the planning for payment defaults and, consequently, the actual drawdown of the second loss guarantee are subject to significant uncertainty due to the very long planning horizon, which can influence the future development of the Bank to a greater degree than expected. The main uncertainty factors result, for example, from the movement in key market parameters such as freight and charter rates, ship values as well as the US dollar exchange rate. A key driver of the amount of loan loss provisions is also the breakdown of impaired loan commitments into "capable of recovery" (and therefore recognition of a specific loan loss provision based on the assumption of the continuation of the borrower's business) or "not capable of recovery" (and therefore recognition of a specific loan loss provision based on the

assumption of a workout). Estimates concerning long-term loan loss provisions assume a recovery in the shipping markets, in particular in the container shipping industry, as well as the continuation in general of the current commitment strategy and therefore assumes that HSH Nordbank is willing to continue to provide financing in order to achieve the planned significant reversals of impairment losses in the future.

Developments over the past years have shown that the ability to make forecasts in a volatile environment is limited. The difficult market conditions in the shipping industry are also lasting longer than expected.

In this section, HSH Nordbank will address in detail the material opportunities and risks of the forecasts for the key management parameters as well as the going-concern assumptions. Opportunities are defined as possible future developments or events that may give rise to a positive divergence from the forecast or an objective for HSH Nordbank. In contrast, as part of the forecast report, risks are defined as possible future developments or events that may give rise to a negative divergence from the forecast or an objective for HSH Nordbank. The risk types specific to the Bank are then separately explained in the "Risk Report" chapter.

Unless otherwise explicitly stated below, the following forecast relates solely to HSH Nordbank's operating company, which was established following the legal separation of the present HSH Nordbank into an operating company and holding company as agreed under the EU decision. This separation relieved the operating HSH Nordbank from the additional premium obligations, the obligation to pay base premiums on the drawn down portions of the guarantee and to pay a substantial proportion of the base premium (reduction by 1.8% from the previous 4%) on indrawn portions of the guarantee from 2016 onwards. Corresponding obligations were assumed by the holding company.



## ANTICIPATED UNDERLYING CONDITIONS

Unless otherwise stated, statements made regarding the underlying conditions are based on internal assessments and estimates.

### 2017: Elections in the eurozone and uncertainty in US economic policy

Whilst the economic indicators are providing encouraging signs of a slight acceleration in global economic growth, there is considerable political uncertainty that may also influence the investment decisions of companies. For example, the economic direction of the new US government, especially with regard to the extent of the expected protectionism, is unclear. Many market participants could also become unsettled, if populist and euro critical parties were to make stronger gains in the numerous elections in the eurozone. HSH Nordbank expects increased nervousness in the financial markets in the first half of 2017, which could have an adverse impact on investment activity. The political situation is likely to calm down in the second half of 2017. The global economy should grow overall by 3.4%, a slightly faster pace than in the previous year (2016: 3.1%).

### Europe's growth adversely impacted by political uncertainty

HSH Nordbank expects a sharp acceleration in growth in the USA following a weak 2016. The USA should be able to carry over the robust upwards momentum of the second half of 2016 into 2017. The announced tax reductions are also likely to stimulate economic growth. Inflation is expected to rise slightly, as it appears that the capacity of the labour market is being increasingly utilised.

China's economic growth will again be slightly lower than in the previous year but will still be over 6%. The risks of high levels of indebtedness and increased capital flight have increased. However, the Chinese government has already reacted to the higher stability risks by introducing, among other things, restrictions on the movement of capital. The Bank expects a revival in the economies of Brazil and Russia mainly as a result of higher oil and iron ore prices.

In the eurozone, HSH Nordbank anticipates a politically induced reluctance to invest in the first half of 2017. The elections in the Netherlands, France and probably Italy as well as the Brexit negotiations are likely to create uncertainty. The willingness to invest should increase again in the second half of 2017. This should not be affected by the German Bundestag elections in September. The Bank expects economic growth of around 1.3% for 2017 as a whole (2016: 1.6%).

In view of the uncertainty in Europe the Bank assumes that, in Germany, there may also be a temporary reluctance to invest. The risk posed by other referendums regarding EU membership is likely to affect the political and economic stability in Europe and may adversely impact the heavily export-oriented German economy.

### Further hikes in the key interest rate in the USA, unchanged monetary policy in the eurozone

Trends in the financial markets will probably be determined in 2017 by both political developments and the monetary policy of the US Federal Reserve. The numerous elections in the eurozone could trigger fears of another euro crisis and cause increased nervousness in the financial markets. A slightly unpredictable economic policy of the US government may also have a negative effect on some markets. In this environment, HSH Nordbank expects the US Federal Reserve to make two further interest rate moves. As announced, the ECB is likely to maintain its bond purchase programme and not make any changes to key interest rates over the short term.

Long-term yields will probably increase further but a sell-off of government bonds with a related sharp rise in yields is not anticipated by the Bank.

The euro remains susceptible to a depreciation against the US dollar in 2017, as new referendums in euro countries should also not least raise the question concerning the stability of the eurozone. The oil price will move in a sideways trend following the sharp increase of last year, because the new supply from the USA should depress the market.

### Outlook for relevant markets

A continuing very tense situation is expected in the shipping markets over the short term.

Only a weak recovery trend for container ships is likely to emerge in the current year. The Bank expects that, although charter rates will slowly increase to levels moderately above operating costs, over the medium term they will not move to a level consistently above that necessary to meet debt servicing requirements. Although demand should rise slightly, fleet capacity will also increase more strongly, as new deliveries in 2017 will probably be higher again. The indications are that fleet utilisation will only be higher with an attendant market recovery from 2018 onwards. Any trade restrictions imposed by the new US government could become a dampening factor for container traffic.

It is also expected that there will only be a slight improvement in the demand trend for bulkers. However, in light of the new orders currently outstanding, growth in the supply of tonnage should fall even further in the second half of 2017. In conclusion, it can be expected that charter rates and ship values will stabilise initially. On average in 2017 they should be slightly above the previous year's level.

The oil tanker market will probably go through a trough in 2017. Although an increase in demand at the long-term historical average is expected, supply is likely to increase at an appreciably faster pace due to the upcoming deliveries. However, the absence of new orders indicates a withdrawal of investors from this market. Against this backdrop the Bank expects a scenario of a soft landing with lower, but still adequate, rates. A recovery is expected to start from 2018 onwards.

HSH Nordbank uses a weighted average of independent external forecasts of the leading market research institutions, Marsoft and MSI, for its assessment of future developments in the shipping industry.

The German real estate markets should continue to benefit in 2017 from the favourable underlying conditions and develop positively overall. However, demand is falling slightly in the housing markets of most large cities despite the continuing increase in the level of immigration. More and more homes are coming onto the market while building activity is increasing at the same time with the effect that the reduction in the vacancy rate is likely to gradually decrease to a very low level. The retail sector currently benefits from the positive consumer sentiment and increasing household income. However, demand for space is growing at a noticeably slower pace. In the office real estate markets, declining vacancy rates can be expected due to only a slight increase in completions and a demand for space that is hardly flagging and is even buoyant. Office rents are likely to increase further, not least in central but also secondary locations. A considerably more moderate rate of growth is expected for retail real estate. Residential rents should also increase more slowly with an increase in completions. The statutory limits placed on rent increases on the re-letting of homes should only start to take effect in the medium term and after supplementary measures. After the very strong growth in the previous year and gradually increasing interest rates housing prices and market values of commercial properties are likely to only increase moderately in 2017.

Prospects for renewable energies also remain mixed in 2017: Whilst the capacity added is likely to stagnate at an overall good level in Europe, there are certainly growth opportunities globally. However, a distinction must be made between wind and solar energy: The substantial increase in capacity added over recent years should continue in the German wind energy segment. Demand should increase particularly as a result of the conversion to bidding procedures passed in the amendment to the Renewable Energies Act (EEG). New installations are also likely to increase again in the rest of Europe. The absolute increase in generation capacity in the solar energy sector in Germany – and also in Europe as a whole – should stabilise at a moderate level over the coming years. The more moderate outlook is due mainly to the implemented and intended restrictions on state subsidies.

The increase in transport demand as a result of stronger global economic growth on the one hand and high maintenance requirements on the other are providing positive stimuli for investments in transport infrastructure. Institutional investors are likely to continue to be important. Revenues of companies in the logistics sector should increase in the 2017 financial year at a slightly faster rate than in 2016. However, this cyclical sector is subject to the risks of a general macro-economic downturn and a weakening in global trade, also possibly as a result of increasing protectionist measures. It is not expected that any noticeable real economic effects on the logistics economy and trade flows with Great Britain will yet be felt at the beginning of 2017. The business climate indicator for the German logistics sector reached its highest level for more than half a decade at the end of 2016. However, this could change in subsequent years with the commencement of negotiations and depending on the specific Brexit structure.

It is not only the economic slowdown in China that discomforts heavily export-oriented sectors of the manufacturing industry such as automotive, engineering, electronics and chemicals. The consequences of the Brexit vote cannot yet be predicted, but should become increasingly clearer in 2017 as the exit negotiations are about to start. Furthermore it remains to be seen to what extent the new US government will actually implement the protectionist measures announced in the election campaign. This represents in total a significant downside risk for the global economy. The economic upswing in the USA as a result of the announced expansive fiscal measures (including infrastructure spending, tax reductions) and the weak euro can be regarded as positive over the short term. The positive growth rates will therefore be sustainable. The food industry will probably continue to grow due to the satisfactory consumer confidence of private households.

The outlook is less positive for the international business of companies in the wholesale and foreign trade sector due to the lack of any significant growth dynamics in German industry. As a result, the cyclical intermediate industries in particular will suffer.

The positive underlying conditions caused by the good employment situation are continuing to have a beneficial effect on the retail sector. However, momentum is likely to slow slightly, as increases in real wages of private households will probably be lower as a result of increasing inflation. E-commerce will also remain a growth driver in 2017.

Investment budgets of companies should initially remain at least stable sector-wide due to strong domestic demand in 2017, which could have a positive effect on loan demand at banks. As competition between banks remains intense in Germany, the strong pressure on credit margins will continue.

### Ongoing challenging environment for banks

Against the backdrop of increasing geopolitical and economic uncertainty in conjunction with the economic policies of the new US government, the implementation of the vote of the British electorate to leave the EU (Brexit) and possibly continued high volatility on the financial markets as well as the significant slowdown in growth in important emerging markets, the macroeconomic environment is also likely to remain challenging for banks in 2017.

In view of the macroeconomic uncertainty, the ECB in particular is likely to maintain its expansive monetary policy with the effect that the pressure on net interest income resulting from the low interest rate environment will continue to increase gradually. Institutions will attempt to offset this negative effect on profitability by expanding income sources not dependent on interest rates (for example commission income) and by further reducing costs.

Intense competition for medium-sized clients, particularly in Germany, is also putting additional strain on bank earnings. In addition, the comprehensive regulatory requirements, which demand increasingly more resources, are reflected in administrative expenses of the institutions. The European bank levy for the Single Resolution Fund, which was again significantly higher in 2016, is also making itself felt.

At the same time, the regulators and market participants are continuing to increasingly focus on a comprehensive view of the capital adequacy of banks. Besides the introduction of additional capital buffers (capital retention, early warning and systemically relevant buffers) this is particularly important regarding the extent to which banks are prepared for future regulatory standards for bail-in eligible liabilities. These relevant capital requirements that form part of the resolution mechanism include in particular the institution-specific minimum requirements for regulatory capital and eligible liabilities (MREL) to be defined by the national banking supervisory authorities and resolution authorities.

Other fundamental adjustments can already be identified alongside to these capital requirements that are being increasingly defined. The changes discussed under Basel IV, which, amongst other things, will serve to improve the comparability of RWA profiles and the reduction of complexity concerning risk identification, are at the same time aimed at the harmonisation of supervisory practices in the EU and are to improve transparency vis-à-vis the markets. The change projects include in particular capital floors when using internal models (so-called "CSA floor"), limiting capital savings through the use of internal risk parameters ("IRB constrained"), greater consideration of interest rate risk in the banking book and an adjustment of the approaches adopted for capital backing of securitisations.

Even though an agreement on the application of the Basel IV rules had not been reached at the beginning of 2017, and there is still uncertainty regarding this, an increasing trend of higher capital requirements can be expected.

### New accounting rules and reporting requirements - preparations for IFRS 9 and BCBS 239

In addition to the various new requirements regarding future capital adequacy, focus is being increasingly placed on preparations for the new accounting rules for financial instruments under IFRS 9 that come into effect from 2018, which will entail changes in the classification of financial assets and determination of loan loss provisions. The final version of the IFRS 9 Standard published in July 2014 replaces the existing provisions set out in IAS 39 and must be applied compulsory for the first time from 1 January 2018.

Reference is made to Note 1 in the Group explanatory notes regarding the material changes in accounting policies expected as a result of the introduction of IFRS 9.

Since the end of 2014 HSH Nordbank has been making intensive preparations as part of several projects for the first-time application of IFRS 9. The objective of these projects is the timely implementation of the new classification and measurement requirements, especially impairment and hedge accounting, in the IT systems and processes concerned as at 1 January 2018.

It is currently not possible to quantify the effects of IFRS 9 for HSH Nordbank in a manner that satisfies the disclosure requirements for external reporting. The impact will be estimated in test calculations, which will be gradually refined on the basis of the further development of models, systems and data. Based on the current, but not final status of the project and analysis this will entail changes to the measurement categories with regard to the new classification model for certain portfolios or individual financial asset transactions held in HSH Nordbank's portfolio. This results in an increase in the portfolio of instruments measured at fair value.

With respect to the new loan loss provision model a significant increase in loan loss provisions for the non-defaulted business (levels 1 and 2 in the new loan loss provision model) and a corresponding reduction in equity can be expected at initial application.

Furthermore, the Basel Standard 239 (BCBS 239) gives rise, for example, to comprehensive future requirements regarding risk data aggregation including the IT architecture and risk reporting by banks. In this connection, it is likely that most banks will have noticeable investment needs in order to develop a comprehensive reporting system



to meet the regulatory requirements (AnaCredit). The increasing focus on the issue of cyber security will also require adjustments to IT systems to meet the new challenges.

The introduction of a tax on trading in financial instruments (financial transaction tax), which is currently under discussion, would result in a significant reduction in income from the capital markets business. However, an agreement on the draft currently under discussion is not expected before the middle of 2017. In view of the varied regulatory requirements accompanied, on the one hand, by noticeably higher costs and, on the other, by exacting regulatory requirements regarding capital adequacy, banks will be required to continuously review their business models and constantly improve efficiency to be able to ensure sufficient profitability and maintain the ability to build up capital from their own resources.

The Bank is preparing itself for the regulatory and accounting rules listed above in a targeted manner. The necessary management measures were also put in place at an early stage with regard to the challenges posed by the low interest rate environment. Additional requirements should arise from the further development of the Basel III Framework (Basel IV), for example for securitisations such as HSH Nordbank's second loss guarantee and capital backing under the credit risk standard approach.

In this context, the focus is placed on the detailed definition of the requirements for HSH Nordbank and on ensuring that the new standards are applied on a timely basis. In general, quantitative effects, if known, arising, for example, from the expected IFRS 9 requirements have been included in HSH Nordbank's bank planning.

## EXPECTED BUSINESS PERFORMANCE OF HSH NORDBANK

### 2017 – the year of privatisation

The final decision in the current EU proceedings and structural measures already implemented, particularly the sale of non-performing shipping loans of € 5 billion to hsh portfoliomanagement AöR, the market portfolio transaction signed in January 2017 and the formation of a holding structure and associated with that the relief from legacy assets and guarantee fees provided to the Bank are a good basis for vigorously driving forward the already begun privatisation process. Nevertheless, the total amount of NPE relief agreed as part of the EU decision is small which is why significant legacy portfolios continue to adversely impact the Bank's balance sheet and could make the privatisation process more difficult.

In principle, new business transacted in 2017 is expected to be only slightly below the previous year's level based on the Bank's improved financial

and risk situation resulting from the implementation of the structural measures. At the same time, the winding down of high risk portfolios and reduction of the NPE ratio is to be continued at an accelerated pace. In addition, the ongoing cost reduction programme will be systematically continued to further build on the noticeable progress already made at the cost and process level and thereby enhance the Bank's performance over the long term.

### Earnings forecast

HSH Nordbank is adapting itself to the current market environment for the 2017 financial year with regard to new business and the achievable margins. Against this backdrop the Bank expects a new business volume for 2017 that is slightly below that of the 2016 financial year. Furthermore, HSH Nordbank expects that the new business margins will continue to be risk-commensurate but at moderately lower levels than in the previous year due to the challenging competitive environment. At the same time, sales of the range of services offered over and above loan financing will continue to be driven forward to optimally exploit the business and earnings potential.

The earnings base will continue to be strengthened by the focussed new business development and product sales, whereby the restrictions (regional and functional) imposed by the EU are still to be observed until the change in ownership. This will be offset by the elimination of income as a result of the ongoing winding down of non-strategic portfolios and increase in impaired shipping loans. In total, HSH Nordbank expects a marked increase in total income at the Group level for 2017 as a whole, which also includes effects from the recognition of unrealised gains on the sales of securities according to the plan assumptions.

Overall satisfactory operating earnings driven by all segments are expected for the Core Bank. Furthermore, the positive effects from the release of unrealised gains are mainly included in the Treasury & Markets segment. A significant reduction in the balance sheet is planned for the Non-Core Bank in 2017, through which risk positions should be reduced and the NPE ratio significantly decreased. The focus will be on winding-down measures, particularly as part of the ongoing commitment strategies in different asset classes. Total income for the Non-Core Bank will also stagnate at an overall low level in the future in view of the continuing reduction in the portfolio. The active winding down of the portfolio can only be realised to a limited extent due to the complex settlement conditions under the guarantee agreement.

The commitments undertaken in accordance with the list of conditions and commitments were reflected in the Bank's planning. Under these the Bank is required to limit annual new shipping business to € 1.2 billion. Furthermore, total assets may not exceed € 98 billion at the end of 2017 (on an average EUR/USD exchange rate of 1.10).

Asset-based aircraft financing business, which had already been discontinued, will not be resumed. The existing restriction on external growth by prohibiting the acquisition of control in other companies and extension of the ban on proprietary trading will continue to apply. Furthermore, the list of conditions and commitments contains conditions in respect of corporate client business (limited to German clients and their domestic and foreign investments as well as foreign clients, provided they are seeking to execute transactions in Germany).

### Opportunities and risks in the earnings forecast

#### Opportunities

The business opportunities in the corporate clients area as mentioned in the list of conditions and commitments, particularly the opportunity to finance German clients including their foreign investments as well as foreign clients, provided they are seeking transactions in Germany, could have a positive impact on the new business planned for the corporate clients sector.

A sharper increase in income of the Core Bank could arise, if, for example, new business and product distribution with clients develops better than expected, for example as a result of higher margins achieved in the market, stronger than planned product sales or an unexpected high loan demand.

Furthermore, a sharper, strategic focus of the Corporate Clients division on the renewable energy sector among others as well as other possible strategic alignments such as, for example, the planned expansion of asset management activities for institutional clients could have a positive impact on the Core Bank's total income.

As long as the shipping markets remain in the familiar restructuring phase and the conclusion of new business at adequate margins is not possible, potential new business remains very limited. If the shipping markets make tangible sustained progress, for example, through a significant reduction on the supply side, an increase in new business can again be expected.

A sharper than planned increase in the US dollar viewed in isolation would have a positive impact on income generated by the US dollar business.

#### Risks

Any deterioration in the macroeconomic environment and conditions in relevant markets would probably result in a lower than assumed demand for loan financing. The competitive situation could also put more pressure on margins than expected. Total income could also be lower than expected due to a more marked rise in the amount of impaired loans.

The Bank's increased funding costs due to its restricted access to the capital markets and resulting increased margin requirements may limit the volume of new business planned and, as a result, reduce the earnings base. Reference is made to the "Opportunities and risks in the funding forecast" section with regard to further risks that may lead to an increase in refinancing costs.

Despite the significant reduction in the amount of high risk securities held higher measurement losses on debt instruments and derivatives arising as a consequence of market developments or tensions in the financial markets also cannot be ruled out. IFRS measurement effects resulting from movements in the US dollar or interest rates as well as basis swaps could have a more adverse impact than expected, although US dollar sensitivity has already decreased markedly after the planned portfolio transactions have been executed and will further decrease. Future planned results may be adversely impacted by a further appreciation in the US dollar. Total income may also be adversely impacted by uncertainties (for example, due to significant changes in exchange rates following an increase in interest rates) in the case of the planned recognition of unrealised gains on sales of securities.

The implementation of the commitments made as part of the EU decision, particularly in relation to the business model and reduction in total assets, may have an adverse impact on the development of new business, cross-selling and refinancing of the Bank, and thereby also on the Bank's earnings situation. Furthermore, the existing restrictions may have a negative effect on potential transactions. Delayed settlement under the guarantee of losses arising on the realised as well as possible further sales of loan portfolios may have a negative impact on HSH Nordbank's earnings situation (for example, as a result of the reduction in the relief from premium payments for the guarantee).

A privatisation process that does not progress according to plan would also possibly have a negative effect on new business performance. An unsuccessful conclusion of the sales process would result in the cessation of new business under the list of conditions and commitments and thereby have a significantly negative effect on the earnings situation.

If uncertainties arise in connection with the risks described in the "RWA forecast" and "Formal decision in the EU state aid proceedings" sections, and also in the event that the viability review required in connection with the change in ownership is not positive and approval by the EU Commission is not obtained, this may then adversely impact the new business, cross-selling and funding performance as well as the future earnings situation. Delays in the planned and announced privatisation progress in the 2017 financial year may lead to uncertainties and therefore restrictions on new business as well as a resulting negative impact on earnings.

If sales of asset positions are more extensive than planned and new business expansion is consciously curtailed, this could result in a sharper reduction in total income at the Group level due to the elimination of interest income.

Concerning the contractually agreed sale of aircraft financing transactions, there are further closing conditions, including technical inspections of the aircraft, which may have further consequences (for example, adjustments to the sales price or withdrawal from the contracts) with a negative impact on the earnings situation.

Furthermore, a higher than expected employee turnover in sales divisions could make it more difficult to achieve the new business and income objectives.

If the expected increase in interest rates does not occur as planned, this would lead, viewed in isolation, to lower income from the investment of liquidity position.

Furthermore, potential adjustments to the business model and the planned expansion of asset management activities may not be reflected in earnings as expected.

#### Forecast for administrative expenses

The aim of HSH Nordbank on the cost side is to continue to gradually reduce administrative expenses significantly, in order to achieve an appropriate cost income ratio for the Bank on a sustained basis of in principle less than 50% by 2019.

Within the scope of the planning process, HSH Nordbank has planned a noticeable decrease in administrative expenses and in the cost income ratio for the Group and Core Bank for the 2017 financial year compared to 2016. Thereby, the guidelines of the Management Board were fully incorporated in the cost reduction programme (2018PLUS), which was intensified in May 2016. The plan includes, for example, an accelerated reduction in staff and further decreases in operating expenses. The reason for this is that the implementation of the personnel measures could be more rapidly implemented based on the reconciliation of interests and social plan agreed with the Works Council. Details regarding the additional operating expense measures have been specified during the course of business in 2016 and will be implemented in 2017. In general, according to the list of conditions and commitments, which forms the basis for the formal decision of the EU Commission, the Bank is obligated to gradually reduce administrative expenses during the divestiture period to € 540 million (excluding any potential IFRS 10 effects) in 2017. This requirement will be clearly exceeded in 2017 from today's perspective.

The cost reduction programme, which has existed since 2014 and was last adjusted on a needs basis in May 2016, is generally aimed at a further streamlining of the organisational structure, simplification of key processes, optimisation of the product portfolio and realignment of the Bank's IT and had a significant impact in the past financial year. Thus, the controllable administrative expenses for operating activities decreased noticeably compared to the previous year. Nevertheless, additional expenses arising from the consolidation of companies on applying IFRS 10 as well as part of the revaluation of property, plant and equipment (especially aircraft in IFRS 10 companies) had to be considered. Due to opposite income effects (Other operating income) from these companies, these additional expenses are partially offset in the Group. Concerning the planned interim servicing of hsh portfolio management AöR by HSH Nordbank, the Bank was able to reach an agreement that additional incurred expenses for IT, personnel etc. will be fully reimbursed taking applicable fiscal requirements into account.

Gradually, the number of employees will be significantly reduced by 2019 as part of the extended cost reduction measures. An additional moderate reduction is planned for the year 2017 as a whole. However, there remains the important task of retaining qualified staff at HSH Nordbank in order to secure key competences and limit operational risk.

#### Opportunities and risks in the forecast of administrative expenses

##### Opportunities

HSH Nordbank is confident that it will achieve its stated objectives after also taking account of the successes already achieved in the past. Successful implementation of the programme would make a substantial contribution to increasing the Bank's efficiency on a sustained basis.

The individual measures implemented, such as organisational changes and extensive adjustments in the IT area, will be continuously reviewed as part of the measures controlling process to ensure the successful implementation of the cost plan.

The Bank assumes that measures initiated to reduce costs will also continue to be implemented successfully with regard to the expected reduction in the number of employees. In this context, employee turnover higher than that assumed in the Bank's plan would have a positive effect on planned personnel expenses.



In the case of reductions in total assets, and therefore refinancing requirements, there may result savings in terms of the Bank's planned expenses for the bank levy and deposit guarantee fund, while other calculation parameters (for example the institution risk factor) remain the same.

### Risks

If the cost-saving measures are not implemented as planned, it cannot be ruled out that some costs cannot be reduced to the extent desired or not as quickly as planned. In addition, unexpected cost increases in individual divisions resulting from, inter alia, the constantly increasing regulatory requirements and support for the privatisation process, could exceed the cost reductions achieved in other areas. The extent is difficult to estimate, but unavoidable consequences for administrative expenses are possible.

It cannot be excluded that the reduction in headcount associated with the measures is not implemented as planned or results in an increase in operational risk due to higher turnover or implementation risk, for instance, in the area of internal bank projects. The risk of losing key expertise may also be increased as a result of the personnel measures taken.

It may not be possible to identify or implement other measures required in connection with the initiated and continuing cost reduction programme to achieve cost savings to the extent necessary or such measures may only be implemented by incurring higher restructuring expenses, resulting in the planned cost savings not being achieved.

HSH Nordbank may also be required to make special payments because of its membership of the support fund of the Landesbanks and the European bank levy in the event that future compensation and support measures result in the underfunding of these organisations. It is currently not possible due to the calculation method used, which is based on the relative development of institution-specific parameters compared to the sector, to assess whether and to what amount such payments will arise. However, such payments may adversely impact earnings in general.

Changes in calculation parameters (for example, the institution risk factor) may result in increased contributions payable by the Bank for the bank levy and deposit guarantee fund.

Furthermore, new, as yet unidentified, primary expenses or additional project-specific costs for implementing the relevant requirements might arise as a result of regulatory changes (for example, the introduction of a financial transaction tax, new regulatory changes), which may adversely impact future administrative expenses.

### Forecast for loan loss provisions

HSH Nordbank assumes that further significant loan loss provisions will have to be recognised for 2017 due to the continuing difficult shipping markets. The Bank estimates that net additions to be recognised in the Group and Non-Core Bank in 2017 will still be considerable, however, noticeably below the highly significant level of the 2016 financial year. The focal point of loan loss provisions will continue to be the non-performing shipping loans in the legacy portfolio, especially in the container ship segment. The Bank also expects a further noticeable reduction in the NPE ratio in the Group, especially in the Non-Core Bank, due to the ongoing winding down of non-performing loans. The NPE ratio for the Core Bank will remain at the low level reached. It is also expected that the coverage ratio in the Group and Non-Core Bank will gradually increase at a moderate pace in view of further net additions to loan loss provisions.

The Bank also expects the full balance sheet utilisation of the guarantee in the first half of 2017 with the effect that further additions to loan loss provisions in the guaranteed portfolio will no longer be compensated for by the guarantee and will therefore be recognised directly through profit or loss.

Moreover, it can be expected that loan loss provision measures will also be required especially in the shipping industry for transactions not covered by the guarantee in view of the still difficult sector environment.

Currency translations gains or losses recorded in loan loss provisions are heavily influenced by the movement in the EUR/USD exchange rate and would also have a discernible effect on loan loss provisions on an increasing weakness of the euro. Hedging instruments will continue to be used in principle to hedge foreign exchange positions held in portfolios no longer covered by the guarantee or in the absence of any residual hedging effect.

HSH Nordbank uses a weighted average of independent external forecasts of the leading market research institutions, Marsoft and MSI, for its assessment of future developments in the shipping industry.

The loan loss provision plan is based on valuation models that also take into account the regulatory environment, the expected development of risk parameters over time as well as the Bank's empirical values in critical situations in addition to portfolio developments and key macroeconomic data (including the EUR/USD exchange rate, charter rates and ship values). A key driver of the amount of loan loss provisions is also the breakdown of impaired loan commitments into "capable of recovery" (and therefore recognition of a specific loan loss provision based on the assumption of the continuation of the borrower's business) or "not capable of recovery" (and therefore recognition of a specific loan loss provision based on the assumption of a workout). The estimates concerning long-term loan loss provisions are based on the assumption of a recovery in the shipping markets and/or a recovery in the container shipping industry as well as the continuation in general of the current engagement strategies and therefore the assumption of HSH Nordbank's willingness to continue to finance problem loans remaining after the planned transactions have been executed in order to achieve the planned significant reversals of impairment losses in the future.

Details on the loan loss provision plan and expected payment defaults are set out in the Default risk section (Planning for loan loss provisions and losses) in the risk report.

### Opportunities and risks in the forecast for loan loss provisions

#### Opportunities

Loan loss provisions would be lower than expected, if the relevant market parameters and macroeconomic environment developed more favourably than assumed. It is conceivable that the global economy might grow more strongly in the 2017 financial year than forecast, which in turn could support a gradual recovery of the shipping markets and therefore entail a lower need for loan loss provisions.

A greater level of restructuring successes than expected and a rapid winding down of the non-performing loans could reduce loan loss provisions in the future more sharply than expected.

An appreciation of the EUR/USD exchange rate would accordingly reduce total loan loss provisions for the guaranteed US dollar portfolio as a result of the currency effect and would tend to reduce the amount of expected payment defaults in future.

#### Risks

Estimates regarding the long-term trend in loan loss provisions as well as loss planning and, consequently, the final drawdown of the second loss guarantee are subject to considerable uncertainty due to the long planning horizon. This applies in particular to the movement in the US dollar exchange rate and key market parameters in the shipping industry such as cargo and charter rates as well as ship values, which are key input parameters for determining the loan loss provisions. In view of the existing overcapacity in the shipping markets, it cannot be

ruled out that the extent and timing of the market recovery and recoverability of individual commitments may not be achieved in the planning period as assumed in the loan loss provision plan. Due to this and particularly in the case of falling charter rates, loan loss provisions required may continue to increase significantly. This could have a significant long-term impact on the total expected payment defaults and thereby on the drawdown of the guarantee. This would adversely impact HSH Nordbank mainly as a result of higher than planned loan loss provisions after also taking account of the expected full balance sheet utilisation of the guarantee. Reference is made to the explanations in the "Opportunities and risks in the capital and RWA forecast" section regarding the impact of the non-occurrence of the recovery in the shipping markets assumed as part of the planning.

Developments regarding the situation in other sectors may also be worse than expected and require higher loan loss provisions as a result.

Furthermore, it can also not be ruled out that the euro debt crisis in Europe will once again become the centre of attention or, following the Brexit vote in Great Britain, the cohesion of the EU will be further weakened, which could lead to a weakening in the relevant markets. This in turn could result in additional impairment losses having to be recognised. Market turbulence in emerging countries and geopolitical risks could also have negative effects.

Furthermore, unplanned losses could also be incurred, if additional assets were to be sold in an unfavourable environment as part of a further acceleration in the reduction in risk or the restructuring strategy, particularly the Bank's willingness to continue to finance non-performing loans, were to be changed. A change in the restructuring strategy and, as a result, the recognition of loan loss provisions based on the assumption of the workout of loan commitments could restrict the recognition of planned future reversals of loan loss provisions due to the recovery in the shipping markets assumed in the plan.

Individual restructuring measures for large commitments or restructuring solutions, which require a change to commitment strategies (for example, extensive waivers of debt), may result in a significant increase in the need for loan loss provisions.

A fall in the EUR/USD exchange rate would cause the amount of payment defaults in the US dollar portfolios to increase and would therefore result in an increase in loan loss provisions for unhedged portfolios, as loan loss provisions are partly held in US dollars.

With respect to the sale of and reduction in loan portfolios, including sales of portfolios in the market, and related assumed improvement in the NPE ratio, implementation of the winding down strategy may not be feasible as to the amount, transaction prices and/or date assumed by the Bank. If the actual transaction prices achieved by the relevant winding down measures are below the carrying amounts after loan loss provisions, or also in the event of changes to the composition of the portfolios selected by the Bank for a and, if necessary, further portfolio sale(s), could result in a significant additional need for loan loss provisions and, on the other hand, the NPE ratio would not be reduced as assumed. Additional loan loss provisions may also be needed in the event of unplanned asset sales. The main reason for this is that, according to the requirements of the guarantee agreement, only the loan value based on the credit rating and not the current market price is applied in the settlement under the guarantee.

Inspections of the aircraft included in the market portfolio transaction signed in January 2017 could result in subsequent unfavourable adjustments to the sales price and thus to an additional need for loan loss provisions.

If it transpires in course of the Bank's privatisation process that the total sale of HSH Nordbank AG as an overall bank, i.e. the sale of all shares held in the Bank by the seller including all assets and liabilities as the preferred solution without any significant early disposals of assets or parts of divisions below their carrying amounts as the key assumption of the Bank's corporate planning, cannot be implemented, extensive sales of loan portfolios, particularly in the Non-Core Bank, could be required, which may result in a significant increase in loan loss provision expense. Additional measures to support HSH Nordbank AG could be required in this event in order to be able to still comply with the necessary capital requirements.

The amount of losses settled on the drawdown of the second loss guarantee may be lower than the assumptions made by the Bank regarding the hedging effect of the guarantee (for example, if certain losses are not recognised by the guarantor) and result in a charge to profit and loss from the corresponding reversal of the compensation previously recognised under the second loss guarantee.

New accounting rules (such as IFRS 9 from 2018) may also have a significant adverse impact on loan loss provisions over and above the conversion effects incorporated in the current plan. For example, potentially higher than planned required general loan loss provisions as a result of a deterioration in the risk parameters or a much more extensive application of fair value accounting under IFRS 9 than previously assumed, may adversely impact loan loss provisions in the lending business or capital on the adoption date.

This applies in particular to a currently unanticipated situation, in which further portfolios are also assigned in connection with the possible outcome of HSH Nordbank's privatisation process to a business model as defined in IFRS 9 which is different to that in the current plan and requires the portfolio to be measured at fair value.

### Capital and RWA forecast

For 2017, HSH Nordbank assumes that the capital ratios will continue to be significantly above the SREP requirements. HSH Nordbank expects to be able to continue to disclose a regulatory CET1 ratio of around 13.0% despite more stringent requirements resulting from the gradual implementation of Basel III in accordance with the Basel III transitional rules (phase-in). HSH Nordbank has already included in this any additional charges arising during the remainder of 2017, such as exchange rate or counterparty risk relating to the shipping portfolio. Changes in RWA are primarily influenced by new business, the continuing reduction in the legacy portfolio under consideration of further portfolio sales as well as by risk and market parameters, particularly the trend in the shipping markets and the EUR/USD exchange rate. Based on a stable EUR/USD exchange rate HSH Nordbank assumes a moderate increase in RWA for 2017 as a whole due to the expected new business taking account of the planned portfolio sales from the legacy portfolio and active RWA management. The relief provided by the market transactions signed at the beginning of the year should take effect in the first half of 2017.

The transfer of the majority of the shares in HSH Nordbank AG from the current shareholders to the holding company has resulted in the creation of a financial holding group subject to banking supervision, at the level of which banking supervision requirements, particularly minimum capital requirements (CET1 4.5%) as well as additional capital buffer requirements, are to be complied with. According to the plan the Pillar 1 minimum capital requirements pursuant to CRR (CET1 4.5%) and additional capital buffer requirements are complied with at this banking supervisory application level, which is temporarily relevant until the sale of HSH Nordbank AG is completed.

### Opportunities and risks in the capital and RWA forecast

#### Opportunities

Opportunities for the capital ratios and RWA result from more favourable trends in the relevant market and risk parameters, particularly in the case of a stronger euro against the US dollar, and a more rapid reduction in risk in the guaranteed legacy portfolio.



## Risks

Material risks for the capital ratios and RWA result from a potential deterioration in market and risk parameters in the Bank's core markets including a stronger US dollar, a lower than planned reduction in the portfolios and the regulatory environment, for instance from interpretation decisions or audits. There is the risk that defaults of individual and/or also major borrowers with significant loan volumes, for instance in the absence of a market recovery in the shipping industry, will result in a marked increase in losses and put considerable pressure on the capital ratios.

Developments that result in an increase in risk-weighted assets (RWA) in the hedged portfolio (these include, for example, declining charter rates or a lower EUR/USD exchange rate), have a direct, adverse impact on the Bank's CET1 ratio due to the guarantee buffer of the federal state guarantee having been exhausted from a regulatory perspective. Non-occurrence of the recovery in the shipping markets assumed in the plan may result in a significant negative impact on the capital ratios. The impact of such developments in the guaranteed portfolio on the capital ratio was correspondently offset in the past by the guarantee buffer.

It is also possible that additional individual and increased capital requirements or additional requirements will arise from the regular SREP process carried out in the Banking Union. Additional discretionary decisions made by the supervisory authorities and sector-wide capital requirements (capital buffer for systemic and cyclical risk) could increase capital requirements and significantly reduce the effectiveness of the guarantee.

Discretionary decisions made by the supervisory authorities regarding compliance with the material transfer of risk as defined in Article 244 of the Capital Requirements Regulation (CRR) for the regulatory recognition of the second loss guarantee may substantially reduce the regulatory relieving effect of the guarantee and put significant pressure on the capital ratios. It is possible that the material transfer of risk is rejected by the supervisory authorities in light of the significant increase in the economic utilisation of the guarantee as at 31 December 2016. In this case, the capital ratios would clearly decrease and measures to strengthen the capital ratios would become necessary.

If it transpires in course of the Bank's privatisation process that the total sale of HSH Nordbank AG as an overall bank, i.e. the sale of all shares held in the Bank by the seller including all assets and liabilities as the preferred solution without any significant early disposals of assets or parts of divisions below their carrying amounts as the key assumption of the Bank's corporate planning, cannot be realised, extensive additional loan loss provision expenses (cf. Opportunities

and risks in the loan loss provision forecast section) and significant write-downs of deferred taxes could be required. In total, this could have a significant adverse impact on the capital ratios. In this case and particularly in this scenario in combination with other risks described for capital ratios, additional measures to strengthen HSH Nordbank AG's capital ratios may be required on the part of the owners and/or third parties in order to be able to comply with the necessary capital requirements.

If the recovery in the shipping industry assumed in the plan does not materialise, measures would be required to strengthen the capital ratios (for example, reduction in new business, sales of loan portfolios, sales of securities portfolios) in order to comply with the regulatory minimum requirements at the sub-group level. On the basis of the financial holding group, further additional measures over and above capital-strengthening measures that the Bank can implement from its own resources may be required on the part of shareholders and/or third parties to comply the Pillar 1 minimum capital requirements pursuant to CRR (4.5%, CET1).

With regard to the financial holding group subject to banking supervision, there is a risk that not all capital buffer requirements, which exceed the Pillar 1 minimum requirements pursuant to CRR (CET1 4.5%), can be fully complied with at the financial holding group level due to the high premiums payable for the federal state guarantee. Non-compliance with the capital buffer requirements, which exceed the Pillar 1 minimum requirements pursuant to CRR, would mean that a capital conservation plan would have to be prepared for the Group in accordance with Section 10i (3) KWG and, until its approval, additional restrictions under Section 10i (3) KWG, for example regarding the possibility of making distributions on equity instruments, would have to be observed.

There is also the risk that even the Pillar 1 minimum requirements pursuant to CRR (CET1 4.5%) could not be complied with in the planning period (e.g. on a significant deterioration in market and risk parameters, non-occurrence of the recovery in the shipping industry assumed in the plan) without implementing additional capital strengthening measures involving the owners and/or third parties. Non-compliance with the minimum capital requirements could have serious repercussions for the operating business. Capital strengthening measures on the part of the owners and/or third parties would be required to avert such a scenario.

Even in the case of a downside scenario the Pillar 1 minimum requirements pursuant to CRR (CET1 4.5%) could only be complied with after the implementation of capital strengthening measures by the Bank itself (for example, reduction in new business, sales of loan portfolios, sales of securities portfolios) and under the assumption of the deferral (supervisory phasing-in) of the capital impact arising from the first-time application of IFRS 9 over a period of three years.

There is also the risk that the banking supervisory authorities could set additional capital requirements for the financial holding group subject to banking supervision over and above the Pillar 1 minimum requirements pursuant to CRR and the buffer requirements consistently applied across institutions. The banking supervisory authority has considerable discretionary powers in respect of the above-mentioned risks regarding non-compliance with capital requirements.

The capital forecast for the financial holding group is based on the assumption of full settlement under the guarantee by 2022. If there are delays regarding the full settlement date and therefore the expiry of the guarantee, additional premium expenses would adversely affect the capital ratio at the holding company level.

The forecast of the medium-term CET1 ratio is based on the assumption that the operation of the guarantee structure remains unchanged under the regulations currently applicable to securitisations. A tightening of the supervisory set or rules regarding securitisations due to the further development of the Basel III framework (Basel 3.5), which could come into force as from 2020 for HSH Nordbank through its implementation in the EU, could significantly reduce the RWA relieving effect and therefore the efficiency of the guarantee as of this date.

Delays in the planned implementation in the first half of 2017 of the portfolio sales signed at the beginning of 2017 and further portfolio sales in the market or the delayed settlement under the guarantee of the resulting losses incurred could have a negative effect on the planned capital ratios. An overall delay in the settlement for the entire second loss guarantee relative to the current settlement assumptions in the plan would result in significant pressure being put on the capital ratios at the holding company level (HSH Beteiligungs Management GmbH), as, in such a case, further guarantee premiums would be payable for the deferral period.

The capital ratios may be significantly impacted in future by the intended changes to the regulatory requirements (partly referred to as "CRR II/Basel IV"), presumably as from 2020. A large number of changes in the area of market, operational and counterparty risk are consolidated in this regard under CRR II. For HSH Nordbank, stricter rules concerning counterparty risk resulting from Basel IV will be of particular relevance. HSH Nordbank extensively uses models approved by the supervisory authorities to map counterparty risk (Internal Ratings Based Approach – IRBA). The supervisory authority are planning under Basel IV to significantly restrict the benefits resulting from the use of IRBA models by basing the capital backing more closely on the standard approach (CSA floor), by limiting the use of the IRBA model to certain exposure classes as well as limiting the use of internal risk parameters (Constrained IRB).

New accounting rules (for example, IFRS 9 from 2018) will adversely impact capital adequacy over and above the regulatory requirements. These risks are addressed in detail in the "Forecast of loan loss provisions" section.

Movements in the EUR/USD exchange rate – particularly against the backdrop of the elimination of the guarantee buffer in the reporting year – have a significant influence on the RWA trend. An exchange rate below expectations would ceteris paribus lead to an increase in RWA and immediately reduce the Bank's CET1 ratio.

The transposition of the Bank Recovery and Resolution Directive – BRRD) into national law (Recovery and Resolution Act – Sanierungs- und Abwicklungsgesetz – SAG) will result in new capital requirements in 2018. The European Single Resolution Board will set an institution-specific ratio for the regulatory capital and eligible liabilities to be maintained at a minimum for institutions directly supervised by the ECB and therefore for HSH Nordbank (Minimum Requirements on Eligible Liabilities – MREL).

There are risks for German institutions regarding compliance with the MREL ratio in the discussions still in progress at the European Commission (trilogue) about the qualitative requirements for eligible liabilities for non-global systemically important institutions and the recognition of sub-senior liabilities existing since 1 January 2017 under Section 46f KWG (grandfathering) with regard to any requirement of the EBA to also set a minimum requirement for non-senior liabilities for non-global systemically important banks. Any potential tightening of requirements for non global systemically important institutions may be mitigated by a transitional period.

If any of the above-described risks for capital ratios materialise in combination with each other, additional measures to strengthen capital on the part of the owners and/or third parties may be required at all regulatory levels.

With the formation of HSH Beteiligungs Management GmbH HSH Nordbank as the "parent institution" is required under Article 11 (2) CRR to also comply with the large exposure regulations at the financial holding group level. HSH Nordbank AG's large exposure limit (CRR Part 4) is therefore based on the regulatory capital at the group level of the financial holding group. However, as this is significantly lower than in the sub-group of the HSH Nordbank Group due to premium obligations assumed under the guarantee of the federal states of Hamburg and Schleswig-Holstein, this limit represents a powerful limiting factor in the Bank's large exposure management.

HSH Nordbank has also taken over the lower regulatory capital at the Group level of HSH Beteiligungs Management GmbH and has partially set limits for its trading and credit lines as a precautionary measure to reduce the risk of exceeding the large exposure limit.

The large exposure limit at the financial holding group level amounted to €930 million as at 31 December 2016, whereas that of the HSH Nordbank Group (sub-group) is €800 million higher at €1,730 million. A reduction in the large exposure limit may result in restrictions on the choice of restructuring instruments that can be used for loan recoveries.

If additional measures to strengthen capital are required in the event that one of the risks described in this section materialises, which cannot be implemented by the Bank itself or without state aid, this could result in the resolution of HSH Nordbank. Reference is made to the “Opportunities and risks of the formal decision in the EU state aid proceedings” regarding the impact of this.

### Funding forecast

The Bank expects to continue to successfully implement its diversified funding strategy in 2017. The Bank’s asset business will continue to be refinanced primarily by providing bond products for the client business of the savings banks and other financial institutions and placing secured and unsecured bonds with institutional investors and the deposit business transacted with the Bank’s corporate clients.

The funding plan is based on access to the relevant markets including the German Savings Banks Association and other financial institutions. In addition, the retention of the investment grade rating is a key prerequisite for the implementation of the funding strategy. Another focus is on the issuing of covered bonds (Pfandbriefe) as private placements as well as on the public sector capital market, to the extent permitted by market conditions. Additional forms of potential funding are asset-based transactions, to which HSH Nordbank attaches great importance especially for the refinancing of the US dollar asset business.

For the remainder of 2017, the Bank expects the regulatory liquidity ratio as defined in the Liquidity Regulation (LiqV) to be at the high level prevailing at the 2016 year end. HSH Nordbank also expects that the trend of the liquidity coverage ratio (LCR) and net stable funding ratio (NSFR) will be stable compared to the 2016 year end and consequently that the corridor of 80% to 120% provided for in the list of conditions and commitments will be complied with. HSH Nordbank also expects that all other supervisory requirements such as the survival period in the liquidity development report for the combined stress scenario will continue to be complied with and the key ratios will remain more or less at the currently high level.

Deposit business is a key component of the Bank’s refinancing mix. HSH Nordbank intends to make further improvements to deposit and depositor structure. The regulatory liquidity ratios and requirements will be complied with at all times, also under stress conditions. Details regarding this can be found under Liquidity risk in the Risk report section.

The sales of portfolios in the market contractually agreed at the beginning of 2017 and further sales in the market as well as any returns from winding down measures will also lead to a further improvement in the liquidity situation in the first half of 2017. In this regard, the Bank assumed in its liquidity planning that the sales prices will be paid on the respective transaction dates and the liquidity effect of the associated settlement of losses for the market portfolio will occur six to nine months after the respective transaction date. The funding plan assumes that the first significant portion of the sold market portfolio will be completed as at 31 March 2017 with a further portion still to be sold by 30 June 2017. Market portfolio sales over and above these would have a positive effect on the current funding plan.

Stable access, also in unfavourable market conditions, to refinancing sources that are not dependent for the most part on events in the capital markets such as the German Savings Banks Association and other financial networks as well as to collateralised refinancing sources such as Pfandbriefe and asset-based funding, which is also important for refinancing US dollar business, is paramount.

Under the list of conditions and commitments, which forms the basis for the EU decision and was accordingly reflected in the Bank’s planning, the proportion of USD business in the Core Bank refinanced by primary USD funding (and not by derivatives) is to be at least 55% as at the 2017 and 2018 year ends.

The two rating agencies, Moody’s and Fitch, regard the conclusion of the EU proceedings as important milestones and assess the structural measures, which lead to an improvement in the financial and risk profile, as positive in principle. This applies in particular to the portfolio transfer which relieves the Bank of non-performing loans. Nevertheless, the agencies especially consider the uncertainty during the divestiture period and ambitious time frame for a change in ownership to be a burden. The Bank’s future rating position will be determined by the planned further implementation of the structural measures against the backdrop of a challenging market environment as well as the progress made in the Bank’s sales process.



## Opportunities and risks in the funding forecast

### Opportunities

The fulfilment of the funding objectives is mainly influenced by external factors. A positive capital market environment should support the implementation of the issuing strategy in 2017. A sustained expansive monetary policy on the part of the ECB and the associated expansion of liquidity is likely to tend to have a positive impact on the refinancing options and costs.

The currently limited access to the capital markets would gradually improve by the continuing and successful implementation of the intended privatisation of HSH Nordbank in line with the plan, as this would reduce an important uncertainty factor. This is also of key importance for assessments made by the rating agencies. Like this, ratings that are continued to be confirmed as investment grade would significantly underpin the implementation of the funding targets.

Movements in the EUR/USD exchange rate are also relevant for the liquidity situation, as changes in the US dollar exchange rate have an effect on the amount of liquidity to be provided as cash collateral for derivatives (for example basis swaps) used partly for US dollar funding purposes. The cash collateral to be provided would decrease on a depreciation of the US dollar, thereby improving the liquidity position.

### Risks

Execution of funding measures in the market would be made more difficult by potential tensions in the financial markets. A more than expected restrictive monetary policy adopted by the major central banks could also significantly limit the refinancing options and increase funding costs.

There is still no unrestricted access to the capital markets despite the refinancing successes achieved in the past year. The privatisation of HSH Nordbank required under the list of conditions and commitments, the viability review of the new corporate structure required in this connection and approval of the acquisition by the EU Commission might also lead to possible investor reluctance in the long-term area which could have a significant adverse impact on the Bank's funding.

If the implementation of the formal decision and list of conditions and commitments, particularly the privatisation to be completed by 28 February 2018 and the viability review of the new corporate structure required in this connection as well as the approval of the acquisition by the EU Commission, is not, not fully or not successful within the currently specified time frame or should the Bank be subject to an privately managed orderly wind-down (geordnete wirtschaftliche Abwicklung), this could have a significant adverse

impact on funding and funding costs, trigger outflows of short-term funds or fundamentally restrict HSH Nordbank's funding options. In this case, additional measures would be required on the part of the owners and/or third parties to strengthen the liquidity situation.

Should there be delays in the settlement of losses or sales prices relating to the sub-portfolios sold in the market in January 2017 or to be sold in the future, this may negatively affect the Bank's planned liquidity position at each settlement date. Furthermore, the planned liquidity relief could be delayed if the speed at which losses are settled is lower than that assumed in the plan, particularly in the case of the settlement of losses arising on the sale of market portfolios.

Potential rating downgrades, which cannot be excluded despite the recently confirmed investment grade rating during the privatisation process, particularly in the case of unplanned developments, would fundamentally restrict the refinancing options via the capital markets, trigger outflows of short-term funds and increase funding costs. A rating downgrade by both Moody's as well as by Fitch would result in a rating outside investment grade. Adverse developments, particularly during the privatisation period (for example a decrease in capitalisation, non-compliance with the minimum capital requirements, liquidity problems, unplanned deterioration in earnings or setbacks in the privatisation process) may negatively affect the rating or directly put significant pressure on funding and funding costs, trigger significant outflows of short-term funds or fundamentally restrict HSH Nordbank's funding options. In the event of a rating downgrade, the Bank would have to take additional measures to secure an appropriate liquidity position due to the very short-term refinancing (see Group explanatory note 54: Residual maturity breakdown of financial instruments) and the existing depositor concentration on institutional investors.

HSH Nordbank's liquidity and funding plan is based on assumptions about client behaviour based on the deposit base and durations, especially with regard to the trend of short-term deposits. Even in critical, exceptional situations there is the risk that the relevant behavioural assumptions used for the simulation scenarios prove to be incorrect resulting in considerable unplanned liquidity outflows.

Should access to other refinancing sources such as the German Savings Bank's Association and other financial institutions significantly be hampered, this would also severely limit the funding options and would adversely impact the rating of the Bank.

Most of the assets denominated in foreign currency are refinanced via derivatives (for example, via EUR/USD basis swaps). An appreciation in the US dollar results in an increase in the cash collateral to be provided and therefore exerts pressure on the liquidity situation under otherwise similar conditions.

Because of the marked influence of the EUR/USD exchange rate on the Bank's liquidity position due to the need to provide collateral for EUR/USD basis swaps the focus continues to be placed on the reduction of US dollar assets in different asset classes in the course of the winding down of portfolios in the Non-Core Bank. Furthermore, the restrictions on US dollar business will be maintained.

The regulatory liquidity ratio of the German Liquidity Regulation (LiqV) as well as other liquidity ratios such as the LCR, NSFR and minimum survival period in the combined stress scenario would deteriorate regardless of any intentional control measures taken such as, for example, the reduction in short-term deposits. Additional liquidity requirements could arise under the ECB's SREP process as a result of discretionary decisions.

It is also possible that additional requirements in various prudential regulatory areas such as liquidity may arise from the regular SREP process carried out in the Banking Union within the scope of discretionary decisions of the banking supervisory authorities.

If additional measures to strengthen liquidity are required in the event that one of the risks described in this section materialises, which cannot be implemented by the Bank itself or without state aid, this could result in the resolution of HSH Nordbank. Reference is made to the "Opportunities and risks of the formal decision in the EU state aid proceedings" regarding the impact of this.

Further information on liquidity risk is set out in the Risk report section.

#### **Formal decision in the EU state aid proceedings**

The replenishment of the second loss guarantee from €7 billion to €10 billion by the federal state owners in June 2013 against the backdrop of changed underlying conditions and future regulatory requirements was initially provisionally approved by the EU Commission on 2 May 2016. This guarantee measure was provisionally approved by the EU Commission in the 2013 financial year and has strengthened the Bank's CET1 capital ratio since then. At the same time, the EU Commission had instituted state aid proceedings to investigate whether the replenishment of the guarantee is consistent with the state aid rules. These state aid proceedings were concluded by the decision of the EU Commission.

The EU decision is based on a list of conditions and commitments, under which the Federal Republic of Germany as representative of HSH Nordbank's federal state owners and the EU Commission agreed measures to provide legacy asset relief to the Bank.

These measures are generally in line with the informal agreement already announced in the 2015 financial year. These include in particular the reduction in guarantee fees, formation of a holding structure and sale of non-performing loans in an initial amount of €5 billion to the federal state owners and in the amount of up to €3.2 billion in the market as well as a one-off payment of €210 million from HSH Nordbank to the holding company in connection with the premium obligations taken over by the holding and the provision of liquidity in the amount of €50 million to the holding company to ensure its operations.

The planned structural measures and resulting expected effect on the net assets, earnings and financial position are taken into account in the Bank's currently applicable planning for the coming years. Key structural measures were implemented in line with the plan over the past months, such as the formation of the holding structure in order to relieve the operating HSH Nordbank from guarantee obligations, sale of non-performing loans of €5 billion as at 30 June 2016 to hsh portfoliomanagement AöR (federal state owners), sale of a portion of the market portfolio in January 2017 and possibly further sales in the market over the coming months.

Following the relief recognised in the 2015 annual and Group financial statements a large proportion of the long-term structural improvements for the Bank's financial and risk situation, primarily due to the significant reduction in the base premium and noticeable improvement in the NPE ratio, has been achieved. This will improve the conditions for a sustainable long-term business model for the Bank. The aim is an accelerated reduction in the significant legacy portfolios remaining at the Bank, which continue to be covered by the guarantee facility provided by the federal states. Nevertheless, the targeted improvements are restricted given the complex settlement conditions, particularly with regard to the options for winding down legacy assets based on purely economic criteria as part of an active portfolio management and thereby counteract the build-up of a high NPE volume.

HSH Nordbank's capital backing is to be strengthened by improved profit retention opportunities. Furthermore, the Bank's funding requirements, particularly for the US dollar business, will also decrease in the future due to the sale of loan transactions primarily denominated in US dollar. This also strengthens the Bank's liquidity situation affected by movements in the US dollar.

The replenishment of the second loss guarantee has been technically classified by the EU Commission as so-called resolution aid, and HSH Nordbank is regarded as not being viable in terms of state aid prior to the restructuring. The operating company is to be restructured in such a way that enables the successful sale of this company by

28 February 2018. This divestiture period is met with the signing of a sales agreement and may be extended by six months with the consent of the EU Commission, if the technical implementation of the model is delayed due to circumstances over which the federal states have no direct influence. The transfer in rem of the shares to a buyer (closing) may be made at a later date. The sale is intended to be made in an open, non-discriminatory, competitive and transparent process, in which other Landesbanks may also participate. Public savings banks may also take a minority interest in an acquisition by a private third party or by one or several Landesbanks, if the buyer is independent of HSH Nordbank AG and the public sector (Landesbanks are regarded as being independent of the public sector for these purposes). The participating bidders must have the necessary financial resources and proven sector expertise to manage the operating company as a profitable and active competitor.

Shares representing 94.9% held directly by HSH Beteiligungs Management GmbH ("HoldCo") are to be sold as part of the intended sale of the Overall Bank. The federal states of Hamburg and Schleswig-Holstein and (to a much lesser extent) other (indirect) shareholders of HSH Nordbank AG stand behind the HoldCo. The acquisition of the remaining shares of 5.1% held by the fund managed by J.C. Flowers & Co. LLC is also possible under certain conditions. Under the EU decision the federal states are entitled to retain their investment in the holding company up to 25% of the shares in the operating company for a period of up to four years following completion of the sale.

The owners are responsible for the sale of the shares, HSH Nordbank's Management Board supports the sale accordingly.

After the sale announcement published on 23 January 2017 it is conceivable in principle that, besides the preferred sale of the Bank as a whole in the form of the sale of all shares held by the seller in the Bank including all assets and liabilities to one or several investors (bidder consortium) that bidders, who have no interest in acquiring the overall bank, specify in their bid which divisions or assets they do not want to take over on the acquisition of the Bank.

In selecting bidders for the next stage of the process those, whose bid is based on the acquisition of the Bank at a positive sales price (with retention of the guarantee) are preferred.

Following the successful completion of the sales process resulting in an offer that does not require state aid and an offer price that is positive (while retaining the guarantee) the intended acquisition will be subject to a viability assessment of the new corporate structure by the EU Commission prior to implementation and has to be approved by the EU Commission. Should the divestment procedure not lead to offers not requiring state aid (while maintaining the guarantee) with a

positive price being offered before the expiry of the deadline or should the Commission in the course of its viability assessment come to the conclusion that the integration of the operating company into the new corporate structure will not lead to a viable business model that is profitable in the long term, the operating company will cease new business according to the list of conditions and commitments and manage its assets as far as legally permissible with the aim of privately managed orderly wind-down. Under the list of conditions and commitments the restructuring of existing loans in recovery, certain transactions entered into for liquidity management purposes, prolongations at the same terms or to avoid losses as well as derivative transactions entered into to manage the Bank's overall market risk positions, are still permitted in this connection.

Regarding the prohibition of dividends and distributions, the EU decision stipulates that the operating company may not make any payments during the divestment period on profit-related equity instruments (such as hybrid financial instruments and profit participation certificates), unless such are contractually or legally owed. These instruments are also to participate in losses, if the balance sheet of the operating company were to disclose a loss excluding the reversal of reserves. Furthermore, the operating company will not pay any dividends until the sale is completed. The exceptions to this are dividend payments in the amount legally permitted from the operating company to the holding company to be formed.

Based on the information available as at the balance sheet date, the Bank assumes that, on the successful conclusion of the privatisation process, it will again be able to pay dividends and make distributions on hybrid capital for the 2019 financial year at the earliest in 2020.

Furthermore, provisions regarding the reduction in total assets and the business model are to be complied with during the restructuring phase, which ends with the sale of the operating company, and the restriction on external growth through the acquisition of control in other companies is also to be observed (see also the Earnings forecast report including opportunities and risks in this section).

### **Opportunities and risks resulting from the formal decision in the EU state aid proceedings**

#### **Opportunities**

The successful implementation of the measures undertaken and still outstanding would create a further improved basis for establishing a sustainable business model for the Bank and enabling a successful privatisation process.



The successful implementation of the structural measures provided for in the list of conditions and commitments in the EU decision, particularly privatisation and a positive viability review of a new corporate structure required in this regard, and approval by the EU Commission would significantly improve the Bank's business activities and funding situation and end the uncertainty for clients and employees as well as capital market participants.

The business opportunities in the corporate sector included in the list of conditions and commitments, particularly the opportunity to finance German clients including their foreign investments as well as foreign clients, provided they are seeking transactions in Germany, could have a positive impact on the new business planned for the corporate clients sector.

Acquisition of an ownership position by another strong partner as part of the planned privatisation of HSH Nordbank would increase business and refinancing opportunities of the Bank and thereby contribute to the further strengthening of the business model. Consolidation with Landesbanks could have a positive effect for the business model.

### Risks

Should the implementation of the remaining structural measures provided for in the EU decision and the privatisation not be successful in full or in part or within the specified time frame, this would significantly jeopardise the further implementation of the business model and thereby the Bank's future prospects.

Should the scope of the higher relief proposed and agreed by the Bank for the NPE portfolio on the basis of the EU decision prove to be too low on a sustained basis, this would significantly jeopardise the further implementation of the business model and thus the Bank's prospects.

There is the risk that the privatisation is not successful or is not successful in due time. In this event, HSH Nordbank must cease new business and manage its assets to the extent legally permitted with the objective of a privately managed orderly wind-down. The long-term survival of HSH Nordbank in its present form would not be ensured in this case.

In view of the fact that cessation of new business would also include the deposit business, such a situation would have a significantly adverse impact on funding and funding costs, trigger significant outflows of short-term funds or fundamentally restrict HSH Nordbank's funding options. In this case, additional measures on the part of the owners and/or third parties and, where necessary, extensive sales of receivables with corresponding losses on disposal would be required to strengthen the liquidity situation.

In this regard, the Bank analyses different scenarios as a precaution in coordination with the supervisory authorities in order to ensure sufficient process certainty in a theoretically possible adverse privatisation process. Reference is made to the "Opportunities and risks in the funding forecast" and "Opportunities and risks in the capital and RWA forecast" sections regarding the direct impact of adverse developments.

Furthermore, it cannot be excluded that in the event that the privatisation process does not progress in line with the plan, in the event of a privately managed orderly wind-down or in other situations the resolution conditions laid down in Regulation (EU) no. 806/2014 (SRMVO) are met, this could result in resolution measures being ordered by the competent resolution authorities (for example, conversion of equity instruments and debt capital into core Tier 1 capital, a so-called "bail-in"). The long-term survival of HSH Nordbank would not be ensured even in this case.

If it transpires in course of the Bank's privatisation process that the total sale of HSH Nordbank AG as an overall bank, i.e. the sale of all shares held in the Bank by the seller including all assets and liabilities as the preferred solution without any significant early disposals of assets or parts of divisions below their carrying amounts as the key assumption of the Bank's corporate planning, cannot be implemented, extensive sales of loan portfolios, particularly in the Non-Core Bank, could be required, which may result in a significant increase in loan loss provision expenses and also put significant pressure on the capital ratios. Significant write-downs of deferred tax assets may also be required. Additional measures to strengthen HSH Nordbank AG's capital measures may be required in this case and particularly in this scenario in combination with other risks described for capital ratios in order to be able to comply with the necessary capital requirements.

In addition, there is the risk that the implementation of the EU decision will fail due to statutory, supervisory or contractual conditions or it is not implemented within the specified time frame, which could have a negative effect on HSH Nordbank's access to the capital markets, HSH Nordbank's rating, planning and ultimately its long-term survival.

The measurement of the portfolios possibly to be sold in the market could be lower at the actual dates of sale than previously assumed in the planning and calculation of loan loss provisions. In addition, execution of the portfolio sale could be delayed. Subsequent changes in the composition of the portfolios to be sold in the market, for example, in the course of the implementation of the transactions, may also have an additional adverse impact on loan loss provisions. The above-mentioned effects may have an adverse impact on the earnings, net assets and financial position as well as the CET1 ratio.

Furthermore, tax risks could arise in connection with the transfer of assets, particularly to foreign jurisdictions, as part of the implementation of the portfolio transaction. These may result, on the one hand, in higher loan loss provision expenses or other expenses and, on the other, in changes to the portfolio still to be selected for sale in the market in contrast to the assumed planning. Changes in the portfolio selected may also result in increasing loan loss provision expenses in connection with the planned portfolio transactions.

Under the list of conditions and commitments, the Bank is required to limit annual new shipping business to € 1.2 billion. Furthermore, total assets may not exceed € 98 billion at the end of 2017 (on an average EUR/USD exchange rate of 1.10). In addition, the list of conditions and commitments contains restrictions relating to the Corporate Clients division (restricted to German clients and their investments in Germany and abroad as well as foreign clients, provided that they are seeking transactions in Germany), a waiver on the part of the Bank not to resume the already discontinued asset-based aircraft financing business, a restriction on external growth by prohibiting the acquisition of control in other companies and an extension of the ban on proprietary trading. In the event that the trend in the shipping markets is significantly better than planned or good business opportunities arise in other business sectors, these restrictions could have a negative effect on potential transactions.

In light of the agreement in principle recently reached with the EU Commission HSH Nordbank AG remains a member of the Savings Banks Finance Group during the sales process. All issues of HSH Nordbank AG (excluding equity/instruments with equity characteristics, notably under paragraphs 41, 44 of the EU Commission Communication 2013/C 216/01 of 30 July 2013 ("Banking Communication")) therefore fall under the voluntary institutional protection of the guarantee fund of the Savings Banks Finance Group (Section 39 (1) of the Framework Statute). Under the voluntary institutional protection there is no legally binding entitlement to support funds vis-à-vis the protection scheme in the event of the occurrence of a guarantee case. Should HSH Nordbank AG's membership in the Savings Banks Finance Group end at a date not currently known, its membership in the guarantee fund of the Savings Banks Finance Group would continue to apply for a further two years in accordance with Section 94(4) of the Framework Statute.

In the event of a change in ownership as the result of a sale to private investors HSH Nordbank would cease to be a member of the DSGV, and therefore of the protection scheme of the Savings Banks Finance Group as well, after the expiry of a two year transition period.

This could increase HSH Nordbank AG's refinancing costs, make access to funding channels more difficult and have a substantial negative impact on the external rating issued by the rating agencies.

The assumption of the Bank as a going concern for accounting and measurement purposes and the assumption of the continued going concern of HSH Nordbank AG and significant group companies is based in particular on the following assumptions:

(i) the agreements required for the implementation of the decision taken by the EU Commission in the EU state aid proceedings on the replenishment of the second loss guarantee are entered into comprehensively and on a timely basis and that the decision will be implemented by HSH Nordbank AG and its shareholders in full and on a timely basis.

(ii) the operating company, HSH Nordbank AG, is sold at a positive sales price in an open, non-discriminatory, competitive and transparent process not involving state aid until 28 February 2018 and the EU Commission grants its approval for the acquisition following a viability assessment of the new corporate structure. Should the divestment procedure not lead to offers not requiring state aid with a positive price being offered before the expiry of the deadline or should the EU Commission in the course of its viability assessment come to the conclusion that the integration of the operating company into the new corporate structure will not lead to a viable business model that is profitable in the long term, the operating company will cease new business and manage its assets as far as legally permissible with the aim of a structured winding down of its business. In the event that the bank is wound down as a result of the above or for other reasons, or if its rating is downgraded or other adverse developments emerge during the privatisation period, it could trigger outflows of short-term funds and fundamentally restrict HSH Nordbank's funding options. In the case of major unexpected fund outflows, additional measures will need to be taken by the owners and/or third parties to strengthen the liquidity situation.

(iii) as part of the ongoing privatisation process of HSH Nordbank AG, HSH Nordbank AG will be sold in full as a whole bank, i.e. the shares in the Bank held by the seller will be disposed of, including all assets and liabilities, without any material early disposals of assets or sub-segments at prices below the carrying amount in the event of outstanding bids for an overall sale. If extensive sales of loan portfolios, particularly in the Non-Core Bank, are required, it could result in significant additional loan loss provision expenses that are not compensated for by the guarantee, and could require material depreciation of deferred taxes.

(iv) the minimum capital requirements at all regulatory levels can be adhered to in accordance with the corresponding SREP resolutions passed by the European Central Bank and the statutory provisions during the forecast period. If there is a need for significant additional loan loss provision expenses and material depreciation of deferred taxes (e. g. in the scenario described above) or if the recovery of the shipping market that has been assumed in the Bank's corporate planning does not materialise as planned, or the significant risk transfer for the second loss guarantee is no longer ensured from the perspective of the banking supervisory authority, it could put considerable pressure on the capital ratios and additional measures may need to be taken by the owners and/or third parties to strengthen the capital ratios in order to be able to adhere to the minimum capital requirements, particularly at the level of the financial holding group. If such measures are not taken, it could result in the winding down of HSH Nordbank.

It is further required that acceptance by market participants and other relevant stakeholders necessary for the successful implementation of HSH Nordbank AG's business model and the requirements under the formal decision of the EU Commission is maintained or gained.

#### **Overall appraisal and net income forecast**

In view of the milestones achieved in preparing for and implementing the EU decision and overall satisfactory economic developments since the end of the past financial year, HSH Nordbank remains confident that a good foundation has been laid for a successful privatisation process. Following the promising start to the privatisation process the Bank together with its federal state owners is optimistic that it will be able to overcome the challenges of a naturally very complex sales process.

The Bank will continue to intensively support its owners in this and, at the same time, systematically drive forward the client business in 2017 on the basis of the operating progress achieved and implement in parallel the ongoing strategic and operating optimisation measures in a focussed manner to ensure sustainable competitiveness. The aim is also to quickly wind down the non-performing loans combined in the Non-Core Bank, which are still secured by the guarantee facility issued by the federal states, over and above the adjustments planned as part of the market transactions concluded at the beginning of 2017.

Overall, the basis for a sustainable alignment of the Bank is further strengthened and a business model created for HSH Nordbank which, at a minimum, should convince clients, employees and investors as well as potential bidders and facilitate a successful change in ownership.

Major risks for the future performance of HSH Nordbank arise primarily from a sales process not progressing in line with the plan. The continuing very difficult market conditions in the shipping industry represent a significant challenge with regard to the operating performance. In this regard, the future trend of charter rates and ship values as well as estimates of the long-term trend of loan loss provisions are subject to significant uncertainty. The Bank assumes that there will be a further significant need for loan loss provisions in 2017, primarily in the guaranteed legacy portfolio. Against this backdrop the Bank expects full balance sheet utilisation of the guarantee in the first half of 2017. There will be further challenges associated with the low level of interest rates and highly competitive environment, volatility in the financial and currency markets (the USD in particular), changing assessments of the rating agencies and increasing requirements of the European banking regulation.

It is extremely important that, despite a multitude of influencing factors (recovery of the shipping markets, regulatory effectiveness of the second loss guarantee, discretionary decisions on the part of the banking supervisory authorities, uncertainty regarding the impact of the IFRS 9 conversion, potential losses on the sale of loan portfolios), the minimum capital ratios are complied with both at the level of the HSH Nordbank sub-group and the holding company level and the liquidity position is maintained at all times despite adverse developments in the privatisation process or, for instance, in the event of reactions of the rating agencies.

There are additional challenges, primarily for the ongoing privatisation process, arising from the very high amount of legacy loans, which were entered into as part of the significant business expansion up to 2009 and not decisively reduced in 2016 as a result of the EU decision. Despite the changes already made the Bank still has a high NPE ratio in a sector comparison, which is attributable not least to the guarantee construction, which makes the swift winding down of non-performing portfolios more difficult as well as to the overall only moderate relief provided to the Bank under the EU proceedings.

This results in related uncertainty as to whether the developments forecasted for 2017 and beyond will occur. HSH Nordbank is nevertheless confident that it will be able to further develop the Bank on a forward-looking basis in line with its restructuring plan. The implementation of the structural measures and operating progress made on the income and cost side will make a considerable contribution to strengthening of HSH Nordbank.



Over the coming years, the future results of HSH Nordbank are likely to benefit noticeably from the implementation of the structural measures and further implementation of the strategy. The Bank expects to generate net income before taxes at the Group level for 2017 that is at the previous year's level and a return on equity slightly above that of the previous year's level. A moderate increase in net income before taxes and a further noticeable improvement in the return on equity are expected for the Core Bank in 2017. Net income before taxes for the Non-Core Bank is to decrease even more markedly due to the ongoing winding down of the portfolio and the planned loan loss provisions on a full balance sheet utilisation of the guarantee.

The Bank will make continuous efforts to ensure a competitive cost income ratio. The cost income ratio benefits in the 2017 financial year from further reductions in administrative expenses. Structurally, the Bank's results will be improved by the implementation of the measures, especially by the gradual increase in the relief provided with regard to guarantee fees and the planned optimisation of the business model. Nevertheless, the Bank remains cautious in its earnings forecast for the whole of 2017 given the continuing challenging environment for banks in general and HSH Nordbank in particular.

In light of the EU decision, the Bank expects not to make any coupon payments on the hybrid capital instruments during the divestiture period as part of the implementation of the structural measures. Against this backdrop the Bank assumes that, on the successful conclusion of the change in ownership, it will again be able to pay dividends and make distributions on hybrid capital for the 2019 financial year at the earliest in 2020.

In order to fulfil the net income forecast for the financial year 2017, HSH Nordbank's planning needs to be implemented as intended and the risks described in this management report do not materialise.

Details on the bank-specific risk types are explained in the following Risk report section.

## RISK REPORT

### RISK MANAGEMENT SYSTEM

#### Principles of risk management

Active risk management represents a core component of the overall bank management at HSH Nordbank. The current version of the Minimum Requirements for Risk Management (MaRisk) laid down by the Supervisory Authorities serves as the main framework for the design of our risk management system. In addition, comprehensive requirements resulting from the European Supervisory Review and Evaluation Process (SREP) have to be observed.

HSH Nordbank defines risk as the threat that unfavourable future developments may adversely affect the Bank's assets, earnings or financial position.

In order to identify material risks as defined by MaRisk, HSH Nordbank conducts an annual risk inventory. This includes a review of the existing quantitative and qualitative criteria for determining materiality taking due account of the Bank's risk tolerance and if necessary such criteria are redefined. Amongst the material risk types at HSH Nordbank that can be quantified are default risk, market risk, liquidity maturity transformation risk as a type of liquidity risk as well as operational risk, which also includes legal and compliance risks. These risk types are taken into account in the calculation of the risk-bearing capacity. In addition to the risk of insolvency as a second type of liquidity risk other material risk types of HSH Nordbank also include the business strategy risk and reputation risk. Due to the business model of HSH Nordbank, the default risk is the most significant type of risk.

The newly drafted 'Strategic Risk Framework (SRF)' document, which describes the focus of the Bank's risk management activities and lays the foundation for the risk culture, sets out, in addition to the results of the risk inventory, the basic risk strategy principles, quantitative and qualitative risk appetite statements, the overall risk and sub-risk strategies and the limit system. Risk management objectives and the measures used to achieve these objectives are defined in the SRF on the basis of the planned development of the main business activities. The focus is on securing and allocating scarce resources such as economic and regulatory capital and liquidity, taking into account risk tolerance, strategic business goals, the market environment and both the existing and planned portfolio. The risk strategies are supplemented by guidelines for granting loans (Credit Standards) and Investment Guidelines which contain detailed rules and regulations concerning the individual business areas of HSH Nordbank. The SRF forms the risk framework for the business strategy and planning.

The major rules on the methods, processes and internal organisation used for risk management are documented in the Credit Manual of HSH Nordbank, in process descriptions as well as in illustrations of the internal organisation and are published throughout the Bank.

The risk management system is designed to identify, make transparent and manage risks arising from future developments. The Bank's management system is generally aimed at optimising the risk-reward profile of the Bank.

In view of the decision made by the European Commission on 2 May 2016 on the privatisation of HSH Nordbank by February 2018, the risk management system/risk strategy focus is also being optimized further to provide positive support to the privatisation process.

#### Organisation of risk management

The organisation of risk management at HSH Nordbank is aligned primarily to the requirements of the business model while at the same time also taking regulatory requirements into account.

The Risk Committee of the Supervisory Board is in particular responsible for reviewing HSH Nordbank's current and future overall risk tolerance and strategy. In addition it advises the Supervisory Board on the current and future overall risk tolerance and strategy and supports the Supervisory Board in monitoring the implementation of this strategy by the Management Board. The Risk Committee is regularly informed of the Bank's risk position and risk management by the Management Board in meetings.

The responsibility for risk management of HSH Nordbank lies with the Management Board. This also includes the methods and procedures to be applied for measuring, managing and monitoring risk. As a member of the Management Board, the Chief Risk Officer (CRO) is responsible for the risk controlling of HSH Nordbank AG, including risk monitoring, as well as for the back office functions of the Core Bank and Non-Core Bank. In detail this includes the divisions Group Risk Management, Credit Risk Management, Special Credit Management as well as Loan and Collateral Management.

The Group Risk Management business unit develops the methods and tools for identifying, measuring, managing and monitoring risks and, by setting risk limits and risk guidelines, supports operative portfolio management, for which the BU Bank Management is largely responsible.

Credit Risk Management is responsible, among other things, for the credit risk analysis, including the preparation and setting of the internal rating and drafting of the credit applications. Credit Risk Management is also responsible for designing the processes and rules that apply to the lending business within HSH Nordbank. Special Credit Management, a new area that was set up in November 2016, is responsible for managing loan exposures in the Non-Core Bank portfolio, as well as workout and restructuring loan exposures. Loan and Collateral Management is responsible for the settlement and administration of the lending business as well as for obtaining and ongoing valuation of loan collateral.

Trading transactions are settled and controlled in the Transaction Banking and Group Risk Management divisions.

The market and trading divisions are directly responsible for risks and income within the scope of their business activities and thereby make an active contribution to risk management in the Core Bank.

The internal Non-Core Bank of HSH Nordbank (formerly known as the Restructuring Unit), which was established in 2009 and includes positions of business areas that are no longer of strategic importance and non-strategic portfolios comprising legacy assets, has been largely incorporated into the existing organisation, meaning that it is still subject to the group risk management system of HSH Nordbank in full.

Internal Audit reviews the effectiveness, efficiency and appropriateness of risk management, the internal control system and the monitoring processes in a targeted and systematic manner. It monitors and validates the timely elimination of deficiencies identified by the Bank's own activities or external audits. As a tool used by HSH Nordbank's Overall Management Board it is an essential component of corporate governance. It regularly provides the Overall Management Board and Audit Committee of the Supervisory Board with information on the findings of its audits, which are carried out on the basis of a risk-based audit plan that is approved by the Overall Management Board on an annual basis. Internal Audit provides independent, objective and risk-based audit and advisory services that cover all business activities and processes of the Bank, as well as outsourcing arrangements and equity holdings, and also includes projects and changes in operational processes and structures.

The CRO makes decisions independently of the member of the Management Board responsible for the market or trading divisions and provides the Overall Management Board and the Risk Committee with regular information on the risk situation of the HSH Nordbank Group. In this way the separation of functions required under the regulatory rules between the market and trading divisions on the one hand and risk controlling, settlement and control as well as back office on the other is taken into account at all levels of the Bank from an organisational perspective.

Business areas are managed in line with uniform Group standards on the basis of a global head principle. Based on this, the heads of the individual divisions as the respective Global Heads are responsible on a worldwide basis for the strategy of the business areas assigned to them and have the disciplinary responsibility for the employees active in their business area. The Global Heads are supported by the head of the respective foreign branch (General Manager) in the implementation of the strategy on site in the foreign branches whilst maintaining the separation of duties in accordance with MaRisk. The General Manager is responsible for compliance with local legal and regulatory requirements. The global head principle also applies to risk control-

ling to ensure that a Group-wide coordinated risk controlling process is in place.

HSH Nordbank has stipulated rules according to the MaRisk specifications under which formalised audit processes are gone through prior to entering into transactions in new products or new markets (NMNP processes). This ensures that the products are properly considered under risk aspects in the relevant systems and are reflected in the relevant processes, as well as guaranteeing their cost-effectiveness and ensuring that transactions involving new products or on new markets are only entered into with the approval of the Management Board. There is also an NPNM review process in place to check the appropriate mapping of older products on a regular basis.

HSH Nordbank uses an "economic scope of consolidation" as the basis for the Group-wide risk management. It includes those companies that are to be specifically monitored at the Group level due to material risks. The risks of other companies are fully taken into account at the aggregate level (for instance in the form of equity holding risks in the default risk management process).

#### **Risk management by a central committee structure**

The Management Board has established committees that support it in monitoring and managing all material risks. The committee structure was revised and reorganised in the last financial year. The committees comprise not only members of the Management Board, but also the heads of the risk and other departments. This ensures a regular exchange of information on issues relating to risk. Insofar as internal or external regulations do not permit delegation of decisions to the committees, such decisions are prepared by these committees for approval by the Overall Management Board.

The Bank Steering Committee led by the Chief Financial Officer (CFO) and the Chief Risk Officer (CRO) is the body responsible for the management and allocation of financial resources within the framework of the risk limits and the targets. Its duties include responsibility for monitoring and managing the risks associated with the bottleneck resources (incl. risk concentration, credit, liquidity, FX and interest rate risks) taking all sorts of control mechanisms into account (return and costs, risks, liquidity and capital). This ensures an integrated view of key financial and risk indicators. The Bank Steering Committee also looks at market risk positions that serve the Bank's strategic goals. In order to ensure that all material risks affecting HSH Nordbank are monitored and managed and to ensure the Bank's risk-bearing capacity at all times based on its risk tolerance level, the Bank Steering Committee also looks at reports and analyses on the individual types of risk, the results of stress tests and the methodological further developments of the risk management models. This means that the Bank Steering Committee prepares decisions on strategic guidelines, the type of management, targets, restrictions and other requirements for the corporate investment portfolio. The corresponding decisions are made by the Overall Management Board. The risk limits passed by the Management Board are monitored by the entities



with operational responsibility. Scenarios in which risk limits are exceeded are escalated to the Management Board together with recommended courses of action, and the implementation of the measures/resolution of the risk limit breaches is monitored. In addition, the Bank Steering Committee is the body responsible for preparing the decision to transition to/remain in the phases defined in the recovery plan, as well as for convening and appointing the specific members of the teams that prepare for the implementation of the options identified and – insofar as the Management Board has passed a resolution on their implementation – implement them.

The scenario management circle provides key support to the Bank Steering Committee by monitoring the development of market indicators and making decisions on the simulation assumptions and scenarios (of both a macroeconomic and segment-specific nature). The simulation scenarios, their main assumptions and the analysis of the results are presented both to the Bank Steering Committee and to the Overall Management Board.

The Credit Committee (CC) is a body that makes independent decisions at the level of material individual loan transactions that is led by the Head of Credit Risk Management (CRM) and involves the CRO on a case-by-case basis. The CC is responsible, among other things, for the operational management of limited resources, i.e. liquidity, economic and regulatory capital, in particular where overall bank management requires the active control of capital and liquidity requirements relating to lending transactions. In this respect, the CC takes the requirements concerning resource management of the Group defined by the Bank Steering Committee as a basis. The committee also performs an active portfolio management function to achieve ongoing improvements in portfolio quality (profitability, diversification, granularity) and makes individual lending decisions from a credit risk perspective.

The Business Area Management Dialogue (BAMD), chaired by the CFO and with the involvement of the Management Board member responsible for the Market divisions as well as members of selected division heads, regularly monitors the achievement of targets by the divisions with regard to new business, income and costs and discusses other general topics of strategic importance. The analysis is used as a basis for identifying any plan variances and initiating any necessary measures at an early stage, such as the review of income or cost targets.

### Risk reporting and measurement systems

HSH Nordbank maintains a central data storage system, which takes into account supervisory requirements, for the purposes of analysing, monitoring and reporting risks. Risk reporting is generally ensured by means of the management and reporting systems of the Group Risk Management division. The risk management systems ensure effective risk management and are adequate with regard to HSH Nordbank's profile and strategy.

The following key reports are prepared for the overall risk:

- In 2016, the MaRisk Risk Report was the core element of risk reporting to the Management Board and the Risk Committee. It was prepared quarterly and shows HSH Nordbank's overall risk position together with detailed information on the material risk types.
- The HSH Management Report, a holistic finance and risk report on HSH Nordbank's overall situation with respect to the key value drivers, especially income, costs, liquidity, capital and risk, and on the development of the recovery plan indicators, is submitted to the Bank Steering Committee, the Management Board and, as of 2017, also to the Risk Committee (relevant excerpts only). Adherence to the risk limits and risk guidelines that are relevant for economic capital management is monitored with the help of this report. The HSH Management Report is prepared on a monthly basis as a general rule. It is also updated at weekly intervals in respect of selected key figures.

The Management Reporting Policy sets out the management requirements with respect to the structure, content, frequency, deadlines and form of the internal reporting bundled in the HSH Management Report for the purposes of ensuring both BCBS 239 compliance and the sustainability of internal reporting.

Other overall risk reports include the Disclosure Report under Part 8 of the Capital Requirements Regulation (CRR), the Risk Report in the Annual Report. In addition to reports on the overall risk there are reporting tools based on the risk type, which are described in the following chapters.

### Internal control system

#### Bank-wide internal control system

The Management Board of HSH Nordbank bears the overall responsibility for ensuring that a proper business organisation is in place at the HSH Nordbank Group, including an appropriate and effective internal control system (ICS).

The ICS of HSH Nordbank is based on a bank-wide main and sub-process structure (process map), which also includes the domestic and foreign branches. A person responsible for the process is designated for all main processes. Furthermore, an ICS cycle is implemented, which is to be run regularly with the following steps:

- classification of (sub-)processes in accordance with inherent risk;
- updating/collecting of the process, risk and control documentation;
- conceptual assessment of the appropriateness of the controls;
- assessment and review of the effectiveness of the controls (testing of controls);
- determination and implementation of measures to be taken with regard to the need for improvement identified in the controls;

- re-assessment and second review of the effectiveness of the control(s) after implementation of the measures (re-testing).

The top priority of this ICS assessment is the structured and systematic examination of potential and/or known process risks together with the definition of and the decision on measures to be taken to mitigate them. Furthermore, the ICS makes a significant contribution to the effectiveness of the processes by specifying uniform rules that apply throughout the Bank. The ICS cycle also ensures that the ICS is continuously enhanced with respect to its correctness, appropriateness and effectiveness. Central responsibility for the management and monitoring of the ICS cycle as well as methodological requirements and their enhancement lies with the ICS Office within the “Methods & Tools” organisational unit.

Corresponding roles and responsibilities are defined within the ICS cycle to ensure that the tasks are performed in a proper manner. The ICS Office is responsible for the steps to be taken in connection with the control cycle. It performs a process-independent quality assurance in particular of the testing on a random basis and centrally defines the ICS methodology to be used. The ICS Office also ensures proper reporting to the Management Board and Supervisory Board.

In order to ensure that the system is functioning on a sustained basis, the process is closely monitored by means of continuous communication and governance throughout the Bank.

The sub-processes of the Bank are defined annually for running the control cycle based on the risk level established and the last cycle run for each process. Approximately 45 % of the sub-processes were scheduled for a run of the control cycle in 2016. The need for improvement identified in respect of these sub-processes was implemented in full. The ICS office also reports to the Management Board on an annual basis on the management of the ICS for the outsourcing of material functions.

Furthermore, subsidiaries of HSH Nordbank are classified annually as to the materiality of their respective processes for the Bank's ICS. The processes of all subsidiaries classified as material are integrated into ICS management processes of the Bank.

#### **Internal control system with regard to the accounting process**

The Finance division is responsible for the process of preparing the consolidated and single-entity financial statements and the correctness of the Group accounting methods. The internal control system for the accounting process should ensure compliance with the rules to be applied and the generally accepted accounting principles. This should maintain a quality standard that ensures a true and fair view of net assets, financial condition and earnings situation. The written rules including all internal instructions and regulations form the essential basis of the ICS.

The accounting process is reviewed on a regular basis by the responsible member of staff in charge of the process and adjusted to the current framework conditions and requirements. The focus is on the identification of material risks and the implementation of measures to prevent these. In addition the accounting process is audited by the Internal Audit division from a process-independent perspective.

The organisational structure of the Finance division supports the internal control system. A comprehensive quality assurance by another organisational unit is performed for the functions responsible for the accounting of lending transactions and capital market transactions in Germany and the transactions in subsidiaries and foreign branches. Amongst other things, it is the responsibility of this organisational unit to combine the accounting information and to prepare the annual and consolidated financial statements. In addition this unit centrally monitors amendments to legislation concerning financial statements, in order to ensure uniform application of the law.

#### **Regulatory requirements**

HSH Nordbank determines the amount of regulatory capital backing for default, market and operational risks as well as for risks resulting from credit valuation adjustment (CVA) of OTC derivatives on the basis of the CRR. In this context the so-called IRB Advanced Approach is applied for default risk, for which the supervisory authority has issued the relevant authorisation to the Bank. The Credit Risk Standardized Approach (CRSA) is used for a small part of the portfolio. This means that the Bank takes consistent parameters into account for regulatory reporting (COREP) and internal default risk management purposes. HSH Nordbank determines the amounts allocated to market risk positions in accordance with the predefined or optional standard procedures. HSH Nordbank takes account of operational risk under the standard approach. HSH Nordbank uses the standard method for CVA.

Regulatory figures are set out in the section Net assets and financial position. The requirements that resulted from the further implementation of the Basel III rules in 2016 were implemented within the framework of projects. For example, the implementation of new liquidity ratios (LCR based on Commission Delegated Regulation (EU) 2015/61 and the NSFR) was driven forward in the reporting year. In accordance with the requirements of Part 8 CRR in conjunction with Section 26a (1) Sentence 1 KWG HSH Nordbank publishes material qualitative and quantitative information on equity capital and risks incurred in a separate Disclosure Report. As an institution that uses the IRB Advanced Approach for nearly the whole portfolio, particular requirements apply to HSH Nordbank in this context. The document provides more information than statements made in this Annual Report on the basis of the accounting principles applied, as it provides a comprehensive insight into the regulatory framework and the current risk situation of the Bank based on regulatory figures. The Disclosure Report as at 31 December 2016 is available on our website, [www.hsh-nordbank.de](http://www.hsh-nordbank.de), four weeks following publication of this Annual Report. With its publication HSH Nordbank complies with the

third pillar of the Basel Accord (market discipline). The requirements regarding the disclosure of risk management objectives and policies in accordance with Article 435 (1) CRR and (2)(e) CRR are implemented in this Risk Report.

### Risk-bearing capacity

HSH Nordbank has integrated a capital adequacy process (ICAAP) into its risk management pursuant to MaRisk in order to monitor and safeguard its risk-bearing capacity on a sustained basis. The management of the risk-bearing capacity takes place within the context of equity capital and risk management.

As part of the monitoring of its risk-bearing capacity HSH Nordbank regularly compares the total economic capital required to cover all major quantifiable types of risk (overall risk) to the available amount of economic risk coverage potential and reports it to the supervisory authorities of the Bank. HSH Nordbank analyses its risk-bearing capacity comprehensively on a quarterly basis as well as within the framework of its annual planning process.

The primary management process for our calculation of risk-bearing capacity is a liquidation approach which focuses on protection of creditors (so-called gone concern approach). In addition to equity capital modified for economic purposes, the risk coverage potential takes into account, amongst other things, unrealised gains and losses arising on securities, equity holdings, the lending business and the corresponding hedging transactions (line items) as well as the liabilities. The risk coverage potential has been reduced by the second loss guarantee by the amount retained by HSH Nordbank of € 3.2 billion.

As at 31 December 2016, the risk coverage potential amounted to € 8.5 billion (31 December 2015: € 10.2 billion). The drop of € 1.7 billion is largely due to the maturities of subordinated capital. The overall risk takes into account default risk, market risk, operational risk as well as the liquidity maturity transformation risk as an element of liquidity risk. Economic capital required as an expression of unexpected losses is determined monthly for default, liquidity and market risks in a methodical consistent manner with a confidence level of 99.9 % and a risk horizon of one year. The economic capital requirements for the individual risk types are aggregated to an overall economic risk. In doing so, no risk-reducing correlations are utilised. Overall economic risk increased by € 0.4 billion compared to the end of 2015 and amounted to € 2.9 billion as at the reporting date (31 December 2015: € 2.5 billion). This year-on-year increase is due, in particular, to the marked increase of € 0.6 billion in the default risk potential (details on the development of the default risk potential can be found under "Default risk management").

The utilisation of risk coverage potential amounted to 34 % as at the reporting date (31 December 2015: 25 %). The risk-bearing capacity was secured at all times during the period under review.

The following table shows the economic risk coverage potential of the HSH Nordbank Group, the economic capital required for the individual risk types, the remaining risk coverage potential buffer and the utilisation of risk coverage potential.

### RISK-BEARING CAPACITY OF THE GROUP

(€ bn)	31.12.2016	31.12.2015
<b>Economic risk coverage potential<sup>1)</sup></b>	<b>8.5</b>	<b>10.2</b>
<b>Economic capital required</b>	<b>2.9</b>	<b>2.5</b>
of which for default risks <sup>2)</sup>	1.9	1.3
for market risks	0.6	0.8
for liquidity risks	0.1	0.2
for operational risks	0.2	0.2
<b>Risk coverage potential buffer</b>	<b>5.6</b>	<b>7.6</b>
<b>Utilisation of risk coverage potential (in %)</b>	<b>34</b>	<b>25</b>

<sup>1)</sup> After deduction of the amount retained under second loss guarantee of the federal states of Hamburg and Schleswig-Holstein in the amount of € 3.2 billion.

<sup>2)</sup> Taking the second loss guarantee into account.



As part of the regular review of the Strategic Risk Framework and the bank planning process, the risk appetite is derived on the basis of the risk coverage potential, keeping a capital buffer available. The latter is to be set in a way that ensures capital adequacy, also in stress scenarios.

### Stress tests

In addition to stress tests specific to risk types, we regularly conduct stress tests across all risk types in order to be able to better estimate the effects of potential crises on key parameters such as utilisation of the risk-bearing capacity, regulatory capital ratios and liquidity and thus HSH Nordbank's overall risk position. Within the scenario management circle, resolutions are passed on simulation assumptions on a regular basis if corresponding market developments are observed. These result in simulation scenarios on which resolutions are passed by the Bank Steering Committee and the Overall Management Board. Both integrated macroeconomic scenarios, such as a severe economic downturn, a delayed recovery of the shipping markets as well as historical scenarios are calculated in this connection. Furthermore, the risk of excessive debt is analysed in the form of a stressed leverage ratio and reported. The results are incorporated in HSH Nordbank's internal reporting system every quarter and are analysed on a regular basis by the Management Board within the framework of an action-oriented management dialogue. Besides the review of the appropriateness of the buffer available for risk coverage potential, regulatory capital and liquidity maintained to offset stress effects, this analysis serves to discuss the need for options to strengthen the financial stability of HSH Nordbank.

HSH Nordbank's recovery plan under the Act on the Recovery and Resolution of Credit Institutions (*Sanierungs- und Abwicklungsgesetz, SAG*) has a comparable objective. It serves both the purpose of the early identification of any resource bottlenecks using appropriate indicators and their elimination in crisis situations by means of pre-defined options. The effectiveness of the options identified, the selected recovery plan indicators and related processes are reviewed in the recovery plan by means of specific stress scenarios. As at 31 December 2016, HSH Nordbank is in the early warning phase of the recovery plan.

The particular purpose of both processes is to ensure that the Bank is able to comply with the regulatory minimum requirements even under stress conditions. In addition, HSH Nordbank carries out inverse stress tests at least once a year to identify scenarios which could endanger HSH Nordbank's ability to survive. The potential impact of the persistent low interest rate environment is also analysed. This information is also used by HSH Nordbank's Management Board as additional guidance for explaining and deciding upon the action required for reviewing the sustainability of the business model in the event of developments that threaten the Bank's existence.

In addition to stress tests across all risk types HSH Nordbank established procedures for the early identification of negative developments

at the level of individual risk types, which are discussed in the following sections.

### DEFAULT RISK

HSH Nordbank breaks down its default risk into credit, settlement, country and equity holding risk.

In addition to the traditional credit risk, credit risk also includes counterparty and issuer risk. The conventional credit risk is the risk of complete or partial loss in the lending business as a result of deterioration in the counterparty's credit standing. A counterparty default risk exists in the case of derivatives and refers to the risk that a counterparty defaults during the term of a transaction and HSH Nordbank must cover the shortfall for the residual term by means of a new contract on the market at the price prevailing at that time which might be less favourable. Issuer risk denotes the risk that a loss is incurred on a financial transaction as a result of the default or deterioration in the creditworthiness of the issuer.

Settlement risk consists of clearing risk and advance performance risk. Clearing risk arises in the case of possible loss of value if delivery or acceptance claims pertaining to a transaction that is already due, have not been met by both parties. Advance performance risk arises where HSH Nordbank has performed its contractual obligations but consideration from the contracting party is still outstanding.

HSH Nordbank understands country risk as the risk that agreed payments are not made or only made in part or delayed due to government-imposed restrictions on cross-border payments (transfer risk). The risk is not related to the debtor's credit rating.

The equity holding risk is the danger of financial loss due to the impairment of equity holdings.

All elements of default risk referred to are taken into account within the context of equity capital management. For risk concentrations and equity holding risks additional management measures are in place.

### Organisation of default risk management

The organisational structure of HSH Nordbank reflects the functional separation of duties between market and back office departments and/or risk controlling, also at Management Board level.

Credit Risk Management is responsible for the risk analysis for the lending business including the preparation and setting of the internal rating and drafting of the credit applications. Furthermore, the organisation of the bodies of rules for the lending business, including the related processes, is the responsibility of Credit Risk Management. The Loan Collateral Management division is responsible for the settlement of new lending business, the administration of the existing portfolio as well as the valuation and monitoring of collateral. The Special Credit Management business unit is responsible for managing restructuring and workout cases and the associated operational re-

structuring activities. As soon as a loan exposure is classified as a restructuring case, it is handed over by the market department in question to Special Credit Management and to the corresponding restructuring analysis team within Credit Risk Management. The workout loan exposures are processed in the restructuring analysis teams within Credit Risk Management in close collaboration with the manager from Special Credit Management. Lending decisions for normal and intensive management loan exposures are made jointly by the market department in question and the back office, while lending decisions on restructuring and workout loans are made jointly by Special Credit Management and Credit Risk Management. A decision against the recommendation made by the back office entity Credit Risk Management is excluded in each case.

Loan loss provision management falls within the remit of Credit Risk Management.

HSH Nordbank makes use of the option to dispense with the involvement of the back office departments within the meaning of the MaRisk opening clause for lending transactions in certain types of business and below certain amounts classified as not material in terms of risk.

The trading lines for counterparty and issuer risk are set and monitored by the Group Risk Management division. As part of the trading line monitoring the so-called potential future exposure on currency and interest rate derivatives is recalculated daily for each client on the basis of a 95 % quantile and compared to the respective trading limit. The Group Risk Management division is also responsible for the independent analysis and monitoring of risks at the portfolio level, independent reporting and the management of country risk. This includes ensuring portfolio transparency and independent business area analysis (including scenario simulations) and the operation of an early warning system at individual transaction level for identifying loan exposures on a timely basis that are beginning to show signs of increased risk.

The principles and regulations contained in the Credit Manual of HSH Nordbank, in particular on lending competencies (definition of decision-making powers for credit decisions made by the Bank and definition of decision-making powers for entering into, changing and terminating participations), on limiting and reporting the concentration of counterparty default risks, on the determination of the rating, on the treatment of collateral, loan monitoring and commitment monitoring, form the basis for the operating activities within the lending business. Thereby, credit risks, recognised based on the definition of a loan under Article 389 of the Capital Requirements Regulation (CRR), are considered and treated differently based on collateral, loan type, rating category and type of credit risk. The basis is HSH Nordbank Group's aggregate exposure per group of connected clients (GCC) in accordance with Article 4 (1) no. 39 CRR, whereby the bearer of the economic risk is always to be regarded as the relevant borrower.

The Bank has defined valuable collateral in order to differentiate between collateralised and non-collateralised loans. The focus is placed on meeting the requirements of the CRR (e.g. availability of a market value, ability to realise the collateral, no correlation to the collateralised loan, legal enforceability, and maturity match). The range of approved collateral can be expanded following an assessment carried out by a team independent of the market divisions consisting of specialists from the Credit Risk Management, Group Risk Management and Legal & Taxes divisions.

Credit risk management for single risks is supplemented in particular by instructions on loan monitoring and early identification of risks.

#### Default risk management

In line with the HSH Nordbank's business strategy focus as a "Bank for Entrepreneurs" with lending as its anchor product, default risks account for the lion's share of the Bank's overall risk potential. In order to measure and manage these risks, Group Risk Management uses procedures and methods that are continually reviewed and enhanced to ensure they are appropriate.

Key default risk parameters are the expected and unexpected loss. The expected loss is equivalent to the default which is expected within one year on a given probability of default (PD), loss given default (LGD) and exposure at default (EaD) for a borrower. The EaD is the expected loan amount outstanding taking into account a potential (partial) drawdown of commitments and contingent liabilities, that will adversely impact the risk-bearing capacity in the event of a default. The maximum amount, by which an actual loss can exceed the expected loss with a specified probability (99.9 %) within a specified time period (one year) is described as the unexpected loss. PD, LGD and EaD are also relevant risk parameters in this context. Economic capital required is determined for internal steering purposes on the basis of the calculation of the equity capital backing in accordance with CRR taking due account of any adjustments that are justified on economic grounds. In addition, institution-specific asset correlations and granularity surcharges for covering existing risk concentrations are taken into account in determining the economic capital required for default risks.

As a result of the adverse developments on the shipping market, economic capital required for default risk increased significantly from € 1.3 billion to € 1.9 billion as at the reporting date after taking account of the second loss guarantee made available by the federal states of Hamburg and Schleswig-Holstein. The increase in the economic capital required for default risk results in the second loss guarantee facility being exceeded by € 0.9 billion in the reporting period. This part of the default risk that is no longer covered by the federal state guarantee results in an increase in the risk exposure.

Non-performing exposure (NPE), i.e. the total of all positions of borrowers in default, serves as an important management indicator that has also been defined as a risk guideline in the SRF. Information

on the non-performing portfolio is shown in the table “Default risk structure by rating category”. In addition, the coverage ratio (ratio of total loan loss provisions on the non-performing exposure to the total non-performing exposure) is monitored at overall bank level as a MaSan indicator. In accordance with the decision made by the EU Commission on 2 May 2016, HSH Nordbank is to be relieved of some of its troubled legacy portfolios. In line with the EU decision, for example, non-performing loans in an initial amount of € 5 billion were sold to the federal state owners based on market prices. The EU decision provides for the sale of additional portfolios on the market, with contractual agreements already being reached for a large part of these portfolios at the start of 2017. Progress has also been made with regard to the organic winding down of legacy portfolios. The loans in default were reduced considerably from € 18.4 billion to € 14.6 billion despite a counter-trend resulting from defaults on further shipping financing arrangements, and will drop further as a result of the sale of the market portfolios, which in turn will lead to a continued general improvement of HSH Nordbank’s non-performing exposure (NPE) ratio at Group level.

The syndication of lending transactions is also helping to actively shape the composition of the portfolio. In order to maintain the greatest possible degree of flexibility with regard to being able to sell financing arrangements again, either in full or in part, the Bank subjects all potential new business as of a certain volume limit to a market conformity assessment and a syndication assessment performed by the credit syndicate within the Credit Solutions department as part of the Credit Committee Pre-Check (CCPC). The CCPC/Credit Risk Management then makes a joint decision together with the credit syndicate and the deal team sales employees as to whether syndication should be arranged as part of the new business process. The existing portfolio is also reviewed for saleability on a quarterly basis as part of the MaSan procedure (and on an ad hoc basis where appropriate).

#### **Rating procedures, LGD and CCF**

HSH Nordbank collaborates intensively with other banks in the further development and ongoing validation of various internal rating modules. This is done in the association of Landesbanks via RSU Rating Service Unit GmbH & Co. KG (RSU) and in cooperation with Sparkassen Rating und Risikosysteme GmbH (SR), a subsidiary of the German Savings Bank Association (DSGV).

HSH Nordbank uses rating modules for banks, corporates, international sub-sovereigns, country and transfer risk, insurance companies, leveraged finance, Sparkassen StandardRating and leasing as well as for special financing for ships, real estate, projects and aircraft. These also use qualitative in addition to quantitative characteristics in determining the rating. The result is a probability at default (PD) for each borrower and hence an allocation to a concrete rating category. The Bank uses an identical rating master scale for all modules which not only allows comparison of differing portfolio segments but also mapping with external ratings.

In order to determine the expected drawdown for continent liabilities and commitments in case of possible default, so-called credit conversion factors (CCF) are calculated empirically and applied. The loan amount outstanding weighted by CCF is described as EaD.

HSH Nordbank uses a differentiated LGD methodology to forecast loss given default (LGD). Collateral-specific recovery rates and borrower-specific recovery rates are estimated based on historic loss information. The respective default amount expected is determined from the EaD using the LGD.

As part of the annual validation process the predictive accuracy of the rating modules was reviewed in the reporting year with regard to the predicted probabilities of default using anonymous, aggregated data. In addition, the LGD and CCF processes were also validated and are being continually refined. All reviews have confirmed the full applicability of the models.

#### **Risk concentrations**

Within the framework of regular business segment analyses potential counterparty default risk concentrations, for example with regard to groups of connected clients (GcC), regions or industrial sectors in a broader sense, are identified and their trend is monitored. At the end of 2016, the material risk concentrations of HSH Nordbank in credit risk were in the real estate portfolio, which accounted for 20% of the overall portfolio (previous year: 19%) and in the shipping portfolio, which accounted for 20% of the overall portfolio (previous year: 24%). Other concentration risks relate to the US dollar business, which accounted for 25% of the overall portfolio (previous year: 30%). The shipping loan portfolios denominated in US dollars are included in both key figures. Despite a drop in the concentration in shipping financing and in financing denominated in USD, the key capital and liquidity figures remain sensitive, albeit less sensitive than before, to developments on the shipping market and in the EUR/USD exchange rate.

An internal process, which ensures adherence to the regulatory requirements, is in place to monitor large exposure limits in accordance with Article 395 CRR. As a supplementary measure, the material counterparty concentrations in the portfolio are identified on the basis of a risk-oriented parameter (risk of loss as the total of expected loss and unexpected loss) and reported quarterly to the Management Board and Risk Committee. Net rating-based upper limits are applied to new business to prevent future counterparty concentrations.

Country risk limitation is an additional management dimension within the management of risk concentrations. Country limits are set for country risk concentrations at the Group level. Utilisation of the limits is monitored continuously and centrally by the country risk management. In the event that a limit is fully utilised the decision regarding each new business transaction rests with the Overall Management Board.



### Equity holding risk

The regulatory authorities state that equity holdings must be consolidated, deducted from equity or backed with equity capital in the receivable class equity holdings. In this context, regulatory law considers equity holding risk to be a sub-category of the default risk. HSH Nordbank has significantly reduced its equity holding portfolio and thereby equity holding risk over recent years, thus successfully bringing it in line with the Bank's strategic realignment. The acquisition of equity holdings only takes place, if it meets the strategic objectives of HSH Nordbank. The risks and rewards associated with a potential equity holding are analysed extensively prior to the conclusion of the transaction.

A regular company valuation represents an important instrument for monitoring and managing equity holding risk. At least once a year, impairment tests are performed on all equity holdings of HSH Nordbank. Important equity holdings are subject to a more detailed analysis in this context.

Furthermore, all equity holdings in the portfolio are analysed once a year, with a focus on the identification of risks in the individual companies, amongst other things. Measures are derived from the analysis in order to be able to actively counter the identified risks.

The articles of association and by-laws are formulated so as to ensure that the most intensive management possible can be exercised for the benefit of HSH Nordbank.

### Management of default risk in pricing and actual costing

HSH Nordbank applies a uniform method across the Bank for the pricing of lending transactions through calculating the present value of the expected and unexpected losses arising on default risk positions. In addition to liquidity and standard processing costs, the rating, LGD and CCF risk parameters determined internally on an individual transaction basis are incorporated in the ex-ante calculation pricing by means of the standard risk costs. In the same way, an actual costing (profit centre accounting) is made for all transactions on a monthly basis, taking the cost elements stated above into account. Based on the current risk parameters of the individual transactions, standard risk costs and the resulting contribution margins are determined. Furthermore, utilisation of the regulatory default limits set as part of the Bank's annual plan were determined regularly at the division level for the purposes of managing default risk. When a limit is overdrawn, new transactions and prolongations are subject to stricter approval requirements. The objective of this dual limit system is to ensure that both the risk-bearing capacity and regulatory ratios are adhered to.

### Default risk exposure

The figures in the following tables showing default risk exposure are based on the EaD. The EaD corresponds to the volume of loan receivables, securities, equity holdings, derivative financial instruments (positive market values after netting) and off-balance-sheet transactions (taking credit conversion factors into account). The EaD does not include any risk-reducing effects (e.g. allocation of collateral). The total EaD amount outstanding was € 83,626 million as at 31 December 2016.

The EaD broken down by internal rating categories is presented in the following table. The EaD with an investment grade rating (rating category 1 to 5) at Group level accounts for € 49,092 million or 59 % of the total exposure (previous year: € 53,927 million or 55 %). The loan amount outstanding for investment grade exposures amounts to € 35,521 million or 69 % (previous year: € 35,043 million or 67 % based on the new segment structure) for the Core Bank and € 3,375 million or 16 % (previous year: € 5,320 million or 17 % based on the new segment structure) for the Non-Core Bank. 34 % of the Overall Bank portfolio is covered by the second loss guarantee (previous year: 42 %). For the Core Bank a share of 20 % is guaranteed (previous year: 25 % based on the new segment structure) and for the Non-Core Bank 85 % (previous year: 88 % based on the new segment structure). At 87 % (previous year: 92 %) the share of the guaranteed portfolio is particularly high in the default categories 16 to 18.

**DEFAULT RISK STRUCTURE BY RATING CATEGORY<sup>1)</sup>**

(€ m)	2016				of which guaranteed (in %)
	Core Bank	Non-Core Bank <sup>3)</sup>	Other and Consolidation <sup>3)</sup>	Total	
1(AAAA) to 1(AA+)	13,684	700	6,726	21,110	17
1(AA) to 1(A-)	6,889	755	2,006	9,650	18
2 to 5	14,948	1,920	1,464	18,332	19
6 to 9	11,270	1,373	66	12,709	27
10 to 12	1,609	569	–	2,178	52
13 to 15	2,296	2,394	69	4,759	60
16 to 18 (default category)	1,006	13,610	–	14,616	87
Other <sup>2)</sup>	–	87	186	273	–
<b>Total</b>	<b>51,703</b>	<b>21,406</b>	<b>10,517</b>	<b>83,626</b>	<b>34</b>

<sup>1)</sup> Mean default probabilities (as %): 1 (AAAA) to 1 (AA+): 0.00–0.02; 1 (AA) to 1 (A-): 0.03–0.09; 2 to 5: 0.12–0.39; 6 to 9: 0.59–1.98; 10 to 12: 2.96–6.67; 13 to 15: 10.00–20.00; 16 to 18: 100.00.

<sup>2)</sup> Transactions, for which there is no internal or external rating available, are reflected in the “Other” line item, such as receivables from third parties of our consolidated equity holdings, for example

<sup>3)</sup> Following the changes made to the segment structure as at 30 September 2016, the figures reported for the prior year have been adjusted accordingly.

**DEFAULT RISK STRUCTURE BY RATING CATEGORY<sup>1)</sup>**

(€ m)	2015				of which guaranteed (in %)
	Core Bank <sup>3)</sup>	Non-Core Bank <sup>3)</sup>	Other and Consolidation <sup>3)</sup>	Total	
1(AAAA) to 1(AA+)	12,226	1,687	9,157	23,069	19
1(AA) to 1(A-)	6,113	1,229	2,793	10,135	29
2 to 5	16,704	2,404	1,614	20,722	23
6 to 9	13,692	3,403	29	17,124	38
10 to 12	1,736	1,675	–	3,412	66
13 to 15	847	3,905	87	4,839	75
16 to 18 (default category)	1,090	17,319	–	18,408	92
Other <sup>2)</sup>	1	120	207	328	–
<b>Total</b>	<b>52,409</b>	<b>31,742</b>	<b>13,886</b>	<b>98,037</b>	<b>42</b>

<sup>1)</sup> Mean default probabilities (as %): 1 (AAAA) to 1 (AA+): 0.00–0.02; 1 (AA) to 1 (A-): 0.03–0.09; 2 to 5: 0.12–0.39; 6 to 9: 0.59–1.98; 10 to 12: 2.96–6.67; 13 to 15: 10.00–20.00; 16 to 18: 100.00.

<sup>2)</sup> Transactions, for which there is no internal or external rating available, are reflected in the “Other” line item, such as receivables from third parties of our consolidated equity holdings, for example.

<sup>3)</sup> Following the changes made to the segment structure as at 30 September 2016, the figures reported for the prior year have been adjusted accordingly.

The EaD broken down by sectors important for HSH Nordbank is presented in the following table.

#### DEFAULT RISK STRUCTURE BY SECTOR

(€ m)	2016			Total
	Core Bank	Non-Core Bank <sup>1)</sup>	Other and Consolidation <sup>1)</sup>	
Industry	7,709	1,682	–	9,391
Shipping	6,542	9,555	42	16,139
Trade and transportation	3,428	851	–	4,279
Credit institutions	3,301	591	3,946	7,838
Other financial institutions	1,849	2,120	531	4,500
Land and buildings	10,343	3,832	29	14,204
Other services	5,377	1,121	942	7,440
Public sector	12,796	1,172	5,005	18,973
Private households	357	483	22	862
Other	–	–	–	–
<b>Total</b>	<b>51,703</b>	<b>21,406</b>	<b>10,517</b>	<b>83,626</b>

<sup>1)</sup> Following the changes made to the segment structure as at 30 September 2016, the figures reported for the prior year have been adjusted accordingly.

#### DEFAULT RISK STRUCTURE BY SECTOR

(€ m)	2015			Total
	Core Bank <sup>1)</sup>	Non-Core Bank <sup>1)</sup>	Other and Consolidation <sup>1)</sup>	
Industry	7,561	2,325	–	9,886
Shipping	7,914	14,905	–	22,819
Trade and transportation	3,283	1,228	–	4,511
Credit institutions	4,055	724	4,333	9,112
Other financial institutions	1,897	3,461	1,032	6,390
Land and buildings	10,212	4,881	–	15,092
Other services	5,276	1,538	1,051	7,866
Public sector	11,734	2,101	7,457	21,292
Private households	477	579	13	1,069
Other	–	–	–	–
<b>Total</b>	<b>52,409</b>	<b>31,742</b>	<b>13,886</b>	<b>98,037</b>

<sup>1)</sup> Following the changes made to the segment structure as at 30 September 2016, the figures reported for the prior year have been adjusted accordingly.



The following table shows the EaD broken down by residual maturities:

#### DEFAULT RISK STRUCTURE BY RESIDUAL MATURITIES

(€ m)	2016			Total
	Core Bank	Non-Core Bank <sup>1)</sup>	Other and Consolidation <sup>1)</sup>	
Up to 3 months	7,474	4,189	829	12,493
> 3 months to 6 months	2,227	836	311	3,374
> 6 months to 1 year	3,384	998	572	4,954
> 1 year to 5 years	22,660	8,545	6,436	37,641
> 5 years to 10 years	9,696	3,410	1,989	15,095
> 10 years	6,262	3,429	379	10,070
Other	-	-	-	-
<b>Total</b>	<b>51,703</b>	<b>21,406</b>	<b>10,517</b>	<b>83,626</b>

<sup>1)</sup> Following the changes made to the segment structure as at 30 September 2016, the figures reported for the prior year have been adjusted accordingly.

#### DEFAULT RISK STRUCTURE BY RESIDUAL MATURITIES

(€ m)	2015			Total
	Core Bank <sup>1)</sup>	Non-Core Bank <sup>1)</sup>	Other and Consolidation <sup>1)</sup>	
Up to 3 months	7,220	5,058	458	12,735
> 3 months to 6 months	1,573	873	345	2,792
> 6 months to 1 year	2,548	1,626	568	4,743
> 1 year to 5 years	23,254	12,759	8,421	44,434
> 5 years to 10 years	11,238	7,536	3,632	22,406
> 10 years	6,576	3,890	462	10,927
<b>Total</b>	<b>52,409</b>	<b>31,742</b>	<b>13,886</b>	<b>98,037</b>

<sup>1)</sup> Following the changes made to the segment structure as at 30 September 2016, the figures reported for the prior year have been adjusted accordingly.

The following table provides an overview of the foreign exposure by region, which reached € 33,617 million as at 31 December 2016 (previous year: € 39,650 million).

#### FOREIGN EXPOSURE BY REGION

(€ m)	2016			Total
	Core Bank	Non-Core Bank <sup>1)</sup>	Other and Consolidation <sup>1)</sup>	
Western Europe	10,808	8,907	3,146	22,861
thereof: eurozone countries	8,280	5,441	1,214	14,935
Central and Eastern Europe	550	582	–	1,132
thereof: eurozone countries	51	2	–	53
Africa	568	253	–	821
North America	1,302	1,770	52	3,124
Latin America	298	288	–	586
Middle East	44	650	–	694
Asia-Pacific region	1,307	2,399	1	3,707
International organisations	94	–	598	692
<b>Total</b>	<b>14,971</b>	<b>14,849</b>	<b>3,797</b>	<b>33,617</b>

<sup>1)</sup> Following the changes made to the segment structure as at 30 September 2016, the figures reported for the prior year have been adjusted accordingly.

#### FOREIGN EXPOSURE BY REGION

(€ m)	2015			Total
	Core Bank	Non-Core Bank <sup>1)</sup>	Other and Consolidation <sup>1)</sup>	
Western Europe	10,219	10,783	3,906	24,907
thereof: eurozone countries	7,697	6,595	1,553	15,845
Central and Eastern Europe	444	928	–	1,371
thereof: eurozone countries	52	42	–	94
Africa	755	461	–	1,215
North America	1,828	2,725	41	4,595
Latin America	498	588	–	1,086
Middle East	46	809	–	856
Asia-Pacific region	1,740	3,037	–	4,777
International organisations	149	–	694	843
<b>Total</b>	<b>15,679</b>	<b>19,331</b>	<b>4,641</b>	<b>39,650</b>

<sup>1)</sup> Following the changes made to the segment structure as at 30 September 2016, the figures reported for the prior year have been adjusted accordingly.

The basis for the allocation of the transactions to the regions is the country of the customer relevant for transfer risk taking account of any collateral relevant for the transfer risk. At customer level, the country relevant for transfer risk is the country from where HSH Nordbank receives the cash flows. If this cannot be unambiguously assigned at customer level, the place of business where management is exercised is applied.

Due to their unfavourable fiscal and economic data, a number of European countries are subject to increased monitoring. These include in particular Croatia, Cyprus, Greece, Italy, Portugal and Spain. The exposure to Russia is also being monitored more closely as a result of the tense economic situation and the EU sanctions, as is the exposure to Turkey due to Turkey's interior and geopolitical development.

The following table shows the EaD of the exposures in the European countries stated. HSH Nordbank's total exposure to these countries has decreased by 4 % compared to the previous year and amounted to

€ 5,925 million in total as at 31 December 2016 (previous year: € 6,180 million).

**EXPOSURE AT DEFAULT IN SELECTED EUROPEAN COUNTRIES**

(€ m)	Country		Banks		Corporates/Other		Total	
	2016	2015	2016	2015	2016	2015	2016	2015
Greece	-	-	-	-	1,478	1,163	1,478	1,163
Italy	425	445	-	-	602	639	1,027	1,084
Croatia	-	-	-	-	101	106	101	106
Portugal	219	223	-	4	26	29	245	256
Russia	-	-	3	4	74	135	77	139
Spain	151	156	46	58	1,215	1,328	1,412	1,542
Turkey	-	-	31	22	379	473	410	495
Cyprus	-	-	-	-	1,175	1,395	1,175	1,395
<b>Total</b>	<b>795</b>	<b>824</b>	<b>80</b>	<b>88</b>	<b>5,050</b>	<b>5,268</b>	<b>5,925</b>	<b>6,180</b>

The direct country exposure continues to be manageable. The loan exposures in the Corporates/Other sector for Greece, Turkey and Cyprus relate primarily to ship financings, which do not entail transfer risk due to the existing collateral.

Note 57 includes more information on the selected European countries.

**Loan loss provisions**

Within the framework of risk management, HSH Nordbank pays the most attention to default risk. Impairments of a loan exposure are shielded through the creation of specific loan loss provisions for loans and advances and provisions for contingent liabilities in the amount of the potential loss in accordance with Group-wide standards. HSH Nordbank also recognises general loan loss provisions for latent default risks, which have already occurred but the amount of which is not yet known to the Bank as at the balance sheet date.

All restructuring and workout loan exposures, as well as intensified loan management cases with a rating greater or equal to 13, are subject to a comprehensive two-step review process every quarter. In a first step, a review is carried out on the basis of objective criteria (so-called trigger events) to determine whether the receivable could be impaired (impairment identification). If this is the case, the loans identified are reviewed in a second step to determine whether a loan loss provision is actually required and the amount thereof (impairment measurement). The amount of the loan loss provision is calculated by deducting the present value of all expected future incoming payments from the IFRS carrying amount of the receivable. The expected incoming payments comprise in particular all expected interest and redemption payments, as well as payments from the liquidation of collateral.



The following tables show the loan loss provision trend by segment:

### CHANGES IN LOAN LOSS PROVISIONS

(€ m)	01.01. – 31.12.2016							
	Specific loan loss provisions	General loan loss provisions	Loan loss provisions before currency translation and compensation	Net income from foreign currency from loan loss provisions	Compensation item	Total	Hedging effect of credit derivative second loss guarantee	LLP incl. hedging effect credit derivative
Corporates	39	1	40	0	-45	-5	0	-5
Shipping	-92	63	-29	-8	89	52	0	52
Real Estate Clients	1	0	1	0	-1	-	0	-
Treasury & Markets	0	0	-	0	0	-	0	-
<b>Total Core Bank</b>	<b>-52</b>	<b>64</b>	<b>12</b>	<b>-8</b>	<b>43</b>	<b>47</b>	<b>0</b>	<b>47</b>
Non-Core Bank <sup>1)</sup>	-1,776	182	-1,594	-66	2,241	581	-475	106
<b>Other and Consolidation<sup>1)</sup></b>	<b>4</b>	<b>1</b>	<b>5</b>	<b>-2</b>	<b>0</b>	<b>3</b>	<b>0</b>	<b>3</b>
<b>Group</b>	<b>-1,824</b>	<b>247</b>	<b>-1,577</b>	<b>-76</b>	<b>2,284</b>	<b>631</b>	<b>-475</b>	<b>156</b>

<sup>1)</sup> Following the changes made to the segment structure as at 30 September 2016, the figures reported for the prior year have been adjusted accordingly.

### CHANGES IN LOAN LOSS PROVISIONS<sup>1)</sup>

(€ m)	01.01. – 31.12.2015							
	Specific loan loss provisions	General loan loss provisions	Loan loss provisions before currency translation and compensation	Net income from foreign currency from loan loss provisions	Compensation item	Total	Hedging effect of credit derivative second loss guarantee	LLP incl. hedging effect credit derivative
Corporates	51	5	56	0	-66	-10	0	-10
Shipping	-25	-181	-206	-137	174	-169	0	-169
Real Estate Clients	0	0	-	0	11	11	0	11
Treasury & Markets	0	0	-	0	0	-	0	-
<b>Total Core Bank</b>	<b>26</b>	<b>-176</b>	<b>-150</b>	<b>-137</b>	<b>119</b>	<b>-168</b>	<b>-</b>	<b>-168</b>
Non-Core Bank <sup>1)</sup>	-2,794	-75	-2,869	-311	2,958	-222	658	436
<b>Other and Consolidation<sup>1)</sup></b>	<b>-1</b>	<b>-</b>	<b>-1</b>	<b>37</b>	<b>-</b>	<b>36</b>	<b>-</b>	<b>36</b>
<b>Group</b>	<b>-2,769</b>	<b>-251</b>	<b>-3,020</b>	<b>-411</b>	<b>3,077</b>	<b>-354</b>	<b>658</b>	<b>304</b>

<sup>1)</sup> Following the changes made to the segment structure as at 30 September 2016, the figures reported for the prior year have been adjusted accordingly.

Loan loss provisions were once again characterised by considerable additions of around € 1.8 billion in the shipping portfolio in the reporting year. The additional loan loss provision expense for legacy shipping portfolios was required in order to take account of the very difficult market developments, which were evident from the dramatic slump in charter rates and ship values, in particular. In the reporting period, they were attributable primarily to loans for bulkers and container vessels. In the Corporate Clients and Real Estate segments, on the other hand, risk developments remained unremarkable.

All in all, total loan loss provisions before compensation under the guarantee came to € -1,577 million as at 31 December 2016 (previous year: € -3,020 million). In the previous year, the loan loss provisions had been shaped primarily by the implementation of the EU decision. Within this context, € -1,584 million in additional loan loss provisions were set up for the federal state transaction portfolios alone in the previous year.

The loan loss provisions set up again for legacy portfolios, in particular, in the reporting year were still compensated for by the guarantee to the extent that they related to portfolios hedged by the guarantee.

The compensation provided by the second loss guarantee for the guaranteed portfolio, which is reported within the loan loss provisions, came to € 2,208 million after adjustments to reflect exchange rate effects (previous year: € 2,666 million). Taking the ongoing loan loss provision expenses into account, this produces loan loss provisions, in particular following the compensation provided by the second loss guarantee, totalling € 631 million (previous year: € -354 million). Allowing for the hedging effect resulting from the credit derivative in the amount of € -475 million (previous year: € 658 million), the loan loss provisions after the impact of the guarantee would come to a total of € 156 million (previous year: € 304 million).

The loan loss provision result is influenced positively by the results of the loss settlements via the compensation provided by the second loss guarantee. In connection with the settlement of losses under the guarantee with HSH Finanzfonds AöR, the Bank was able to compensate not only for credit losses incurred, but also for interest payments lost in the past.

The hedging effect of the guarantee resulted in a cash draw down of the guarantee for the first time in the reporting year, also taking into account the transfer of non-performing shipping loans to the federal state owners. The Bank's first loss piece (€ 3.2 billion) had been exceeded on the balance sheet date by € 2.3 billion due to losses, particularly also in connection with the settlement of losses from the federal state transaction. The balance sheet drawdown under the second loss guarantee amounts to € 9.9 billion (including guarantee payments already received in the amount of € 1.9 billion) as at 31 December 2016 (31 December 2015: € 8.1 billion). The 2017 plan year is expected to bring the full balance sheet and regulatory utilisation of the guarantee facility, and the full drawdown of the guarantee by way of full settlement is expected by 2022.

Detailed information on the development of loan loss provisions in the individual divisions is set out in the Segment reporting section.

The loss rate in the Group amounted to 3.63 % in the reporting year (previous year: 1.35%). The loss rate is calculated based on the actually realised defaults as a ratio of the credit risk exposure. The total amount of actually realised defaults in 2016 was € 3,046 million (previous year: € 1,136 million) and the credit risk exposure € 83,969 million (previous year: € 97,554 million). The credit risk exposure includes all balance sheet and off-balance sheet assets, taking account of the specific and general loan loss provisions for loans and advances to customers and banks that are subject to default risk.

The individual elements of loan loss provisions are shown in the table below:

#### TOTAL LOAN LOSS PROVISIONS

(€ m)	2016	2015
Loans and advances to customers	50,910	56,575
Loans and advances to banks	4,192	5,595
Volume of impaired loans	10,541	15,766
Non-current assets held for sale and discontinued operations (IFRS 5)	1,382	5,082
Specific loan loss provisions for loans and advances to customers	- 6,336	- 7,601
General loan loss provisions for loans and advances to customers	- 375	- 611
Specific loan loss provisions for loans and advances to banks	-	- 14
General loan loss provisions for loans and advances to banks	- 1	- 1
<b>Total loan loss provisions for balance sheet items</b>	<b>- 6,712</b>	<b>- 8,227</b>
Provisions for individual risks in the lending business	- 67	- 57
Provisions for portfolio risks in the lending business	- 43	- 50
<b>Total loan loss provisions for off-balance sheet items</b>	<b>- 110</b>	<b>- 107</b>
<b>Total loan loss provisions (before compensation item)</b>	<b>- 6,822</b>	<b>- 8,334</b>
Compensation item	7,854	7,162
<b>Total loan loss provisions (including compensation item)</b>	<b>1,032</b>	<b>- 1,172</b>

Total loan loss provisions within the Group, following the compensation by the second loss guarantee, came to € 1,032 million as at 31 December 2016 (previous year: € -1,172 million). The compensation item, which exceeds the loan loss provisions, can be attributed to the fact that the compensation item also includes the hedging effect for other transactions covered by the guarantee (e.g. securities). In such cases, corresponding impairments are recognised with an offsetting effect not in loan loss provisions, but in other items of the income statement (e.g. net income from financial investments).

The specific loan loss provisions comprise the specific loan loss provisions for loans and advances to banks of € -6,336 million (previous year: € -7,615 million), the specific loan loss provisions for contingent liabilities and irrevocable loan commitments totalling € -65 million (previous year: € -55 million) and the specific loan loss provisions for other off-balance sheet transactions of € -2 million (previous year: € -2 million) and totalled € -6,403 million (previous year: € -7,672 million).

The general loan loss provisions totalled € -419 million (previous year: € -662 million) and comprise general loan loss provisions for loans and advances to customers and banks of € -376 million (previous year: € -612 million) and € -43 million (previous year: € -50 million) for contingent liabilities and irrevocable loan commitments.

Details regarding the total loan loss provisions are presented in Notes 15, 27 and 43.

### Planning for loan loss provisions and losses

Loan loss provisions are planned as part of the annual Bank plan under the plan assumptions specified therein. The planning includes the annual changes in the amounts of the specific and general loan loss provisions, broken down by the amounts covered by and not covered by the second loss guarantee and including new business. Other components of the plan are the change in the utilisation of the second loss guarantee as well as the actual losses invoiced and the total loss to be expected from the second loss guarantee.

In planning additions to as well as utilisations and reversals of loan loss provision HSH Nordbank mainly relies on models that simulate the expected loss at the individual transaction level over the planning period based on parameters specific to the transaction. Scenario analyses based on cash flows and historical data regarding changes in loan loss provisions based on the expected loss or migrations from general loan loss provisions to specific loan loss provisions are also taken into account.

The effects arising from the sale, an agreement on which was signed in January 2017, of parts of the portfolios to be sold on the market in accordance with the EU decision (largely real estate, aviation and energy) have been taken into account for 2017, assuming the extensive settlement of the resulting losses against the guarantee. Further information on the EU state aid proceedings is set out in the Forecast, opportunities and risks report section.

In addition to the amount of the specific loan loss provisions as described above that is recognised on the guaranteed portfolio less any individually retained amounts the plan for the guarantee utilisation (without effects from premiums) includes the actual losses invoiced under the second loss guarantee as well as amounts utilised in the past but not yet invoiced (less individually retained amounts), impairment losses on securities (less individually retained amounts) as well as any general loan loss provisions on the guaranteed portfolio.

The payment defaults expected in the portfolio covered by the second loss guarantee will increase further in 2017 and result in further actual payments under the second loss guarantee. Further details on the second loss guarantee can be found in Note 3.

A key driver of the amount of loan loss provisions is the breakdown of impaired loan exposures into “capable of recovery” (and therefore recognition of a specific loan loss provision based on the assumption of the continuation of the borrower’s business) or “not capable of recovery” (and therefore recognition of a specific loan loss provisions based on the assumption of a workout). The estimates concerning long-term loan loss provisions are based on the assumption of a recovery of the shipping markets, in particular a recovery in container shipping, as well as basically a continuation of the current recovery

strategy and therefore the assumption of HSH Nordbank’s willingness on a case by case basis to continue to finance problem loans remaining after the intended transactions, with the aim of achieving the planned write-up potential in the future. Further information on the loan loss provision forecast and uncertainties associated with the long-term loan loss provision plan is set out in the Forecast, opportunities and risks report section.

### Reports on default risk

The Management Board and Risk Committee are regularly informed regarding the risk content and the trend in the individual asset classes and/or sub-portfolios, as well as the risk concentrations and recommended measures as part of the regular reporting process.

The new HSH Management Report that was introduced in 2016 contains information on the development of the relevant key default risk figures, as well as structural analyses on business areas, information on conspicuous individual loan exposures and reports on problem loans and new business. The HSH Management Report also includes the profit centre accounting, rating validation results and rating migration development, as well as information on the monitoring and management of the country risk.

### MARKET RISK

Market risk represents the potential loss that can arise as a result of adverse changes in market values on positions held in our trading and banking book. Market movements relevant to the Bank are changes in interest rates and credit spreads (interest rate risk), exchange rates (foreign exchange risk), stock prices, indices and fund prices (equity risk) as well as, up until the end of 2016, commodity prices (commodity risk) including their volatilities.

### Organisation of market risk management

The Management Board determines the methods and processes for measuring, limiting and steering market risk, and budgets an overall limit percentage for market risks. Against the background of this upper loss limit, the risks of all business bearing market risk are limited by a dynamic system of loss and risk limits.

Market risk was actively managed in the Treasury & Markets division in the year under review. The Bank Management business unit is responsible for the central management of interest rate and foreign exchange risks in the banking book. The Overall Management Board is responsible for selected strategic positions exposed to market risks.

An organisational separation between market risk controlling, financial controlling and settlement and control, on the one hand, and the trading divisions responsible for positions, on the other, is ensured at all levels in accordance with MaRisk. All major methodological and operational tasks for risk measurement and monitoring are consolidated in the Group Risk Management division.



**Market risk management**

**Market risk measurement and limitation**

Our system for measuring and managing market risk is based, on the one hand, on the economic daily profit and loss and, on the other, on a value-at-risk approach. The economic profit and loss is calculated from the change in present values compared to the end of the previous year. The market risk of a position represents the loss in value (in euros) which will not be exceeded until the position is hedged or realised within a predetermined period with a predetermined probability.

The value-at-risk (VaR) is determined by HSH Nordbank using the historical simulation method. It is calculated for the entire Group based on a confidence level of 99.0 % and a holding period of one day for a historical observation period of 250 equally weighted trading days.

The main market risks at HSH Nordbank are interest rate risk (including credit spread risk) and foreign exchange risk. In addition to these risk types, the VaR of HSH Nordbank also covers equity and commodity risk for both the trading book and the banking book. The basis risk is also taken into account in determining the VaR. The basis risk constitutes the risk of a potential loss or profit resulting from changes in the proportion of prices or interest rates on similar financial products within a portfolio. The individual market risk types are not restricted by separate limits. Limitation is applied within the VaR limit for the overall market risk of the Bank. Limits are set for the VaR for the different reporting units for the purposes of managing market risk, whereas losses incurred are restricted through stop loss limits. There are clearly defined processes for limit adjustments and breaches.

Where necessary, HSH Nordbank enters into hedging transactions to manage or reduce market risk in order to offset the impact of unfavourable market movements (e.g. with regard to interest rates, exchange rates) on its own positions. Derivative financial instruments in particular, such as interest rate and cross-currency interest rate swaps, for example, are used as hedging instruments. The impact of the hedging relationships entered into are included in the disclosed VaR. Further information on this and the type and categories of the hedging instruments and hedging relationships entered into by HSH Nordbank as well as the type of risks hedged is presented in the Notes. In particular we refer to Section I. F) of Note 8 Accounting policies, Note 11 Result from hedging, Note 28 Positive fair values of hedging derivatives, Note 41 Negative fair values of hedging derivatives and Note 62 Report on business in derivatives.

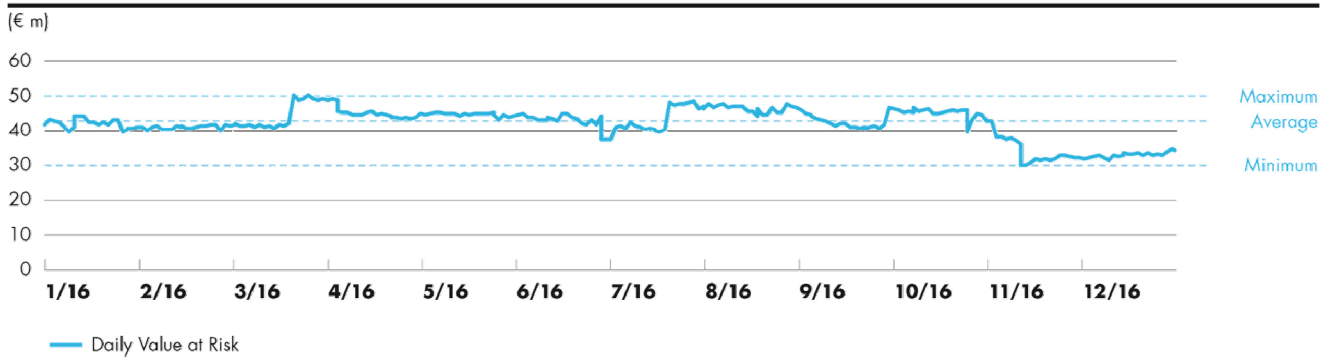
Market risks arising from the lending business and liabilities of the Bank are transferred to the trading divisions and taken into account in the corresponding risk positions. There they are managed as part of a proactive portfolio management process and hedged through external transactions.

The VaR model used and continuously enhanced by HSH Nordbank contains all of the Bank's significant market risks in an adequate form.

**Daily value-at-risk during the year under review**

The following chart illustrates the movement in the daily VaR for the total trading and banking book positions of HSH Nordbank over the course of 2016.

**DAILY VALUE-AT-RISK IN THE COURSE OF 2016**



Market risk fluctuated between € 30 million and € 50 million. This figure fell from € 41 million on the last day of 2015 to € 34.5 million on the last day of 2016. The main drivers behind this drop in overall VaR included the portfolio reduction and lower market volatility compared with the previous year.

The VaR of the trading book positions amounted to € 0.5 million as at 31 December 2016, while that of the banking book transactions amounted to € 35 million.

The overall VaR, which cannot be derived from the total VaR of the trading and banking book positions due to risk-mitigating correlation effects, amounted to € 34.5 million as at the reporting date. This resulted in a limit utilisation of 49 % based on a VaR limit of € 70 million.

The following table shows the change in overall VaR by individual market risk type. The maximum and minimum represent the range over which the respective risk amount moved in the course of the year under review.

#### DAILY VALUE-AT-RISK OF THE GROUP

(€ m)	Interest rate risk <sup>1)</sup>		Credit spread risk <sup>1)</sup>		Foreign exchange risk		Equity risk		Commodity risk		Total <sup>2)</sup>	
	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015
Average	9.7	18.3	25.1	23.0	18.1	19.5	2.0	2.9	–	–	41.8	41.6
Maximum	19.9	24.9	27.1	28.0	25.8	25.4	4.1	6.2	–	0.2	49.9	57.3
Minimum	4.6	11.4	21.6	17.7	9.1	10.3	0.9	1.1	–	–	30.2	24.7
Period end amount	12.3	19.4	22.9	24.0	18.3	21.3	1.4	4.1	–	–	34.5	40.9

<sup>1)</sup> Credit spread risk is a sub-type of interest rate risk. It is not disclosed as part of interest rate risk but as a separate item due to its significance for HSH Nordbank.

<sup>2)</sup> Due to correlations the VaR does not result from adding up individual values.

With regard to the risk types there mainly was a drop in interest rate risk. This is due primarily to the incorporation of pension liabilities into the market risk measurement. The pension liabilities have a positive interest rate sensitivity and largely compensate for the negative interest rate sensitivity of the other portfolios of the Group. The commodity business was abandoned in 2016 and the last of the portfolio had been wound down by the end of the year. This means that there is no longer any commodity risk to be reported at the year end.

The market risk of the Core Bank is primarily characterised by interest rate and foreign exchange risk arising from the lending business, funding and the trading book, which predominantly contains positions resulting from trading in interest rate and currency derivatives with customers and bond trading. The market risk also includes the credit spread risk from the securities positions in the liquidity buffer and cover pool portfolios, which are characterised by good credit ratings. In 2016, the majority of the public cover pools of the Non-Core Bank were transferred to the Core Bank. There are only marginal equity risks.

The market risk of the Non-Core Bank arises predominantly from the credit investment business or the credit investment portfolio in the banking book. Accordingly, credit spread risk is the dominant factor.

#### Backtesting

HSH Nordbank performs regular backtests to verify the appropriateness of its VaR forecasts. On the assumption of unchanged positions, the daily profit and loss achieved in theory due to the market developments observed are compared with the VaR values of the previous day, which were forecast using historical simulation. Based on the

assumption of the confidence level of 99.0% applied by HSH Nordbank, up to four outliers indicate that the forecasting quality for market risks is satisfactory. In 2016, there were no more than four outliers in any month at the level of the HSH Nordbank Group.

#### Stress tests

In addition to the limit-based management of the daily VaR, at least weakly stress tests are performed that analyse the effects of unusual market fluctuations on the net present value of the Bank's positions.

When it comes to market risk, HSH Nordbank makes a distinction between standardised, historical and hypothetical stress scenarios. Whereas standardised scenarios are defined for specific risk types (e.g. shift in or rotation of the interest rate curve), historical and hypothetical stress tests apply to several market risk factors at the same time. In this regard historical scenarios actually map correlations between risk factors that occurred in the past, whereas hypothetical scenarios are based on fictitious changes in risk factors. With regard to the hypothetical scenarios it is also distinguished between economic scenarios that simulate a downturn in the macroeconomic environment and portfolio-specific scenarios that can represent a potential threat for the value of individual sub-portfolios of HSH Nordbank. The hypothetical scenarios are periodically adjusted depending on changes in the market environment.

#### Reports on market risk

The Management Board is informed on a daily basis with regard to the trend in market risk and results as well as limit utilisations. In addition, weekly or monthly reporting to the Overall Bank Management Committee takes place.

## LIQUIDITY RISK

HSH Nordbank divides its liquidity risk into risk of insolvency and liquidity maturity transformation risk.

The risk of insolvency refers to the risk that present or future payment obligations cannot be met in part or in full. This is referred to as liquidity risk in the narrower sense. The key driver of this liquidity risk is the cash flow structure in the liquidity development report, which is determined by the assets (maturity/currency structure) and liabilities (funding structure by maturity/currency/investor). In this regard the market liquidity risk, i.e. the danger, that transactions cannot be sold or only at unfavourable conditions because of a lack of market depth, is reflected in the liquidity development report as a component of the insolvency risk. Another component of insolvency risk is the refinancing risk, i.e. the danger, of not being able to obtain liquidity or not at the expected conditions if required. The refinancing risk is determined by the refinancing structure. Information on the refinancing structure can be found in Note 54 Residual maturity breakdown of financial instruments to the consolidated financial statements.

Liquidity maturity transformation risk refers to the risk that a loss will result from a mismatch in the contractual maturities of assets and liabilities, the so-called liquidity maturity transformation position, and from the change in the Bank's refinancing surcharge.

### Organisation of liquidity risk management

Strategic liquidity management is the responsibility of the Bank Management business unit. The objective of liquidity management is to ensure the solvency of HSH Nordbank at all times, at all locations and in all currencies, to adhere to the regulatory liquidity ratios, to manage the marketability of the liquid assets of the liquidity buffer and to avoid concentration risks in the refinancing structure. The Treasury & Markets division is responsible for funding and marketing.

The Group Risk Management division is responsible for the methods used to measure and limit liquidity risk within the Group and performs daily risk measurement and limit monitoring. The risk measurement results support the Bank Management business unit in managing liquidity for all time buckets and enable it to counter possible risks at an early stage.

The Bank Steering Committee is the central committee responsible for managing the resource liquidity and is assisted by the Credit Committee in this task by means of an active portfolio management at the level of material individual transactions.

HSH Nordbank has a liquidity contingency plan which contains regulated procedures and responsibilities should a liquidity crisis occur. Institution-specific, risk-oriented and capital market-oriented early warning indicators are also taken into account as part of the contingency process in order to avert a liquidity emergency. The

liquidity contingency plan is closely linked to the Recovery Plan as defined in the SAG.

### Liquidity risk management

#### Measurement and limitation of liquidity risk

The transactions in the Group impacting liquidity are presented as cash flows and the resultant inflows and outflows allocated to time buckets (liquidity development report) for the purposes of measuring the risk of insolvency or funding requirements. The difference between inflows and outflows represents a liquidity surplus or deficit (gap) in the relevant time buckets. The gaps are presented accumulated from day one to twelve months in order to map future liquidity requirements. They are compared to the respective liquidity potential which is applied to close the cumulative gaps of the individual time buckets and consequently represents the respective limit for insolvency risk. The net liquidity position, which shows the extent of the insolvency risk, is determined as the net amount from the gaps and the respective liquidity potential. This means that the net liquidity position already includes the measures used to generate liquidity in normal market phases.

In addition to all on-balance sheet business, loan commitments already granted, guarantees, transactions with forward value dates and other off-balance sheet transactions are incorporated in the liquidity development report. Maturity scenarios are used for a number of positions to map economic maturities more effectively. In doing so any possible minimum levels of deposits as well as liquidation periods and realisation amounts of assets, for example, are modelled conservatively as a matter of principle. The modelling assumptions are regularly reviewed, also in accordance with the MaRisk requirements.

The liquidity potential available to close gaps is composed of a securities portfolio held as a crisis precaution measure (liquidity buffer), further highly liquid and liquid securities, according to how liquid they are, and industrial loans eligible for refinancing with central banks. Most of the portfolio of securities is invested in liquid markets and can be liquidated via the refinancing channels, namely central banks, Eurex repo market, bilateral repo market or the cash market.

The components of the liquidity potential – such as the liquidity buffer required under MaRisk for example – are monitored continuously and validated in accordance with internal and external minimum requirements. Safety buffers and risk discounts are incorporated into the limits in order to keep the probability of full utilisation or overdrawing the limits as low as possible. These discounts are, for example, haircuts or other safety margins that reflect the uncertainty about the future development of the respective component of liquidity potential. Permanent market access to the funding sources relevant for HSH Nordbank is also monitored on a regular basis. This is achieved firstly through the ongoing market observation of all funding sources by the Bank's divisions. Secondly, Group Risk Management daily



reviews the funding potential based on the expected prolongation ratios for short-term deposits. The Bank Management business unit also prepares actual/plan analyses regarding long-term funding.

The liquidity-value-at-risk (LVaR) as a reflection of liquidity maturity transformation risk is calculated monthly through historical simulation (confidence level 99.9%) of the liquidity spread and their present value effects on transactions, which would be necessary theoretically in order to immediately close the current maturity transformation position. In doing so, it is assumed that these hypothetical close-out transactions could actually be effected in the market and that full funding is therefore possible. LVaR limits are set at Group level and are a part of the risk-bearing capacity concept.

#### **Liquidity management**

The short-term liquidity base and the regulatory liquidity ratios are operationally managed by the Treasury & Markets division based on general parameters specified by the Bank Management business unit. In addition to the regulatory requirements the liquidity development reports are relevant amongst other things to determine these general parameters. Any setting of or change to the individual parameters or the framework requirements is decided by the Bank Steering Committee/the Management Board. This places HSH Nordbank in the position to react flexibly to market developments.

HSH Nordbank uses the so-called expected case liquidity development report as well as the stress case forecast, which contain expected/stressed cash flows and are prepared for a period extending beyond the current financial year, as the basis for managing the medium-term liquidity base. The Management Board defines the limits for the funding requirements of the individual divisions.

The collateral pool of HSH Nordbank consisting of cash balances, securities and loan receivables that are eligible for funding is coordinated by the Bank Management business unit in order to be able to utilise the potential for secured funding in the best possible manner.

#### **Stress tests**

The selection of our stress tests is the result of an analysis of historical events and hypothetical scenarios. The selection is reviewed on an annual basis and adapted to current developments where necessary.

Within the different stress modelling processes additional market-specific scenarios (e.g. Market liquidity crisis, severe economic downturn) and institution-specific scenarios (e.g. rating downgrade of HSH Nordbank AG, capital market rumours) are assessed for insolvency risk on a monthly basis in addition to the daily preparation of the stress liquidity development report (stress case). A stressed US dollar (gradual appreciation) is taken into account in the scenarios market liquidity crisis and severe economic downturn.

In addition, the Bank performs a monthly US dollar stress test which is based on the normal case liquidity development report and simu-

lates an immediate as well as a gradual appreciation in the US dollar affecting the US dollar cash flows and the cash collateral for US dollar derivatives. The stress factor for the appreciation is determined based on an analysis of the historical movement of the EUR/USD exchange rate.

Within the framework of a stress test for the liquidity maturity transformation risk it is analysed how the LVaR moves on increasing liquidity spreads and stressed liquidity gaps. The stress LVaR serves as an indicator for the sensitivity of the LVaR to an increase in the spread/liquidity costs and constitutes an additional piece of management information.

Furthermore, events that could have a critical impact on HSH Nordbank's solvency were analysed in the reporting year within the framework of the periodic implementation of inverse stress tests.

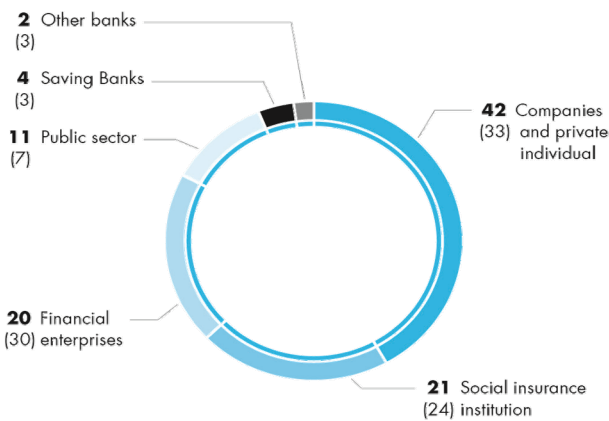
#### **Risk concentrations**

HSH Nordbank has established a monitoring system for managing concentrations of both asset and liability instruments. Special emphasis is placed on deposits that are analysed and reported on with regard to the depositor structure (investor, sectors), maturities (original and residual maturities) and deposit drain risk. The deposit structure is characterised by a high level of concentration relating to a small number of large institutional investors that are dependent on interest rates and ratings. In addition, a large proportion (more than 20% of the total refinancing) are overnight deposits.

The following chart shows the structure of our deposits by sector:

**DEPOSITOR STRUCTURE AS AT 31 DECEMBER 2016<sup>1)</sup>**

(in %, previous year figures in brackets<sup>2)</sup>)



<sup>1)</sup> In addition to call an term deposits this illustration also includes demand deposits for the first time.  
<sup>2)</sup> The figures reported for the prior year have been adjusted to the new structure of our deposits by sector.

Quantitative measures are calculated for the purposes of analysing existing risk concentrations. Furthermore, an analysis is performed not only on the structure but especially on the risk content, in order to

be able to derive according control impulses from the quantitative measures in combination with a qualitative discussion.

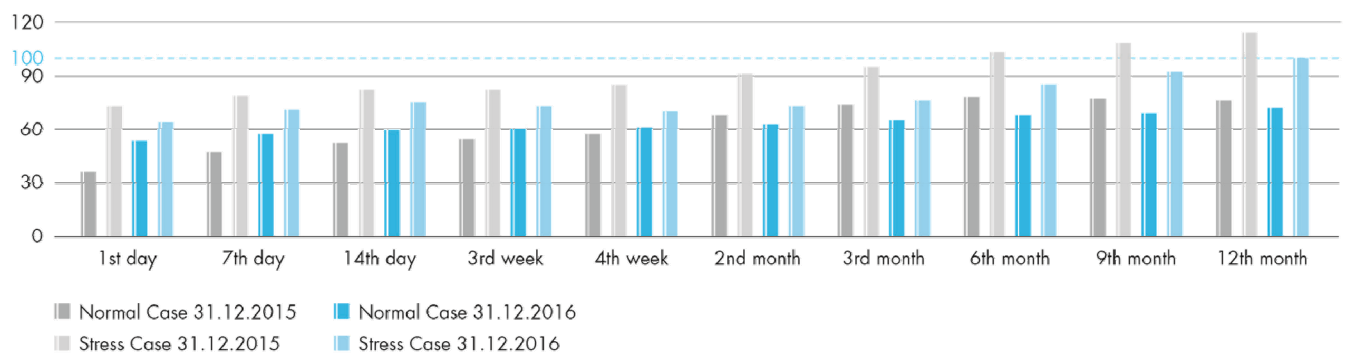
In addition to the analysis of the depositor structure with regard to existing depositor concentrations, risk concentrations are examined with regard to the US dollar asset/liability position. This shows a dependency of the liquidity situation on the movement in the US dollar, which is still to be regarded as relevant. This is due to the amount of US dollar assets that are refinanced through EUR/USD basis swaps amongst other things. A decrease in the EUR/USD exchange rate will increase the cash collateral to be provided on foreign currency derivatives, representing a burden on liquidity. For the purposes of analysing the dependency on the US dollar, a US dollar liquidity development report is prepared and sensitivity analyses are performed regularly. In addition a US dollar stress test of the liquidity development report is performed.

**Quantification of liquidity risk**

The following illustration shows the relative utilisation levels of the liquidity potential for individual cumulative liquidity gaps in the normal case and stress case as at 31 December 2016 as well as at the end of 2015. Utilisation represents the share of the cumulative gap in total liquidity potential, which also includes the liquidity buffer required under supervisory law.

**LIMIT ON CUMULATIVE LIQUIDITY GAPS**

(Utilisation of liquidity potential in %)



Risk tolerance of HSH Nordbank with regard to liquidity risk is reflected, amongst other things, in the definition of a minimum survival period, which describes how long a utilisation of a liquidity potential lower than 100 % is to be maintained under the normal and stress cases for insolvency risk.

In the normal case assessment that is based on the assumption of business development in an ordinary market environment with nor-

mal market fluctuations, the liquidity potential had a peak utilisation of 72 % in the twelfth month as at the reporting date. All limits within the minimum survival period of twelve months defined by the Bank were thereby adhered to. The stress case liquidity development report (combined scenario-economic downturn and rating downgrade – based on the assumption of a gradual increase in the US dollar, amongst other things) shows that the liquidity potential was also not exceeded within the minimum survival period of one month estab-

lished taking Minimum Requirements for Risk Management (MaRisk) into account. In fact, the limits as at the end of 2016 are even adhered to for a period of ten months. Compared to the 2015 year end, utilisation levels have decreased in the normal case as of the second month and in the stress case in all maturity bands. The improvements are due, among other things, to the sale of loan portfolios with a volume of € 5 billion to hsh portfoliomangement AöR on 30 June 2016, and to the targeted further development of the long-term refinancing. Critical limit utilisation levels were recorded neither in the normal case nor in the stress case liquidity development report in the course of the period under review.

The results of the market-specific and Bank-specific stress scenarios determined in addition to the stress case liquidity development report show that as at December 2016 the liquidity requirement of HSH Nordbank was covered for ten months up to twelve months despite the worst case assumptions for each scenario. A minimum survival period of one month is thereby maintained in all scenarios. The results show that HSH Nordbank is prepared accordingly for the crisis scenarios assessed.

In the year under review, the LVaR as an expression of the liquidity maturity transformation risk decreased to € 83 million (31 December 2015: € 239 million). The decrease is attributable to the reduction of long-term financing requirements as well as the elimination of historical scenarios during the period of historical simulation.

### Regulatory liquidity ratios

The regulatory management parameter for liquidity risks is the liquidity ratio defined by the German Liquidity Regulation (LiqV). With values between 1.51 and 2.06, HSH Nordbank's liquidity ratio remained above the regulatory minimum value at all times throughout the reporting year. The average value for 2016 was 1.78 (previous year: 1.89), and 1.92 as the reporting date (31 December 2015: 1.89).

Under Basel III/CRR Delegated Regulation (EU) 2015/61, the Liquidity Coverage Ratio (LCR) was specified as an additional liquidity ratio to ensure liquidity in an acute stress phase of 30 days. When calculating the LCR the amount of highly liquid assets is compared to the net outflows over the next 30 days. The ratio is to be complied with since the Delegated Regulation (EU) 2015/61 entered into force in October 2015, whereby the compliance rate increases from an initial 60 % to 100 % in 2018. As at the reporting date, the LCR was 229 % within the framework of the data capture sheet of the Delegated Regulation (EU) 2015/61 (previous year: 115 % within the framework of Delegated Regulation (EU) 2015/61) which means that it was above the future minimum threshold.

The Net Stable Funding Ratio (NSFR), which must be adhered to from 2018 at the earliest, is calculated as the ratio of available funding resources across all maturities to the funding required and also must be at least 100 % after full implementation. As at 31 December 2016,

the NSFR under the QIS (Basel framework) amounted to 111 % (previous year: 95 %).

### Refinancing situation

The implementation of the funding strategy was successfully driven forward during the course of the financial year thereby improving the liquidity profile of the Bank. The measures stepped up in the year to date to reduce risk positions, thereby releasing liquidity, had a positive impact. Besides the issuing activities a stable level of deposits contributed to the refinancing of the business. However, there is no unrestricted access to the capital markets.

Future funding and HSH Nordbank's rating continue to be key challenges despite this positive development. In the reporting year HSH Nordbank accelerated the winding down of legacy portfolios, particularly in the US dollar area, to reduce the effect of changes in exchange rates on, inter alia, the Bank's liquidity. Restrictions were also placed on new US dollar business. In the event of a sustained appreciation in the US dollar HSH Nordbank has prepared measures that aim at further reducing the asset volume to be refinanced. Further information on HSH Nordbank's refinancing situation is set out in the Earnings, net assets and financial position and Forecast, opportunities and risks report sections.

### Reports on liquidity risk

The CRO and divisions concerned are informed daily of the change in insolvency risk in the normal case and stress case. In addition, the Bank Steering Committee and the Overall Management Board receive a liquidity risk report at least every month. This includes in addition to the analysis of insolvency risk and maturity transformation risk in the normal case and stress case an analysis of other stress scenarios, of liquidity risk arising on US dollar positions and depositor concentration risk.

### OPERATIONAL RISK

HSH Nordbank defines operational risk (OpRisk) as the risk of direct or indirect losses caused by the inappropriateness or failure of the internal infrastructure, internal procedures or staff or as a result of external factors (risk categories). This definition includes the risk of loss resulting from legal risk and compliance risk.

Operational risks are determined in accordance with the modified regulatory standardised approach for the purposes of managing the risk-bearing capacity. The corresponding economic capital required amounted to € 0.2 billion as at 31 December 2016 (31 December 2015: € 0.2 billion).

### Organisation of operational risk management

The management of operational risk at HSH Nordbank is organised in a decentralised manner. The risks are identified and managed directly in the individual organisational units of the Bank. Accordingly, the division heads are responsible for the management of operational risk and the quality of such management in their respective areas of



responsibility. The operational implementation is supported by OpRisk officers in the individual divisions.

The OpRisk Controlling department in the Group Risk Management division defines the basic principles of operational risk management applicable throughout the Bank and develops the central methods and instruments to be used in the identification, measurement, management and monitoring of operational risk.

A Bank-wide steering committee dealing with operational and other risks in the Group, the OpRisk Steering Committee convenes every quarter. It provides support to the Overall Management Board in the implementation of the OpRisk Strategy under the chairmanship of the Head of Group Risk Management. The objective of the interdisciplinary OpRisk Steering Committee is to promote dialogue between the persons involved at all hierarchy levels and to determine appropriate measures for reducing operational risk.

### Operational risk management

The identification, analysis, evaluation and monitoring of operational risk and the promotion of a corresponding risk culture in the Group represents an important success factor for HSH Nordbank. Different procedures and instruments are used in this process.

### Loss event database

The loss events arising from operational risk are consolidated into a central loss event database for HSH Nordbank and relevant subsidiaries. The loss events are recorded locally by the divisions affected and forwarded to OpRisk Controlling. The results of the analyses of actual loss events provide a starting point to eliminate existing weaknesses. The OpRisk Steering Committee is informed on a quarterly basis regarding loss events and measures undertaken related thereto. The Management Board is immediately informed of material operational risk events.

The loss event database includes all loss events with a gross loss of at least € 2,500 and all material near-loss events.

In the reporting year 38% (previous year: 49%) of the operational loss events reported were incurred in the Employee risk category. This risk category includes, for example, processing errors or unauthorised actions. The proportion of operational loss events reported under the Internal processes risk category amounted to 26% (previous year: 24%). These include, for example, deficient or missing processes. The proportion of operational loss events reported under the External influences category (e.g. criminal acts, regulatory and statutory requirements) amounted to 35% (previous year: 23%). The proportion of loss events reported under the Internal infrastructure category (e.g. system failures, functionality or security) amounted to 1% (previous year: 4%).

HSH Nordbank participates in the exchange of operational loss event data as part of the operational risk data pool (DakOR). Thus,

HSH Nordbank obtains a more comprehensive database for the evaluation of risk scenarios and external comparisons.

### Risk inventory

HSH Nordbank performs a risk inventory for operational risk each year for the whole Group. Information about the risk situation of the divisions gained from this inventory supplements the reporting and serves the purpose of preventive management and monitoring of operational risk. The Bank performs the risk inventory based on defined scenarios, which take into account both actual as well as potential loss events.

### Control of measures

Based on an analysis of the causes of significant loss events and the results of the risk inventory, suitable measures are established in order to avoid future losses as far as possible. The measures identified are to be appropriate under cost-benefit aspects. In doing this, the instruments of risk mitigation consist above all of a large number of organisational safeguarding and control measures which are also applied in the context of the internal control system. OpRisk Controlling monitors the actual implementation of the measures determined using the measures controlling procedures.

### Risk indicators

Risk indicators are collected on a quarterly basis and incorporated in the OpRisk reporting. The indicators are selected based on the estimated risk situation and are periodically reviewed to ensure that they are up-to-date. The aim is to identify risks at an early stage and prevent their causes by the use of ongoing and comparative analysis of loss events and risk indicators.

In addition to the methods mentioned above, specific procedures and responsibilities have been instituted within HSH Nordbank for the operational risk elements listed below.

### Management of personnel risks

Personnel risk refers to the risk of losses that may occur as a result of the unplanned departure of key personnel of HSH Nordbank, shortage of skilled employees or poor motivation of employees. This risk could materialise particularly in light of the current reduction in staff. The Human Resources division is therefore focusing increasingly on measures to reduce personnel risk. A large number of personnel management tools for employee retention are used to prevent the unscheduled departure of key personnel. In addition, succession planning is performed, and regularly reviewed, for relevant positions.

### IT risk management

The IT division is responsible for IT risk management. In the IT strategy the division has defined as the primary objective of IT risk management to identify IT risks at an early stage, in order to be able to avert or reduce serious damage on the basis of clear responsibilities in particular.

IT-specific risk tools are used by means of which risks are actively managed in projects and in the line functions and reduced by a monitored implementation of measures.

### Business continuity management

HSH Nordbank is exposed to risks arising from unforeseeable events that may lead to an interruption of business operations and, as a result, losses and additional costs. Group Risk Management has established with the involvement of the relevant divisions processes to limit the risks arising from the fact that the information technology fails or service providers or employees are unavailable. The objective of the business continuity plans to be prepared and periodically reviewed by each division is to ensure the functional capability of critical business processes and activities, even in the event of an emergency.

### Internal control system

Operational risk is closely linked to the internal control system (ICS) of HSH Nordbank. A major objective of the ICS is to optimise the internal bank processes in order to avoid losses that may arise as a result of, for example, processing errors. Detailed information on the ICS is set out in the Risk management system section.

### Management of legal risk

Legal risks also fall under operational risk. Legal risks includes economic risks arising as a result of non-compliance or incomplete compliance with regulations or with the framework defined by case law, in particular commercial law, tax law and company law. In case any of these risks materialise, this may lead to a higher financial burden than planned.

The Legal and Taxes division is responsible for managing these risks. In order to reduce, limit or prevent risk all divisions are given comprehensive legal advice by regularly trained staff and external consultants.

HSH Nordbank recognised provisions of € 34 million (previous year: € 37 million) for tax risks as at the reporting date. In addition, contingent liabilities of € 32 million (previous year: € 40 million). Contingent liabilities relating to legal disputes result from several individual cases involving claims of up to € 7 million. A major portion of the provisions for litigation risks relates to the legal proceedings mentioned below.

Since 2005 HSH Nordbank AG has been involved in legal proceedings with a Turkish shipping group and up to now had to pay a total amount of \$ 54 million in the year 2013 due to decisions of Turkish

courts. The plaintiffs have filed new claims under which damages are asserted based on the same facts. Appropriate provisions have been recognised for this.

HSH Nordbank AG was also sued in January 2015 by a borrower for damages of approximately € 215 million. In March 2016, the claim was increased to approx. € 278 million. The underlying facts of the case had already been the subject of several court proceedings between the Bank and the borrower, in which the Bank has always succeeded before different courts apart from relatively small amounts. In the Bank's view, claims newly asserted by the borrower regarding the known facts of the case are unfounded. They do not contain any legally significant changes regarding the known facts and therefore do not provide any grounds for the previous legal assessment of this case to be revised. As the probability of success for the current legal action is assessed as small, no provision or contingent liability has been recognised.

HSH Nordbank AG recognised other provisions relating to legal risks in the amount of € 6.1 million on the basis of current German case law of the Federal Court of Justice (BGH) regarding liability for advice provided on swap transactions.

Tax risks are a component of legal risks and mainly result from the fact that the binding interpretation of rules that can be interpreted in specific cases may only be known after several years due to the long period between tax audits. The tax audits have not yet been finalised for the years starting from 2003.

HSH Nordbank recognised provisions/liabilities (including interest) totalling € 72 million (previous year: € 56 million) for tax risks as at the reporting date. € 33 million of this amount is attributable to HSH Nordbank AG and € 39 million to fully consolidated subsidiaries. A major portion of this relates to tax risks with respect to the tax audits (in connection with internal cost allocations to foreign entities, structured transactions, reimbursement of value-added tax on inputs, and risks resulting from the tax treatment of investment income).

There are contingent liabilities with regard to tax risks in connection with the tax audits that are ongoing at present. In particular, there is uncertainty surrounding how the tax authorities will interpret current trends in the court decisions made by the fiscal courts on various tax-related issues. The Bank, however, deems its legal positions to be correct, meaning that there is no need to set up corresponding provisions in this regard.

### Management of compliance risk

Compliance risk arises as a result of non-compliance with legal regulations and requirements that may lead to sanctions being imposed by the legislator or supervisory authorities, financial losses or a negative impact on the Bank's reputation.

The Compliance division is responsible for compliance risk management. Compliance with the different legal requirements is also ensured by the respective divisions concerned. Compliance monitors adherence to codes of conduct with respect to the topics of capital markets compliance, prevention of money laundering, terrorism financing and other criminal offences in accordance with Section 25h KWG as well as compliance with financial sanctions and embargoes. In addition the division performs the compliance function as defined in AT 4.4.2 MaRisk and in this context strives to ensure that the essential legal regulations and standards are implemented at HSH Nordbank and complied with.

The Code of Conduct summarises the requirements of different legal sources and internal guidelines. It applies to all employees as well as the Management Board of HSH Nordbank AG and is a mandatory part of the overall Bank objectives. The behavioural requirements of the Compliance division are set out in detail in internal instructions.

Staff of the Bank is regularly trained in compliance-relevant topics. The objective of the training is to firmly anchor compliance as part of corporate culture, to disseminate relevant standards and changes thereto, and to enable new staff to quickly become familiar with corporate practices and to ensure compliance with legal requirements in this way.

The Bank receives notification of suspicious cases of misconduct via internal reporting channels and the so-called "whistle-blowing office", and forwards these to the responsible internal and external bodies. The whistle-blowing office is staffed by independent ombudsmen from BDO Deutsche Warentreuhand Aktiengesellschaft Wirtschaftsprüfungsgesellschaft and enables anonymous reporting of suspicious cases.

### Reports on operational risk

The OpRisk Steering Committee receives a quarterly report regarding the development of the risk position, material loss events and management measures addressed. The Overall Management Board is informed once a year regarding the capital required, the loss event trend and material loss events and loss potential, as well as any measures required.

### OTHER MATERIAL RISKS

Amongst other material risk types of HSH Nordbank are business strategy risk and reputation risk.

### Business strategy risk

The business strategy risk refers to the risk of financial damage being incurred due to long-term strategic decisions based on incorrect assumptions. Should HSH Nordbank not be successful in identifying changes in markets relevant for it on a timely basis, this could have a negative impact on its competitiveness. Changes to laws and regulations or new regulatory requirements for instance could also jeopardise the implementation of HSH Nordbank's business model.

This risk is managed via the regular review and updating of the business strategy by the Strategy business unit and the closely related overall Bank planning process established in the Bank. The responsibility for the strategy of HSH Nordbank rests with the Overall Management Board, while the Strategy and Board Advisory Service business unit is responsible for the process. An action-oriented management dialogue, including on the strategic business objectives, is conducted during the year as part of the monthly Business Area Management Dialogues.

### Reputation risk

Reputation risk is the risk of a direct or indirect loss caused by damage to the reputation of the company. Damage to reputation means a public loss of confidence in HSH Nordbank or a loss of esteem of the Bank from the viewpoint of individual stakeholder groups (e.g. capital markets, clients, shareholders, investors, the general public, employees).

Damage to reputation can be directly caused by the behaviour of internal staff, external stakeholders or by the social environment as a whole or indirectly in connection with another risk type. HSH Nordbank can suffer adverse consequences in both cases, for instance due to a loss of clients.

HSH Nordbank manages reputation risk particularly by means of preventive measures via the review of specific transactions, on the one hand, and via process-related rules, on the other, in order to prevent the occurrence of reputational damage if possible. The reputation risk strategy that is adopted every year defines the bank-wide principles for managing reputation risk as a supplement to the existing regulations and instructions, such as the Code of Conduct.



## SUMMARY OF RISK ASSESSMENT AND OUTLOOK

The 2016 financial year was characterised by the continuing winding down of high-risk, non-strategic lending and capital markets transactions held in the portfolios belonging to the “Non-Core Bank” segment as well as by the progress made in implementing the business model. In addition to the sale of the federal state portfolio, for example, progress was also made as a result of the organic reduction of the Non-Core Bank portfolio.

The risk-bearing capacity of HSH Nordbank was maintained at all times during the year under review with a maximum utilisation of the risk coverage potential of 35 %. The guarantee facility as well as the ongoing winding down of risk positions made a positive contribution in this regard.

There are still some challenges facing the Bank in particular with regard to risk concentrations in the shipping loan portfolios, in the US dollar business and with regard to the deposit structure of HSH Nordbank. Within this context, the ongoing difficult conditions on the shipping markets, in particular, are having a negative impact, even though a drop in the number of new orders, increased scrapping, increasing consolidation and rising freight rates in 2016 can be seen as the first signs of a moderate improvement on the shipping market.

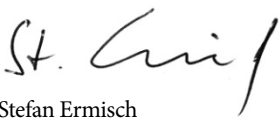
The requirement relating to the privatisation of HSH Nordbank in 2018 linked to the European Commission’s decision poses a further challenge for the risk organisation. In addition to the need for a highly effective and efficient CRO unit, one of the key duties of the risk organisation lies in stabilising the Bank during the privatisation process, in particular by ensuring risk-bearing capacity and appropriate capital and liquidity resources at all times. As far as the privatisation process is concerned, there will also still be a need to optimise the cost base, revenue planning and competitive position and to align the risk organisation with the future strategy and targets.

For information on further key challenges in connection with the privatisation process and the risks associated with maintaining appropriate capital and liquidity resources, we refer to the statements in the Forecast, opportunities and risks report.

The implementation of the new supervisory requirements will be another focus of our activities in 2017. The Basel Standard 239 (BCBS 239) gives rise, for example, to comprehensive future requirements regarding the capacity to aggregate risk data including the IT architecture and risk reporting by banks. In addition, the requirements of the EBA/ECB resulting from the supervisory review and evaluation process (SREP) and the expected update to the “Supervisory assessment of bank-internal capital adequacy concepts” guidelines have to be met. The requirements mentioned above will be implemented within projects.

The risk and bank management systems described in this report are aligned to take account of risk on a systematic basis. This also applies to our expectations regarding future market and business developments. We believe that we have appropriately presented the overall risk profile of HSH Nordbank Group as well as the opportunities and risks inherent in the future development of our business activities in the Forecast, opportunities and risks report section and in this Risk report in an appropriate and comprehensive manner.

Hamburg/Kiel, 14 March 2017



Stefan Ermisch



Oliver Gatzke



Ulrik Lackschewitz



Torsten Temp

**GROUPE  
FINANCIERE  
STATISTIQUE**

# FINANCIAL STATEMENTS

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## GROUP STATEMENT OF INCOME FOR THE PERIOD 1 JANUARY TO 31 DECEMBER 2016

(€ m)	Note	2016	2015	Change in %
Interest income		3,466	4,397	-21
Negative interest on investments and derivatives		-191	-55	> 100
Interest expenses		-2,733	-3,443	-21
Positive interest on borrowings and derivatives		183	29	> 100
Net income from hybrid financial instruments		-118	104	> -100
<b>Net interest income</b>	(9)	<b>607</b>	<b>1,032</b>	<b>-41</b>
Net commission income	(10)	87	114	-24
Result from hedging	(11)	-4	12	> -100
Net trading income	(12)	88	84	5
Net income from financial investments	(13)	140	54	> 100
Net income from financial investments accounted for under the equity method	(14)	3	-	> 100
<b>Total income</b>		<b>921</b>	<b>1,296</b>	<b>-29</b>
Loan loss provisions in the lending business	(15)	631	-354	> -100
Hedging effect of credit derivative under the second loss guarantee	(3)	-475	658	> -100
Administrative expenses	(16)	-634	-634	-
Other operating income	(17)	58	38	53
Expenses for bank levy and deposit guarantee fund	(18)	-56	-50	12
<b>Net income before restructuring and privatisation</b>		<b>445</b>	<b>954</b>	<b>-53</b>
Net income from restructuring and privatisation	(19)	-110	-31	> -100
Expenses for government guarantees	(20)	-214	-473	-55
<b>Net income before taxes</b>		<b>121</b>	<b>450</b>	<b>-73</b>
Income taxes	(21)	-52	-352	-85
<b>Group net result</b>		<b>69</b>	<b>98</b>	<b>-30</b>
Group net result attributable to non-controlling interests		2	-1	> 100
Group net result attributable to HSH Nordbank shareholders		67	99	-32

### EARNINGS PER SHARE

(€)	Note	2016	2015
Undiluted	(23)	0.22	0.33
Diluted	(23)	0.22	0.33
<b>Number of shares (millions)</b>		<b>302</b>	<b>302</b>

## GROUP STATEMENT OF COMPREHENSIVE INCOME FOR THE PERIOD 1 JANUARY TO 31 DECEMBER 2016

### RECONCILIATION WITH TOTAL COMPREHENSIVE INCOME/LOSS

(€ m)	2016	2015
<b>Group net result</b>	<b>69</b>	<b>98</b>
<b>Income and expense that have been reclassified to the statement of income or may be reclassified at a later date</b>		
Changes in fair value of AFS financial instruments		
Unrealised gains and losses (before taxes)	67	30
Gains and losses (before taxes) reclassified to the statement of income	-36	-43
of which from exchange rate effects	-	11
Income taxes recognised	-7	8
of which from exchange rate effects	-	1
	<b>24</b>	<b>-5</b>
Differences resulting from currency translation	18	57
	<b>18</b>	<b>57</b>
<b>Subtotal</b>	<b>42</b>	<b>52</b>
<b>Income and expenses that will not be reclassified to the statement of income at a later date</b>		
Changes resulting from the revaluation of net defined benefit liabilities (before taxes)	-88	94
Income taxes recognised	28	-30
	<b>-60</b>	<b>64</b>
<b>Subtotal</b>	<b>-60</b>	<b>64</b>
<b>Other comprehensive income for the period</b>	<b>-18</b>	<b>116</b>
<b>Total comprehensive income</b>	<b>51</b>	<b>214</b>
Total comprehensive income attributable to non-controlling interests	2	-2
Total comprehensive income attributable to HSH Nordbank shareholders	49	216

## GROUP STATEMENT OF FINANCIAL POSITION AS AT 31 DECEMBER 2016

### ASSETS

(€ m)	Note	2016	2015	Change in %
Cash reserve	(24)	3,491	3,394	3
Loans and advances to banks	(25)	4,192	5,595	-25
Loans and advances to customers	(26)	50,910	56,575	-10
Loan loss provisions	(27)	1,142	-1,065	> -100
Credit derivative under the second loss guarantee	(3)	199	663	-70
Positive fair values of hedging derivatives	(28)	508	783	-35
Positive adjustment item from portfolio fair value hedges		403	408	-1
Trading assets	(29)	5,433	7,356	-26
Financial investments	(30)	15,493	16,636	-7
Financial investments accounted for under the equity method	(31)	13	2	> 100
Intangible assets	(32)	14	16	-13
Property, plant and equipment	(33)	236	474	-50
Investment property	(33)	12	64	-81
Non-current assets held for sale and disposal groups	(34)	1,382	5,082	-73
Current tax assets	(35)	65	79	-18
Deferred tax assets	(36)	767	748	3
Other assets	(37)	105	163	-36
<b>Total assets</b>		<b>84,365</b>	<b>96,973</b>	<b>-13</b>

**LIABILITIES**

(€ m)	Note	2016	2015	Change in %
Liabilities to banks	(38)	9,501	14,398	-34
Liabilities to customers	(39)	40,172	44,567	-10
Securitised liabilities	(40)	16,624	18,616	-11
Negative fair value of hedging derivatives	(41)	290	727	-60
Negative adjustment item from portfolio fair value hedge		786	872	-10
Trading liabilities	(42)	5,981	6,758	-11
Provisions	(43)	1,521	1,517	0
Liabilities relating to disposal groups	(45)	65	1	> 100
Current tax liabilities	(46)	87	151	-42
Deferred tax liabilities	(47)	7	-	> 100
Other liabilities	(48)	845	1,029	-18
Subordinated capital	(49)	3,536	3,452	2
Equity	(50)	4,950	4,885	1
Share capital		3,018	3,018	-
Capital reserve		75	175	-57
Retained earnings		1,617	1,464	10
Revaluation reserve		127	103	23
Currency conversion reserve		60	42	43
Group net result		67	99	-32
Total before non-controlling interests		4,964	4,901	1
Non-controlling interests		-14	-16	-13
<b>Total equity and liabilities</b>		<b>84,365</b>	<b>96,973</b>	<b>-13</b>



## GROUP STATEMENT OF CHANGES IN EQUITY

(€ m)

	Note	Share capital	Capital reserve
<b>As at 1 January 2015</b>		<b>3,018</b>	<b>487</b>
Group net result		-	-
Changes resulting from the revaluation of net defined benefit liabilities		-	-
Changes in fair value of AFS financial instruments		-	-
Exchange rate changes		-	-
thereof resulting from currency translation		-	-
thereof resulting from changes in scope of consolidation		-	-
Other comprehensive income		-	-
<b>Comprehensive income as at 31 December 2015</b>		<b>-</b>	<b>-</b>
Compensation for the Group net loss for the previous year		-	-312
Changes in the scope of consolidation		-	-
<b>As at 31 December 2015</b>		<b>3,018</b>	<b>175</b>
<b>As at 1 January 2016</b>		<b>3,018</b>	<b>175</b>
Group net result		-	-
Changes resulting from the revaluation of net defined benefit liabilities		-	-
Changes in fair value of AFS financial instruments		-	-
Exchange rate changes		-	-
thereof resulting from currency translation		-	-
thereof resulting from changes in scope of consolidation		-	-
Other comprehensive income		-	-
<b>Comprehensive income as at 31 December 2016</b>		<b>-</b>	<b>-</b>
Compensation for the Group net loss for the previous year		-	-100
Changes in the scope of consolidation		-	-
<b>As at 31 December 2016</b>	(50)	<b>3,018</b>	<b>75</b>

	Retained earnings	Currency conversion reserve	Revaluation reserve	Group net result	Total before non-controlling interests	Non-controlling interests	Total
	<b>929</b>	<b>- 16</b>	<b>108</b>	<b>159</b>	<b>4,685</b>	<b>- 13</b>	<b>4,672</b>
	-	-	-	99	99	-1	98
	64	-	-	-	64	-	64
	-	-	-17	-	-17	-	-17
	-	57	12	-	69	-1	68
	-	1	-	-	1	-	1
	64	58	-5	-	117	-1	116
	<b>64</b>	<b>58</b>	<b>-5</b>	<b>99</b>	<b>216</b>	<b>-2</b>	<b>214</b>
	471	-	-	-159	-	-	-
	-	-	-	-	-	-1	-1
	<b>1,464</b>	<b>42</b>	<b>103</b>	<b>99</b>	<b>4,901</b>	<b>-16</b>	<b>4,885</b>
	<b>1,464</b>	<b>42</b>	<b>103</b>	<b>99</b>	<b>4,901</b>	<b>-16</b>	<b>4,885</b>
	-	-	-	67	67	2	69
	-60	-	-	-	-60	-	-60
	-	-	24	-	24	-	24
	-	17	-	-	17	-	17
	-	1	-	-	1	-	1
	-60	18	24	-	-18	-	-18
	<b>-60</b>	<b>18</b>	<b>24</b>	<b>67</b>	<b>49</b>	<b>2</b>	<b>51</b>
	199	-	-	-99	-	-	-
	14	-	-	-	14	-	14
	<b>1,617</b>	<b>60</b>	<b>127</b>	<b>67</b>	<b>4,964</b>	<b>-14</b>	<b>4,950</b>

## GROUP CASH FLOW STATEMENT

### CASH FLOW STATEMENT

(€ m)	2016		2015	
Net result for the period		69		98
Reconciliation with cash flow from operating activities				
Depreciation, impairments and write-ups on loans and advances, property, plant and equipment, financial investments, intangible assets and investment property		1,656		3,173
a) Loans and advances to customers and banks	1,586	-	3,111	-
b) Financial investments	-30	-	-5	-
c) Property, plant and equipment/intangible assets/investment property	100	-	67	-
Changes in provisions		164		-50
Other non-cash expenses/income		-2,308		-2,494
Profit/loss from disposal of financial investments and property, plant and equipment/investment property		-153		-74
a) Financial investments	-152	-	-65	-
b) Property, plant and equipment/investment property	-1	-	-9	-
Other adjustments		-562		-1,020
<b>Subtotal</b>		<b>-1,134</b>		<b>-367</b>
Changes in loans and advances		7,973		5,793
a) to banks	1,385	-	1,314	-
b) to customers	6,588	-	4,479	-
Changes in trading assets		2,630		2,253
Changes in other assets from continuing operations		1,631		59
Changes in liabilities		-9,265		1,364
a) to banks	-4,889	-	-114	-
b) to customers	-4,376	-	1,478	-
Changes in securitised liabilities		-2,020		-8,966
Changes in trading liabilities		-1,148		-3,046
Changes in other liabilities from continuing operations		-302		-168
Interest and dividends received		3,212		4,380
Interest paid		-2,733		-3,738
Income tax payments		-104		4
<b>Cash flow from operating activities</b>		<b>-1,260</b>		<b>-2,432</b>
Receipts from disposals of		2,483		4,900
a) securities	2,430	-	4,755	-
b) interests in affiliated companies and equity holdings	10	-	18	-
c) property, plant and equipment	43	-	127	-
Purchases of		-1,126		-2,547
a) securities	-1,059	-	-2,429	-
b) interests in affiliated companies and equity holdings	-22	-	-12	-
c) property, plant and equipment	-45	-	-106	-
<b>Cash flow from investing activities</b>		<b>1,357</b>		<b>2,353</b>

**CASH FLOW STATEMENT**

(€ m)	2016	2015
Payments received (+) from subordinated capital	-	-
Payments made (-) from subordinated capital	-	-2,097
<b>Cash flow from financing activities</b>	<b>-</b>	<b>-2,097</b>
<b>Cash and cash equivalents at the beginning of the period</b>	<b>3,394</b>	<b>5,967</b>
Cash flow from operating activities	-1,260	-2,432
Cash flow from investing activities	1,357	2,353
Cash flow from financing activities	-	-2,097
Changes in cash and cash equivalents due to exchange rate fluctuations	-	-397
<b>Cash and cash equivalents at the end of the period</b>	<b>3,491</b>	<b>3,394</b>

Cash and cash equivalents are equivalent to the Cash reserve item in the statement of financial position and comprise cash on hand, balances at central banks, treasury bills, discounted treasury notes and similar debt instruments issued by public-sector bodies and bills of exchange.

The cash flow from operating activities is calculated using the indirect method, whereby the Group net income/loss for the year is adjusted for non-cash expenses (increased) and non-cash income (reduced) and for cash changes in assets and liabilities used in operating activities.

The following cash flows resulted from the obtaining or loss of control over subsidiaries during the financial year:

**CASH FLOW**

(€ m)	Obtaining control	Loss of control
Amount of cash and cash equivalents	2	1

Assets and liabilities of subsidiaries, over which control was obtained or lost during the financial year, comprise the following:

**ASSETS**

(€ m)	Obtaining control	Loss of control
Financial investments accounted for under the equity method	8	-
Investment property	-	10
Other assets	-	1

**LIABILITIES**

(€ m)	Obtaining control	Loss of control
Other liabilities	1	2



# GROUP EXPLANATORY NOTES

## GENERAL INFORMATION

### 1. ACCOUNTING PRINCIPLES

HSH Beteiligungs Management GmbH, Hamburg, is the parent company and, at the same time, the top-level parent company of HSH Nordbank AG, which prepares Group financial statements.

HSH Nordbank AG has issued debt instruments as defined in Section 2 (1) sentence 1 of the German Securities Trading Act (WpHG) on an organised market as defined in Section 2 (5) WpHG and is thus obliged, as a publicly traded company as defined in Regulation (EC) 1606/2002 (IAS Regulation) of the European Parliament and of the Council of 19 July 2002 in conjunction with Section 315a (1) of the German Commercial Code (HGB) to draw up its Group financial statements in accordance with the International Financial Reporting Standards. International accounting standards, hereinafter IFRS or standards, refer to the International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS) and the associated interpretations by the Standing Interpretations Committee (SIC) and the International Financial Reporting Interpretations Committee (IFRIC), published by the International Accounting Standards Board (IASB) and adopted under the IAS Regulation as part of the EU endorsement.

The supplementary provisions of Section 315a HGB are taken into account and are shown individually in Note 69.

The Group financial statements are prepared in accordance with IFRS as published by the IASB and adopted as European law by the European Union (EU).

The Group financial statements of HSH Nordbank are prepared in line with IFRS 10 according to uniform Group-wide measurement and accounting policies. In accordance with IAS 1, the Group financial statements consist of the statement of income, the statement of comprehensive income, the statement of financial position, the statement of changes in equity, the cash flow statement and the explanatory notes, including segment reporting. In addition to the Group financial statements a Group management report in accordance with Section 315 HGB was prepared.

Group income and expenses are accrued on a pro rata temporis basis. They are recognised and disclosed in the period to which they must be assigned economically. Accounting for assets, liabilities, income and expenses takes place on a consistent basis. Deviations are only made in justified exceptional cases which are explained separately in the Notes on the relevant items in the HSH Nordbank Group financial statements.

Unless explicitly stated otherwise, all amounts are in millions of euros (€ m).

The reporting year corresponds to the calendar year.

IFRS 7.31 et seqq. contains rules on presenting risks arising from financial instruments. In this regard, IFRS 7.B6 allows for the possibility of disclosing risk in a suitable medium separate from the Group financial statements. Availing itself of this option, HSH Nordbank has published disclosures about financial instruments as permitted by IFRS 7.31 et seqq. predominantly in the Group risk report within the Group management report. Specifically, this relates to the overall qualitative and quantitative risk information disclosed under IFRS 7.33 et seqq. and the total market risk reporting under IFRS 7.40–42 as well as the description of how liquidity risk is managed as required by IFRS 7.39 (c).

In addition, as part of the supplementary German commercial regulations the Group observed the following German Accounting Standards (GAS) in preparing these Group financial statements and this Group management report:

- GAS 20 Management Reporting
- GAS 17 Reporting on the Remuneration of Members of Governing Bodies.

Apart from the new standards and interpretations stated below, which may have a significant influence on the Group financial statements a number of additional standards and interpretations were adopted which, however, are expected not to have any influence on the Group financial statements.

During the current financial year, the following accounting standards need to be applied for the first time as a matter of principle:

#### **Amendments to IFRS 10, IFRS 12 and IAS 28 - Investment Entities: Applying the Consolidation Exception**

The amendments serve to clarify various questions relating to the application of the exemption from the consolidation obligation under IFRS 10, if the parent meets the definition of an “investment entity”. Parents are accordingly also released from the obligation to prepare consolidated financial statements if the higher-level parent does not

consolidate its subsidiaries, but accounts for them at fair value in accordance with IFRS 10.

Distinctions are applied as follows concerning the accounting treatment of the subsidiaries of an investment entity: Subsidiaries that themselves are investment entities are to be accounted for at fair value in line with the general principle of the investment entity exception. In contrast, those subsidiaries that are not investment entities but provide services relating to the parent company's investment activities, and so could be regarded as an extension of the parent's operation, have to be consolidated.

Finally, it is clarified that an investor which does not meet the definition of an investment entity and applies the equity method to an associate or joint venture may retain the fair value measurement which the investment company applies to its equity holdings in subsidiaries.

In addition, the amendments envisage that an investment entity which measures all its subsidiaries at fair value must provide the information on investment entities as prescribed by IFRS 12.

#### **Amendments to IFRS 11 – Accounting for Acquisitions of Interests in Joint Operations**

IFRS 11 contains rules on the recognition of joint ventures and joint operations on the balance sheet and statement of income. Whilst joint ventures are accounted for using the equity method, the depiction of joint operations as foreseen in IFRS 11 is similar to proportionate consolidation.

With the amendments to IFRS 11, the IASB provides for the accounting treatment of the purchase of shares in a joint operation representing a business entity as defined in IFRS 3 Business Combinations. In such cases the purchaser is to apply the principles of accounting for business combinations as set out in IFRS 3. In addition, the disclosure requirements of IFRS 3 also apply in these cases.

#### **Amendments to IAS 1 – Disclosure Initiative**

The amendments relate to various disclosure issues. It is made clear that information only needs to be included in the Notes if the content is not immaterial. This explicitly also applies if an IFRS requires a list of minimum disclosures. In addition, explanations concerning the aggregation and disaggregation of items in the statement of financial position and statement of comprehensive income are included. Furthermore, it is clarified how shares in the Other operating income of entities measured at equity are to be recorded in the statement of comprehensive income. Finally, the structure template for the Notes no longer applies in order to give greater consideration to the relevance of information for the individual entity.

#### **Amendments to IAS 16 and IAS 38 – Clarification of Acceptable Methods of Depreciation and Amortisation**

With these amendments the IASB provides additional guidelines to define an acceptable method of depreciation and amortisation. Revenue-based methods of depreciation are thus not permitted for property, plant and equipment and are only permitted for intangible assets in certain exceptional cases (refutable presumption of inadequacy).

#### **Amendments to IAS 19 – Defined Benefit Plans: Employee Contributions**

The amendments clarify the rules relating to the allocation of employer contributions or contributions from third parties to service periods, if the contributions are linked to the service period. Furthermore, exemptions are granted, if the contributions are not dependent on the number of completed years of service.

#### **Improvements to IFRS 2010 – 2012**

Amendments to seven standards were made as part of the annual improvement project. Amendments to the wording of the individual IFRS/IAS should serve to clarify the existing rules. There are also amendments that affect the note disclosures. The standards IFRS 2, IFRS 3, IFRS 8, IFRS 13, IAS 16, IAS 24 and IAS 38 are affected by this.

The amendments to IFRS 2 and IFRS 3 are to be applied for transactions that take place on or after 1 July 2014 despite the applicability of the provisions to financial years beginning on or after 1 February 2015.

#### **Improvements to IFRS 2012 – 2014**

Changes were made to four standards as part of the Annual Improvement Project. Amendments to the wording of the individual IFRS/IAS should serve to clarify the existing rules. The standards IFRS 5, IFRS 7, IAS 19 and IAS 34 are affected by this.

The changes to the standards specified as set out above did not materially affect the accounting of HSH Nordbank.

HSH Nordbank is not planning the early application of the following new or amended Standards or Interpretations for which application is only mandatory in later financial years, with the exception of the disclosure requirements under IFRS 9 for financial liabilities designated for measurement at fair value through profit or loss. To the extent not indicated otherwise, all effects on the financial statements of HSH Nordbank are currently under review.

*Already endorsed by the EU:*

### **IFRS 9 – Financial Instruments**

The final version of IFRS 9, published in July 2014, replaces the existing guidelines contained in IAS 39 on the recognition and measurement of financial instruments with regard to classification and measurement, impairment and general hedge accounting.

IFRS 9 is to be applied for the first time, as a mandatory requirement, in financial years beginning on or after 1 January 2018. Early application is permitted. HSH Nordbank will be applying IFRS 9 as of 1 January 2018. IFRS 9 does, however, permit the isolated early application of the financial liabilities designated for measurement at fair value through profit or loss before the date of mandatory initial application of the Standard. HSH Nordbank will be making use of this option and, as of 1 January 2017, will be reporting the credit risk-induced fair value changes in its own liabilities for which the fair value option was exercised (see Note 8) in other comprehensive income (OCI), i.e. not through profit or loss. Application shall be retrospective within the framework of the categorisation provisions set out in the valid IAS 39. As a result of the early application of the recognition provision, the effect from the credit risk-induced valuation of the Bank's own liabilities, which was recognised in the income statement in the past, in the amount of € 13 million (in cumulative terms from the previous years in retained earnings) will be reclassified from retained earnings to the new reserve for credit risk-induced valuation results of liabilities designated at fair value within equity. This means that, as of 1 January 2017, future credit risk-induced valuation effects will no longer be recognised in the income statement, but rather in other comprehensive income, i.e. not through profit or loss; accumulated contributions to earnings recognised in other comprehensive income will be recognised in equity in the reserve for credit risk-induced valuation results of liabilities designated at fair value. The valuation results from the Bank's own credit risk recognised in equity via the other comprehensive income will not be recognised through profit or loss via the income statement at any time, i.e. not even upon repayment or repurchase.

HSH Nordbank has been making intensive preparations as part of several projects since the end of 2014 for the initial application of IFRS 9. The purpose of the projects is to fully implement the new requirements related to classification, hedge accounting and the determination of loan loss provisions (impairment) into the IT systems and processes concerned. Besides adjustments to existing IT systems, new software will also be introduced. This applies in particular to the topic of the complex new rules for determining loan loss provisions. Another objective of the projects is to initially classify and measure all instruments within the scope of IFRS 9 and to prepare an opening balance sheet as at 1 January 2018 in accordance with IFRS 9 including a reconciliation with the closing balance sheet as at 31 December 2017. The first interim financial statements in 2018 will therefore be prepared in accordance with IFRS 9.

The projects have completed the first functional specification phase. At the moment, the functional concepts are being updated to reflect the most recent status of interpretation and new findings. The IT implementation phase is ongoing in parallel. The first few IT implementation projects have already been completed and successfully tested. The IT implementation projects are scheduled for completion in 2017, the aim being to start the integration test in the second quarter.

The new regulations set out in IFRS 9 will result in valuation effects to be recognised in equity in the opening balance sheet at the time of initial application. A sufficiently reliable, precise quantification of the impact of IFRS 9 is currently not yet possible. The impact is being estimated in several test calculations that are gradually being refined on the basis of the further development of models, systems and data.

The following sections compare the main changes resulting from the application of IFRS 9 compared with IAS 39. They also address the likely material, specific effects for the Bank and the use of options based on the current status of the implementation projects at HSH Nordbank. The statements are based on the current specification/decision-making status of the implementation projects. Amendments and supplements may be made as the projects progress up until the time of initial application. This also includes the potential for changes in the interpretation of certain IFRS 9 requirements.

#### **A) Classification and measurement**

IFRS 9 introduces a new categorisation model for financial assets. They are classified into measurement categories on the basis of the business model (portfolio level) or the contractual terms or cash flow characteristics (instrument level). A distinction is made between the amortised cost (AC), fair value through other comprehensive income (FVOCI, measurement at fair value directly in equity) and fair value through profit or loss (FVPL, measurement at fair value through profit or loss) measurement categories.

The new IFRS 9 categorisation model will result in different valuation categories compared with IAS 39 for certain portfolios/individual transactions involving financial assets within HSH Nordbank's portfolio. This will likely expand the scope of instruments to be valued at FVPL/FVOCI.

As a result of the business model condition, HSH Nordbank expects, based on the current analysis status of the implementation project, the following effects at the time of initial application of IFRS 9, insofar as these effects can be predicted at present (the assessment is based on the business model/circumstances at the time of initial application):

Within the securities portfolio (capital markets business), a large part of the portfolio that is not held for trading and is allocated to the LaR category under IAS 39 (AC valuation category) is expected to be reclassified to the FVOCI category under IFRS 9.

In the loan portfolio (lending business), the business model is expected to be a “hold” business model at the time of initial application meaning that – provided that the cash flow condition at the level of the individual instrument does not stand in the way of this – measurement will be at AC, as under IAS 39. By way of derogation from this principle, syndication shares from new business syndication are to be allocated to a separate portfolio that is to be measured at FVPL.

Due to the cash flow condition, HSH Nordbank expects, based on the current analysis status of the implementation project, the following effects at the time of initial application of IFRS 9:

The vast majority of the securities portfolio (capital market business) is likely to meet the criterion relating to the cash flow condition. There are also structured holdings that will breach the cash flow condition. Material reclassifications from the IAS 39 LaR category (AC valuation category) to the IFRS 9 FVPL category will be made for securitisation items in the credit investment business (contractually linked instruments, e.g. asset backed securities). This is because certain categories do not satisfy the cash flow criterion due to specific contractual features or due to the credit risk test at tranche level provided for in IFRS 9.

As far as the loan portfolio (lending business) is concerned, the overwhelming majority of the instruments are to be classed as basic lending arrangements within the meaning of IFRS 9, i.e. the contractual terms of these transactions satisfy the cash flow condition. There will also be loans that breach the cash flow condition, meaning that, at the time of initial application, they will be reclassified from the IAS 39 LaR category (AC valuation category) to the IFRS 9 FVPL category. The reason for the breach of the cash flow condition lies in certain detrimental side agreements or non-recourse financing where there was a substantial property/project risk on the commitment date, meaning that the payments depend, in economic terms, to a considerable degree on the property being financed.

Based on the current decision-making status – which is not yet final – HSH Nordbank does not plan to make use of the FVOCI categorisation option for equity instruments within the scope of IFRS 9.

The provisions governing the classification and measurement of financial liabilities remain largely unchanged compared with IAS 39. There will, however, be changes to disclosures for financial liabilities designated at fair value. As far as these liabilities are concerned, fair value changes resulting from the Bank's own credit risk are no longer to be disclosed through profit or loss in the income statement, but rather directly in equity in other comprehensive income (OCI) as a

general rule (cf. also the comments made on the early isolated application of this recognition provision at the beginning of this section).

Under IFRS 9, the separation rules for embedded derivatives will only apply for host contracts that are financial liabilities or not of a financial nature.

## **B) Impairment**

The introduction of IFRS 9 will replace the current model used to calculate loan loss provisions/impairments under IAS 39, which is based on incurred losses, with a model based on the expected credit losses. The scope of the new model consistently includes all financial instruments that are recognised at amortised cost or at fair value through other comprehensive income, irrevocable loan commitments and financial guarantees that are not recognised at fair value through profit or loss, leasing receivables and contract assets.

The calculation of loan loss provisions under the new impairment model will involve making a distinction between provisioning levels. Allocation to a provisioning level is based on whether the loan default risk associated with a financial instrument has increased significantly since it was first added to the portfolio and/or whether the financial instrument has an impaired credit rating, i.e. is credit-impaired. The minimum loan loss provisions correspond to the 12-month expected loss (level 1). If the loan default risk associated with a financial instrument has increased significantly since it was first added to the portfolio and/or it is credit-impaired, then the loan loss provisions set up correspond to the lifetime expected loss (level 2/3).

HSH Nordbank calculates expected credit losses at levels 1 and 2 based on the following credit risk parameters:

- Probability of default (PD)
- Loss given default (LGD)
- Exposure at default (EAD)

The internal credit risk models which – where necessary – are adjusted for the purposes of IFRS 9 are taken as a basis in this regard.

Any necessary adjustments/expansions of the existing models relate primarily to the implementation of methods for multiannual estimates. Within this context, HSH Nordbank uses PD profiles based on migration matrices for its multiannual estimates. These reflect the observed rating migrations from debtors within a year and are calculated based on an extensive cross-economic historical observation period. The forward projection of the LGD over the multiannual period is based primarily on the expected collateralisation ratio of the financial instrument, which comprises the expected collateral value and the expected amount of the receivable. EAD modelling for the on-balance sheet business is used to project the gross carrying amount forward over the multiannual period, taking amortisation and repayment effects into account. Within this context, fixed cash flows that have been contractually agreed and expectations regarding the exercise of



options and their impact on the cash flows are taken into account. For off-balance sheet business, the estimate of the expected future draw-down is based on the borrower's expected drawing behaviour over a multiannual period.

In addition, the credit risk parameters are expanded to include information relating to the future – if necessary.

The 12-month expected loss is calculated by multiplying the (one-year) credit risk parameters. The lifetime expected loss is calculated by multiplying the period-specific credit risk parameters determined during the term. Discounting to the balance sheet date is based on the effective interest rate in each case.

In order to assess a significant increase in the loan default risk of a financial instrument, HSH Nordbank uses internal ratings as the main characteristic. Other characteristics (e.g. default days) are also used to allocate financial instruments to specific levels.

The extent giving rise to a significant deterioration in credit quality (significance threshold) is to be determined for each portfolio or rating category segment in a manner that is specific to the initial rating and on the basis of a statistical quantile assessment. If a change in rating that is defined as significant is exceeded, then the financial instrument in question is allocated to level 2. Otherwise, it remains in level 1.

A financial instrument is transferred from level 2 to level 1 if the loan default risk is no longer significantly increased based on the rating-based classification described above.

Defining level 3 of the impairment model involves assessing, on each balance sheet date, whether there are objective indications of an impairment that could have a detrimental impact on the expected future cash flows from the financial instrument. The criteria for impairment are consistent with those that apply to supervisory law default and essentially include major financial difficulties for the borrower and indications that, based on current information, interest payments cannot be made and an improvement in the financial situation cannot be demonstrated.

Loans and securities with objective evidence of impairment are accounted for by setting up specific loan loss provisions for the receivable in question. To calculate the amount of the specific loan loss provisions, the net present value of the anticipated cash flows arising from the loan or advance – that is, achievable amount – is compared to its gross carrying amount. The anticipated cash flows may comprise capital repayments, interest payments or the proceeds from disposal of collateral less liquidation costs. The realisable amount is calculated using various scenarios and compared against the gross carrying amount.

If the gross carrying amount is higher than the realisable amount for the scenario in question, then this scenario results in a loss in the amount of the difference. The specific loan loss provision is set up in the amount of the weighted average losses from among the various scenarios.

In the subsequent periods, loan loss provisions are adjusted to reflect changes in the estimates for the expected cash flows and changes in the gross carrying amount. Changes in the gross carrying amount result not only from incoming payments that reduce the gross carrying amount, but also from interest claims. These claims increase the gross carrying amount and, as a result, the loan loss provisions. This increase is to be recognised with no effect on profit and loss. The collection of the interest for credit-impaired instruments, which is recognised through profit or loss, is based on the net carrying amount, as under IAS 39.

Compared to the existing model under IAS 39, the new impairment model results in loan loss provisions being recognised earlier and in a higher amount. For those transactions that are to be allocated to levels 1 and 2 of the new loan loss provisioning model, loan loss provisions are expected to increase considerably compared with IAS 39 at the time of initial application.

As well as the new provisions governing impairment, IFRS 9 also contains new requirements governing how contractual modifications are taken into account. In cases involving substantial modifications resulting in the derecognition of the financial instrument in the balance sheet, the provisions continue to apply unchanged as against the IAS 39 provisions. In cases involving modifications not classed as substantial that do not result in the derecognition of the asset in the balance sheet, the gross carrying amount of the asset is adjusted. The new gross carrying amount is given by the present value of the modified cash flows using the financial instrument's original effective interest rate for discounting. The adjustment of the gross carrying amount results in a modification gain or loss that has to be recognised through profit or loss.

Based on the current findings of the implementation project, the overwhelming majority of modified assets will have to be allocated to level 3. At this level, the adjustment of the carrying amount generally results in an offsetting adjustment to the loan loss provisions in the same amount.

**C) Hedge accounting**

IFRS 9 includes various changes to hedge accounting rules compared to IAS 39. However, new rules for the recognition of (dynamic) portfolio or macro hedges respectively are not included in IFRS 9. As a result, options apply allowing for the continued application of existing IAS 39 provisions. HSH Nordbank will make use of the option provided for in IFRS 9.6.1.3 to apply the hedge accounting provisions set out in IAS 39 to portfolio fair value hedges on interest rate change risks.

**IFRS 15 – Revenue from Contracts with Customers as well as amendments to IFRS 15: Date of initial application of IFRS 15**

IFRS 15 Revenue from Contracts with Customers sets out a comprehensive framework for determining whether, at what level and when revenue is recognised. It replaces existing guidelines on recognising revenue, including IAS 18 Revenue, IAS 11 Construction Contracts and IFRIC 13 Customer Loyalty Programmes.

IFRS 15 is to be applied for the first time in financial years beginning on or after 1 January 2018. Early application is permitted.

Based on the current status of its analyses, HSH Nordbank does not expect to see any material impact on the Group financial statements.

*EU endorsement still pending:*

**IFRS 16 Leases**

IFRS 16 provides a single model regarding how lessees are to recognise leases in their balance sheets. A lessee recognises a right-of-use asset, representing its right to use the underlying asset, and a lease liability, representing its obligation to make lease payments. Exceptions apply to short-term leases and leases for low-value assets. Accounting at the level of the lessor is comparable to the current standard – i.e. the lessor continues to classify leases as finance or operating leases.

IFRS 16 replaces the existing guidelines on leases, including IAS 17 Leases, IFRIC 4 Determining Whether an Arrangement Contains a Lease, SIC-15 Operating Leases – Incentives and SIC-27 Evaluating the Substance of Transactions in the Legal Form of a Lease.

Subject to the still-pending adoption into EU law, IFRS 16 needs to be applied for the first time in the first reporting period in a financial year starting on or after 1 January 2019. Early application is permitted for companies that apply IFRS 15 Revenue from Contracts with Customers at the time of the initial application of IFRS 16 or before.

The planned changes are not expected to have any significant impact on accounting at HSH Nordbank.

**Amendments to IFRS 10 and IAS 28 – Sale or Contribution of Assets between an Investor and its Associate or Joint Venture**

The amendments address a known inconsistency between the provisions in IFRS 10 and those in IAS 28 (2011) in the event of the sale of assets to an associate or joint venture and/or the contribution of assets to an associate or joint venture.

Under IFRS 10 a parent must recognise total profit or loss from the sale of a subsidiary on the statement of income when control is lost. In contrast, the currently applicable IAS 28.28 requires that the sale proceeds in the case of sales transactions between an investor and an equity holding measured at equity – whether it is an associate or a joint venture – are only recognised in the amount of the share of the other shareholders in this entity.

In future, the entire profit or loss on a transaction is only to be recognised if the sold or received assets constitute a business operation as defined in IFRS 3. This applies regardless of whether the transaction is structured as a share or asset deal. Conversely, if the assets do not constitute a business operation, it is only permissible to recognise proportionate net income.

Initial application of the amendments was postponed for an indefinite period of time by the IASB on 17 December 2015.

**Amendments to IFRS 15 – Clarifications to IFRS 15**

The changes include, for one thing, clarifications regarding various provisions of IFRS 15 and, for another, simplifications regarding the transition to the new standard.

Over and above the clarifications, the amended standard includes two further expedients designed to reduce the cost and complexity associated with the transition to the new standard. These relate to options relating to the presentation of contracts that were either concluded at the start of the earliest period shown or were amended before the start of the earliest period shown.

Subject to the still-pending adoption into EU law, the changes are to be applied for the first time as at 1 January 2018.

Based on the current status of its analyses, HSH Nordbank does not expect to see any material impact on the Group financial statements.

#### **Amendments to IAS 7 – Disclosure Initiative**

The amendments aim to improve the information on changes to the company's debt. In line with the amendments, companies have to provide information on the changes in financial liabilities whose inflows and outflows are shown under cash flow from financing activities in the cash flow statement. Corresponding financial assets are also to be included in the disclosures (e.g. assets from hedging transactions).

Information is to be provided on cash changes, changes arising from the acquisition or disposal of companies, changes relating to foreign exchange rates, changes in fair values and other changes.

The IASB proposes that the information be provided in the form of a reconciliation between the opening and closing balances in the statement of financial position, but also allows for other forms of presentation.

Subject to the still-pending adoption into EU law, the changes need to be applied for the first time in the first reporting period in a financial year starting on or after 1 January 2017. Earlier application is permitted.

#### **Amendments to IAS 12 – Recognition of Deferred Tax Assets for Unrealised Losses**

The amendments clarify the recognition of deferred tax assets for unrealised losses that are related to debt instruments measured at fair value.

Subject to the still-pending adoption into EU law, the changes need to be applied for the first time in the first reporting period in a financial year starting on or after 1 January 2017. Earlier application is permitted.

The planned changes will not have any significant impact on accounting at HSH Nordbank.

#### **Amendments to IAS 40 – Transfers of Investment Property**

The amendment to IAS 40 serves to clarify the cases in which properties start/stop being classified as "investment property" if they are under construction or development. The previous exhaustive list in IAS 40.57 did not set out clear provisions on the classification of properties that had not yet been completed. The list is now explicitly designated as non-exhaustive, meaning that properties that have not yet been completed now also fall under the scope of the provisions.

Subject to the still-pending adoption into EU law, the amendment needs to be applied for the first time in the first reporting period in a

financial year starting on or after 1 January 2018. Early application is permitted.

#### **IFRIC 22 Foreign Currency Transactions and Advance Consideration**

IFRIC 22 addresses a question relating to the application of IAS 21 The Effects of Changes in Foreign Exchange Rates. The Interpretation clarifies the time at which the exchange rate is to be calculated for the translation of foreign currency transactions that include the receipt or payment of advance consideration. According to the Standard, the decisive date for the purpose of determining the exchange rate for the underlying asset, income or expense, is the date of initial recognition of the asset or liability resulting from the advance consideration.

Subject to the still-pending adoption into EU law, the Interpretation needs to be applied in the first reporting period in a financial year starting on or after 1 January 2018. Early application is permitted.

#### **Improvements to IFRS 2014 – 2016**

The Annual Improvements to IFRSs (2014 – 2016) amended three IFRSs. In IFRS 12, the amendments clarify the scope of the standard by specifying that the disclosure requirements in IFRS 12, except for those in IFRS 12.B10–B16 (financial information), also apply to an entity's interests in subsidiaries, joint ventures or associates that are classified as held for sale in accordance with IFRS 5. IAS 28 clarifies that the election to measure an investment in an associate or a joint venture that is held by an entity that is a venture capital organisation, or other qualifying entity, can be exercised differently for each investment. The short-term exemptions in IFRS 1.Appendix E (IFRS 1.E3 – E7) were also deleted for entities applying the IFRS for the first time.

Subject to adoption into EU law, the amendments to IFRS 12 are to be applied for the first time in the first reporting period in a financial year starting on or after 1 January 2017, while the amendments to IFRS 1 and IAS 28 are to be applied for the first time in the first reporting period in a financial year starting on or after 1 January 2018. Early application is permitted.

#### **Going concern assumption**

Accounting and measurement are based on the assumption that the Bank is a going concern. The Bank's corporate planning forms the basis for the going concern assumption. Assessments, which form the basis for the corporate planning and in particular the planning for the

movement in loan loss provisions over the long-term, the payment default plan and the resultant actual drawdown of the second loss guarantee, take information available to us at this point in time into account. These assessments are dependent on factors that are mostly outside the control of the Bank and are therefore subject to a significant degree of uncertainty. This applies, for example, to expectations regarding macroeconomic trends, exchange rates, freight and charter rates or changes in the regulatory framework. Furthermore, the very long planning horizon for the long-term loan loss provision planning is causing significant uncertainty. One key assumption used in corporate planning in view of the ongoing sale process of HSH Nordbank AG is the overall sale of HSH Nordbank AG as a whole, i.e. the sale of all shares in the Bank held by the seller, including all assets and liabilities, as a preferred solution without any material early disposals of assets or sub-areas at amounts below the carrying amount in the event of outstanding bids for an overall sale. In its forecasts and assumptions, the Bank has assumed the sale of the overall bank, as scheduled, adhering to the time schedule agreed in the agreed list of conditions and commitments. Within this context, it is assumed that the viability assessment to be performed by the European Commission following a successful change of ownership will have a positive outcome, meaning that the Bank will comply with all of the agreements reached in the EU proceedings. As it is not possible to objectively predict the course and outcome of the privatisation process, the process involved in the sale of HSH Nordbank AG creates considerable uncertainty regarding the implementation of the corporate planning, the determination of the loan loss provisions and accounting and measurement. Additional assumptions, uncertainties, opportunities and risks of corporate planning as well as the structural measures are discussed in the Group Management Report in the section Forecast, opportunities and risks report.

The assumption of the Bank as a going concern for accounting and measurement purposes and the assumption of the continued going concern of HSH Nordbank AG and significant group companies is based in particular on the fact that

- (i) the agreements required for the implementation of the decision taken by the EU Commission in the EU state aid proceedings on the replenishment of the second loss guarantee are entered into comprehensively and on a timely basis and that the decision will be implemented by HSH Nordbank AG and its shareholders in full and on a timely basis.
- (ii) the operating company, HSH Nordbank AG, is sold at a positive sales price in an open, non-discriminatory, competitive and transparent process not involving state aid until 28 February 2018 and the EU Commission grants its approval for the acquisition following a viability assessment of the new corporate structure. Should the divestment procedure not lead to offers not requiring state aid with a positive price being offered before the expiry of the deadline or should the EU Commission in the course of its viability assessment come to the conclusion that the integration of the operating company into the new corporate structure will not lead to a viable business model that is profitable in the long term, the operating company will cease new business and manage its assets as far as legally permissible with the aim of a structured winding down of its business. In the event that the Bank is wound down as a result of the above or for other reasons, or if its rating is downgraded or other adverse developments emerge during the privatisation period, it could trigger outflows of short-term funds and fundamentally restrict HSH Nordbank's funding options. In the case of major unexpected fund outflows, additional measures will need to be taken by the owners and/or third parties to strengthen the liquidity situation.
- (iii) as part of the ongoing privatisation process of HSH Nordbank AG, HSH Nordbank AG will be sold in full as a whole bank, i.e. the shares in the Bank held by the seller will be disposed of, including all assets and liabilities, without any material early disposals of assets or sub-segments at prices below the carrying amount in the event of outstanding bids for an overall sale. If extensive sales of loan portfolios, particularly in the Non-Core Bank, are required, it could result in significant additional loan loss provision expenses that are not compensated for by the guarantee, and could require material depreciation of deferred taxes.
- (iv) the minimum capital requirements at all regulatory levels can be adhered to in accordance with the corresponding SREP resolutions passed by the European Central Bank and the statutory provisions during the forecast period. If there is a need for significant additional loan loss provision expenses and material depreciation of deferred taxes (e.g. in the scenario described above) or if the recovery of the shipping market that has been assumed in the Bank's corporate planning does not materialise as planned, or the significant risk transfer for the second loss guarantee is no longer ensured from the perspective of the banking supervisory authority, it could put considerable pressure on the capital ratios and additional measures may need to be taken by the owners and/or third parties to strengthen the capital ratios in order to be able to adhere to the minimum capital requirements, particularly at the level of the financial holding group. If such measures are not taken, it could result in the winding down of HSH Nordbank.



It is further required that acceptance by market participants and other relevant stakeholders necessary for the successful implementation of

HSH Nordbank AG's business model and the requirements under the formal decision of the EU Commission is maintained or gained.

## 2. EVENTS AFTER THE REPORTING DATE

### Sale of the first tranche of the market portfolio

As part of the decision made by the European Commission in the EU state aid proceedings on the replenishment of the second loss guarantee on 2 May 2016, the sale of non-performing loans totalling € 3.2 billion on the market was approved. Within this context, the Bank selected key portfolios that were to be sold on the market by mid-year 2017 (market portfolio). The winding-down of the NPE portfolio will gradually improve the portfolio quality and continue to relieve the Bank of considerable legacy burdens. The defined market portfolio consists of the four non-strategic legacy portfolios Aviation, Continental European Commercial Real Estate (Scandinavia, Netherlands, Germany), Energy and International Real Estate.

As at 27 January 2017, purchase agreements were signed for the first tranche of the market portfolio, which includes, among other things, aircraft financing (volume of around € 0.8 billion EaD) and continental European commercial real estate (volume of around € 0.5 billion EaD). The aircraft portfolio was bought by the Australian investment bank Macquarie, while the real estate loans were purchased by Bank of America Merrill Lynch. The parties to the transaction agreed not to

disclose any information on the purchase price. The purchase agreements are subject to the approval of the antitrust authorities, which, insofar as it has not yet been granted, is scheduled to be granted in the second quarter of 2017. There are further closing conditions for the aircraft financing, including technical aircraft assessments that could have further implications (e.g. purchase price adjustments or withdrawal from the agreements). As a result, the transfer in rem of the commitments and, as a result, the de facto removal from the balance sheet is likely to take place in the first half of 2017 (closing). The deal relating to the real estate loans was closed on 3 March 2017. The impact on the valuation of the receivables and aircraft concerned was taken into account in the Group financial statements as at 31 December 2016.

HSH Nordbank achieved further relief in connection with the market transaction of around € 0.3 billion with individual sales to further investors and as a result of repayments within the portfolio that was originally up for sale.

## 3. PROVISION OF A GUARANTEE FACILITY

### I. Second loss guarantee of HSH Finanzfonds AöR

#### Basics of the effect of the second loss guarantee

On 2 June 2009, the Federal State of Schleswig Holstein and the Free and Hanseatic City of Hamburg granted HSH Nordbank AG a guarantee facility in the amount of € 10 billion via the HSH Finanzfonds AöR as the guarantor in order to secure the future of the Bank. This agreement on the provision of a guarantee facility as well as a related recapitalisation of the Bank are subject to approval by the European Commission in accordance with the law regarding state aid. The EU Commission concluded these state aid proceedings at the end of September 2011 and entered into an agreement on commitments with all the parties involved and imposed conditions. The conditions include a prohibition on the payment of dividends until and including the financial year 2014, among other things. The guarantee of the federal states is split into two partial guarantees for financial reporting purposes. Partial guarantee One is recognised in the Group financial

statements as a financial guarantee contract in accordance with IAS 39.9. Partial guarantee Two is recognised as a credit derivative.

The guarantor guarantees actual rating-related defaults on financial instruments selected based on certain defined criteria that form part of the assets of HSH Nordbank AG.

The amount of default on a specific commitment is determined by the amount outstanding, taking into account the specific loan loss provision existing as at 31 March 2009. The amount outstanding is at the most the amount repayable as at 31 March 2009, plus all interest owed and other ancillary payments. Losses may only be allocated under the guarantee once the guarantee case has been examined and approved by the guarantor.

The guarantee expires when it is returned to the guarantor after the last reference commitment in the hedged portfolio has been met irrevocably and in full or has resulted in a guarantee case for the full

amount. Since 2014 it is possible for HSH Nordbank AG to terminate the guarantee in full.

2011 the guarantee was reduced by a total of € 3 billion to € 7 billion. The guarantee facility was replenished as at 30 June 2013 by € 3 billion to the original amount of € 10 billion. The guarantee agreement was adjusted by way of an appropriate amendment agreement. Under this agreement the fee provisions for the replenished guarantee remain essentially unchanged. A one-off payment of € 275 million became payable, however, for the re-increased amount on the coming into force of the amendment agreement. Through this the guarantor is put in a position as if the guarantee had never been reduced. The one-off payment represents a fee for a time-related service and is amortised over the period of the expected benefit. In 2016, € 22 million was recognised through profit or loss in the Expenses for government guarantees line item (previous year: € 69 million).

The amendment agreement also included new stipulations concerning the capital protection clause which took effect on 1 January 2014. Insofar as the obligation to pay the additional premium would have the effect of decreasing the Tier 1 capital ratio (both from an ex post and ex ante perspective) excluding hybrid capital (common equity ratio) of HSH Nordbank to below 10% (minimum common equity ratio) or of increasing an already existing shortfall, the guarantor is obliged to waive the portion of the entitlement that would result in the ratio falling below the minimum common equity ratio against the issue of a debtor warrant (so-called capital protection clause).

Since January 2014, HSH Nordbank calculates the supervisory capital ratio on the basis of IFRS data (until 31 December 2013 HGB data were used). To cover a scenario in which the common equity ratio fell below 10%, a waiver by the guarantor HSH Finanzfonds AöR was recognised to income from the additional premium. However, under the new provisions of the capital protection clause, a debtor warrant was no longer issued immediately upon declaration of the debt waiver but was subject to certain conditions. Only when these conditions are met did the obligation from the debtor warrant arise.

In exchange for the guarantee HSH Nordbank AG paid a contractually agreed base premium of 4% p.a. on the guarantee volume outstanding at the time up until 31 December 2015. Drawdowns did not reduce the calculation basis. The recurring base premium payable was recognised through profit or loss on an accrual basis in the Expenses for government guarantees line item.

As long as and insofar as a cash drawdown of the guarantee is not yet made through the invoicing of losses that in total exceed the first loss piece of € 3.2 billion to be borne by the Bank, a claim for compensation against HSH Finanzfonds AöR cannot be recognised. Against this background the hedging effect of partial guarantee One recognised in the balance sheet is accounted for on a net basis. The Bank initially determines specific and general loan loss provisions without taking the hedging effect of the second loss guarantee into account and then

records the balance sheet hedging effect through the use of a compensation item that reduces the loan loss provision amount disclosed on the balance sheet accordingly. The specific and general loan loss provisions recognised are not changed by the accounting applied to the hedging effect. The hedging effect of partial guarantee Two is not disclosed separately as a compensation item in Loan loss provisions but in a separate line item in the statement of financial position and the statement of income within the framework of accounting for the credit derivative at fair value.

The compensation item was reduced by the additional premium imposed by the EU Commission in the amount of 3.85% p.a. This additional premium was only to be paid to HSH Finanzfonds AöR in the case of an actual drawdown of the guarantee. The additional premium was payable at the latest until 31 December 2019 and was to cease to apply retroactively in the event that the guarantee was not drawn down. The current hedging effect of the second loss guarantee was used as the measurement basis for calculating the additional premium (ex post). The anticipated total loss payable by the guarantor was the measurement basis for the calculation of the additional premium (ex ante).

Insofar as it was more likely than not that the guarantee would be drawn down, the premiums to be paid in the future also needed to be recognised (on a present value basis) as loan collateral expense, as, according to the guarantee agreement, drawdowns did not reduce the basis for calculating the guarantee premiums. The future premiums resulted in a reduction of the compensation item as does the additional premium. The present value calculation gave rise to an interest effect, which was disclosed under Net interest income.

If, during the restructuring and workout programme, measures consistent with the guarantee are implemented in respect of hedged commitments that conflict with recognition of the hedging instrument in the financial statements as a financial guarantee under IAS 39.9, commitments may be transferred to the partial guarantee Two under the framework agreement that falls under the definition of a credit derivative under IFRS, subject to approval from the trustee appointed by the guarantor. The maximum guarantee amount is not altered by the revival of partial guarantee Two and the respective partial amounts offset each other.

#### **Decision made by the European Commission in the EU state aid proceedings**

On 2 May 2016 the EU Commission issued a formal decision in the current EU state aid proceedings and thereby approved the replenishment of the second loss guarantee provided by the federal states from € 7.0 billion to € 10.0 billion. The decision is based on a catalogue of conditions and commitments provided by the Federal Republic of Germany to the EU Commission. Based on this catalogue, HSH Nordbank has to provide the holding with liquidity in the amount of

€ 50 million to ensure its operations and make a one-off payment of € 210 million to the holding company.

The holding company was set up as HSH Beteiligungs Management GmbH on 20 May 2016 and was entered in commercial register B of the Local Court (Amtsgericht) of Hamburg on 13 June 2016. The abovementioned payments were made on 30 June 2016. They had already been included in the compensation item "Remaining payment obligations for guarantee premiums" as at 31 December 2015, meaning that they were utilised in the financial year.

In exchange for the guarantee HSH Nordbank AG has been paying a contractually agreed base premium of 2.2% p.a. on the guarantee volume that has not yet been drawn down since 1 January 2016. The recurring base premium payable is recognised through profit or loss on an accrual basis in the Expenses for government guarantees line item. The guarantee premium expense that is attributable to partial guarantee Two (credit derivative) is taken into account when calculating the market value of the credit derivative. The other fee components of the guarantee (base premium on the utilised portion of the guarantee, base premium of 1.8% p.a. on the nominal amount of the guarantee, additional premium) were assumed by the newly established holding company.

Due to a binding statement of the Free and Hanseatic City of Hamburg and the Federal State of Schleswig-Holstein vis-à-vis HSH Nordbank AG already existing as at the reporting date 31 December 2015 with regard to the assumption of guarantee obligations (additional premium and parts of the base premium), it had become unlikely that future premium payments excluding those payments still to be expected after the decision of the EU Commission (one-off payment of € 210 million and provision of liquidity of € 50 million to the holding company) would be made by HSH Nordbank. As a result, the obligations recognised in the compensation item in the past, as well as the debt waiver, had already been derecognised through profit or loss as at 31 December 2015.

#### **Accounting impact of the second loss guarantee in the 2016 financial year**

The hedging effect of the financial guarantee granted by the Free and Hanseatic City of Hamburg and the Federal State of Schleswig-Holstein via HSH Finanzfonds AöR, which was reported on the face of the balance sheet for the first time as at 31 December 2010, amounted to € 7,854 million as at 31 December 2016 (previous year: € 7,422 million).

As at 31 December 2016 a compensation item disclosed on the balance sheet of € 7,854 million (31 December 2015: € 7,162 million) results from the hedging effect of partial guarantee One which is offset under the Loan loss provisions item. An amount of € 2,284 million (previous year: € 3,077 million) has been taken into account, with a positive effect, under loan loss provisions in the statement of income.

The compensation item on the balance sheet includes compensation claims of HSH Nordbank AG vis-à-vis the guarantor in the total amount of € 409 million, as the settled payment defaults under the guarantee exceeded the first loss piece to be borne by the Bank of € 3.2 billion as at 31 December 2016. This means that HSH Nordbank AG now has a contractual entitlement to loss compensation with regard to the main claims in default and the interest accrued. The payments already made amount to € 1.9 billion as at 31 December 2016.

The partial guarantee Two is disclosed as a credit derivative under the "Credit derivative under the second loss guarantee" line item. Changes in the measurement of the credit derivative at fair value are disclosed under the "Hedging effect of the credit derivative second loss guarantee" line item in the statement of income. The fair value of the partial guarantee Two was € 199 million as at 31 December 2016 (previous year: € 663 million). Expense of € -475 million (previous year: income of € 658 million) has been recognised under the "Hedging effect of credit derivative under the second loss guarantee" line item in the statement of income.

The drop in the fair value of the credit derivative as at 31 December 2016 is due to the sale of the loan receivable portfolio that is secured under partial guarantee Two to hsh portfoliomanagement AöR. The reduction in the positive market value of the credit derivative resulting from the settlement of losses associated with the transactions hedged using the second loss guarantee and the associated expense entry under the "Hedging effect of credit derivative under the second loss guarantee" line item in the statement of income is offset by the capitalisation, affecting income, of a compensatory claim under partial guarantee Two vis-à-vis the guarantor in the compensation item in the balance sheet in the amount of € 32 million, as well as payments already made in the amount of € 740 million (previous year € 0 million).

In addition, transactions had to be reallocated from partial guarantee One to partial guarantee Two because they no longer met the requirements for recognition under the financial guarantee.

**HEDGING EFFECT OF THE SECOND LOSS GUARANTEE**

(€ m)	2016		2015		2016		2015		
	Balance sheet		Balance sheet		Statement of income		Statement of income		
	Loan loss provisions	Credit derivative	Loan loss provisions	Credit derivative	Loan loss provisions	Hedging effect credit derivative	Loan loss provisions	Interest	Hedging effect credit derivative
Hedging effect before guarantee costs	7,854	–	7,422	–	432	–	2,423	–	–
Additional premium ex post	–	–	–	–	–	–	1,123	–	–
Debt waiver	–	–	–	–	–	–	–781	–	–
Base and additional premium ex ante	–	–	–	–	–	–	572	3	–
Claim for compensation of interest	–	–	–	–	–	–	–	8	–
Remaining payment obligations for guarantee premiums	–	–	–260	–	–	–	–260	–	–
<b>Compensation under the second loss guarantee</b>	<b>7,854</b>	<b>–</b>	<b>7,162</b>	<b>–</b>	<b>432</b>	<b>–</b>	<b>3,077</b>	<b>11</b>	<b>–</b>
Payments to HSH Finanzfonds AöR	–	–	–	–	1,852	–	–	–	–
Fair value credit derivative	–	199	–	663	–	–475	–	–	658
<b>Hedging effect of the guarantee</b>	<b>7,854</b>	<b>199</b>	<b>7,162</b>	<b>663</b>	<b>2,284</b>	<b>–475</b>	<b>3,077</b>	<b>11</b>	<b>658</b>

Taking into account the compensation payments of HSH Finanzfonds AöR already received for credit losses in the hedged portfolio of € 1,852 million (previous year: € 0 million) and the hedging effect resulting from the credit derivative measured on the reporting date (protection leg) in the amount of € 204 million, the utilisation of the guarantee as at 31 December 2016 comes to € 9,911 million (previous year: € 7,422 million). Since the 2009 reporting year the Bank has recorded premium expense totalling € 3,706 million for the provision of the second loss guarantee. € 3,659 million has been paid to date, of which € 2,624 million is attributable to the current base premium and € 1,035 million to one-off payments (thereof € 260 million to HSH Beteiligungs Management GmbH).

## II. Synthetic securitisation transaction

In the fourth quarter of 2016, largely for capital management reasons, HSH Nordbank AG securitised loan receivables from the Corporate Clients and Real Estate Clients areas accounting for a volume of € 3 billion in total. By way of a financial guarantee, this involves the transfer of the default risk associated with a mezzanine tranche (with an initial amount of € 235 million) to an unconsolidated structured entity in Luxembourg (Horizon 2016 S.A.), which has, in turn, passed the

default risk on to an investor. The financial resources that the investor received from the structured entity were deposited as cash collateral for the guarantee at HSH Nordbank AG. HSH Nordbank AG in turn provides the structured entity with securities as collateral for this cash deposit.

A vertical tranche approach is used in accordance with Art. 405 (1a) CRR. This means that loan receivables are included in the reference portfolio at a maximum of 95% of their nominal value. The resulting first loss piece of at least 5% is not treated as an additional retained tranche, but rather as unsecuritised outside of the Horizon transaction and as ranking pari passu with the securitised share regarding the allocation of losses.

The use of the financial guarantee allows the risk weighting of the secured loan portfolio to be reduced. This allows the two following objectives to be achieved:

- Risk management (reduction of credit risks in the portfolio)
- Relief on equity capital (reduction in regulatory equity capital requirements)



HSH Nordbank AG pays an annual premium on the respective outstanding mezzanine tranche. The premium to be paid in each case is determined primarily by the extent to which the guarantee has actually been utilised. The premium is recognised through profit or loss in commission expense. In 2017, the Bank expects to incur premium expense totalling a maximum of around € 26 million. The contractual term of the guarantee is 9 years.

As long as and insofar as the cash drawdown of the guarantee is not yet made through the invoicing of losses that in total exceed the first loss piece to be borne by HSH Nordbank AG (on the securitised portfolio) in an initial amount of € 30 million (the aforementioned first loss piece comprises a first loss tranche of € 22.5 million and an initial excess spread, i.e. a loss buffer to be determined on an annual basis, of € 7.5 million), then there is no claim for compensation against the guarantor that is eligible for capitalisation. Against this

background the hedging effect of the financial guarantee recognised in the balance sheet is accounted for on a net basis. The Bank initially determines specific and general loan loss provisions without taking the hedging effect of the financial guarantee into account and then records the hedging effect (if the first loss piece is exceeded by the specific and general loan loss provisions) on the face of the balance sheet through the use of a compensation item, which reduces the amount recognised under loan loss provisions in the lending business in the balance sheet accordingly. The specific and general loan loss provisions recognised are not changed by the accounting applied to the hedging effect. At the end of the year, no compensation item was recognised because the specific and general loan loss provisions did not exceed the initial first loss piece of € 30 million. The maximum possible hedging/compensation effect of the guarantee is limited to the volume of the mezzanine tranche in the amount of € 235 million.

#### 4. ADJUSTMENTS TO PREVIOUS YEAR COMPARATIVE FIGURES

##### I. Correction in accordance with IAS 8.41 et seqq.

These financial statements contain changes to the comparative figures.

The adjustment made was reviewed in accordance with the requirements of IAS 8 and classified as correction of errors in accordance with IAS 8.41 et seqq.

The correction relates to information on the fair value hierarchy as defined under IFRS 13 and has no impact on the balance sheet or the net result.

When calculating the transfer information in connection with the fair value hierarchy for financial instruments measured at fair value, a data collection error led to incorrect transfer information relating to the securities portfolios (active portfolios) for levels 1 and 2.

In Note 55, the information in the “Transfer, assets” table on the securities portfolios (active portfolios) in the categories HfT, AfS and DFV as comparative figures as at 31 December 2015 has been corrected accordingly.

In the previous year's financial statements, the transfer from level 1 to level 2 was € 5,311 million too high, and the transfer from level 2 to level 1 was € 5,385 million too high.

##### II. Changes in presentation

These financial statements contain changes in presentation compared to previous reporting dates.

The changes relate to the segment structure (see Note 51).

Changes were also made to the information on restructured/modified loans (see Note 59).

The previous year figures have been adjusted accordingly. These were not errors pursuant to IAS 8.41 et seqq.

## 5. CONSOLIDATION PRINCIPLES

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The Group financial statements present the parent company HSH Nordbank AG together with the consolidated subsidiaries as an economic unit. Subsidiaries also include structured entities that are controlled by HSH Nordbank. Structured entities are entities in which voting rights and similar rights do not constitute the dominant factor in assessing control. These also include entities whose relevant activities are predetermined by a narrow objective defined in the articles of association/partnership agreement or in other contractual agreements or in which there is a lasting restriction of the decision-making powers of the management. HSH Nordbank mainly includes ABS conduits and other securitisation and refinancing vehicles as well as investment funds (including private equity funds) within structured entities. Structured entities are included in the scope of consolidation if they are subsidiaries and are material to the presentation of the net assets, financial condition and earnings or to the assessment of the risk situation of the HSH Nordbank Group. Disclosures of the nature of the risks in connection with shares in consolidated structured entities are included in Note 6. Reference is made to Note 60 with regard to unconsolidated structured entities.

Control over a subsidiary prevails when HSH Nordbank is exposed to variable incoming cash flows from the exposure to this entity or has rights to such cash flows and is able to influence the cash flows through its decision-making power over the entity. HSH Nordbank possesses decision-making power over an entity if it has rights that confer on it, either directly or indirectly via third parties, the current possibility of controlling the entity's relevant activities. Relevant activities are deemed to be those which materially affect the entity's incoming cash flows depending on the nature and purpose of the entity. Variable incoming cash flows are all those which can vary depending on the entity's performance. Incoming cash flows from the exposure to another entity may accordingly be positive as well as negative. Variable incoming cash flows include dividends, fixed and variable interest, remuneration and fees, fluctuations in the value of investments and other financial advantages.

The assessment as to whether decision-making power exists is made on the basis of the relevant activities of the entity and the powers of HSH Nordbank to influence them. Voting rights as well as other contractual rights are considered in reviewing the control of relevant activities provided there are no economic or other obstacles to the exercise of the existing rights and HSH Nordbank would benefit from exercising those rights. The Bank has decision-making power based on voting rights if as a result of equity instruments or contractual agreements HSH Nordbank holds more than 50% of the voting rights and this proportion of the voting rights is allied to a substantial decision-making right with regard to the relevant activities. Other contractual rights that may facilitate a controlling influence are primarily rights to appoint members of executive bodies, recall them, to liquidate and to make other decisions. HSH Nordbank controls a

subsidiary if based on the total contractual rights it has the possibility to control the relevant activities of the entity.

A subsidiary is also controlled by HSH Nordbank if the decision-making power is exercised by third parties in the interests of and for the benefit of HSH Nordbank. Whether such delegated decision-making power exists is judged by considering the existing powers to appoint members of executive bodies, the legal and de facto scope for making decisions and the structure of the economic incentives. HSH Nordbank itself does not exercise any delegated powers to make decisions that would benefit third parties.

Due to agreements ceding control and insolvency proceedings currently pending, HSH Nordbank in individual cases holds equity interests in companies exceeding 50% which are not tied to any corresponding voting rights and therefore do not result in any controlling influence. In such cases, for purposes of defining the scope of consolidation as well as for purposes of preparing the list of shareholdings, the voting rights ratios were adjusted to the extent deemed reasonable under the special circumstances described above. Conversely, HSH Nordbank possesses a controlling influence in individual cases based on contractual rights, although it holds less than 50% of the voting rights.

Shares held by third parties in the equity of the subsidiary are shown as non-controlling interests in Group equity, provided these are not shares of external shareholders in consolidated commercial partnerships. Non-controlling interests are that part of the net results for the period and net assets of a subsidiary related to shares not directly held by the parent company or by a Group subsidiary. Non-controlling equity shares in subsidiaries and the resulting profit or loss as well as summarised financial information on subsidiaries with material non-controlling shares are presented in Note 5. Shares of external shareholders in consolidated commercial partnerships constitute puttable financial instruments, which are to be classified as debt in the Group financial statements under IAS 32 and disclosed under Other liabilities. Changes in value are recognised in Other operating income/expenses in the consolidated statement of income.

Subsidiaries are included by way of full consolidation in the Group financial statements of HSH Nordbank. In consolidating the capital the carrying amount of the equity holding in each subsidiary is set off against the share of HSH Nordbank in the subsidiary's equity capital. Goodwill connected to this is accounted for using the acquisition method in accordance with IFRS 3. Intra-Group receivables, liabilities and income are eliminated within the framework of debt and/or expense and income consolidation for the purpose of the Group financial statements. Expenses and gains arising from the transfer of assets within the Group are eliminated as well.

Shares in subsidiaries which were not consolidated because of their subordinate importance for HSH Nordbank Group's net assets, financial condition and earnings are accounted for as available for sale (AFS) financial instruments using the recognition and measurement guidelines of IAS 39.

Structured entities within the meaning of IFRS 12 are entities designed so that voting rights or similar rights do not represent the dominant factor in terms of assessing whether control is being exercised. Voting rights in such entities only relate to contractually specified administrative functions. Similar rights would refer, for example, to potential voting rights such as options on voting rights. Structured entities like securitisation vehicles are controlled by HSH Nordbank and included as subsidiaries in the Group financial statements if HSH Nordbank has decision-making power over the relevant activities and is subject to variable return flows from these activities.

HSH Nordbank does not classify single asset companies and project companies as structured entities, because as a rule they are not designed to ensure that holding voting rights is only for the purpose of performing contractually governed administrative functions. Structured entities are also characterised by a narrowly defined business purpose, a limited field of activity and comparatively low equity capital. If a company is not controlled by voting rights but by means of contractual rights, it is classified as a structured entity.

Joint arrangements are based on contractual agreements under which two or more partners establish an economic activity under shared management. Joint management is present if the partners have to cooperate in order to steer the relevant activities of the joint arrangement and decisions require unanimous approval from the participating partners. Such a joint arrangement is a joint venture if the partners who exercise joint management hold rights and obligations to the net assets of the arrangement.

If, conversely, the partners have direct rights to the assets or liabilities attributable to the joint arrangement for their debts, the arrangement is a joint operation. If a joint arrangement is embodied in a legally independent partnership or corporation with its own assets, so that HSH Nordbank only has a proportionate claim to the net assets of the company based on its shares in the company, this entity is normally a joint venture. In order to determine whether a joint venture or a joint operation is concerned in the case of joint arrangements, the contractual provisions and the purpose of the joint arrangement are used in addition. If neither the legal form nor the contractual provisions or other facts and circumstances provide an indication that HSH Nordbank has direct rights to the assets and/or obligations for the debts of the joint arrangement, it is a joint venture.

Associates are companies where the HSH Nordbank AG can exercise a significant but not controlling influence directly or indirectly via subsidiaries. Significant influence refers to the possibility of influencing decisions affecting the financial and business policy of another entity but not controlling it. Significant influence is found in principle if HSH Nordbank as an investor directly or indirectly holds 20% or more of the voting rights through subsidiaries. It may also be an associate if HSH Nordbank has less than 20% of the voting rights but because of other factors has the possibility of influencing the company's decisions concerning financial and business policy. This in particular includes the representation of HSH Nordbank in the entity's decision-making body and contractual rights to manage or dispose of assets including investment decisions in the case of investment funds. If HSH Nordbank only holds rights to approve, agree or veto, significant influence is not presumed to exist.

Interests in joint ventures and associates that are material to the proper presentation of the Group's net assets, financial position and results of operations are consolidated under the equity method. In doing so, the Group's interest in a joint venture/share in an associate is initially measured at cost of acquisition and thereafter increased or decreased depending on the Group's share in the joint venture's/associate's profit or loss. The relevant shares are stated in the statement of financial position under a separate line item. Details of the risks associated with the shares of HSH Nordbank in joint ventures and associates as well as summarised financial information on these entities are presented in Note 6. With regard to joint ventures and associates that in themselves are not material, the summarised financial information is presented in aggregate form in Note 30.

Interest in joint ventures and associates, respectively, which were not consolidated under the equity method because of their subordinate importance for HSH Nordbank Group's net assets, financial condition and earnings have been accounted for as financial instruments of the category AfS using the reporting and measurement guidelines of

IAS 39 and are disclosed under financial investments. Where HSH Nordbank has no information as of the reporting date which would allow for the fair value of these interests to be reliably determined, measurement is based on acquisition cost.

## **6. SCOPE OF CONSOLIDATION**

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In addition to the parent company, HSH Nordbank AG, Hamburg/Kiel, the scope of consolidation includes 57 fully consolidated subsidiaries (previous year: 61).

One associate and one joint venture consolidated under the equity method (as in the previous year) as at the balance sheet date were included in the Group financial statements.

The following subsidiaries, associates and joint ventures are included in the Group financial statements of HSH Nordbank:



**CONSOLIDATED COMPANIES**

Subsidiaries in which HSH Nordbank AG directly or indirectly holds 100% of the equity interests

	Registered office	2016 Share of equity capital in %	2015 Share of equity capital in %
1. Avia Management S.à.r.l.	Luxembourg	100.0	100.0
2. BINNENALSTER-Beteiligungsgesellschaft mbH	Hamburg	100.0	100.0
3. Bu Wi Beteiligungsholding GmbH	Hamburg	100.0	100.0
4. CAPCELLENCE Dritte Fondsbeteiligung GmbH <sup>4)</sup>	Hamburg	100.0	100.0
5. CAPCELLENCE Erste Fondsbeteiligung GmbH <sup>3)</sup>	Hamburg	100.0	100.0
6. CAPCELLENCE Holding GmbH & Co. KG <sup>2)</sup>	Hamburg	100.0	100.0
7. CAPCELLENCE Zweite Fondsbeteiligung GmbH <sup>4)</sup>	Hamburg	100.0	100.0
8. DEERS Green Power Development Company S.L. <sup>1) 13)</sup>	Madrid	100.0	100.0
9. FSL Asset Management Pte. Ltd. <sup>4)</sup>	Singapore	100.0	–
10. FSL Holdings Pte. Ltd. <sup>7)</sup>	Singapore	100.0	20.0
11. FSL Trust Management Pte. Ltd. <sup>5)</sup>	Singapore	100.0	–
12. GODAN GmbH	Hamburg	100.0	100.0
13. HSH Auffang- und Holdinggesellschaft mbH & Co. KG	Hamburg	100.0	100.0
14. HSH Facility Management GmbH	Hamburg	100.0	100.0
15. HSH Gastro+Event GmbH <sup>8)</sup>	Hamburg	100.0	100.0
16. HSH N Finance (Guernsey) Limited	St. Peter Port	100.0	100.0
17. HSH N Residual Value Ltd.	Hamilton	100.0	100.0
18. HSH Nordbank Securities S.A.	Luxembourg	100.0	100.0
19. HSH Private Equity GmbH	Hamburg	100.0	100.0
20. Ilex Integra GmbH <sup>1)</sup>	Hamburg	100.0	100.0
21. ISM Agency LLC <sup>10)</sup>	New York	100.0	100.0
22. Neptune Finance Partner S.à.r.l.	Luxembourg	100.0	100.0
23. Neptune Finance Partner II S.à.r.l.	Luxembourg	100.0	100.0
24. Solar Holdings S.à.r.l. <sup>13)</sup>	Luxembourg	100.0	100.0
25. Unterstützungs-Gesellschaft der Hamburgischen Landesbank mit beschränkter Haftung	Hamburg	100.0	100.0
26. 2200 Victory LLC	Dover	100.0	100.0

**CONSOLIDATED COMPANIES**

Subsidiaries with non-controlling interests	Registered office	2016 Share of equity capital in %	2015 Share of equity capital in %
27. Adessa Grundstücksverwaltungsgesellschaft mbH & Co. Vermietungs KG <sup>12)</sup>	Mainz	–	–
28. Amentum Aircraft Leasing No. Five Limited <sup>12)</sup>	Dublin	49.0	49.0
29. Amentum Aircraft Leasing No. Seven Limited <sup>12)</sup>	Dublin	49.0	49.0
30. Amentum Aircraft Leasing No. Six Limited <sup>12)</sup>	Dublin	49.0	49.0
31. Capcellence Vintage Year 06/07 Beteiligungen GmbH & Co. KG <sup>2)</sup>	Hamburg	83.3	83.3
32. Capcellence Vintage Year 07/08 Beteiligungen GmbH & Co. KG <sup>2)</sup>	Hamburg	83.3	83.3
33. CAPCELLENCE Vintage Year 11 Beteiligungen GmbH & Co. KG <sup>2)</sup>	Hamburg	83.3	83.3
34. CAPCELLENCE Vintage Year 13 Beteiligungen GmbH & Co. KG <sup>2)</sup>	Hamburg	83.3	83.3
35. CAPCELLENCE Vintage Year 16 Beteiligungen GmbH & Co. KG <sup>2)</sup>	Hamburg	83.3	–
36. Castellum ABF S.A. <sup>12)</sup>	Luxembourg	–	–
37. GmbH Altstadt Grundstücksgesellschaft <sup>12)</sup>	Mainz	50.0	50.0
38. HSH Care+Clean GmbH <sup>8)</sup>	Hamburg	51.0	51.0
39. HSH Move+More GmbH <sup>8)</sup>	Kiel	51.0	51.0
40. HSH N Funding II <sup>12)</sup>	George Town	56.3	56.3
41. Life Insurance Fund Elite LLC <sup>12)</sup>	New York	–	–
42. Life Insurance Fund Elite Trust <sup>12)</sup>	Minneapolis	–	–
43. Mitco Real Estate A S.à.r.l. <sup>12) 13)</sup>	Canach	–	–
44. Mitco Resolution 1 S.à.r.l. <sup>12) 13)</sup>	Canach	–	–
45. Mitco Resolution 2 S.à.r.l. <sup>12) 13)</sup>	Canach	–	–
46. Mitco Resolution 3 S.à.r.l. <sup>12) 13)</sup>	Canach	–	–
47. Mitco Resolution 4 S.à.r.l. <sup>12) 13)</sup>	Canach	–	–
48. Mitco Resolution 5 S.à.r.l. <sup>12) 13)</sup>	Canach	–	–
49. Next Generation Aircraft Finance 2 S.à.r.l. <sup>12)</sup>	Findel	49.0	49.0
50. Next Generation Aircraft Finance 3 S.à.r.l. <sup>12)</sup>	Findel	49.0	49.0
51. OCEAN Funding 2013 GmbH <sup>12)</sup>	Frankfurt a.M.	–	–
52. RDM Limited <sup>12) 13)</sup>	George Town	–	–
53. RESPARCS Funding Limited Partnership <sup>12)</sup>	Hong Kong	0.0	0.0
54. RESPARCS Funding II Limited Partnership <sup>12)</sup>	St. Helier	0.0	0.0
55. Senior Assured Investment S.A. <sup>12)</sup>	Luxembourg	–	–
56. Senior Preferred Investments S.A. <sup>12)</sup>	Luxembourg	–	–
57. Stratus ABF S.A. <sup>12)</sup>	Luxembourg	–	–

## COMPANIES CONSOLIDATED AT EQUITY

	Registered office	2016 Share of equity capital in %	2015 Share of equity capital in %
<b>Associates consolidated under the equity method</b>			
1. First Ship Lease Trust	Singapore	25.2	–
<b>Joint ventures consolidated under the equity method</b>			
2. Kontora Family Office GmbH	Hamburg	51.0	51.0

<sup>1)</sup> Subsidiary of Bu Wi Beteiligungsholding GmbH.

<sup>2)</sup> Subsidiary of CAPCELLENCE Holding GmbH & Co. KG.

<sup>3)</sup> Subsidiary of Capcellence Vintage Year 06/07 Beteiligungen GmbH & Co. KG.

<sup>4)</sup> Subsidiary of Capcellence Vintage Year 07/08 Beteiligungen GmbH & Co. KG.

<sup>5)</sup> Subsidiary of FSL Asset Management Pte. Ltd.

<sup>6)</sup> Subsidiary of FSL Holdings Pte. Ltd.

<sup>7)</sup> Subsidiary of GODAN GmbH.

<sup>8)</sup> Subsidiary of HSH Facility Management GmbH.

<sup>9)</sup> Subsidiary of HSH Private Equity GmbH.

<sup>10)</sup> Subsidiary of Life Insurance Fund Elite LLC.

<sup>11)</sup> Subsidiary of Solar Holdings S.à.r.l.

<sup>12)</sup> Structured entity.

<sup>13)</sup> A disposal plan within the meaning of IFRS 5.8A is in place.

## I. Information on subsidiaries – changes to the scope of consolidation

### A) Additions

The following companies were included for the first time in the scope of consolidation on a fully consolidated basis:

- Amentum Aircraft Leasing No. Seven Limited, Dublin
- CAPCELLENCE Vintage Year 16 Beteiligungen GmbH & Co. KG, Hamburg
- FSL Asset Management Pte. Limited, Singapore
- FSL Holdings Pte. Ltd., Singapore (hereinafter referred to as: FSL Holdings)
- FSL Trust Management Pte. Limited, Singapore

Amentum Aircraft Leasing No. Seven Limited is a subsidiary of HSH Nordbank due to a principal-agent relationship. The company became material for the first time in the reporting year and is included in the Group financial statements as a fully consolidated subsidiary with retroactive effect from 1 January 2016.

The company CAPCELLENCE Vintage Year 16 Beteiligungen GmbH & Co. KG, which was set up on 17 March 2016 and in which HSH Nordbank holds the majority of voting rights, is included for the first time in the scope of consolidation on a fully consolidated basis.

HSH Nordbank obtained control over the abovementioned companies in the FSL Group on 23 January 2016. FSL Holdings is a company whose principal asset is a 25.2% interest in the listed First Ship Lease Trust, Singapore (hereinafter referred to as FSL Trust). The acquisition

of the equity interest in FSL Trust was mainly financed by a loan provided by HSH Nordbank. As at 31 December 2015, HSH Nordbank already held 20% of the shares in FSL Holdings via its subsidiary, GODAN GmbH. This company was not consolidated as an associate as at 31 December 2015 because of its immateriality with regard to the net assets, financial position and earnings of the Group.

Following the changes made to the shareholder structure of FSL Holdings, which were completed on 23 January 2016 (redemption of capital shares held by all other shareholders) as part of loan restructuring at the level of HSH Nordbank AG, the HSH Nordbank Group holds 100% of the voting rights and therefore has control over this company and its subsidiaries, FSL Asset Management Pte. Limited and FSL Trust Management Pte. Limited (both service companies) from that moment in time. FSL Trust, whose business activities mainly comprise the chartering of its own ship portfolio, will be included in the Group financial statements of HSH Nordbank AG under the equity method as an associate as of 23 January 2016.

Before obtaining control over FSL Holdings, the interests in this company had been stated in the Group financial statements of HSH Nordbank with a carrying amount of € 1. There was no income effect resulting from the remeasurement of the shares, pursuant to IFRS 3.42, in connection with the initial consolidation of the FSL Group.

The business combination means that existing business relationships between HSH Nordbank and FSL Holdings are deemed to have ended. The termination of the abovementioned loan relationship and an interest rate swap agreed in connection with the lending relationship did not have any material effect on income.

The loan receivable and the interest rate swap totalling € 9.6 million were derecognised as consideration for the business combination. No cash consideration was paid in connection with the transaction. The business combination does not result in any difference.

The main asset of the FSL Group is the equity holding in FSL Trust, which has been recognised at a fair value of € 7.8 million. The equity holding is shown under the item "Financial investments accounted for under the equity method". The other assets and liabilities assumed by the FSL Group are insignificant.

The cumulative results of the FSL Group included in the Group financial statements as at 31 December 2016 amount to € 6.5 million. These include the pro rata net result for the period of FSL Trust, which is accounted for under the equity method, in the amount of € 3.2 million, which is reported under Net income from financial investments accounted for under the equity method. The revenue of the FSL Group as at 31 December 2016 amounts to € 2.9 million and mainly relates to income from the performance of services. It is reported under Other operating income.

## B) Disposals

Contrary to the inclusion as at 31 December 2015, the following companies are no longer included in the scope of fully consolidated companies:

- Amentum Aircraft Leasing No. Three Limited, Dublin
- CAPCELLENCE Vintage Year 09 Beteiligungen GmbH & Co. KG, Hamburg
- CAPCELLENCE Vintage Year 10 Beteiligungen GmbH & Co. KG, Hamburg
- CAPCELLENCE Vintage Year 12 Beteiligungen GmbH & Co. KG, Hamburg
- CAPCELLENCE Vintage Year 14 Beteiligungen GmbH & Co. KG, Hamburg
- CAPCELLENCE Vintage Year 15 Beteiligungen GmbH & Co. KG, Hamburg
- CHIOS GmbH, Hamburg
- Neptune Ship Finance (Luxembourg) S.à.r.l. & Cie, S.e.c.s., Luxembourg
- SPE II Pissarro SAS, Paris

Amentum Aircraft Leasing No. Three Limited is a special purpose company in the field of aviation where the decision-making power had been exercised by third parties in the interests of and for the benefit of HSH Nordbank. The material assets of the company were sold in the fourth quarter of 2016. Since it is planned to liquidate the

company in the short term and no material income effects are to be expected until this moment for the Group statement of income of HSH Nordbank, the subsidiary was deconsolidated. A loss in the amount of € 10.8 million resulted from the deconsolidation, which is recognised under the item Other operating income.

With economic effect from 30 November 2016, the five abovementioned companies in the CAPCELLENCE Group were transferred to CAPCELLENCE Holding GmbH & Co. KG by way of a collapse merger. The entry in the commercial register was made on 7 December 2016.

With economic effect from 1 January 2016, CHIOS GmbH merged with the fully consolidated subsidiary HSH Auffang- und Holdinggesellschaft mbH & Co. KG. The entry in the commercial register was made on 6 July 2016.

Die Neptune Ship Finance (Luxembourg) S.à.r.l. & Cie, S.e.c.s. was not included in the scope of consolidation due to its liquidation on 11 October 2016. The deconsolidation did not have any material effect on income.

Insolvency proceedings regarding the assets of SPE II Pissarro SAS were commenced on 15 December 2016. Following the commencement of insolvency proceedings HSH Nordbank no longer has any decision-making powers over the relevant activities of this company. A loss of € 10.7 million resulted from the deconsolidation, which is disclosed under Other operating income.

## II. Details of subsidiaries with material non-controlling shares

There are no subsidiaries with non-controlling shares material to HSH Nordbank as of the reporting date.

## III. Information on shares held in associates and joint ventures accounted for under the equity method

### A) General information

In contrast to the situation as at 31 December 2015, the following company is included in the scope of consolidation under the equity method for the first time:

- First Ship Lease Trust, Singapore

For information on the background in this regard, we refer to Section I of this Note.

The following company included in the scope of consolidation as at 31 December 2015 is no longer consolidated under the equity method:

- SITUS NORDIC SERVICES ApS, Copenhagen



All shares held in SITUS NORDIC SERVICES ApS were sold as at 8 March 2016. The associated deconsolidation did not have any material effect on income.

The shares in the associate Relacom Management AB that were reclassified in accordance with IFRS 5 in the 2015 financial year were sold in full as at 19 December 2016.

The effects of entities no longer consolidated under the equity method can be found in Note 14.

Although HSH Nordbank AG holds the majority of the voting rights in Kontora Family Office GmbH, it cannot exert control over this company because decisions regarding its relevant activities require a qualified majority of 75%.

After the reporting date, the shares in Kontora Family Office GmbH fulfilled the requirements for being classified as held for sale. The shares in the joint venture are allocated to the Core Bank segment and are highly likely to be sold in the second quarter of 2017.

There were no associates and joint ventures accounted for under the equity method deemed to be material to HSH Nordbank as at the reporting date.

## B) Summarised financial information

The section below sets out the summarised financial information for associates and joint ventures included in the Group financial statements under the equity method that are not material taken in isolation and as a whole for HSH Nordbank.

### OTHER SHARES HELD IN ASSOCIATES ACCOUNTED FOR UNDER THE EQUITY METHOD

(€ m)	2016	2015
Share of the following attributable to HSH Nordbank:		
Net income/loss for the year	3	–
Other comprehensive income	–	–
Total comprehensive income	3	–
<b>Cumulative carrying amount</b>	<b>12</b>	<b>1</b>

### OTHER SHARES HELD IN JOINT VENTURES ACCOUNTED FOR UNDER THE EQUITY METHOD

(€ m)	2016	2015
Share of the following attributable to HSH Nordbank:		
Net income/loss for the year	–	–
Other comprehensive income	–	–
Total comprehensive income	–	–
<b>Cumulative carrying amount</b>	<b>1</b>	<b>1</b>

The inclusion of First Ship Lease Trust as at 31 December 2016 is based on financial statements prepared by the Trust as at 30 September 2016. It is not possible to obtain the financial information relating to the Trust as at 31 December 2016 before the preparation of the Group financial statements of HSH Nordbank. There is no information suggesting that material business transactions or other material events between this cut-off date for the financial statements and the balance sheet date of HSH Nordbank would have to be taken into account.

## C) Risks and restrictions

In connection with companies accounted for in the Group financial statements under the equity method, HSH Nordbank is neither exposed to risks from unrecognised obligations to these companies nor are there any restrictions within the meaning of IFRS 12.22 vis-a-vis these companies.

Additional information on companies accounted for under the equity method may be found under Notes 14 and 31.

## II. Information on consolidated structured entities

HSH Nordbank's scope of consolidation includes 24 fully-consolidated structured entities. These companies are controlled due to contractual rights and/or principal-agent relationships. The HSH Nordbank Group also holds the majority of the voting rights for three of these companies.

The following disclosures represent the type of risks in connection with business relationships with consolidated structured entities:

HSH Nordbank AG is the sponsor of a consolidated structured entity and benefits from this company through the expanded funding volume. For this asset-based funding transaction, HSH Nordbank AG has transferred claims to the company for which, because of the opportunities and risks remaining with HSH Nordbank AG there has been no derecognition of the assets on the balance sheet. The structured entity is funded exclusively by the granting of a junior loan by HSH Nordbank AG. A previous senior promissory note bond that served to fund the company was repaid in the reporting year. In the case of the structured entity HSH Nordbank AG has a repurchase

obligation applying to the receivables being transferred should specific contractually defined events occur.

HSH Nordbank AG is the sponsor of securitisation vehicles whose business purpose is the placement of acquired Silent Participations of HSH Nordbank AG through the issuance of securities on the capital market. HSH Nordbank has provided these consolidated structured entities with a guarantee facility. This guarantee facility serves to hedge the payment obligations of the structured entities in respect of the holders of the securities. These payment obligations arise if payment claims result for the structured entities against HSH Nordbank AG from the Silent Participations held by them.

HSH Nordbank AG has granted liquidity and credit facilities to consolidated structured entities. In terms of the amounts, these are of minor significance for the Group's financial position.

HSH Nordbank AG has a contractual obligation to bear the operating expenses for consolidated structured entities.

During the reporting year, HSH Nordbank did not provide consolidated or unconsolidated structured entities with any non-contractual support.

As of the balance sheet date there is no current intention to provide a consolidated structured entity any financial or other support within the definition of IFRS 12.17.

## 7. MANAGEMENT ESTIMATES AND DISCRETIONARY DECISIONS

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As permitted, estimates and assumptions for the measurement of assets and liabilities have been incorporated into the Group financial statements of HSH Nordbank. All estimates and judgments necessary for accounting and measurement according to IFRS were undertaken in accordance with the appropriate standard in each case, are continuously reassessed and are based on past experience and other factors including expectations of future events which appear reasonable under the circumstances. Specifically, the determination of the loan loss provisions taking into account the effects of the guarantee (see Note 8.I.C.), determination of impairment losses in order to sell non-current assets held for sale and disposal groups (see Note 34 and Note 27, respectively), future cash flows of hybrid financial instruments (see Note 8.I.E.), deferred taxes (see Note 8.III.6), the determination of fair values (see Note 8.I.D.), provisions for pensions and similar obligations and other provisions (see Note 8.III.5) are affected by uncertainty.

As at the reporting date, 31 December 2016, the Group financial statements of HSH Nordbank are prepared assuming that the Bank will be sold in full as part of an overall sale as part of the privatisation process. This means that all of the shares held by the seller in the Bank, including all assets and liabilities, will be transferred to a third party in a transaction without any material early disposals of assets or sub-areas at amounts below the carrying amount in the event of outstanding bids for an overall sale. The question as to whether the sale of the Bank as a whole will be successful depends on whether, as part of the sale process in 2017, bids are made for the acquisition of the overall Bank as part of an overall sale at a positive purchase price. If only alternative purchase bids are made for a part of the Bank, it may be necessary to sell assets or sub-areas of the Bank at amounts below the

carrying amount. In the event of corresponding large-scale sales of loan portfolios, particularly in the Non-Core Bank, there could be a need for significant additional loan loss provision expenses if the sale of the overall Bank is no longer more likely than not and, as a result, the loan loss provisions are to be calculated based on likely transaction prices for these assets. As at 31 December 2016, the carrying amount of the loan portfolio of the Non-Core Bank is approx. € 15.9 billion.

As at the reporting date of 31 December 2016, the loan loss provisions for credit portfolios that are to be sold in the 2017 financial year as a result of the decision made by the EU Commission in May 2016 were calculated based on likely transaction prices at the planned time of sale. The market transaction also includes aircraft and real estate in consolidated subsidiaries that were written down as at the reporting date to the sale price that is likely to be achieved in accordance with IFRS 5 (see Note 34). Regarding the carrying amounts of the components of the market portfolio, reference is made to Note 34. The carrying amount of the market portfolio is uncertain. Additional pressure on earnings could, for example, arise if the transaction prices that are actually realised are lower than the current carrying amounts of the assets. In addition, the composition of the market portfolio could change again after the reporting date, which would also result in changes in the likely loan loss provisions. This could put further pressure on earnings.

Also in the event that further loan portfolios are sold on the market, a need for significant additional loan loss provisions could arise if the transaction prices are lower than the carrying amount.

For information on further significant uncertainties relating to estimates used to calculate loan loss provisions, reference is made to the comments below and to the comments in the Group management report in the section entitled "Opportunities and risks in the forecast for loan loss provisions".

Where there is greater uncertainty regarding estimates relating to other aspects, the underlying assumptions are presented in greater detail in the relevant note.

With the exception of estimates, major discretionary decisions by management in the application of accounting and measurement methods include:

- use of the fair value option for financial instruments (see Note 8.I.A);
- not classifying financial instruments as held to maturity (HtM);
- applying the current reclassification rules under IAS 39 (see Note 53);
- determining fair values for certain financial instruments, including a judgement regarding the existence of an active or inactive market;
- assessing whether HSH Nordbank controls another entity.

## 8. ACCOUNTING POLICIES

### I. Financial instruments

#### A) Categorisation of financial assets and liabilities

A financial instrument is an agreement which simultaneously creates a financial asset for one company and a financial liability or equity instrument for the other company. Under IAS 39 all financial assets and liabilities including financial derivatives must be stated in the statement of financial position and measured according to the category to which they are assigned.

Financial assets and liabilities are stated in the statement of financial position if HSH Nordbank is counterparty under the contract for the corresponding financial instrument. Expected future transactions or contracts are not recognised.

Provided that they fulfil the criteria of IAS 39, pending transactions in the form of derivatives must always be stated in the statement of financial position as financial assets or liabilities and measured at fair value on the trading date. Spot transactions in non-derivative financial assets (so-called regular way contracts) are recognised as of the settlement date. The change in fair value between the trading date and settlement date is recognised according to the measurement rules for the category of asset. This means that changes in value of financial instruments in the category available for sale must be recognised in the revaluation reserve, while changes in value for the categories designated at fair value and held for trading are recognised in the statement of income in Net trading income.

Other non-derivative financial assets which do not result from spot transactions, for example loans granted, are recognised as of the settlement date.

Non-derivative financial liabilities are recognised if one of the two parties to the contract has fulfilled the contract (settlement date).

Initial recognition is measured at fair value, which generally corresponds to the acquisition cost of the financial instrument.

Derecognition of a financial asset takes place on the settlement date. In the case of derivatives, derecognition takes place on the trading date.

Subsequent measurement of financial assets and liabilities depends on which IAS 39 category they were assigned to at the time of acquisition. The following distinctions are made here:

1. Financial assets and liabilities which are financial instruments at fair value recognised in profit or loss include both instruments held for trading (HfT) as well as instruments which are voluntarily and irrevocably designated at fair value (DFV) at the time of first recognition:
  - a. All financial instruments held for trading and derivatives which are not part of a hedge accounting transaction are classified as held for trading (HfT).

They are initially and subsequently measured at fair value. Transaction costs are recognised through profit or loss on acquisition date. In accordance with IAS 39.43, transaction costs are only included in the initial recognition in the case of financial assets or liabilities not measured at fair value and recognised in profit or loss. Where a market price exists in the form of an exchange quotation, this is used for the purposes of measurement. In other cases, the market price of comparable instruments or recognised measurement models, especially net present value methods and option pricing models, are used to determine fair value.

These trading instruments and derivatives are stated under Trading assets or Trading liabilities on the statement of financial position. Ongoing measurement gains and losses and realised gains and losses on these financial instruments are incorporated into Net trading income. Interest income and expenses as well as dividends arising from HfT transactions are recorded under Net interest income.

- b. In addition, certain complex structures arising from issued instruments and assets that contain derivatives requiring separation, as well as certain financial instruments which are a component of an economic hedge without satisfying the requirements of IAS 39 for hedge accounting, are also classified as designated at fair value (DFV). Furthermore, the fair value option may be applied at HSH Nordbank to portfolios whose management and performance measurement is done on a fair value basis in accordance with the documented risk management strategy. This is possible, for example, with special funds and similar assets to be consolidated.

The designation at HSH Nordbank serves to avoid or reduce accounting mismatches from securities and loans hedged with interest rate derivatives. In addition, the fair value option is generally applied to any structures otherwise required to be segregated.

Financial assets designated as DFV primarily relate to positions in the credit investment portfolio (asset-backed securities, synthetic collateralised debt obligations, credit linked notes) and convertible bonds. Financial liabilities designated as DFV specifically comprise structured registered and bearer instruments with embedded interest, currency, equity and other risks.

Financial instruments in the fair value option are stated at fair value. These financial instruments are stated under Loans and advances to banks, Loans and advances to customers, Financial investments and Liabilities to banks, Liabilities to customers, Securitised liabilities and Subordinated capital. Gains or losses arising from ongoing measurement and realised gains or

losses are stated under Net trading income. Interest income and expenses for these financial instruments are stated under Net interest income. To the extent dividend income is received, it is disclosed under Net interest income.

2. Loans and receivables, which are stated in the statement of financial position at amortised cost:

Non-derivative financial assets with fixed or determinable payments not traded on an active market when first recognised are shown under IAS 39.9 as loans and receivables (LaR). Exceptionally, this category also includes financial instruments which originally complied with the classification requirements as LaR and which have been reclassified from the HfT and AFS categories in accordance with the changes in IAS 39 (rev. 2008) because there was no longer any active market and there is an intention and ability to hold the financial asset for the foreseeable future or to maturity.

An active market exists when quoted prices are regularly provided, e.g. by an exchange or a broker, and these prices are representative of actual transactions between arms-length third parties.

Financial instruments in this category are stated at cost of acquisition, equivalent to fair value at the time of initial recognition and taking transaction costs into account. They are measured subsequently at amortised cost; whereby premiums or discounts are amortised according to the effective interest method over the term and recognised in Net interest income. Financial instruments in the LAR category are shown under Cash reserves, Loans and advances to banks and Loans and advances to customers, Financial investments, Non-current assets held for sale and disposal groups or Other assets.

3. Financial assets available for sale (AfS) recognised at fair value under OCI and not taken through the statement of income:

The category available for sale (AfS) encompasses all non-derivative assets which cannot be assigned to any of the other categories. The Group's AfS holdings relate primarily to marketable fixed income securities, investment fund units and equity instruments such as interests in affiliated companies and equity holdings which are recognised in accordance with IAS 39. They are recognised under Cash reserves, Loans and advances to banks, Loans and advances to customers, Financial investments, Non-current assets held for sale and disposal groups or Other assets.



The initial measurement of financial assets available for sale is at the fair value at the time of acquisition plus transaction costs. Fair value at the time of acquisition generally corresponds to the transaction price. Subsequently, financial instruments AFS are measured at fair value in accordance with IAS 39.46, to the extent that this can be reliably determined. Particularly for equity securities which are not listed and whose fair value cannot be determined reliably by other methods, subsequent measurement takes place at cost in accordance with IAS 39.46 (c) in conjunction with IAS 39.A81. These are primarily equity instruments of unlisted companies for which no active market exists and realistic estimates of the parameters determining market value are not possible because future expectations are difficult to forecast.

Insofar as changes in value of AFS instruments measured at fair value are not attributable to impairment, they are recognised as Changes in fair value of AFS financial instruments under Other comprehensive income (OCI), taking deferred taxes into account, without affecting net income. By contrast, where hedged AFS instruments are concerned, the fluctuation relating to the hedged risk is recognised in the statement of income under Result from hedging and is separately disclosed as an adjustment item arising from the portfolio fair value hedge.

When an asset is sold or impaired, the revaluation reserve is released through the statement of income so that the profit or loss is reflected in the statement of income. Any write-ups required after

impairment are recognised directly in equity in Other comprehensive income (OCI) for equity securities and recognised in profit or loss for debt securities.

Amortisation of the difference between costs of acquisition and repayment amount for interest-bearing securities is stated under Net interest income, using the effective interest method.

#### 4. Other liabilities (LIA):

Other liabilities (LIA) include liabilities which are neither part of the trading portfolio nor classified as DFV.

Financial liabilities are recognised at fair value at the time of issue plus transaction costs. Fair value at the time of acquisition generally corresponds to the transaction price. In subsequent periods, they are measured at amortised cost using the effective interest method.

#### **B) Classification of financial instruments**

The classification of financial instruments required for reporting by IFRS 7.6 is similar to the categorisation of financial instruments according to IAS 39 for the items in the statement of financial position, in order to ensure a uniform and clear picture of the financial position and performance. The table below shows the classes of financial instruments at HSH Nordbank:

Measurement method	Classes			
	IAS 39 category	Statement of financial position item/sub-item		
Financial instruments measured at amortised cost	Loans and Receivables (LaR)	Cash reserve		
		Loans and advances to banks		
		Loans and advances to customers		
		Financial investments		
		Non-current assets held for sale and disposal groups		
		Other assets		
		Other Liabilities (LIA)	Liabilities to banks	
			Liabilities to customers	
			Securitised liabilities	
			Liabilities relating to disposal groups	
Financial instruments measured at cost	Available for Sale (AFS)	Subordinated capital		
		Other liabilities		
		Financial investments		
Financial instruments measured at fair value	Held for Trading (HfT)	Non-current assets held for sale and disposal groups		
		Other assets		
		Trading assets		
		Credit derivative under the second loss guarantee		
		Non-current assets held for sale and disposal groups		
		Trading liabilities		
		Liabilities relating to disposal groups		
		Designated at Fair Value (DFV)	Designated at Fair Value (DFV)	Loans and advances to banks
				Loans and advances to customers
				Financial investments
Non-current assets held for sale and disposal groups				
Liabilities to banks				
Liabilities to customers				
Securitised liabilities				
Liabilities relating to disposal groups				
Subordinated capital				
Available for Sale (AFS)	Available for Sale (AFS)			Cash reserve
Financial instruments measured on the basis of other standards	n/a	Loans and advances to banks		
		Loans and advances to customers		
		Financial investments		
		Non-current assets held for sale and disposal groups		
		Positive fair values of hedging derivatives		
		Negative fair value of hedging derivatives		
		Off-balance-sheet transactions	n/a	Receivables under finance leases
				Contingent liabilities
				Irrevocable loan commitments
				Other obligations

In addition to the holding categories, a distinction is made with regard to the substance, characteristics and risk of the financial instruments for the classification of line items and sub-items in the statement of financial position as listed above that fall within the scope of IFRS 13 for disclosures under IFRS 13. These are defined in each case for non-derivative instruments and derivatives and comprise the following:

Non-derivative financial instruments	Debt instruments
	Contractually linked instruments
	Equity or near-equity instruments
	Other trading portfolios
Derivatives	Interest rate derivatives
	Cross-currency interest rate derivatives
	Currency derivatives
	Credit derivatives
	Structured derivatives
	Other derivatives

Debt instruments are classified as follows for quantitative disclosures under IFRS 13 relating to financial instruments classified as loans and receivables in the Loans and advances to banks and Loans and advances to customers balance sheet line items.

Statement of financial position item/sub-item	IAS 39 category	Classes
Loans and advances to banks	Loans and Receivables (LaR)	Debt instruments Payable on demand
		Debt instruments Other loans and advances
Loans and advances to customers	Loans and Receivables (LaR)	Debt instruments
		Retail customers
		Corporate clients
		Public authorities

### C) Loan loss provision and impairment of financial instruments

At every reporting date, a check is performed to establish whether there is objective evidence for the impairment of a financial asset which is not measured at fair value recognised in profit or loss.

An impairment test is performed if, after initial recognition of a financial instrument, there is objective evidence of an impairment which

would have an impact on the anticipated future cash flows from the financial instrument.

Criteria for impairment are essentially major financial difficulties for the borrower and indications that, based on current information, interest payments cannot be made and an improvement in the financial situation cannot be demonstrated. These also particularly include deferrals of interest and/or principal payments, concessions such as the granting of restructuring loans in particular for the purposes of supporting the liquidity of the borrower as well as the threat of insolvency.

In the case of securities, an initial check is performed as to whether the market value has decreased in the last twelve months, either permanently by at least 10% or once in the last six months by 20% below the cost of acquisition. This applies to both equity and debt instruments. If an equity instrument is involved, it must be written down to fair value in such a case.

However, if debt instruments meet either of these criteria, they are checked as part of a multi-step risk assessment process to see if there are any indicators for impairment. An indicator for an impairment of a security is, for example, a downgrade to non-investment grade. Where a security is already non-investment grade and the rating deteriorates by another three categories, this would be another indicator. Asset-backed security (ABS) transactions are checked to see if the over-collateralisation mechanisms have seen a significant deterioration since purchase or issue. For collateralised debt obligations (CDOs) the par value and interest cover tests can normally be used, for example.

Specific loan loss provisions for interest-bearing securities are generally recognised in the amount of the difference between acquisition cost and fair value.

Identifiable default risks from the lending business are dealt with by making specific loan loss provisions for the loan or advance in question. To calculate the amount of the specific loan loss provisions, the net present value of the anticipated cash flows arising from the loan or advance – that is, achievable amount – is compared to its carrying amount. The anticipated cash flows may comprise capital repayments, interest payments or the proceeds from disposal of collateral less liquidation costs. If the carrying amount is greater than the realisable amount, a specific loan loss provision is created in the amount of the difference.

Assessments as to the need for loan loss provisions are frequently made on the basis of information which is partly provisional in nature (e.g. planned restructuring of borrowers, draft reorganisation reports) or are subject to increased volatility (e.g. collateral value of real estate and ships). This results in increased uncertainty regarding estimates of key parameters of loan loss provisions. In such cases the large degree of uncertainty is mainly due to the assessment of expected cash flows

which are dependent on borrowers, industries, the assessment of the overall economy among other factors. The assumptions made are subject to a periodic review and are adapted to the changed underlying conditions where necessary.

With respect to risks which have already occurred but have not yet been identified, general loan loss provisions are created for groups of assets which are comparable on the basis of their default risk. When determining the general loan loss provisions, current developments in the economic environment are taken into account through parameters from an expected loss approach. The general loan loss provisions are determined as of the reporting date on the basis of risk parameters derived from the determination of internal economic counterparty default risk. For the calculation the parameters probability of default (PD), loss given default (LGD) and for off-balance sheet items the credit conversion factor (CCF) are used. The loss identification period (LIP) in the calculation represents the interval between the occurrence of a default event and its announcement, transforming the expected loss approach to an incurred loss approach.

Additional general loan loss provisions had to be created for risks resulting from the challenging environment in particular in the shipping market.

Risks of uncertainties in assessment for the hedged portfolio are assumed by the guarantor under the second loss guarantee.

As the posting of the loan loss provision depends on the category of financial assets, the following distinctions must be made with regard to measurement:

- a. Financial instruments belonging to the category LaR which are measured at amortised cost

Impairments to loans and advances to banks and customers are recorded in separate loan loss provisions accounts under the item Loan loss provisions. Loan loss provisions thus created are written off at the time when the amount of the actual default of the receivable is determined or the receivable defaults or is derecognised. Irrecoverable receivables for which no specific loan loss provisions existed are written off directly as is the case for losses in the case of impaired receivables which exceed the recorded loan loss provisions. Impairments to LaR securities are recorded by means of direct write-downs to the securities. Recoveries on receivables written-off are recognised in profit or loss.

- b. Financial instruments belonging to the AfS category which are measured at fair value in OCI and not recognised in the statement of income

In the case of permanent or significant impairment to an AfS equity financial instrument, a direct write-down is recognised

in profit or loss. In the process, the cumulative gains taken through the statement of income and recognised as equity are rebooked to net income from financial investments. This approach is used for AfS debt instruments accordingly. In the case of debt securities only, if the reasons for impairment no longer apply a write-up to the maximum of amortised cost is made in profit or loss. Amounts beyond this and write-ups to equity securities are recognised directly in the revaluation reserve in OCI.

- c. Equity securities belonging to the AfS category not quoted on an active market and measured at the cost of acquisition as their fair value cannot be reliably determined

In the case of impairment to an AfS financial instrument measured at acquisition cost depreciation to the financial instrument is made, which is recognised in profit or loss.

Specific and general loan loss provisions are also made for off-balance-sheet transactions and carried on the statement of financial position as provisions in the lending business.

Specific and general loan loss provisions are determined at first without taking the hedging effect of the guarantees received into account (cf. Note 3). The hedging effect is then mapped in the statement of financial position through the recognition of a compensation item, which directly reduces loan loss provisions.

#### **D) Determining fair value**

Under IFRS 13 the fair value represents the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The fair value of financial instruments is determined on the basis of the listed price on an active market (mark-to-market), or if this is not possible on the basis of recognised valuation techniques and models (mark-to-matrix or mark-to-model). Irrespective of whether and to what extent the inputs applied in determining the fair value are observable in the market, financial instruments are assigned to one of the three fair value hierarchy levels as defined in IFRS 13.

Fair value can be determined using the mark-to-market method if a market price is available at which a transaction could be entered into or has been entered into for a similar financial instrument as at the measurement date. This is generally the case for shares traded on liquid markets. Such an unadjusted market price at the measurement date for the identical instrument is classified as level 1 of the valuation hierarchy under IFRS 13.



If such a market price is not available for the identical instrument, the measurement is carried out using valuation techniques or models.

### 1. Valuation techniques and models

When using valuation techniques the market approach is the preferable method for determining the fair value. The fair value is determined to the extent possible on the basis of prices that come from transactions executed on the measurement date. If the fair value cannot be determined from market or transaction prices for the identical financial instrument, prices of comparable financial instruments or indices, which are representative for the financial instrument, are used as an alternative and adjusted where necessary (mark-to-matrix method). The fair value is assigned to level 2 of the fair value hierarchy if the adjustment to the prices or parameters observable in the market is not material. However, if the adjustment is material and affects unobservable inputs, the fair value is assigned to level 3.

The fair value is determined based on an income approach using an appropriate model (e.g. option price model, discounted cash flow method), if the market approach using the mark-to-market or mark-to-matrix method is not possible or is not of sufficient quality. Where available, inputs observable in the market as well as quality assured market data from appropriate pricing agencies or also validated prices from market partners (arrangers) are also used as a primary source for model valuations. Fair values determined by means of model valuations, for which only observable inputs are used or which are only based to an insignificant extent on unobservable inputs, are assigned to level 2 of the fair value hierarchy. Observable market data is usually available for liquid securities and simple OTC derivatives traded on liquid markets (for example interest rate swaps, forward foreign exchange transactions and foreign exchange options in certain currencies as well as derivatives of certain listed equities or indices). If the fair values determined using valuation models are based to a significant extent on unobservable inputs, they are assigned to level 3 of the fair value hierarchy. Valuation models that are based on unobservable market data, and which therefore require assumptions concerning the relevant parameters, are often necessary for structured securities – or for securities whose markets are illiquid and for complex OTC derivatives.

The fair value of receivables and liabilities measured at amortised cost is mainly determined by discounting the cash flows of the financial instruments. In the case of receivables with a default rating, the fair values are determined based on the still to be expected future cash flows.

A portion of the liabilities measured at fair value comes under the guarantee obligation (Gewährträgerhaftung) (credit enhancements). Lower credit spreads are applied in determining the fair

values for such liabilities than is the case for liabilities for which similar obligations of third parties do not exist.

The following section gives an overview of the parameters and assumptions used and the valuation procedures they are based on.

### 2. Parameters used in valuation techniques and models

The following are the parameters used to determine the fair value for each class of financial assets and liabilities. We refer to the information set out in Note 55 regarding the quantitative disclosures on significant, unobservable parameters.

#### a. Trading assets/trading liabilities (HFT):

Securities in the trading portfolio are valued using quoted market prices and prices from the liquid OTC market to a large extent. If a current price from a liquid market is not available, interest-bearing securities are valued using mixed prices of pricing services or the discounted cash flow method based on rating- and sector-dependent yield curves derived from market data of fixed-income securities.

Exchange-traded derivatives are also valued using market prices. If no current price is available, recognised valuation models (such as the Black-Scholes model for European options) that are based on estimates of unobservable parameters to an insignificant extent at most are used.

OTC derivatives are valued using valuation techniques and models. A distinction is drawn between plain vanilla derivatives traded in liquid markets, such as interest rate swaps, cross-currency interest rate swaps, FX forwards, FX options, single-name and index credit default swaps and complex derivatives where markets are illiquid. The former are valued using recognised techniques and models (such as the discounted cash flow method for simple interest rate and cross currency swaps) that are based on unobservable market parameters to

an insignificant extent at most, while the latter require a significant number of judgements to be made with regard to the selection of both the model and the parameter estimates.

The financial crisis has resulted in derivatives being increasingly concluded on a secured basis in the interbank market (under a collateral agreement, e.g. CSA). At the same time, the collateral is also explicitly taken into account in the valuation of OTC derivatives.

**b. Positive/negative fair value of hedging derivatives:**

This class contains exclusively plain vanilla interest rate and cross-currency interest rate swaps which can be measured using recognised techniques and models.

**c. Financial investments (AfS):**

HSH Nordbank's financial investments comprise mainly fixed income securities. Substantial parts are valued using liquid market prices, such as prices from the liquid OTC market. If a current price from a liquid market is not available, interest-bearing securities are valued using mixed prices of pricing services or the discounted cash flow method based on rating- and sector-dependent yield curves derived from market data of fixed-income securities.

The financial investments also include ABS as partial holdings in the credit investment business. These are valued using the pricing hierarchy described previously.

Fair value is not calculated for unlisted equity instruments (holdings in affiliated companies and equity holdings treated under IAS 39 or IFRS 5) as there is no active market for them and the necessary estimates cannot be made within an acceptable range of variation and suitable probability of occurrence. Therefore these financial instruments are recognised at cost of acquisition.

**d. Credit derivative second loss guarantee (HfT):**

The fair value is calculated on the basis of the discounted expected cash flows and present value of the premium of 2.2% p.a. payable from 1 January 2016 for the undrawn portion of the guarantee for the share of partial guarantee Two.

**e. Assets/liabilities designated at fair value (DFV):**

Assets designated at fair value carried under financial investments and loans and advances to customers or banks primarily comprise structured registered and bearer instruments. The pricing hierarchy mentioned above is used for these products.

Liabilities designated at fair value disclosed under Securitised liabilities, Liabilities to customers or Liabilities to banks and Subordinated capital include complex structured registered and bearer securities with embedded interest, currency and equity, as well as other risks, which are mainly directly hedged by corresponding derivatives (so-called back-to-back transactions). Where current market prices or OTC market prices are available for securitised liabilities on liquid markets, these are used. However, the vast majority of DFV liabilities is measured using valuation techniques and models. These make extensive use of complex techniques and models (such as option price models) which also use market parameters which are not directly observable.

The components of the change in fair value of the DFV positions attributable to the credit rating are determined on the basis of the spreads ascertainable in the market for instruments in the respective rating category. For liabilities categorised as DFV, a distinction is made in assigning an appropriate spread between instruments with and without guarantee obligation (Gewährträgerhaftung).

**f. Assets not measured at fair value on the balance sheet (LaR):**

Cash flows are discounted using the discounted cash flow method to determine the fair value of loans and advances to customers and loans and advances to banks. Sectoral-dependent market interest rate curves as well as rating- and ratio-dependent credit spreads are used as significant parameters in this regard.

Financial instruments in the LaR category disclosed under financial investments are mainly interest-bearing securities. If a stock exchange price or a price from the liquid OTC market is not available, prices obtained from pricing services are used or the discounted cash flow method is applied, whereby rating- and sector-dependent interest rate curves derived from market data for interest-bearing securities are used as parameters for discounting the cash flows.

For current receivables (e.g. current accounts) the carrying amount is taken as the fair value. This also applies to most of the cash reserve, as this comprises credit balances at central banks.

**g. Liabilities not measured at fair value on the balance sheet (LIA)**

The majority of financial instruments disclosed under the Liabilities to banks, Liabilities to customers, Securitised liabilities, Other liabilities and Subordinated capital balance sheet line items is allocated to the LIA category. These mainly comprise non-complex structured loan notes and bearer bonds as well as deposits. If a liquid stock exchange price or a price from the liquid OTC market is not available, mixed prices obtained from pricing services are used or the discounted cash flow method is applied, in order to determine the fair value. The spreads used for this are derived from the type of collateral and the ranking of the financial instrument in relation to other liabilities of the Bank. Any existing cancellation options are also taken into account.

For current liabilities (e.g. current accounts) the carrying amount is shown at fair value.

**3. Value adjustments**

If the value of a financial instrument as determined by a valuation technique or model does not take adequate account of factors such as bid-offer spreads or closing costs, liquidity, model risks, parameter uncertainties, funding costs and benefits as well as credit and/or counterparty default risks, the Bank makes corresponding valuation adjustments, which a purchaser of similar positions would also take into account. The methods applied for this draw to some extent on unobservable market parameters in the form of estimates.

Funding costs and benefits arise on the hedging of the risks relating to an uncollateralised OTC derivative with a collateralised OTC derivative. A funding valuation adjustment is determined as part of the method used to determine fair values for derivatives and is included in the fair value of the uncollateralised OTC derivative for funding costs/benefits arising on the provision or receipt of collateral due to the hedging asymmetry of the derivatives.

Hedge relationships (back-to-back transactions) and corresponding risk-compensating effects are taken into account when determining value adjustments to be made for model risks and uncertainties regarding parameters. The value adjustment for funding costs and benefits as well as credit risk is determined for OTC derivatives at the level of a group of financial instruments of a business partner (so-called portfolio-based valuation adjustment).

This is permitted if the conditions stipulated in IFS 13.49 for a portfolio-based measurement are met.

The portfolio-based valuation adjustment for funding costs and benefits as well as for credit risk is allocated to assets or liabilities in proportion to a corresponding valuation adjustment for the asset or liability respectively, excluding portfolio effects. Allocation only takes place to the assets or liabilities depending on whether there is an excess of assets or liabilities (so-called "relative fair value approach" – net approach).

**4. Day One Profit and Loss**

The use of a valuation model may give rise to differences between the transaction price and the fair value determined using such a valuation model on the initial recognition date. If the applicable market on which the determination of the fair value is to be based differs from the market, in which the transaction was concluded and the valuation model is not based to any great extent on observable parameters, such differences (so-called day one profits and losses) are accrued to day one profit and loss reserve. This reserve is reversed over the term.

The day one profit and loss reserve does not form part of the fair value of the corresponding individual financial instruments. It is included in the carrying amount as well as in the fair value as a discount to the fair value.

**5. Measurement processes**

The Bank has implemented various processes and controls for the purpose of determining the fair values of financial instruments and has embedded principles regarding the use of measurement methods in a guideline in the written rules of procedure. These measures also ensure that financial instruments to be assigned to level 3 of the fair value hierarchy are measured in accordance with IFRS 13. The Group Risk Management division, which is independent from the Bank's market departments, is responsible for ensuring that the measurement methods applied are in accordance with external accounting requirements. Information available on the methods applied by other market participants is also taken into account in this regard.

Fair values of financial instruments assigned to level 3 are determined again on a periodic basis – but at least on a monthly basis.

Any changes in value that have occurred since the previous period are reviewed for plausibility. Where available, observable market information such as transaction prices or attributes of valuation parameters are also used in the internal price validation. If there are material differences between the fair values determined by the Bank and prices offered by counterparties, the valuation model used is subjected to an ad hoc validation process.

Information purchased from pricing service companies is also used. Where possible, the prices and procedures of these service companies are periodically checked for plausibility and reviewed in order to assess the quality of the information provided.

The measurement procedures and models as well as the estimation technique used to determine the level 3 inputs and their parameterisation are periodically reviewed and, if applicable, developed further, recalibrated or replaced by new measurement procedures or models.

#### **E) Hybrid financial instruments**

IAS 39.A8 states that for financial instruments, not to be measured at fair value, the carrying amount of financial assets and liabilities must be adjusted and recognised in profit or loss if the estimated future cash flows associated with the instrument change. The new carrying amount is given by the present value of the newly estimated future cash flows using the financial instrument's original effective interest rate for discounting. In subsequent years the discount effect reduces with constant effective interest rate, leading to a write-up for financial liabilities which is recognised in Net interest income.

Application of IAS 39.A8 had an effect in the year under review on valuation of the hybrid financial instruments issued by HSH Nordbank, as the estimated future cash flows differ from the contractual cash flows.

The term "hybrid financial instruments" covers silent participations, profit participations and bonds issued by consolidated subsidiaries measured at amortised acquisition cost. A key common feature of these instruments is that their interest depends on profit and they participate in an annual net loss of the Bank.

The future cash flows whose amount and payment dates have to be estimated are payments of interest and principal which take into account:

- participations in loss by investors, where these will probably not be made up by the expected redemption date of an instrument;
- any contractually agreed retrospective coupon payments.

The loss situation of the reporting period is not viewed in isolation on the measurement of hybrid instruments in accordance with IAS 39.A8. Specifically, it involves more than assigning the prorated loss in the period under review. In addition, the possible effects of possible future

assignment of loss and the cancellation or postponement of future interest payments must be recognised in profit or loss in the period in which the estimate is changed. This can mean that in future loss-making periods no further loss participations will be recognised in profit or loss, if these future losses correspond to the estimates made previously. The loss participation recognised in profit or loss is accordingly anticipated, rather than being left to the period in which the loss arises. Future loss-related reductions in interest also do not result in full relief to interest expenses, if the reduction in interest has already been taken into account in the estimate. Instead, the reversal of the effect of discounting applied in the year the estimate was changed is recognised in expenses (write-up of the liability due to the passage of time).

The estimation of future cash flows from hybrid financial instruments required in applying IAS 39.A8 requires material assumptions which are associated with uncertainties. The assumptions made are subject to a periodic review and are adapted to the changed underlying conditions where necessary. Among the key sources of uncertainty in estimation are the future income of HSH Nordbank, which depends specifically on the development of the economy. Assumptions are also required about the exercise of termination or extension options associated with the individual transactions. Based on the degree of knowledge about uncertainties at the time financial statements are drawn up, the possibility cannot be excluded that changing information in subsequent periods will require departure from previous assumptions, which would require new adjustments to the carrying amount of hybrid financial instruments recognised in profit or loss. In the case of declining expectations of loss, the participation in loss of investors would also decrease, which would be associated with an increase in our repayment obligations recognised in expenses. The same considerations apply to the reverse case.

Net income from hybrid financial instruments is shown as a separate item under Net interest income, and in addition to current interest expenses it includes the effects of applying IAS 39.A8 (see Note 9). Deferred taxes arise because of the difference between valuation for tax purposes and measurement in the Group financial statements. The associated effects on net income are recognised under income taxes. Hybrid financial instruments are shown either as securitised liabilities or as subordinated capital (see Notes 40 and 49).



## F) Hedge accounting

Under IFRS, changes in value of items in IAS 39 categories AfS, LaR and LIA are not recognised in profit or loss. Changes in the value of derivatives are always recognised in profit or loss. If underlying transactions in IAS 39 category AfS, LaR or LIA are hedged with derivatives, the result is to distort the statement of income so that it does not correspond to the economic reality. One possibility to avoid these distortions is to use fair value hedge accounting. In fair value hedge accounting the changes in value of hedged items, which are attributable to the hedged risk, are recognised in profit or loss.

HSH Nordbank uses derivatives to hedge market risks resulting from loans, issues and securities portfolios. Portfolios of financial instruments are hedged in this way. Up until 30 June 2016, this hedging was also used at individual transaction level (i.e. for individual loans, issues and securities positions).

Portfolio fair value hedge accounting is used to avoid distortions in the statement of income. Currently only hedges of fair value against interest rate risk are taken into account. Fixed-interest rate loans, issued instruments and securities positions are designated as underlying transactions (hedged items), while only interest rate and interest rate currency swaps are designated as hedging instruments. Micro fair value hedge accounting was also used up until 30 June 2016.

Where portfolios of underlying transactions are hedged, the hedging of these items with matching external derivatives is shown under portfolio fair value hedge accounting to the extent that this meets the requirements of IAS 39.

In the case of portfolio fair value hedge for interest rate risks, portfolios of assets and liabilities hedged for interest rate risks are taken into account. This involves an iterative procedure. At the start of a hedging period, the financial instruments in the portfolios are allocated to maturity ranges on the basis of their anticipated maturity or interest adjustment dates, and the hedged amount is then determined for each maturity range. The hedging transactions are also allocated at the start of the hedging period. At the end of the hedging period, the hedge is recognised and measured and a new hedge is designated. The changes in the fair value of the hedged amounts of the underlying transactions due to the hedged risk are recognised in a separate item in the statement of financial position (asset or liability reconciling items from the portfolio fair value hedge). The fair value changes which are not attributable to the hedged risk are treated in accordance with the general rules for the corresponding IAS 39 category.

Where individual lending, issuing or securities transactions were hedged by derivatives with non-Group counterparties and these hedging arrangements satisfied the requirements of IAS 39, micro fair value hedge accounting was applied up until 30 June 2016.

In the case of a micro fair value hedge, the carrying amount of the underlying transaction was adjusted through the statement of income for the fair value change attributable to the hedged risk. The fair value changes which are not attributable to the hedged risk were treated in accordance with the general rules for the corresponding IAS 39 category.

Using fair value hedge accounting requires a series of conditions to be met. These principally relate to the documentation of the hedge and its effectiveness. HSH Nordbank documents all hedging relationships in accordance with the requirements of IAS 39, including the hedging instrument, the hedged item (underlying transaction), the hedged risk and the result and method of measuring effectiveness.

Future changes in value of underlying and hedging transactions are simulated using a regression model within the framework of the prospective effectiveness test. Any actual changes in value are used in retrospective effectiveness testing. In portfolio fair value hedge accounting, HSH Nordbank uses the dollar offset method to measure effectiveness retrospectively. This tests whether the relationship between the changes in value of underlying and hedging transactions lies within an interval of 80% to 125%. The results of retrospective and prospective effectiveness measurement in micro fair value hedge accounting were analysed using regression analyses.

Changes in value of underlyings and hedging transactions in effective hedges which are attributable to the hedged risk are recognised in the Result from hedging.

Income and expenses from the depreciation of reconciling items for the fair value hedge portfolio and proceeds from the closing of the underlying transactions which contributed to reconciliation items are reported as part of the Net interest income.

**G) Derecognition**

A financial asset is derecognised when all material risks and opportunities associated with ownership of the asset have been transferred, i.e. when contractual claims on cash flows from the asset have been extinguished. Where not all risks and opportunities are transferred, the HSH Nordbank carries out a control test to ensure that no continuing

involvement due to opportunities and risks retained prevents it from being derecognised. Financial assets are also derecognised if the contractual rights to cash flows have expired. If the material contractual elements of an asset, particularly a loan, are altered as part of restructuring, this also results in a derecognition. Financial liabilities are derecognised when they are repaid, i.e. when the associated liability is settled or lifted or when due respectively.

**H) Repurchase agreements and securities lending transactions**

HSH Nordbank only enters into genuine repo transactions. Genuine repo transactions, repo agreements or sell-and-buy-back transactions combine the spot purchase or sale of securities with their forward sale or repurchase, the counterparty being the same in both cases.

For genuine repo transactions with assets sold under repurchase agreements, the securities continue to be recognised by HSH Nordbank, as the interest, credit rating and other material risks associated with the securities continue to be borne by HSH Nordbank. According to counterparty, the inflow of liquidity from the repo transaction is shown in the statement of financial position as a liability either to banks or customers. Interest payments are recognised under interest expense over the term of the transaction. Outflows of liquidity caused by reverse repos are reported as loans and advances to banks or customers. Correspondingly, the securities bought under repurchase agreements are not carried or measured in the statement of financial position. Agreed interest payments are booked as interest income over the term of the transaction. Receivables arising from repos are not netted against liabilities from repos involving the same counterparty, since the criteria for netting are not met.

The emphasis in repo transactions is on bonds from German public sector issuers and from bank issuers and the Bank's own bonds. Securities lending transactions are carried on the statement of financial position in a similar way to genuine repurchase agreements. Lent securities remain in the securities portfolio, while borrowed securities are not capitalised on the statement of financial position. Cash collateral furnished for securities lending transactions is shown as a receivable, while collateral received is shown as a liability. Repo and securities lending transactions are carried out primarily in bonds.

**I) Financial guarantee contracts**

Pursuant to IAS 39.9, a financial guarantee is a contract that requires the issuer of the contract to make specified payments to reimburse the holder of the contract for the loss that the holder incurs because a specified debtor fails to make payment when due under the original or amended terms of a debt instrument. A credit derivative is treated as a financial guarantee based on the provisions of IAS 39 if the requirements of IAS 39.9 for the financial guarantee are met. Credit derivatives that do not meet the definition of a financial guarantee are allocated in accordance with the general valuation rules for the HfT category and valued at fair value.

Financial guarantees at HSH Nordbank are provided in the form of warranties, bank guarantees and letters of credit. Corresponding contingent liabilities are based on past events that may result in possible liabilities in the future. These liabilities arise as a result of the occurrence of unspecified future events where the amount required to meet them cannot be estimated with sufficient reliability. Financial guarantees are stated in accordance with the net method. If an adequately reliable estimate of the settlement amount is possible, a provision is recognised. If the premium payment to HSH Nordbank is distributed over the term of the financial guarantee, the guarantee will be stated as zero and the premium payment recognised on an accrual basis. If HSH Nordbank is the holder of a contract, the financial guarantee will be presented as collateral for the Group.

**II. Notes on selected items relating to financial instruments in the statement of financial position****1. Cash reserve**

Cash on hand, balances with central banks, treasury bills and discounted treasury notes are stated under cash reserve.

Both initial and subsequent measurement of assets (LaR) stated under cash reserve takes place at par value, which is equivalent to fair value due to its short-term nature.

Treasury bills and discounted treasury notes recognised under AfS are measured at fair value.

**2. Loans and advances**

Primarily assets from the loans and receivables (LaR) category are recognised in the statement of financial position under Loans and advances to banks and Loans and advances to customers. In addition, financial instruments in the categories DFV and AfS are recognised here. Carrying amounts of receivables which are an element of micro fair value hedge accounting are adjusted by the change in value attributed to the hedged risk.

Loans and receivables of the category LaR are stated gross (before deduction of impairments). Loan loss provisions for impairments are stated in a separate item Loan loss provisions, shown under Loans and advances as a deduction. Financial instruments in the DFV and AfS categories are stated net. Where loans and receivables have been acquired or incurred with the intention of trading, they are stated under trading assets. If the disposal of loans and advances was decided and initiated as at the balance sheet date and it is highly probable that it can be completed within the following twelve months, they are reclassified as Non-current assets held for sale and disposal groups.

Interest income from loans and advances to banks and customers is recorded under Interest income from lending and money market transactions. This also includes early repayment penalties from premature repayment of receivables. Premiums and discounts are accrued over the term of the loans and advances using the effective interest rate method. Accrued interest is also allocated to this item in the statement of financial position.

If it is determined that a loan or advance is impaired, the calculation of interest accruals in accordance with the contractual terms of the loan or advance is discontinued. Interest income is instead determined on the basis of the interest rate used to discount the future cash flows for determining the impairment amount (unwinding).

Fees charged that are directly linked to the granting of a loan are deferred and accrued over the term of the loan or advance. Fees for services that are provided over a certain period of time are recognised over this period in which the service is performed. Commissions associated with the provision of a certain service are recognised as at the date the service has been provided in full.

If, in the case of non-genuine securitisation transactions, our loans and advances are not derecognised and the risk on such loans and advances remains fully with HSH Nordbank, we recognise any necessary loan loss provisions solely on our original loans and advances.

### 3. Positive and negative market value of hedge derivatives

This item shows the market value of derivatives which have a positive or negative fair value and which are used in hedge accounting. Only interest rate and interest rate currency swaps are taken into account as hedging instruments currently. If a derivative is only partially designated under hedge accounting, this item contains the corresponding share of that derivative's fair value. In these cases, the remainder is stated under Trading assets or Trading liabilities.

### 4. Reconciling asset and liability items from the fair value hedge portfolio

The asset-side reconciling item from portfolio fair value hedge accounting contains the value change of the hedged object to be attributed to the hedged risk from portfolio fair value hedges for assets. Similarly, the liability-side reconciling item from portfolio fair value hedge accounting contains the value change of the hedged object to be attributed to the hedged risk from portfolio fair value hedges for liabilities.

### 5. Trading assets and trading liabilities

Only financial assets classified as HfT are stated under Trading assets. These include primary financial instruments held for trading purposes, particularly fixed income securities and pro rata interest, and also equities and other trading portfolios such as precious metals. Loans and loan commitments with hard syndication conditions are also reported here. A significant component continues to be derivatives with a positive market value which are either trading derivatives or not designated as a hedging derivative because they do not meet the requirements of hedge accounting.

Measurement gains and losses are recognised in Net trading income. Interest income and expenses as well as dividend income are disclosed under Net interest income. Dividends are recognised when the right to receive payment is established. Commission income and expenses are disclosed in Net commission income.

In a similar way to trading assets, trading liabilities only include financial obligations belonging to the category held for trading (HfT), which includes derivatives with a negative market value which are either trading derivatives or which have not been designated as a hedging derivatives because they do not meet the requirements of hedge accounting. Delivery commitments from short sales of securities and pro rata interest from these are also stated in this category.

### 6. Financial investments

Financial investments include particularly portfolios in the AfS category, and also securities or holdings in the categories LaR and to a lesser extent in the DFV category. This item includes fixed-interest securities including accrued interest, equities and other non-fixed-interest securities, holdings in unconsolidated affiliated companies, and holdings in joint ventures and associates not carried at equity. Realised gains and losses from financial investments are shown in the statement of financial position in Net income from financial investments to the extent they are not DFV holdings. Net interest income from financial investments is shown in Net interest income.

Dividends on financial assets are recognised when the right to receive payment is established. If the disposal of equity holdings or interests in affiliated companies was decided and initiated at the balance sheet date and it is highly probable that it can be completed within the following twelve months, they are reclassified as Non-current assets held for sale and disposal groups.

#### 7. Financial investments accounted for under the equity method

Shares in associates included in the Group financial statements under the equity method are reported in this item. Such ownership interests are measured in accordance with the guidelines of IAS 28 in conjunction with IFRS 11.

For the impairment testing of financial investments accounted for under the equity method the total carrying amount of the investment measured under the equity method is assessed for impairment as a single asset in accordance with IAS 36. Its realisable amount is always compared with the carrying amount for this purpose, if there are indications on applying IAS 39 that the investment could be impaired.

The realisable amount is defined as the greater of fair value less costs to sell and value in use. (See also Note 8.III.1 for details on the calculation of the value in use).

#### 8. Liabilities

Liabilities include financial liabilities in categories LIA and DFV. They are recognised as Liabilities to banks, Liabilities to customers, Subordinated debt and Securitised liabilities.

Financial liabilities are recognised at fair value at the time of issue plus transaction costs, which generally corresponds to the transaction price. In subsequent periods securities categorised as LIA are measured pursuant to IAS 39.47 at amortised cost applying the effective interest method. Changes in the measurement of LIA financial instruments are only recorded when the relevant instrument is sold. Differences between acquisition costs and repayment amount (e.g. premiums and discounts) are allocated according to the effective interest rate method and taken to net interest income. Current gains and losses from measuring DFV financial instruments are stated under Net trading income.

The carrying amount of hedged liabilities which fulfil the requirements of micro fair value hedge accounting are adjusted by the gains and losses arising from fluctuations in fair value attributable to the hedged risk.

Repurchased own debentures are set off against securitised liabilities.

#### 9. Subordinated capital

Subordinated liabilities, silent participations and profit-sharing certificates are shown under Subordinated capital, due to their different nature from other liabilities. Silent participations are structured as so-called hybrid financial instruments without exception and so are some profit-sharing certificates (cf. Note 8.I.E.). No obligation to other creditors for premature redemption of subordinated liabilities is possible. In the case of liquidation or insolvency, subordinated liabilities may only be repaid after the claims of all senior creditors have been met.

Based on their contractual structure and financial character, the participations of the typical silent partner represent debt, which is why they are stated under subordinated capital.

Subordinated capital categorised as LIA is recognised and measured initially at fair value (taking the transaction costs into account) and at amortised acquisition cost subsequently. Premiums and discounts are allocated on a constant effective interest rate basis.

Current gains and losses from measuring subordinated capital categorised as DFV are stated under Net trading income.

See Note 8.I.E. with regard to the treatment of hybrid financial instruments in the year under review.

### III. Notes on other items in the statement of financial position

#### 1. Intangible assets

Software acquired or developed in-house and acquired goodwill are accounted for under Intangible assets. In accordance with IAS 38.21, HSH Nordbank capitalises software development costs if the production of the in-house software is likely to generate an economic benefit and the costs can be reliably determined. If the criteria for capitalisation are not met, expenses are recognised in profit or loss in the year they are incurred. Subsequent costs are only to be capitalised if they lead to a significant improvement of the software in the form of an expansion of the software's functionality. Since HSH Nordbank does not apply the full goodwill approach, goodwill arises on acquisition of subsidiaries, when the cost of acquisition exceeds the Group's share in the remeasured net assets (shareholders' equity) of the company acquired.



The initial measurement of intangible assets is made at acquisition or production costs in accordance with IAS 38.24. They are subsequently measured at amortised acquisition or production cost.

Software developed in-house is subject to linear depreciation over two to ten years.

If there are indications of impairment, intangible assets are subject to an impairment test. For this test the carrying amount of these intangible assets is compared with the realisable amount. The realisable amount is defined as the greater of fair value less costs to sell and value in use. An asset is impaired if its carrying amount exceeds its realisable amount. Intangible assets with an indefinite useful life, intangible assets not ready for use as well as goodwill are subject to an annual impairment test even if there are no signs which suggest impairment.

Examination of the value of goodwill is carried out on the basis of cash-generating units. Cash-generating units of HSH Nordbank for non-strategic investments are defined based on the internal management level (global head structure). Each global head unit forms an own cash-generating unit. A company is regarded as a non-strategic investment if underlying subsidiaries are integrally involved in the business activities of the respective global heads. However, if the value in use is expected to be realised by cash inflows or an increase in value of a subsidiary alone, then the subsidiary itself continues to be a cash-generating unit (so-called strategic investment). Where the anticipated benefit can no longer be determined, a write-down is made.

The value in use of a cash generating unit is determined on the basis of forecast and discounted net cash flows. Net cash flows are usually determined on the basis of Group planning for a detailed planning period of five years. For subsequent periods the planned cash flows of the last year of the plan are taken into account allowing for a growth trend. The planned cash flows are based on a risk-adequate discount rate.

## 2. Property, plant and equipment

Land and buildings, plant and equipment and leasing assets under operating leases where HSH Nordbank acts as lessor are stated under this item. Property, plant and equipment is stated at cost of acquisition or production less linear depreciation in line with its expected useful life. Subsequent costs of acquisition or production are capitalised provided they increase the economic utility of the asset concerned. Interest paid to finance acquisition costs of property, plant and equipment is recorded as an expense in the period concerned.

Physical wear and tear, technical obsolescence and legal and contractual restrictions are taken into consideration when determining useful life. For property, plant and equipment, linear depreciation is calculated over the following periods:

### CATEGORY OF PROPERTY, PLANT AND EQUIPMENT

	<b>Useful life in years</b>
Buildings	50
Leasehold improvements	Calculation of residual life is based on the remaining term of the rental agreement.
Other operating equipment	3–15
Leasing assets	Customary useful life

Property, plant and equipment is reviewed at each reporting date for signs which suggest impairment.

Gains and losses from the disposal of property, plant and equipment are shown under Other operating income in the statement of income. Repairs, servicing and other maintenance costs are recorded as an expense in the period concerned.

## 3. Investment property

Under the item Investment property properties are disclosed that are held to earn rental income or make capital gains but are not used for own operations. For mixed use properties a percentage allocation of the carrying amount is made. Own-used properties are reported under Property, plant and equipment; rented-out or empty parts are reported as Investment property. The properties are recognised at acquisition cost and depreciated on a straight-line basis.

A useful life of 50 years is used for depreciation purposes. The capitalised income method is used in determining the fair value of investment properties, using market data from internal certified appraisers. The fair value is disclosed in Note 33.

#### 4. Non-current assets held for sale and disposal groups and liabilities relating to disposal groups

Non-current assets whose carrying amounts will be predominantly or primarily realised through a sale and not through continuing use must be classified as held for sale in accordance with IFRS 5 on the condition that a sale has already been decided on and initiated as of the reporting date, and is extremely likely to be completed within the following twelve months.

A disposal group is a group of assets which are sold to the same purchaser in a single transaction and at a single price. A disposal group can also include liabilities, if these are taken over by the purchaser together with the assets.

Non-current assets and disposal groups held for sale are to be measured at the lower of carrying amount or fair value less sale costs. Financial instruments continue to be measured according to the requirements of IAS 39.

#### 5. Provisions

Provisions are created where the Group has existing legal and actual obligations resulting from previous events and it is likely that meeting the obligation will require an outflow of resources and a reliable assessment of the amount of the obligation can be made. Provisions are examined and redetermined at least quarterly.

##### Pension provisions

The majority of employees of HSH Nordbank AG as well as employees of several domestic subsidiaries are entitled to benefits from different staff pension plans, which include both defined contribution and defined benefit plans.

In the case of defined contribution plans, contractual relationships with Provinzial NordWest Lebensversicherung AG for direct insurance policies partly financed by employees exist. As the insurance company is required to be a member of Protektor Lebensversicherungs-AG, the insured employees are protected against its insolvency, so that HSH Nordbank AG is not burdened even in the event of Provinzial NordWest Lebensversicherung AG's insolvency. These direct insurance policies represent insured benefits and are treated as defined contribution plans.

In the case of the defined benefit plans, the amount of benefit depends on various factors, such as age, salary and length of service. Pension plans include specifically retirement and disability pensions and survivor benefits. They are based primarily on employment contracts of Landesbank Schleswig-Holstein Girozentrale, the retirement plan of Hamburgische Landesbank Girozentrale, retirement pension guidelines of the Hamburgische Landesbank Girozentrale relief fund, the pension plan of Hamburgische Landesbank Girozentrale and Section 2 (4) of the Investment Bank Act in the version of 23 January 1998. The pension payment amount depends on the final salary paid immediately prior to retirement, the salary trend up to retirement is irrelevant (no performance components). The pension plans provide for on-going pension payments and no capital payments. Minimum guarantees are not provided for. Pension provisions for defined benefit plans are equivalent to the net present value of the pension entitlements earned as of the reporting date, factoring in anticipated wage and salary increases and the trend in annuities. Calculations are based solely on actuarial reports based on IAS 19, which are prepared by independent actuaries using the projected unit credit method.

These defined benefit plans were closed in 2002.

HSH Nordbank AG also participates in a multi-employer plan which is run by BVV Versorgungskasse des Bankgewerbes e.V. Contributions are regularly paid with participation from the employees. The BVV tariffs provide for fixed pension payments with profit participation. For BVV, employers have a subsidiary liability for the liabilities of their employees. HSH Nordbank AG classifies the BVV plan as a defined-benefit joint pension scheme provided by a number of employers. As the BVV relief fund does not fully allocate its assets neither to the beneficiaries nor the member companies and as the information available for its accounting treatment as a defined benefit plan is insufficient to be able to allocate the assets and pension commitments to the current and former employees of the individual member companies, the plan is treated as a defined contribution plan for accounting purposes. It appears unlikely that there will be any call based on the statutory subsidiary liability.

The remeasurement of net defined benefit liabilities is disclosed under Other net income and under Equity in Retained earnings in the year in which they arise. Pension provisions are discounted as long-term liabilities. The interest expense included in expense for retirement pensions is recognised as part of Net interest income.

The following assumptions are made in calculating direct benefit pension liabilities:

#### ACTUARIAL ASSUMPTIONS

	2016	2015
Discount rate		
Domestic	1.66%	2.37%
Foreign (weighted)	1.66%	2.37%
Salary growth (weighted)	2.0%	2.0%
Adjustment rate for pensions		
Domestic		
Employment contract 1/ old pension provision rules	individual	individual
New pension provision rules (weighted)	2.0%	2.0%
Employment contract 4 (weighted)	2.0%	2.0%
	Based on the 2005 G tables of K. Heubeck	Based on the 2005 G tables of K. Heubeck
Mortality, disability, etc.		

Actuarial assumptions are subject to a sensitivity analysis as described in Note 44.

Defined benefit pension plans are partly financed from assets and qualified insurance policies used exclusively for pensions (plan assets). Plan assets are measured at fair value and recognised in the statement of financial position as reducing provisions.

#### Other provisions

Other provisions include provisions in the lending business, for restructuring, litigation risks and costs, for personnel expenses (without pensions) and other provisions.

Provisions in the lending business are created, among other reasons, for any sudden calls to pay under warranty bonds, guarantees and letters of credit. The parameters used for the calculation are presented in the section Loan loss provisions and impairment of financial instruments (Note 8.I.C).

Provisions for restructuring are created to the extent HSH Nordbank had developed and communicated a sufficiently detailed plan for such measures and had started to implement such plan. As soon as the obligation is sufficiently certain or can be quantified – e.g. through the signing of agreements – it is transferred to Other liabilities or Provisions for pensions and similar obligations as a matter of principle.

In the statement of income, the item “Net income from restructuring and privatisation” is used to report the ongoing expenses incurred in respect of restructuring measures taken in direct connection with the formal decision made in the state aid proceedings by the European Commission on 2 May 2016 on the replenishment of the second loss guarantee, as well as the expenses connected with the privatisation of HSH Nordbank. In addition, further provisions were set up in the first half of 2016 for additional job cuts in the period leading up to 2019. The expenses incurred in the 2016 financial year are explained in more detail in Note 19.

Provisions for litigation costs comprise expected payments for court costs as well as for non-court costs in connection with litigation such as, e.g. attorneys' fees and other costs. For litigation in progress, only costs for the current jurisdictional level may be included within the provision.

Provisions for litigation risks are to be created when HSH Nordbank AG or any of its consolidated subsidiaries is the defendant in an action and the probability that the Bank will lose the action is presumed to be greater than 50%. Provisions include only payments for probable liability for damages and fines as well as costs of litigation at the current level of appeal. The general measurement rules on provisions apply. The mandatory disclosures defined in IAS 37.86 are made for litigation risks that are not considered likely to arise, but which cannot be entirely excluded.

Under Provisions for personnel expenses, in general all outstanding benefits within the personnel expenses are presented with the exception of pension obligations. In the HSH Nordbank, these are in particular provisions for variable performance-related pay, anniversary payments, partial retirement and long-term

credits for hours. Provisions for anniversary payments and partial retirement are accounted for based on actuarial expert reports.

In accordance with IAS 37, provisions are mainly determined based on the best estimate of management. The most likely amount necessary to meet the obligations identifiable on the reporting date is recognised. Long-term provisions are reported at present value to the extent discounting effects are significant. For discounting purposes, interest rates that are valid on the reporting date and are term-appropriate are used based on risk-free interest curves. Addition of accrued interest to be performed during the reporting year is reported under Net interest income.

## 6. Income taxes

Current tax assets and liabilities are stated at the amount of the anticipated refund from, or payment to, the tax authorities, applying the tax provisions of the countries in question.

Deferred tax assets are created for all deductible timing differences between the value of an asset or liability as measured by IFRS standards and its assigned value in tax terms, provided it is probable that taxable income will be available against which such differences can be utilised. Deferred tax liabilities are created for all taxable temporary differences. Deferred taxes on tax loss carry-forwards are stated as the amount likely to be used in future. Deferred taxes are calculated using the tax rates and rules anticipated to be valid at the time when the deferred tax assets are to be realised. The effects of tax rate changes on deferred taxes are taken into account on adoption of the legislative amendment. Deferred tax assets are recognised and measured as deferred income tax claims and deferred tax liabilities as Deferred income tax liabilities.

HSH Nordbank prepares tax results planning for the purpose of assessing deferred tax asset impairment.

Expenses and income from deferred taxes are in principle recognised on an accrual basis in the statement of income under Income taxes, separate from actual tax expenses and income. In doing so, the accounting treatment of the underlying situation is taken into account. Deferred taxes are recognised in the statement of income if the item in the statement of financial position itself is recognised in profit or loss. Deferred taxes are charged or credited directly to equity in OCI, if the underlying item itself is charged or credited directly to equity (IAS 12.61A).

At each reporting date HSH Nordbank makes an assessment as to whether the realisation of future tax benefits is sufficiently probable to recognise deferred tax assets. Amongst other things, this requires a management assessment of the tax benefits that arise from the existing tax strategies and future taxable income as well as the consideration of other positive and negative factors. The deferred tax assets disclosed could decrease, if the estimates of the planned taxable income and the tax benefits achievable under the existing tax strategies are revised downwards or if changes to current tax legislation restrict the timing and extent of the realisability of future tax benefits.

## 7. Other assets and other liabilities

All remaining assets and liabilities not allocable to any other item are stated under Other assets or Other liabilities. These include accrued expenses and income amongst other things.

The general recognition and measurement criteria for assets are observed. Initial recognition is at cost. For financial instruments included in this item the provisions of IAS 39 apply.

## IV. Leasing transactions

Pursuant to IAS 17, the term “lease” refers to the transfer of use for an agreed period in return for a fee. A distinction is made between finance and operating leases. The allocation depends on whether substantially all risks and rewards are transferred to the lessee or not.

A finance lease is considered to be present where the economic risks and rewards as defined by IAS 17 lie with the lessee; consequently, the leased asset is reported in the latter’s statement of financial position. All other leasing arrangements are classified as operating leases. The classification is made at the beginning of each lease.

### 1. Finance leases

In the case of finance leases, HSH Nordbank acts solely as lessor and recognises a receivable in the amount of the net investment value either under Loans and advances to banks or Loans and advances to customers, depending on the lessee.



Leasing rates due are divided into a repayment part which is not recognised in profit or loss and an interest part which is. The part taken to profit or loss is recognised in Net interest income.

Impairments of finance lease receivables attributable to changes in credit risk are recognised in Loan loss provisions. Impairments not attributable to changes in credit risk, such as the impairment of the non-guaranteed residual value of a leasing receivable, are recognised in other operating expense.

## 2. Operating leases

As lessor HSH Nordbank states leasing objects as assets measured at amortised cost under Property, plant and equipment or as Investment property. Leasing instalments received are stated under Other operating income, and the corresponding depreciation stated in Administration expenses.

## V. Currency translation

The Group financial statements of HSH Nordbank are drawn up in euros. The euro is the functional currency of the overwhelming majority of the individual financial statements included in the Group financial statements. However some Group companies have another functional currency.

The following principles are applied when translating foreign currency items within single entity financial statements and for translating the financial statements of Group companies which do not draw up their accounts in euro.

### 1. Presentation of foreign currency transactions in the Group financial statements

Initial measurement of assets and liabilities from all foreign currency transactions takes place at the spot rate for the transaction.

In subsequent measurement, monetary items are translated based on the spot mid-rate as of the reporting date. Non-monetary items that are stated in the statement of financial position at fair value are translated using the spot mid-rate applicable at the time of measurement and any other non-monetary items at the historical rate.

Expenses and income in foreign currency arising from the measurement of items in the statement of financial position are translated using the rates applied for translating the items in question. The transaction rates are used for all other expenses and income.

For monetary and non-monetary items measured at fair value, currency translation differences are always recognised in the statement of income of the period when the result arose. An exception are currency translation gains and losses from the measurement of non-monetary AFS financial instruments recognised at fair value, which are recognised in OCI.

### 2. Translation of financial statements prepared in foreign currency for inclusion in the Group financial statements

Assets and liabilities from financial statements denominated in foreign currencies are translated at the period-end rate. Average rates for the reporting period are used to translate expenses and income. With the exception of the revaluation reserve reported to be included in the financial statements, which is translated at the closing rate, equity is translated at historic rates (date of the transaction).

Any differences arising from this method of translation are reported under OCI and under Equity in the Currency reserve.

## NOTES ON THE GROUP STATEMENT OF INCOME

### 9. NET INTEREST INCOME

NET INTEREST INCOME (€ m)	2016	2015
Interest income from		
Lending and money market transactions	1,245	1,569
Fixed-interest securities	259	329
Trading transactions	5	9
Derivative financial instruments	1,624	2,211
Unwinding	162	207
Sale of promissory note loans	142	26
Current income from		
Equities and other non-fixed-interest securities	8	9
Equity holdings in non-affiliated companies	17	29
Other holdings	4	8
<b>Interest income</b>	<b>3,466</b>	<b>4,397</b>
of which attributable to financial instruments not classified as HfT or DFV	1,561	1,925
Negative interest resulting from		
Lending and money market transactions	-13	-9
Derivative financial instruments	-178	-46
<b>Negative interest</b>	<b>-191</b>	<b>-55</b>
Interest expenses for		
Liabilities to banks	148	219
Liabilities to customers	472	625
Securitised liabilities	299	434
Subordinated capital	25	82
Other liabilities	24	10
Sale of promissory note loans	11	12
Derivative financial instruments	1,754	2,061
<b>Interest expenses</b>	<b>2,733</b>	<b>3,443</b>
of which attributable to financial instruments not classified as HfT or DFV	571	841
Positive interest for		
Liabilities to banks	-2	-
Liabilities to customers	-6	-
Derivative financial instruments	-175	-29
<b>Positive interest</b>	<b>-183</b>	<b>-29</b>
Net income from re-estimating interest and repayment cash flows	-	214
Net income from discounting and compounding	-118	-110
<b>Net income from hybrid financial instruments</b>	<b>-118</b>	<b>104</b>
of which attributable to financial instruments not classified as HfT or DFV	-118	104
<b>Total</b>	<b>607</b>	<b>1,032</b>

Interest income and expenses relating to trading and hedging derivatives are disclosed under interest income and expense from/for trading and hedging derivatives.

Net interest income includes income and expenses arising from the amortisation of the adjustment items for portfolio fair value hedge relationships and corresponding proceeds from the closing of the underlying transactions which contributed to the adjustment item.

The net interest income from impaired loans and advances is determined by compounding the present value of the expected payment flows at the original effective rate of interest (unwinding).

The term hybrid financial instruments covers silent participations, profit participation capital and bonds measured at amortised cost, the return on which is profit-related and which participate in the net loss for the year and accumulated losses of the Bank.

The total of current participation in losses (not allowing for anticipated reversals of impairment losses) relating to the 2016 financial year was € 0 million (previous year: € 39 million).

Net income or loss from hybrid financial instruments includes both the effects on profit/loss resulting from the application of IAS 39.A8 as well as the current interest income from the instruments that fall under the scope of application of this standard.

The cumulative net income from hybrid financial instruments amounts to € 343 million as at 31 December 2016 (previous year: € 461 million). € 1,644 million are attributable to the result from re-estimating interest and principal repayment flows (previous year: € 1,644 million) and € -1,301 million are attributable to the income/loss from discounting and compounding (previous year: € -1,183 million).

The difference between the valuation for tax purposes and measurement under IAS 39.A8 results in deferred tax assets of € 15 million (previous year: € 5 million).

## 10. NET COMMISSION INCOME

### NET COMMISSION INCOME

(€ m)	2016	2015
Commission income from		
Lending business	52	71
Securities business	10	20
Guarantee business	15	22
Payments and account transactions as well as documentary business	25	23
Other commission income	13	13
<b>Commission income</b>	<b>115</b>	<b>149</b>
Commission expense from		
Lending business	4	3
Securities business	6	17
Guarantee business	5	6
Payments and account transactions as well as documentary business	5	4
Other commission expenses	8	5
<b>Commission expenses</b>	<b>28</b>	<b>35</b>
<b>Total</b>	<b>87</b>	<b>114</b>

Financial instruments not classified as HfT or DFV accounted for € 87 million (previous year: € 113 million) of net commission income. The premium expense resulting from the synthetic securitisation transaction (see Note 3.II) is reported under net commission income.

## 11. RESULT FROM HEDGING

The change in value attributable to the hedged risk for designated underlying and hedging transactions in effective hedging relationships is reported under the item Result from hedging. The item contains the corresponding profit contributions from micro and portfolio fair value hedges. Hedge accounting is used solely for interest rate risks.

### RESULT FROM HEDGING

(€ m)	2016	2015
Fair value changes from hedging transactions	-15	-47
Micro fair value hedge	-16	-21
Portfolio fair value hedge	1	-26
Fair value changes from underlyings	11	59
Micro fair value hedge	16	23
Portfolio fair value hedge	-5	36
<b>Total</b>	<b>-4</b>	<b>12</b>

## 12. NET TRADING INCOME

Net trading income comprises realised gains and losses and measurement gains and losses on financial instruments classified as HfT and DFV. Interest income and expense for financial instruments in these categories are disclosed in Net interest income.

Gains and losses arising on currency translation are generally disclosed in this statement of income line item. The results from the translation of loan loss provisions denominated in foreign currency not hedged against foreign exchange risk are disclosed in the loan loss provisions.

Other products comprises the income from foreign exchange transactions, credit derivatives and commodities.

### NET TRADING INCOME

(€ m)	2016	2015
Bonds and interest rate derivatives		
HfT	10	128
DFV	96	29
<b>Total</b>	<b>106</b>	<b>157</b>
Equities and equity derivatives		
HfT	-2	56
DFV	-4	-52
<b>Total</b>	<b>-6</b>	<b>4</b>
Other products		
HfT	-11	-79
DFV	-1	2
<b>Total</b>	<b>-12</b>	<b>-77</b>
<b>Total</b>	<b>88</b>	<b>84</b>

Net trading income includes net income from foreign currency of € -6 million (previous year: € -79 million).

During the reporting period € -18 million (previous year: € -1 million) of the changes in fair value of the financial assets categorised as DFV related to changes in the credit spread rather than changes in market interest rates. In cumulative terms, a total of € -25 million (previous year: € -16 million) is attributable to changes in the credit spread.

In the period under review, changes in value related to changes in the credit spread rather than to market interest rate changes for liabilities in the category DFV amounted to € 9 million (previous year: € 30 million). In cumulative terms, a total of € 13 million (previous year: € 2 million) is attributable to changes in the credit spread.



### 13. NET INCOME FROM FINANCIAL INVESTMENTS

In addition to any realised gains and losses from financial investments classified as loans and receivables (LaR) and available for sale (AfS), write-downs and write-ups and general loan loss provisions are reported under this item. In the case of financial investments classified as AfS, write-ups are only recognised in the statement of income for debt instruments up to a maximum of the amortised cost.

In the year under review, equity instruments classified as AfS not measured at fair value with a carrying amount of € 26 million (previous year: € 42 million) were disposed of. This resulted in realised income of € 0 million (previous year: € 6 million). Remaining instruments of this kind were written down by € 3 million (previous year: € 7 million).

#### NET INCOME FROM FINANCIAL INVESTMENTS

(€ m)	2016	2015
Classified as AfS		
+ Realised gains/losses (-)	69	62
- Write-downs	44	48
+ Write-ups	-	-
<b>Total</b>	<b>25</b>	<b>14</b>
Classified as LaR		
+ Realised gains/losses (-)	41	- 12
- Write-downs	6	16
+ Write-ups	77	43
<b>Total</b>	<b>112</b>	<b>15</b>
+ Reversal of general loan loss provisions (LaR portfolios)	3	25
<b>Total</b>	<b>3</b>	<b>25</b>
<b>Total</b>	<b>140</b>	<b>54</b>

### 14. NET INCOME FROM FINANCIAL INVESTMENTS ACCOUNTED FOR UNDER THE EQUITY METHOD

As at the 31 December 2016 balance sheet date, HSH Nordbank owns shares in one associate and one joint venture (previous year: one associate and one joint venture) that are included in the Group financial statements under the equity method (see Note 6).

The pro rata net income assigned to the Group from financial investments accounted for under the equity method as at 31 December 2016 is summed up below:

#### NET INCOME FROM FINANCIAL INVESTMENTS ACCOUNTED FOR UNDER THE EQUITY METHOD

(€ m)	2016	2015
Pro rata net income for the period	3	-
<b>Total</b>	<b>3</b>	<b>-</b>

Net income from financial investments accounted for under the equity method is disclosed in the segment report as a part of Net income from financial investments. The main net income from financial investments accounted for under the equity method is shown under the Non-Core Bank segment (First Ship Lease Trust).

## 15. LOAN LOSS PROVISIONS IN THE LENDING BUSINESS

### LOAN LOSS PROVISIONS IN THE LENDING BUSINESS

(€ m)	2016	2015
– Expense from additions to loan loss provisions	2,621	3,966
+ Income from the reversal of loan loss provisions	1,178	893
<b>Result from changes in loan loss provisions</b>	<b>- 1,443</b>	<b>- 3,073</b>
– Expenses from allocations to provisions in the lending business	75	36
+ Income from reversals of provisions in the lending business	67	26
<b>Result from changes to provisions in the lending business</b>	<b>- 8</b>	<b>- 10</b>
– Direct write-downs	187	86
+ Payments received on loans and advances previously written down	61	149
<b>Result from other changes to loan loss provisions</b>	<b>- 126</b>	<b>63</b>
<b>Result from changes in loan loss provisions before currency translation gains or losses and compensation</b>	<b>- 1,577</b>	<b>- 3,020</b>
<b>Currency translation gains or losses on loan loss provisions denominated in foreign currency</b>	<b>- 76</b>	<b>- 411</b>
<b>Compensation under the second loss guarantee</b>	<b>2,284</b>	<b>3,077</b>
<b>Total loan loss provisions in the lending business</b>	<b>631</b>	<b>- 354</b>

With regard to the compensation item related to HSH Finanzfonds AöR please refer to Note 3.

Direct write-downs of € 187 million (previous year: € 86 million) relate entirely to Loans and advances to customers.

Loan loss provisions in on-balance-sheet lending business relate exclusively to loans and advances classified as LaR. The following table shows the net changes:

### NET CHANGES IN LOAN LOSS PROVISIONS IN THE LENDING BUSINESS

(€ m)	2016	2015
Specific loan loss provisions	- 1,682	- 2,822
General loan loss provisions	239	- 251
<b>Net change in loan loss provisions in the lending business</b>	<b>- 1,443</b>	<b>- 3,073</b>
Provisions for specific risks	- 16	- 10
Provisions for portfolio risks	8	-
<b>Net change in provisions in the lending business</b>	<b>- 8</b>	<b>- 10</b>

## 16. ADMINISTRATIVE EXPENSES

### ADMINISTRATIVE EXPENSES

(€ m)	2016	2015
Personnel expenses	256	277
Operating expenses	278	302
Depreciation on property, plant and equipment and amortisation on intangible assets	100	55
<b>Total</b>	<b>634</b>	<b>634</b>

### PERSONNEL EXPENSES

(€ m)	2016	2015
Wages and salaries	209	227
Social security contributions	31	33
of which employer contributions to government-sponsored pension plans	15	15
Expenses for pensions and support	16	17
<b>Total</b>	<b>256</b>	<b>277</b>

Please refer to Note 44 for detailed information on expenses for pensions and support as well as expenses for defined contribution plans.

### OPERATING EXPENSES

(€ m)	2016	2015
IT costs	106	108
Costs for external services and project work	62	63
Legal service costs	42	42
Expenses for land and buildings	13	22
Obligatory contributions and expenses related to corporate law	10	9
Costs of advertising, PR and promotional work	6	7
Expenses on plant and equipment	1	1
Other expenses	38	50
<b>Total</b>	<b>278</b>	<b>302</b>

Depreciation on property, plant and equipment and amortisation on intangible assets are broken down as follows:

### DEPRECIATION

(€ m)	2016	2015
Scheduled depreciation on		
Plant and equipment	3	5
Property	3	4
Acquired software	3	7
Software developed in-house	3	6
Leasing assets	20	15
Technical equipment and machinery	2	5
Unscheduled depreciation on		
Property	4	5
Leasing assets	33	8
Technical equipment and machinery	29	–
<b>Total</b>	<b>100</b>	<b>55</b>

Of the scheduled depreciation on property € 1 million (previous year: € 2 million) related to investment property. From unscheduled depreciation on property € 4 million (previous year: € 5 million) related to investment property.

The unscheduled depreciation on real estate, technical equipment and machinery and leasing assets was recognised for assets that form part of a disposal group set up for the first time as at 31 December 2016. Further information in this regard can be found in Note 34.

The total unscheduled depreciations are attributable to the Non-Core Bank segment.

**17. OTHER OPERATING INCOME****OTHER OPERATING INCOME**

(€ m)	2016	2015
Income		
from leasing transactions	41	33
from legal disputes	33	8
from reversal of other provisions and release of liabilities	25	35
from interest on receivables from the tax office	11	-
from investment property (rental income)	5	13
from the reversal of provisions for processing fees in the lending business	2	29
Other income	67	86
<b>Total income</b>	<b>184</b>	<b>204</b>
Expenses		
from additions to other provisions	16	19
for interest expenses pursuant to Section 233 AO	14	-
for investment property	7	8
from the disposal of receivables	-	106
from tax risks	-	23
from the amortisation of goodwill	-	13
Other expenses	67	39
<b>Total expenses</b>	<b>104</b>	<b>208</b>
Income from disposal of property, plant and equipment	1	9
Income/loss arising on the deconsolidation of companies	-23	33
<b>Total</b>	<b>58</b>	<b>38</b>

The item Other operating expenses included expenses from the disposal of receivables in the previous year. These related to receivables in the holding category LaR without any acute default risks. They represent charges from the accelerated winding down of legacy loans from different asset classes (in particular real estate, shipping and energy loans). With regard to the income or loss arising from the deconsolidation of companies please refer to our explanations in Note 6.

**18. EXPENSES FOR BANK LEVY AND DEPOSIT GUARANTEE FUND****EXPENSES FOR BANK LEVY AND DEPOSIT GUARANTEE FUND**

(€ m)	2016	2015
Expenses for European bank levy and deposit guarantee	56	50
<b>Total</b>	<b>56</b>	<b>50</b>

The expenses for the bank levy were recognised in full at the beginning of the year.

The expense for the deposit guarantee of the German Savings Bank Finance Group (Sparkassen Finanzgruppe) is also disclosed under this item. The contribution was levied based on the Deposit Guarantee Act (Einlagensicherungsgesetz).



## 19. NET INCOME FROM RESTRUCTURING AND PRIVATISATION

### NET INCOME FROM RESTRUCTURING AND PRIVATISATION

(€ m)	2016	2015
Personnel expenses due to restructuring	63	1
Operating expenses due to restructuring	52	36
Income from reversals of provisions and liabilities from restructuring	8	6
Expenses from privatisation	3	-
<b>Total</b>	<b>- 110</b>	<b>- 31</b>

The programme for the reduction of operating and personnel expenses initiated in the fourth quarter of 2014 was continued during the 2016 financial year. In particular, expenses were incurred for consultancy in respect of the implementation of defined measures and for IT. In addition, provisions were set up in the first half of 2016 for additional job cuts in the period leading up to 2019. The expenses associated with the privatisation of HSH Nordbank are also reported under net income from restructuring and privatisation. The privatisation expenses consist primarily of one-off expenses for external consultancy and support with the sale process.

## 20. EXPENSES FOR GOVERNMENT GUARANTEES

### EXPENSES FOR GOVERNMENT GUARANTEES

(€ m)	2016	2015
HSH Finanzfonds AöR	214	473
<b>Total</b>	<b>214</b>	<b>473</b>

In June 2013, the guarantee granted by the Federal State of Schleswig-Holstein and the Free and Hanseatic City of Hamburg was replenished to € 10 billion. € 22 million of the one-off payment for the replenishment of the second loss guarantee was recognised on a pro rata temporis basis in the reporting year (previous year: € 69 million). The share of the premium relating to partial guarantee Two (CDS) is disclosed under the line item Hedging effect of the credit derivative in the amount of € 12 million (previous year: € 2 million). The drop in expenses is due to the reorganisation of the guarantee (see Note 3).

## 21. INCOME TAXES

INCOME TAXES		
(€ m)	2016	2015
Corporate tax and solidarity surcharge		
Domestic	20	–
Foreign	–	1
Trade income tax		
Domestic	19	–
<b>Current income taxes</b>	<b>39</b>	<b>1</b>
Income tax from previous years	6	12
<b>Subtotal current income tax</b>	<b>45</b>	<b>13</b>
Income from deferred tax		
from temporary differences	4	254
from losses carried forward	4	91
from consolidation	–1	–6
<b>Subtotal deferred income tax</b>	<b>7</b>	<b>339</b>
<b>Income tax expense (+)/ income (–)</b>	<b>52</b>	<b>352</b>

A write-down of € 64 million of deferred tax assets recognised on temporary differences was required due to the lack of recoverability.

The possibility of using existing tax loss carryforwards is reduced in the future by the formation of the holding company and the expected privatisation. As a result, no deferred tax assets were recognised on tax loss carryforwards.

Deferred taxes on tax loss carryforwards are measured on the basis of a recoverability analysis, which is based on the corporate plan.

RECONCILIATION INCOME TAXES		
(€ m/%)	2016	2015
Group net result	69	98
Income taxes	52	352
Income before taxes incl. income from transfer of losses	121	450
Domestic income tax rate to be applied (in %)	31.67	31.68
<b>Imputed income tax expenses in the financial year</b>	<b>38</b>	<b>143</b>
Tax effects due to		
appreciation/depreciation of deferred taxes on losses carried forward	–67	168
differing effective tax rates in Germany and abroad	–	–16
non-deductible expenses	39	23
corrections to trade taxes	–	–7
changes in tax rate	–	1
Taxes for previous years	6	32
Tax-free income	–5	–14
Appreciation/depreciation of deferred taxes on temporary differences and miscellaneous	41	22
<b>Total tax expense (+)/income (–)</b>	<b>52</b>	<b>352</b>

The tax expense consists primarily of current income taxes for the 2016 financial year and expense resulting from the increase in provisions for tax risks due to changes in the risk assessment as a result of findings from the ongoing tax audit. The change in income tax expense for previous years largely comprises income from the reversal of tax loan loss provisions at head office (€ 22 million) and the expense associated with the recognition of a risk provision for taxes at a consolidated subsidiary (€ –28 million).

In calculating taxes for 2016, a rate of 31.67% (previous year: 31.68%) was used for domestic taxes.

Other material effects result from non-deductible expenses, tax-free income, the use of loss carryforwards that had not previously been valued at head office and with regard to the Luxembourg branch, and the write-down of deferred taxes on temporary differences due to a lack of recoverability.

## 22. NET GAINS AND LOSSES FROM FINANCIAL INSTRUMENTS

Net gains and losses from financial instruments include both realised gains and measurement gains within Net trading income and Net income from financial investments, the hedging effect of the credit derivative under the second loss guarantee as well as loan loss provisions with regard to credit business shown on the statement of financial position, broken down into IAS 39 categories. Neither Net interest nor Net commission income is included in this item.

Derecognition of the fair value changes cumulated in equity associated with value adjustments and sales of financial instruments categorised as AfS is shown in Note 50.

### NET GAINS AND LOSSES FROM FINANCIAL INSTRUMENTS

(€ m)	2016	2015
DFV	91	-21
AfS	25	14
LaR	754	-304
HfT	-478	763
<b>Total</b>	<b>392</b>	<b>452</b>

## 23. EARNINGS PER SHARE

For the calculation of Earnings per share, the Group net result attributable to HSH Nordbank shareholders is divided by the weighted average number of ordinary shares outstanding during the year under review. As in the previous year, HSH Nordbank AG has not issued any diluted forms of capital as at 31 December 2016, i.e. the diluted and undiluted earnings are the same. The calculation was based on non-rounded values.

### EARNINGS PER SHARE

	2016	2015
Attributable Group net result (€ m) – undiluted/diluted	67	99
<b>Number of shares (millions)</b>		
Average number of ordinary shares outstanding – undiluted/diluted	302	302
<b>Earnings per share (€)</b>		
Undiluted	0.22	0.33
Diluted	0.22	0.33

## NOTES ON THE GROUP STATEMENT OF FINANCIAL POSITION

### 24. CASH RESERVE

CASH RESERVE		
(€ m)	2016	2015
Cash on hand	5	6
Balances at central banks	3,368	2,693
of which at the Deutsche Bundesbank	3,342	2,668
Treasury bills, discounted treasury notes and similar debt instruments issued by public-sector institutions	118	695
of which eligible for refinancing at the Deutsche Bundesbank	–	410
<b>Total</b>	<b>3,491</b>	<b>3,394</b>

### 25. LOANS AND ADVANCES TO BANKS

LOANS AND ADVANCES TO BANKS						
(€ m)	2016			2015		
	Domestic	Foreign	Total	Domestic	Foreign	Total
Payable on demand	694	2,257	2,951	760	2,729	3,489
Other loans and advances	1,164	77	1,241	1,966	140	2,106
<b>Total before loan loss provisions</b>	<b>1,858</b>	<b>2,334</b>	<b>4,192</b>	<b>2,726</b>	<b>2,869</b>	<b>5,595</b>
Loan loss provisions	–	1	1	–	15	15
<b>Total after loan loss provisions</b>	<b>1,858</b>	<b>2,333</b>	<b>4,191</b>	<b>2,726</b>	<b>2,854</b>	<b>5,580</b>

€ 245 million (previous year: € 809 million) of Loans and advances to banks have a residual maturity of more than one year.

Loans and advances to banks include money market transactions in the amount of € 3,268 million (previous year: € 3,612 million).

Information on collateral transferred which also contains information regarding securities lending and repurchase agreements can be found in Note 64.



## 26. LOANS AND ADVANCES TO CUSTOMERS

### LOANS AND ADVANCES TO CUSTOMERS

(€ m)	2016			2015		
	Domestic	Foreign	Total	Domestic	Foreign	Total
Retail customers	963	38	1,001	1,273	141	1,414
Corporate clients	22,802	22,103	44,905	23,694	26,040	49,734
Public authorities	4,530	474	5,004	4,800	627	5,427
<b>Total before loan loss provisions</b>	<b>28,295</b>	<b>22,615</b>	<b>50,910</b>	<b>29,767</b>	<b>26,808</b>	<b>56,575</b>
Loan loss provisions	3,321	3,157	6,478	2,889	2,921	5,810
<b>Total after loan loss provisions</b>	<b>24,974</b>	<b>19,458</b>	<b>44,432</b>	<b>26,878</b>	<b>23,887</b>	<b>50,765</b>

Of Loans and advances to customers, holdings of € 31,119 million (previous year: € 35,598 million) have a residual maturity of more than one year.

Loans and advances to customers include money market transactions in the amount of € 1,508 million (previous year: € 1,313 million).

Loans and advances to customers include receivables under finance lease transactions in the amount of € 98 million (previous year: € 106 million). The gross investment value of the leasing transactions is € 105 million (previous year: € 113 million). Further details on leasing transactions can be found in Note 63.

Information on collateral transferred which also contains information regarding securities lending and repurchase agreements can be found in Note 64.

## 27. LOAN LOSS PROVISIONS

### LOAN LOSS PROVISIONS

(€ m)	2016	2015
Loan loss provisions for loans and advances to banks	1	15
Loan loss provisions for loans and advances to customers and non-current assets held for sale and disposal groups	6,711	8,212
<b>Loan loss provisions in the lending business</b>	<b>6,712</b>	<b>8,227</b>
Compensation under the second loss guarantee	-7,854	-7,162
<b>Loan loss provisions for items in the statement of financial position</b>	<b>- 1,142</b>	<b>1,065</b>
Provisions in the lending business	110	107
<b>Loan loss provisions for items in the statement of financial position and off-balance-sheet risk in the lending business</b>	<b>- 1,032</b>	<b>1,172</b>

The individual and general loan loss provisions are determined at first without taking the hedging effect of the guarantee received into account. The hedging effect is then mapped in the statement of financial position through the recognition of a compensation item, which directly reduces loan loss provisions (see Note 3). Impairment losses of € 233 million (previous year: € 2,402 million) are attributable to the Non-current assets held for sale line and disposal groups item in the statement of financial position. In the previous year, € 2,400 million related to the portfolio sold to the resolution institution.

The portfolio which was to be sold on the market at a later date accounted for a further € 730 million in the previous year.

The expected fair values or transfer values are taken into account for determining loan loss provisions of the market portfolio.

The development of loan loss provisions for banks during the period under review was as follows:

### DEVELOPMENT OF LOAN LOSS PROVISIONS FOR LOANS AND ADVANCES TO BANKS BEFORE COMPENSATION

(€ m)	Specific loan loss provisions		General loan loss provisions		Total	
	2016	2015	2016	2015	2016	2015
<b>As at 1 January</b>	<b>14</b>	<b>14</b>	<b>1</b>	<b>1</b>	<b>15</b>	<b>15</b>
Additions	-	-	-	1	-	1
Reversals	-	-	-	1	-	1
Utilisation	14	-	-	-	14	-
<b>As at 31 December</b>	<b>-</b>	<b>14</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>15</b>

Loan loss provisions for customers during the period under review developed as follows:

**DEVELOPMENT OF LOAN LOSS PROVISIONS FOR LOANS AND ADVANCES TO CUSTOMER AND NON-CURRENT ASSETS HELD FOR SALE AND DISPOSAL GROUPS BEFORE COMPENSATION**

(€ m)	Specific loan loss provisions		General loan loss provisions		Total	
	2016	2015	2016	2015	2016	2015
<b>As at 1 January</b>	<b>7,601</b>	<b>5,777</b>	<b>611</b>	<b>343</b>	<b>8,212</b>	<b>6,120</b>
Additions	2,590	3,714	31	251	2,621	3,965
Reversals	908	892	270	-	1,178	892
Utilisation	2,864	1,269	-	-	2,864	1,269
Other changes	-7	-	-	-	-7	-
Unwinding	-162	-207	-	-	-162	-207
Changes in the scope of consolidation	6	60	-	-	6	60
Exchange rate changes	80	418	3	17	83	435
<b>As at 31 December</b>	<b>6,336</b>	<b>7,601</b>	<b>375</b>	<b>611</b>	<b>6,711</b>	<b>8,212</b>

The other changes are attributable to the extension of the scope of consolidation due to the initial consolidation of a subsidiary that was previously considered immaterial (see Note 6).

The loan loss provisions relate exclusively to items categorised as loans and receivables (LaR). The total volume of loans impaired amounts to € 10,541 million (previous year: € 15,766 million), of which € 856 million relate to receivables disclosed under the line item Non-current assets held for sale and disposal groups.

## 28. POSITIVE FAIR VALUES OF HEDGING DERIVATIVES

The positive fair value of derivatives used in hedge accounting is accounted for in this item. Only interest rate and cross currency interest rate swaps are taken into account as hedging instruments currently. If a derivative is only partially designated under hedge accounting, this item contains the corresponding share of that derivative's fair value. In these cases, the remainder is stated under Trading assets. Hedge accounting is used solely for interest rate risks.

### POSITIVE FAIR VALUES OF HEDGING DERIVATIVES

(€ m)	2016	2015
Positive fair value of derivatives used in micro fair value hedges	–	52
Positive fair value of derivatives used in portfolio fair value hedges	508	731
<b>Total</b>	<b>508</b>	<b>783</b>

Of hedging derivatives, holdings of € 477 million (previous year: € 762 million) have a residual maturity of more than one year.

Changes in this item are directly related to changes in the item Negative fair value of the hedging derivatives. The overall changes in this item are mainly due to changes in the portfolio compositions and movements in interest rates in the euro and US dollar capital markets.



## 29. TRADING ASSETS

Only financial assets classified as HfT are stated under Trading assets. Mainly included in this category are original financial instruments held for trading purposes, including accrued interest, and derivatives with a positive fair value which are either not designated as a hedge derivative or are used as hedging instruments but do not meet the requirements of IAS 39 for hedge accounting.

Trading assets of € 4,930 million (previous year: € 6,962 million) have a residual maturity of more than one year.

Information on collateral transferred which also contains information regarding securities lending and repurchase agreements can be found in Note 64.

### TRADING ASSETS

(€ m)	2016	2015
Bonds and debentures		
from public-sector issuers	277	1,264
negotiable and listed	277	1,264
from other issuers	181	488
negotiable and listed	142	454
negotiable and not listed	39	34
<b>Debentures and other fixed-interest securities</b>	<b>458</b>	<b>1,752</b>
Positive fair value of financial derivatives		
Interest rate-related transactions	4,340	4,731
currency-related business	137	238
other business	466	612
<b>Positive fair value of financial derivatives</b>	<b>4,943</b>	<b>5,581</b>
Other, including promissory notes held for trading	23	23
Receivables from syndication transactions	9	–
<b>Total</b>	<b>5,433</b>	<b>7,356</b>

### 30. FINANCIAL INVESTMENTS

Disclosed as financial investments are, specifically, financial instruments not held for trading purposes classified as AfS and LaR and, to a lesser extent, as DFV. This item includes bonds and other fixed-interest securities, equities and other non-fixed-interest securities, holdings in unconsolidated affiliated companies, holdings in joint ventures and associates not carried at equity in the Group financial statements.

#### FINANCIAL INVESTMENTS

(€ m)	2016	2015
Debentures and other fixed-interest securities	15,203	16,216
negotiable and listed	13,946	14,513
negotiable and not listed	1,257	1,703
Shares and other non-fixed-interest securities	170	296
negotiable and listed	6	9
negotiable and not listed	37	145
Equity holdings in non-affiliated companies	119	124
negotiable and listed	43	40
negotiable and not listed	5	7
Interests in affiliated companies	1	-
negotiable and listed	-	-
negotiable and not listed	-	-
<b>Total</b>	<b>15,493</b>	<b>16,636</b>

Financial investments of € 14,119 million (previous year: € 15,114 million) have a residual maturity of more than one year.

Write-downs on debentures and other fixed-interest securities amount to € 162 million (previous year: € 360 million), on shares and other non-fixed-interest securities they amount to € 18 million as at the reporting date (previous year: € 14 million).

General loan loss provisions amount to € 7 million (previous year: € 10 million).

Changes in specific and general loan loss provisions are recognised in Net income from financial investments.

This portfolio also contains shares and other non-fixed-interest securities measured at cost of € 125 million (previous year: € 137 million). Equity capital instruments accounted for at cost that relate to interests in affiliated companies and equity holdings in non-affiliated companies amount to € 78 million (previous year: € 75 million). There are currently no concrete disposal plans for these equity instruments.

Information on collateral transferred which also contains information regarding securities lending and repurchase agreements can be found in Note 64.

Developments with regard to equity holdings and interests in affiliated companies are presented below:

#### DEVELOPMENT IN EQUITY HOLDINGS AND INTERESTS IN AFFILIATED COMPANIES

(€ m)	Equity holdings in non-affiliated companies	Interests in affiliated companies	Total
<b>2016</b>			
<b>Acquisition costs as at 1 January 2016</b>	<b>245</b>	<b>2</b>	<b>247</b>
Additions	15	1	16
Disposals	11	-	11
Reclassifications	-26	-	-26
Exchange rate changes	-	-	-
Changes in the scope of consolidation	-	-	-
<b>As at 31 December 2016</b>	<b>223</b>	<b>3</b>	<b>226</b>
<b>Amortisation as at 1 January 2016</b>	<b>121</b>	<b>2</b>	<b>123</b>
Additions	11	-	11
Disposals	-	-	-
Reclassifications	-8	-	-8
Change in measurement recognised directly in equity	-20	-	-20
Exchange rate changes	-	-	-
<b>As at 31 December 2016</b>	<b>104</b>	<b>2</b>	<b>106</b>
<b>Carrying amount as at 31 December 2016</b>	<b>119</b>	<b>1</b>	<b>120</b>
<b>Carrying amount as at 1 January 2016</b>	<b>124</b>	<b>-</b>	<b>124</b>

#### DEVELOPMENT IN EQUITY HOLDINGS AND INTERESTS IN AFFILIATED COMPANIES

(€ m)	Equity holdings in non-affiliated companies	Interests in affiliated companies	Total
2015			
<b>Acquisition costs as at 1 January 2015</b>	<b>259</b>	<b>3</b>	<b>262</b>
Additions	10	-	10
Disposals	24	-	24
Reclassifications	-	-	-
Exchange rate changes	-	-	-
Changes in the scope of consolidation	-	-1	-1
<b>As at 31 December 2015</b>	<b>245</b>	<b>2</b>	<b>247</b>
<b>Amortisation as at 1 January 2015</b>	<b>95</b>	<b>2</b>	<b>97</b>
Additions	44	-	44
Disposals	9	-	9
Reclassifications	-	-	-
Change in measurement recognised directly in equity	-9	-	-9
Exchange rate changes	-	-	-
<b>As at 31 December 2015</b>	<b>121</b>	<b>2</b>	<b>123</b>
<b>Carrying amount as at 31 December 2015</b>	<b>124</b>	<b>-</b>	<b>124</b>
<b>Carrying amount as at 1 January 2015</b>	<b>164</b>	<b>1</b>	<b>165</b>

### 31. FINANCIAL INVESTMENTS ACCOUNTED FOR UNDER THE EQUITY METHOD

Shares in associates and joint ventures included in the Group financial statements under the equity method are disclosed in this line item.

As at the reporting date, 31 December 2016, the HSH Nordbank Group owns shares in one associate and one joint venture that are included in the Group financial statements under the equity method (previous year: one associate and one joint venture). The carrying amount of these equity holdings was € 13 million as at 31 December 2016 (previous year: € 2 million).

An overview of and detailed information on the associates and joint ventures included in the Group financial statements are set out in Note 6. Net income from financial investments accounted for under the equity method is disclosed in Note 14.

Please see Note 30 for a summary of financial information related to financial investments not accounted for under the equity method.

### 32. INTANGIBLE ASSETS

The Intangible assets item comprises software developed in-house or acquired.

#### INTANGIBLE ASSETS

(€ m)	2016	2015
Software	12	16
developed in-house	5	8
acquired	7	8
Software in development	2	-
acquired	2	-
<b>Total</b>	<b>14</b>	<b>16</b>



Changes in the carrying amounts of intangible assets are shown below:

#### DEVELOPMENT IN INTANGIBLE ASSETS

(€ m)	Software			Software in development		Total
	Goodwill	Software developed in-house	Acquired software	Software developed in-house	Acquired software	
<b>2016</b>						
<b>Acquisition costs as at 1 January 2016</b>	<b>190</b>	<b>98</b>	<b>170</b>	-	-	<b>458</b>
Additions	-	-	2	-	2	4
Disposals	-	-	-	-	-	-
Reclassifications	-	-	-	-	-	-
Changes in the scope of consolidation	-	-	-	-	-	-
<b>As at 31 December 2016</b>	<b>190</b>	<b>98</b>	<b>172</b>	-	<b>2</b>	<b>462</b>
<b>Amortisation as at 1 January 2016</b>	<b>190</b>	<b>90</b>	<b>162</b>	-	-	<b>442</b>
Additions	-	3	3	-	-	6
Disposals	-	-	-	-	-	-
Reclassifications	-	-	-	-	-	-
Changes in the scope of consolidation	-	-	-	-	-	-
<b>As at 31 December 2016</b>	<b>190</b>	<b>93</b>	<b>165</b>	-	-	<b>448</b>
<b>Carrying amount as at 31 December 2016</b>	-	<b>5</b>	<b>7</b>	-	<b>2</b>	<b>14</b>
<b>Carrying amount as at 1 January 2016</b>	-	<b>8</b>	<b>8</b>	-	-	<b>16</b>

#### DEVELOPMENT IN INTANGIBLE ASSETS

(€ m)	Software			Software in development		Total
	Goodwill	Software developed in-house	Acquired software	Software developed in-house	Acquired software	
2015						
<b>Acquisition costs as at 1 January 2015</b>	<b>217</b>	<b>98</b>	<b>170</b>	-	<b>1</b>	<b>486</b>
Additions	13	-	2	-	-	15
Disposals	-	-	3	-	-	3
Reclassifications	-	-	1	-	-1	-
Changes in the scope of consolidation	-40	-	-	-	-	-40
<b>As at 31 December 2015</b>	<b>190</b>	<b>98</b>	<b>170</b>	-	-	<b>458</b>
<b>Amortisation as at 1 January 2015</b>	<b>217</b>	<b>84</b>	<b>158</b>	-	-	<b>459</b>
Additions	13	6	7	-	-	26
Disposals	-	-	3	-	-	3
Reclassifications	-	-	-	-	-	-
Changes in the scope of consolidation	-40	-	-	-	-	-40
<b>As at 31 December 2015</b>	<b>190</b>	<b>90</b>	<b>162</b>	-	-	<b>442</b>
<b>Carrying amount as at 31 December 2015</b>	-	<b>8</b>	<b>8</b>	-	-	<b>16</b>
<b>Carrying amount as at 1 January 2015</b>	-	<b>14</b>	<b>12</b>	-	<b>1</b>	<b>27</b>

As in the previous year, no research costs were incurred in the year under review in connection with the implementation of software developed in-house.

**33. PROPERTY, PLANT AND EQUIPMENT AND INVESTMENT PROPERTY****PROPERTY, PLANT AND EQUIPMENT**

(€ m)	2016	2015
Land and buildings	222	213
Plant and equipment	13	13
Leasing assets	-	163
Assets under construction	1	7
Technical equipment and machinery	-	78
<b>Total</b>	<b>236</b>	<b>474</b>

Further details on the existing leasing business can be found in Note 63.

Under the item Investment property all property (land or buildings) is recorded that is held to earn rent or for capital appreciation but is not used in the production or supply of goods or services of the Bank.

**INVESTMENT PROPERTY**

(€ m)	2016	2015
Investment property	12	64
<b>Total</b>	<b>12</b>	<b>64</b>

The fair value of investment property amounts to € 12 million (previous year: € 64 million). The fair values of investment property are allocated without exception to level 3 of the fair value hierarchy. Market-based and income-based valuation techniques are used to determine fair value.

The development in Property, plant and equipment and Investment property in the financial year was as follows:

#### DEVELOPMENT IN PROPERTY, PLANT AND EQUIPMENT AND INVESTMENT PROPERTIES

(€ m)	Land and buildings	Plant and equipment	Assets under construction	Investment property	Leasing assets	Technical equipment and machinery
<b>2016</b>						
<b>Acquisition costs as at 1 January 2016</b>	<b>222</b>	<b>63</b>	<b>7</b>	<b>106</b>	<b>325</b>	<b>148</b>
Additions	6	2	-	-	9	1
Disposals	-	2	-	4	78	-
Other changes	-	-	-	-	77	-
Reclassifications	5	1	-6	-57	-344	-152
Exchange rate changes	-	-	-	-	11	3
Changes in the scope of consolidation	-	-	-	-31	-	-
<b>As at 31 December 2016</b>	<b>233</b>	<b>64</b>	<b>1</b>	<b>14</b>	<b>-</b>	<b>-</b>
<b>Amortisation as at 1 January 2016</b>	<b>9</b>	<b>50</b>	<b>-</b>	<b>42</b>	<b>162</b>	<b>70</b>
Additions	2	3	-	5	53	31
Disposals	-	2	-	2	39	-
Other changes	-	-	-	-	23	-
Reclassifications	-	-	-	-22	-206	-104
Exchange rate changes	-	-	-	-	7	3
Changes in the scope of consolidation	-	-	-	-21	-	-
<b>As at 31 December 2016</b>	<b>11</b>	<b>51</b>	<b>-</b>	<b>2</b>	<b>-</b>	<b>-</b>
<b>Carrying amount as at 31 December 2016</b>	<b>222</b>	<b>13</b>	<b>1</b>	<b>12</b>	<b>-</b>	<b>-</b>
<b>Carrying amount as at 1 January 2016</b>	<b>213</b>	<b>13</b>	<b>7</b>	<b>64</b>	<b>163</b>	<b>78</b>

The other changes are attributable to the extension of the scope of consolidation due to the initial consolidation of a subsidiary that was previously considered immaterial (see Note 6).

Some items reported under assets under construction were reclassified as land and buildings and as plant and equipment.

There were also reclassifications made from tangible assets to Non-current assets held for sale in the reporting year. A total carrying amount of € 48 million was reclassified from technical equipment and machinery, with a total amount of € 138 million being reclassified from leasing assets.

A total carrying amount of € 35 million was also transferred from Investment Properties to Non-current assets held for sale.

The line item Investment property, under Changes in scope of consolidation, only includes disposals from the scope of consolidation.

Further details on depreciation are presented in Note 16.

**DEVELOPMENT IN PROPERTY, PLANT AND EQUIPMENT AND INVESTMENT PROPERTY**

(€ m)	Land and buildings	Plant and equipment	Assets under construction	Investment property	Leasing assets	Technical equipment and machinery
2015						
<b>Acquisition costs as at 1 January 2015</b>	<b>84</b>	<b>141</b>	<b>3</b>	<b>263</b>	<b>370</b>	<b>71</b>
Additions	-	4	6	3	-	-
Disposals	-	16	-	17	-	-
Reclassifications	-	-66	-2	-	-79	68
Exchange rate changes	-	-	-	1	34	9
Changes in the scope of consolidation	138	-	-	-144	-	-
<b>As at 31 December 2015</b>	<b>222</b>	<b>63</b>	<b>7</b>	<b>106</b>	<b>325</b>	<b>148</b>
<b>Amortisation as at 1 January 2015</b>	<b>7</b>	<b>86</b>	<b>-</b>	<b>78</b>	<b>143</b>	<b>34</b>
Additions	2	5	-	7	23	5
Disposals	-	14	-	1	-	-
Reclassifications	-	-27	-	-	-18	27
Write-ups	-	-	-	1	-	-
Exchange rate changes	-	-	-	-	14	4
Changes in the scope of consolidation	-	-	-	-41	-	-
<b>As at 31 December 2015</b>	<b>9</b>	<b>50</b>	<b>-</b>	<b>42</b>	<b>162</b>	<b>70</b>
<b>Carrying amount as at 31 December 2015</b>	<b>213</b>	<b>13</b>	<b>7</b>	<b>64</b>	<b>163</b>	<b>78</b>
<b>Carrying amount as at 1 January 2015</b>	<b>77</b>	<b>55</b>	<b>3</b>	<b>185</b>	<b>227</b>	<b>37</b>

Changes in the scope of consolidation for land and buildings only include additions due to business combinations.

The line item Investment property only includes disposals from the scope of consolidation.



### 34. NON-CURRENT ASSETS HELD FOR SALE AND DISPOSAL GROUPS

#### NON-CURRENT ASSETS HELD FOR SALE AND DISPOSAL GROUPS

(€ m)	2016	2015
Loans and advances to banks	2	–
Loans and advances to customers	1,133	5,081
Financial investments	18	–
Property, plant and equipment	186	–
Investment property	34	1
Other assets	9	–
<b>Total before loan loss provisions</b>	<b>1,382</b>	<b>5,082</b>
Loan loss provisions	233	2,402
<b>Total after loan loss provisions</b>	<b>1,149</b>	<b>2,680</b>

As at 31 December 2016, this item largely includes assets that will be sold on the market as part of the implementation of the EU decision of 2 May 2016 (market portfolio). The market portfolio includes loans and advances to customers in the LaR category in the amount of € 1,133 million, for which loan loss provisions in the amount of € 233 million have been set up (see Note 27).

The market portfolio transaction also includes loan receivables in the amount of € 419 million from 14 fully consolidated subsidiaries (largely special purpose companies). The Group financial statements of HSH Nordbank recognise the assets and liabilities of these subsidiaries. The loan receivables to be sold are not reported in the Group financial statements as intra-Group obligations. In respect of nine of the fully consolidated subsidiaries, the sale of the loan receivable will result in a loss of control by HSH Nordbank pursuant to IFRS 10. This means that all assets and liabilities of these nine fully consolidated subsidiaries form part of disposal groups held for sale. With regard to five other subsidiaries, while the implementation of the transaction will not lead to a loss of control by HSH Nordbank, certain assets and liabilities of these five subsidiaries are also to be transferred to the buyer of the loan receivable in connection with the sale of the loan receivable. This means that tangible assets and other assets held by these subsidiaries, and provisions reported by these companies, are also held for sale.

The market portfolio consists of the non-strategic sub-portfolios Aviation, Continental European Commercial Real Estate, Energy and International Real Estate, which are to be allocated in full to the Non-Core Bank segment. The last three sub-portfolios mentioned above each constitute a disposal group pursuant to IFRS 5, because the assets and liabilities will be sold to a buyer in one sale transaction each. Within the Aviation sub-portfolio, there are two disposal groups (Aviation I and Aviation II) pursuant to IFRS 5, because although the buyer is identical, the sale takes place in different transactions.

The transaction for the Continental European Commercial Real Estate sub-portfolio was closed in March 2017. The purchase agreements for the Aviation sub-portfolio were signed in January 2017. The transactions are expected to be closed in the second/third quarter of 2017. Sale negotiations regarding the Energy and International Real Estate sub-portfolios are at an advanced stage.

The Aviation I disposal group consists of loans and advances to customers in the LaR category. The Aviation II disposal group includes intra-Group receivables from six consolidated subsidiaries, meaning that this disposal group contains tangible assets and provisions in particular.

The Continental European Commercial Real Estate disposal group largely consists of loans and advances to customers in the LaR category. It also contains the assets and liabilities of six consolidated subsidiaries over which HSH Nordbank will lose control pursuant to IFRS 10. This means that investment property will also be removed from the Group statement of financial position, along with the loans and advances to customers held for sale.

The Energy disposal group contains loans and advances to customers in the LaR category, as well as intra-Group receivables from two consolidated subsidiaries, meaning that this disposal group includes tangible assets, in particular.

The International Real Estate disposal group consists exclusively of loans and advances to customers in the LaR category.

Over and above the market portfolio, this item includes an equity holding of € 18 million that is attributable to the Other and Consolidation segment. The equity holding will be sold in the first quarter of 2017. The change in fair value recognised directly in equity in other comprehensive income as at 31 December 2016 will be realised through profit or loss at the time of the sale.

After the reporting date, shares in a joint venture consolidated under the equity method fulfilled the requirements for being classified as held for sale. The shares in the joint venture are allocated to the Core Bank segment and are highly likely to be sold in the second quarter of 2017.

The loans and advances to customers and investment property reported under this item as at 31 December 2015 were sold in the reporting period. This includes the sale of loans and advances to customers in the amount of € 5,011 million to the resolution institution (hsh portfoliomanagement AöR) formed by the federal states of Hamburg and Schleswig-Holstein as at 30 June 2016. A further part of the loans and advances to customers was sold as part of a disposal group.

This disposal group contained liabilities to customers with a carrying amount of € 1 million.

The shares in the associate Relacom Management AB that were reclassified in accordance with IFRS 5 in the 2015 financial year were sold in full as at 19 December 2016.

### 35. CURRENT TAX ASSETS

#### CURRENT TAX ASSETS

(€ m)	2016	2015
Domestic	60	71
Foreign	5	8
<b>Total</b>	<b>65</b>	<b>79</b>

### 36. DEFERRED TAX ASSETS

Deferred tax assets arose due to temporary differences in the tax base of the following items in the statement of financial position and tax losses carried forward:

#### DEFERRED TAX ASSETS

(€ m)	2016	2015
<b>Assets</b>		
Loans and advances to banks	16	16
Loan loss provisions	330	707
Trading assets	–	81
Financial investments	12	7
Intangible assets	4	3
Other assets	86	54
<b>Liabilities</b>		
Liabilities to customers	15	48
Securitised liabilities	60	80
Negative fair value of hedging derivatives	88	227
Liabilities-side adjustment item from portfolio fair value hedge	239	273
Trading liabilities	240	89
Provisions	300	304
Other liabilities	274	235
Tax losses carried forward	100	99
<b>Subtotal for deferred tax assets</b>	<b>1,764</b>	<b>2,223</b>
of which long-term	205	176
Netting of deferred tax liabilities	–997	–1,475
<b>Total</b>	<b>767</b>	<b>748</b>

Out of the deferred tax assets after offsetting, € 757 million is attributable to Germany and € 10 million to abroad.

Deferred tax assets on loss carryforwards were recognised in the amount of € 100 million (previous year: € 99 million). As at 31 December 2016, these are attributable to the Singapore branch in the amount of € 5 million (previous year: € 0 million), to the former New York branch in the amount of € 90 million (previous year: € 99 million) and to consolidated subsidiaries in the amount of € 5 million (previous year: € 0 million). For the Singapore branch, the recoverability of the deferred taxes on loss carryforwards results from planned future income. The deferred tax assets on loss carryforwards relating to the former New York branch and consolidated subsidiaries are offset by deferred tax liabilities recognised on temporary differences.

There were unused tax loss carryforwards of € 6,143 million as at the reporting date (previous year: € 7,308 million) for which no deferred tax assets were recognised.

The decrease of € 459 million in deferred tax assets is mainly attributable to the sale of the federal state portfolio and to changes in measurement differences for securitised liabilities, the negative market values of hedging derivatives and the negative adjustment item from portfolio fair value hedges.

The recoverability of deferred tax assets results from positive future net income, in particular due to the fact that the Bank has been relieved of guarantee premiums. Deferred tax assets were not recognised on temporary differences of € 201 million due to the lack of recoverability.

€ 28 million of the addition to deferred tax assets relates to deferred taxes for pension obligations recognised directly in equity.

The difference between the valuation for tax purposes of hybrid financial instruments (Note 8.I.E) and the measurement of such instruments under IAS 39.A8 results in deferred tax assets of € 15 million (previous year: € 5 million).

**37. OTHER ASSETS**

<b>OTHER ASSETS</b>		
(€ m)	<b>2016</b>	2015
Receivables from insurance contracts	27	25
Unamortised balance of the one-off payment to HSH Finanzfonds AöR for the replenishment of the guarantee	-	22
Other prepaid expenses	18	9
Receivables from other taxes	7	5
Receivables from fund transactions	7	4
Other assets	46	98
<b>Total</b>	<b>105</b>	<b>163</b>

Other assets in the amount of € 9 million (previous year: € 2 million) have a residual maturity of more than one year.

€ 50 million of the assets reported here relate to financial instruments (previous year: € 86 million).

### 38. LIABILITIES TO BANKS

#### LIABILITIES TO BANKS

(€ m)	2016			2015		
	Domestic	Foreign	Total	Domestic	Foreign	Total
Payable on demand	1,373	170	1,543	623	193	816
Other term liabilities	5,572	2,386	7,958	10,269	3,313	13,582
<b>Total</b>	<b>6,945</b>	<b>2,556</b>	<b>9,501</b>	<b>10,892</b>	<b>3,506</b>	<b>14,398</b>

Liabilities to banks of € 4,976 million (previous year: € 5,776 million) have a residual maturity of more than one year.

The difference between the carrying amount of the liabilities categorized as DFV and their par value, which corresponds to the contractu-

ally agreed repayment amount at the due date, amounted as at 31 December 2016 to € - 5 million (previous year: € - 12 million).

Information on collateral transferred which also contains information regarding securities lending and repurchase agreements can be found in Note 64.

### 39. LIABILITIES TO CUSTOMERS

#### LIABILITIES TO CUSTOMERS BY CUSTOMER GROUP

(€ m)	2016	2015
Corporate clients	26,292	30,836
Public authorities	12,035	11,825
Retail customers	1,845	1,906
<b>Total</b>	<b>40,172</b>	<b>44,567</b>

#### LIABILITIES TO CUSTOMERS

(€ m)	2016			2015		
	Domestic	Foreign	Total	Domestic	Foreign	Total
Savings deposits with agreed notice periods of						
3 months	18	-	18	21	1	22
Other liabilities						
Payable on demand	10,709	1,562	12,271	14,960	2,064	17,024
Term liabilities	25,442	2,441	27,883	24,720	2,801	27,521
<b>Total</b>	<b>36,169</b>	<b>4,003</b>	<b>40,172</b>	<b>39,701</b>	<b>4,866</b>	<b>44,567</b>

Liabilities to customers of € 10,904 million (previous year: € 10,427 million) have a residual maturity of more than one year.

The difference between the carrying amount of the liabilities categorized as DFV and their par value, which corresponds to the contractu-

ally agreed repayment amount at the due date, amounted as at 31 December 2016 to € - 113 million (previous year: € - 160 million).

Information on collateral transferred which also contains information regarding securities lending and repurchase agreements can be found in Note 64.



#### 40. SECURITISED LIABILITIES

##### SECURITISED LIABILITIES

(€ m)	2016	2015
Debentures issued	16,555	18,596
Money market securities issued	69	20
<b>Total</b>	<b>16,624</b>	<b>18,616</b>

Securitized liabilities of € 13,104 million (previous year: € 15,172 million) have a residual maturity of more than one year.

Debentures issued include € 660 million of hybrid financial instruments (previous year: € 606 million). The carrying amount of these hybrid financial instruments was determined based on assumptions (see Note 8.I.E).

In the item Securitized liabilities repurchased own debentures in the amount of € 2,643 million (previous year: € 4,018 million) were deducted.

The difference between the carrying amount of Securitized liabilities categorised as DFV and their par value, which corresponds to the contractually agreed repayment amount at the due date, amounted to € -165 million at 31 December 2016 (previous year: € -175 million).

#### 41. NEGATIVE FAIR VALUE OF HEDGING DERIVATIVES

This item shows the negative fair value of derivatives used in hedge accounting. Only interest rate and interest rate currency swaps are currently taken into account as hedging instruments. If a derivative is only partially designated under hedge accounting, this item contains the corresponding share of that derivative's fair value. The remainder is stated under Trading liabilities. Hedge accounting is used solely for interest rate risks.

##### NEGATIVE FAIR VALUE OF HEDGING DERIVATIVES

(€ m)	2016	2015
Negative fair value of derivatives used in micro fair value hedges	-	105
Negative fair value of derivatives used in portfolio fair value hedges	290	622
<b>Total</b>	<b>290</b>	<b>727</b>

Under the item Negative fair value of hedging derivatives portfolios in an amount of € 285 million (previous year: € 710 million) have a residual maturity of more than one year.

Changes in this item are directly related to changes in the item Positive fair value of the hedging derivatives (see Note 28). The overall changes in this item are mainly due to changes in the portfolio compositions and movements in interest rates in the euro and US dollar capital markets.

## 42. TRADING LIABILITIES

Only financial liabilities classified as HfT are disclosed under Trading liabilities. Mainly included in this category are derivatives with a negative fair value which are either not designated as a hedging derivative or are used as hedging instruments but do not meet the requirements of IAS 39 for hedge accounting.

Trading liabilities of € 5,391 million (previous year: € 6,280 million) have a residual maturity of more than one year.

Information on collateral transferred is presented in Note 64.

### TRADING LIABILITIES

(€ m)	2016	2015
Negative fair value from derivative financial instruments		
Interest rate-related business	5,152	5,998
Currency-related business	191	164
Other business	638	596
<b>Total</b>	<b>5,981</b>	<b>6,758</b>

## 43. PROVISIONS

### PROVISIONS

(€ m)	2016	2015
Provisions for pension obligations and similar obligations	1,152	1,051
Other provisions		
Provisions for personnel expenses	39	43
Provisions in the lending business	110	107
Provisions for restructuring	85	94
Provisions for litigation risks and costs	34	37
Other provisions	101	185
<b>Total</b>	<b>1,521</b>	<b>1,517</b>

Provisions of € 1,249 million (previous year: € 1,221 million) have a residual maturity of more than one year.

Provisions with a maturity of less than one year mainly relate to Provisions for restructuring, Provisions in the lending business as well as provisions for litigation risks. Further information regarding Provisions in the lending business can be found in Note 27.

Provisions for restructuring in the amount of € 54 million (previous year: € 54 million) related to personnel expenses and € 31 million (previous year: € 41 million) to operating expenses.

Other provisions mainly include interest on tax liabilities, provisions for potential legal risks and onerous contracts as well as an expected back payment from the tax audit.

There are uncertainties particularly with respect to provisions in the lending business. For details, please refer to the explanations set out in the Forecast for loan loss provisions section of the Forecast, Opportunities and Risks Report in the Management Report. There are also uncertainties particularly with respect to provisions for litigation risk, uncertainties as regards the outcome of future business decisions or results of settlement negotiations. As a result, actual utilisation by HSH Nordbank may differ from the expected utilisation as estimated at the time the provisions were recognised. Please refer to the Management of legal risks section in the Risk Report for further details with regard to material legal disputes.

Changes in pension provisions are presented in Note 44.

Other provisions changed as follows:

#### CHANGES IN OTHER PROVISIONS

(€ m)	For personnel expenses	In the lending business	For restructuring	For litigation risks and costs	Miscellaneous	Total
<b>2016</b>						
<b>As at 1 January 2016</b>	<b>43</b>	<b>107</b>	<b>94</b>	<b>37</b>	<b>185</b>	<b>466</b>
Additions	25	75	69	6	57	232
Reversals	2	67	4	2	22	97
Other changes	-	-	-	-	18	18
Reclassifications	-	-	-52	-	-62	-114
Changes in exchange rates	-	-	-	-	2	2
Changes in the scope of consolidation	-	-	-	-	-1	-1
Utilisation in the financial year	27	5	22	7	76	137
<b>As at 31 December 2016</b>	<b>39</b>	<b>110</b>	<b>85</b>	<b>34</b>	<b>101</b>	<b>369</b>

Reclassifications were made from Provisions to Provisions for pension obligations in the amount of € 24 million, to Liabilities in the amount of € 28 million and to Liabilities from disposal groups in the amount of € 62 million.

The other changes are attributable to the extension of the scope of consolidation due to the initial consolidation of a subsidiary that was previously considered immaterial (see Note 6).

#### CHANGES IN OTHER PROVISIONS

(€ m)	For personnel expenses	In the lending business	For restructuring	For litigation risks and costs	Miscellaneous	Total
<b>2015</b>						
<b>As at 1 January 2015</b>	<b>41</b>	<b>98</b>	<b>171</b>	<b>50</b>	<b>218</b>	<b>578</b>
Additions	28	36	3	15	105	187
Reversals	1	27	4	17	44	93
Other changes	-	-	-	-	-	-
Reclassifications	-18	-	-62	-	-31	-111
Changes in exchange rates	1	1	2	-	7	11
Changes in the scope of consolidation	-	-	-	-	-	-
Utilisation in the financial year	8	1	16	11	70	106
<b>As at 31 December 2015</b>	<b>43</b>	<b>107</b>	<b>94</b>	<b>37</b>	<b>185</b>	<b>466</b>

Reclassifications were mainly made from Provisions to Provisions for pension obligations in the amount of € 35 million and to Liabilities in the amount of € 48 million.

Provisions in the lending business are composed of the following items:

#### PROVISIONS IN THE LENDING BUSINESS

(€ m)	2016	2015
Specific loan loss provisions for		
Contingent liabilities	25	30
Irrevocable loan commitments	40	25
Other credit risks	2	2
<b>Total</b>	<b>67</b>	<b>57</b>
Portfolio loan loss provisions for		
Contingent liabilities	33	42
Irrevocable loan commitments	10	8
<b>Total</b>	<b>43</b>	<b>50</b>
<b>Total</b>	<b>110</b>	<b>107</b>

#### 44. PENSION OBLIGATIONS AND SIMILAR OBLIGATIONS

In recognising and measuring direct benefit pension plans, the net present value of the obligations is reduced by the fair value of the plan assets.

#### PROVISIONS FOR PENSION OBLIGATIONS AND SIMILAR OBLIGATIONS

(€ m)	2016	2015
Net present value of obligations, wholly or partly financed through funds	11	3
Net present value of obligations not financed through funds	1,150	1,056
<b>Net present value of pension obligations and similar obligations</b>	<b>1,161</b>	<b>1,059</b>
Fair value of plan assets	9	8
<b>Pension plan deficit (provisions for pension obligations and similar obligations)</b>	<b>1,152</b>	<b>1,051</b>

The net present value of defined benefit pension obligations has changed as follows:

#### CHANGES IN NET PRESENT VALUE

(€ m)	2016	2015
Net present value as at 1 January	1,059	1,130
Actuarial losses/gains (-)	-	-
due to changed financial assumptions	125	-86
due to experience-based adjustments	-36	-8
Interest expense	23	21
Past service cost	-	-1
Current service cost	11	15
Benefits paid	-46	-47
Reclassifications	25	35
<b>Net present value as at 31 December</b>	<b>1,161</b>	<b>1,059</b>

Early retirement arrangements were negotiated as part of the restructuring and associated reduction in staff and the corresponding provisions were transferred from restructuring to pension provisions.

The fair value of plan assets has changed as follows:

#### CHANGE IN FAIR VALUE OF PLAN ASSETS

(€ m)	2016	2015
<b>Fair value of plan assets as at 1 January</b>	<b>8</b>	<b>8</b>
Actuarial gains	1	-
<b>Fair value of plan assets as at 31 December</b>	<b>9</b>	<b>8</b>

The change in actuarial gains and losses is mainly attributable to a drop in the discount rate.

The total actuarial losses for the financial year before deferred taxes amounted to € -89 million (previous year: € 94 million). Allowing for deferred taxes, this results in a loss of € -60 million (previous year: € 64 million), which is recognised in Other comprehensive income and disclosed in retained earnings on an accumulated basis. As at 31 December 2016 the balance of actuarial gains/losses in retained earnings before tax amounted to € -242 million (previous year: -154 million) before tax and € -166 million (previous year: € -105 million).

#### BREAKDOWN OF PLAN ASSETS

(€ m)	2016	2015
Qualified insurance policies	8	7
Debentures and other fixed-interest securities	1	1
<b>Total</b>	<b>9</b>	<b>8</b>

The debentures and other fixed-interest securities included in the plan assets are traded on an active market.

Expenses of € 34 million were incurred for defined benefit pension plans in the 2016 reporting year (previous year: € 35 million).

Pension obligations represent future amounts to be paid and are uncertain both as to the amount and the date they fall due. Future fluctuations in the present value of the pension obligations can result particularly from a change in the actuarial assumptions such as the discount rate and life expectancy.

An increase or decrease in the actuarial assumptions (see Note 7) would have had the following impact on the present value of pension obligations as at 31 December 2016:

#### SENSITIVITY OF PENSION OBLIGATIONS

(€ m)	Increase	Decrease
<b>2016</b>		
Discount rate (+/-0.25 %)	-47	50
Inflation trend <sup>1)</sup> (+/-0.25 %)	41	-39
Life expectancy (+ 1 year)	50	-

#### SENSITIVITY OF PENSION OBLIGATIONS

(€ m)	Increase	Decrease
<b>2015</b>		
Discount rate (+/-0.5 %)	-79	90
Inflation trend <sup>1)</sup> (+/-0.25 %)	39	-37
Life expectancy (+ 1 year)	43	-

<sup>1)</sup> A variation in the inflation trend affects the salary trend. An assumption regarding future salary levels has a direct influence on future pension levels because of the fully dynamic pension commitments. The salary and pension trends were therefore not separately varied.

The average duration of the pension obligations determined as at 31 December 2016 was used as the basis for the sensitivity calculations. The impact of the major assumptions on the present value of the pension obligations is presented. As the sensitivity analyses are based on the average duration of the expected pension obligations and expected payment dates are therefore not taken into account, the figures represent only approximate values. Furthermore, where a change in an actuarial assumption is analysed, the other assumptions are kept constant.

HSH Nordbank expects to make payments of € 48 million to beneficiaries under defined benefit pension plan commitments for the 2017 financial year (previous year: € 45 million).

The weighted average duration of the defined benefit obligation is 18.3 years as at 31 December 2016 (previous year: 18.8 years).

Expenses for defined contribution plans were € 17 million in the 2016 reporting period (previous year: € 17 million). Payments to statutory pension schemes in the amount of € 15 million (previous year: € 15 million) are included in this figure.



#### 45. LIABILITIES RELATING TO DISPOSAL GROUPS

##### LIABILITIES RELATING TO DISPOSAL GROUPS

(€ m)	2016	2015
Liabilities to customers	-	1
Provisions	63	-
Other liabilities	2	-
<b>Total</b>	<b>65</b>	<b>1</b>

All of the liabilities included in this item are attributable to the disposal groups in connection with the market portfolio transaction (see Note 34).

#### 46. CURRENT TAX LIABILITIES

##### INCOME TAX LIABILITIES

(€ m)	2016	2015
Current tax liabilities		
Income tax liabilities to tax authorities	28	110
Provisions for income taxes	59	41
<b>Total</b>	<b>87</b>	<b>151</b>

Liabilities to tax authorities include liabilities on income taxes due to domestic and foreign tax authorities.

Provisions for income taxes include tax liabilities for which no legally binding tax assessment notice has been received as at the balance sheet date.

## 47. DEFERRED TAX LIABILITIES

For temporary differences in the tax bases of the following items in the statement of financial position deferred tax liabilities were created.

### DEFERRED TAX LIABILITIES

(€ m)	2016	2015
<b>Assets</b>		
Cash reserve	-	17
Loans and advances to banks	-	3
Loans and advances to customers	87	320
Credit derivative under the second loss guarantee	45	187
Financial investments	249	207
Trading assets	9	-
Positive fair values of hedging derivatives	161	248
Asset-side adjustment item from portfolio fair value hedges	128	129
Property, plant and equipment	45	4
Other assets	-	-
<b>Liabilities</b>		
Liabilities to banks	25	42
Provisions	-	-
Other liabilities	255	318
<b>Total</b>	<b>1,004</b>	<b>1,475</b>
Netting off deferred tax assets	-997	-1,475
<b>Total</b>	<b>7</b>	<b>-</b>

The drop in deferred tax liabilities before netting is mainly attributable to the reduction in temporary differences relating to loans and advances to customers and the credit derivative under the second loss guarantee in connection with the transfer of the federal state portfolio.

€ 6 million of the total change is attributable to reductions recognised directly in equity relating to financial investments.

Deferred tax liabilities of € 2 million (previous year: € 2 million) associated with investments in subsidiaries (so-called outside basis differences) were not recognised in accordance with IAS 12.39, as realisation is not probable.

There were no timing differences as at the reporting date for which deferred tax liabilities had not been recognised.

#### 48. OTHER LIABILITIES

##### OTHER LIABILITIES

(€ m)	2016	2015
Collateral provided for liabilities assumed	657	720
Liabilities for invoices outstanding	52	54
Outstanding payments for the second loss guarantee	45	102
Liabilities for restructuring	28	20
Other tax liabilities	18	46
Deferred income	18	22
Personnel liabilities	9	9
Other	18	56
<b>Total</b>	<b>845</b>	<b>1,029</b>

Other liabilities in the amount of € 668 million (previous year: € 733 million) have a residual maturity of more than one year.

The collateral provided for liabilities assumed serves to hedge leasing transactions of our customers with third parties.

€ 812 million of the liabilities reported here relate to financial instruments (previous year: € 950 million).

#### 49. SUBORDINATED CAPITAL

HSH Nordbank discloses subordinated liabilities, silent participations and profit participation capital under this item.

##### SUBORDINATED CAPITAL

(€ m)	2016	2015
Subordinated liabilities	2,110	2,109
Maturing in less than two years	1,028	1,033
Silent participations	1,412	1,330
Profit participation capital	14	13
Maturing in less than two years	14	13
<b>Total</b>	<b>3,536</b>	<b>3,452</b>

Subordinated capital of € 2,411 million (previous year: € 3,428 million) have a residual maturity of more than one year.

The difference between the carrying amount of the liabilities categorised as DFV and their par value, which corresponds to the contractually agreed repayment amount at the due date, amounted to € -4 million as at 31 December 2016 (previous year: € -9 million).

Hybrid financial instruments included under Subordinated capital include silent participations and profit participation capital. The carrying amount of these hybrid financial instruments was determined based on assumptions (see Note 8 I.E). In addition to Hybrid financial instruments disclosed here, Hybrid financial instruments are also disclosed in the line item Securitised liabilities (cf. Note 40).

## 50. EQUITY

EQUITY		
(€ m)	2016	2015
Share capital	3,018	3,018
Capital reserve	75	175
Retained earnings	1,617	1,464
Cumulative gains and losses arising on the revaluation of net defined benefit liabilities recognised in OCI	-242	-154
Deferred taxes on cumulative gains and losses arising on the revaluation of net defined benefit liabilities recognised in OCI	76	48
Revaluation reserve	127	103
Currency conversion reserve	60	42
Group net result	67	99
<b>Total before non-controlling interests</b>	<b>4,964</b>	<b>4,901</b>
Non-controlling interests	-14	-16
<b>Total</b>	<b>4,950</b>	<b>4,885</b>

### Share capital

The share capital of HSH Nordbank AG is divided into 301,822,453 registered shares each representing a notional of € 10.00 of share capital. All the issued shares have been fully paid up.

As at the reporting date, HSH Beteiligungs Management GmbH, Hamburg, was the largest shareholder with 94.90% of the voting rights (previous year: 0%). HSH Finanzfonds AöR – Gemeinsame Anstalt der Freien und Hansestadt Hamburg und des Landes Schleswig-Holstein – holds an interest of 68.03% (previous year: 65.00%), the Free and Hanseatic City of Hamburg incl. the interest held indirectly via HGV Hamburger Gesellschaft für Vermögens- und Beteiligungsmanagement mbH holds an interest of 11.30% (previous year: 10.80%), the Federal State of Schleswig-Holstein holds an interest of 10.02% (previous year: 9.58%) and Sparkassen- und Giroverband für Schleswig-Holstein holds an interest of 5.55% (previous year: 5.31%) in HSH Nordbank AG, with all of these interests being held indirectly via HSH Beteiligungs Management GmbH. As at 31 December 2016, the nine groups of investors advised by J.C. Flowers & Co. LLC held 5.10% of the voting rights in total (previous year: 9.31%).

HSH Beteiligungs Management GmbH, with its registered offices in Hamburg, notified us in June 2016 in accordance with Section 20(1)/(4) of the German Stock Corporation Act (AktG) that it directly owns more than one-quarter of the shares of HSH Nordbank AG, and at the same time owns a majority interest within the meaning of Section 16(1) AktG.

Neither HSH Nordbank AG nor any company dependent on it or majority-owned companies hold treasury stock. There are no cross-shareholdings as defined by Section 19 AktG.

### CHANGES IN ORDINARY SHARES

(Number of shares)	2016	2015
Number at the beginning of the year	301,822,453	301,822,453
<b>Number at the end of the year</b>	<b>301,822,453</b>	<b>301,822,453</b>

### Retained earnings and dividends

The item Retained earnings mainly shows amounts allocated from previous year profits and the profits of the current year. There are no statutory reserves or legal reserves within the meaning of Section 150(2) of the German Stock Corporation Act (AktG).

Retained earnings include amounts of € 4,919 million (previous year: € 4,819 million) transferred from the capital reserve to disclose a break-even result on the balance sheet offset loss carryforwards of HSH Nordbank AG. € 100 million was transferred from the capital reserve in the 2016 financial year to offset the loss of HSH Nordbank AG carried forward from the previous year.

As was the case for the previous financial year 2015, no dividend payments were made for previous years during the current financial year 2016.

### Capital reserve

An amount of € 100 million was released from capital reserves to offset the losses of HSH Nordbank AG brought forward from 2015 (previous year for the loss brought forward from 2014: € 312 million).

### Revaluation reserve

The effects of the measurement of AfS financial instruments disclosed at fair value directly in equity are recorded in the revaluation reserve.

The changes in value associated with deferred taxes shown in the revaluation reserve are also presented in the revaluation reserve pursuant to IAS 12.61A.

### Currency conversion reserve

Assets and liabilities in financial statements of subsidiaries in foreign currencies are translated at the reporting date exchange rate in preparing the Group financial statements, while average rates for the reporting period are used to translate expenses and income. Equity is translated at historical rates, with the exception of revaluation reserves in Group financial statements reported in foreign currencies, which are translated at the reporting date exchange rate.

Any differences arising from this method of translation compared to complete translation at the reporting date exchange rate are reported in this Equity item.

### Capital management

The capital management of HSH Nordbank aims to comply with regulatory minimum capital ratios. In addition to these minimum requirements, capital management is used as the basis for complying with the capital ratios planned and is designed to ensure that the Bank's capital base meets the risk-bearing capacity requirements. The common equity Tier 1 capital ratio is the key parameter for capital management.

The regulatory capitalisation is in accordance with the provisions of the European Capital Requirements Regulation (CRR) in conjunction with the Supervisory Review and Evaluation Process (SREP). HSH Nordbank determines the capital requirements for counterparty risk in accordance with the approach permitted by the Federal Financial Supervisory Authority based on internal ratings (Advanced IRBA) and based on the CSA (standard approach). The capital base is reported to the regulatory authorities quarterly. The minimum ratios required under supervisory law were complied with on each reporting date in the course of the year under review.

#### REGULATORY FIGURES<sup>1)</sup>

(in %)	2016	2015
Tier 1 capital ratio (incl. market risk position)	18.5	15.7
Overall capital ratio/regulatory capital ratio	24.2	20.1

<sup>1)</sup> Values before adoption of the Group financial statements of HSH Nordbank.

The regulatory capital commitment was monitored closely both at Bank and division level in the course of the financial year.



## SEGMENT REPORTING

## 51. SEGMENT REPORT

(€ m/%)	Corporate Clients		Real Estate		Shipping		Treasury & Markets		Core Bank	
	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015
Net interest income	159	211	170	167	89	131	231	–	649	509
Net commission income	56	52	16	21	10	13	1	6	83	92
Result from hedging	–	–	–	–	–	–	–	–	–	–
Net trading income	36	–11	32	–1	29	–17	89	261	186	232
Net income from financial investments <sup>1)</sup>	–	–	–	–	–1	–	86	17	85	17
<b>Total income</b>	<b>251</b>	<b>252</b>	<b>218</b>	<b>187</b>	<b>127</b>	<b>127</b>	<b>407</b>	<b>284</b>	<b>1,003</b>	<b>850</b>
Loan loss provisions in the lending business incl. credit derivative under the second loss guarantee <sup>2)</sup>	–5	–10	–	11	52	–169	–	–	47	–168
Administrative expenses	–149	–160	–57	–56	–53	–63	–98	–116	–357	–395
Other operating income	4	10	–1	2	2	–32	–3	1	2	–19
Expenses for bank levy and deposit guarantee fund	–7	–6	–10	–7	–6	–5	–8	–6	–31	–24
<b>Net income before restructuring and privatisation</b>	<b>94</b>	<b>86</b>	<b>150</b>	<b>137</b>	<b>122</b>	<b>–142</b>	<b>298</b>	<b>163</b>	<b>664</b>	<b>244</b>
Net income from restructuring and privatisation	–	–	–	–	–	–	–	–	–	–
Expenses for government guarantees	–5	–9	–2	–6	–18	–24	–	–1	–25	–40
<b>Net income before taxes</b>	<b>89</b>	<b>77</b>	<b>148</b>	<b>131</b>	<b>104</b>	<b>–166</b>	<b>298</b>	<b>162</b>	<b>639</b>	<b>204</b>
Cost/income ratio (CIR)	58 %	61 %	26 %	30 %	41 %	66 %	24 %	41 %	36 %	48 %
Return on equity before tax	7 %	8 %	19 %	24 %	24 %	–68 %	38 %	12 %	20 %	7 %
Average equity	1,228	926	780	555	434	243	780	1,303	3,222	3,027

(€ bn)	2016	2015	2016	2015	2016	2015	2016	2015	2016	2015
<b>Segment assets</b>	<b>12</b>	<b>12</b>	<b>11</b>	<b>11</b>	<b>6</b>	<b>8</b>	<b>19</b>	<b>19</b>	<b>48</b>	<b>49</b>

1) Including net income from financial investments accounted for under the equity method.

2) Consolidation of the Loan loss provisions in the lending business and Hedging effect of credit derivative under the second loss guarantee.

(€ m/%)	Core Bank		Non-Core Bank		Other and Consolidation <sup>3)</sup>		Group	
	2016	2015	2016	2015	2016	2015	2016	2015
Net interest income	649	509	15	285	-57	238	607	1,032
Net commission income	83	92	20	29	-16	-7	87	114
Result from hedging	-	-	-	-	-4	12	-4	12
Net trading income	186	232	-53	53	-45	-201	88	84
Net income from financial investments <sup>1)</sup>	85	17	54	40	4	-3	143	54
<b>Total income</b>	<b>1,003</b>	<b>850</b>	<b>36</b>	<b>407</b>	<b>-118</b>	<b>39</b>	<b>921</b>	<b>1,296</b>
Loan loss provisions in the lending business incl. credit derivative under the second loss guarantee <sup>2)</sup>	47	-168	106	436	3	36	156	304
Administrative expenses	-357	-395	-299	-253	22	14	-634	-634
Other operating income	2	-19	62	33	-6	24	58	38
Expenses for bank levy and deposit guarantee fund	-31	-24	-15	-17	-10	-9	-56	-50
<b>Net income before restructuring and privatisation</b>	<b>664</b>	<b>244</b>	<b>-110</b>	<b>606</b>	<b>-109</b>	<b>104</b>	<b>445</b>	<b>954</b>
Net income from restructuring and privatisation	-	-	-	-	-110	-31	-110	-31
Expenses for government guarantees	-25	-40	-189	-433	-	-	-214	-473
<b>Net income before taxes</b>	<b>639</b>	<b>204</b>	<b>-299</b>	<b>173</b>	<b>-219</b>	<b>73</b>	<b>121</b>	<b>450</b>
Cost/income ratio (CIR)	36%	48%	-	-	-	-	65%	48%
Return on equity before tax	20%	7%	-	-	-	-	2%	9%
Average equity	3,222	3,027	1,433	1,282	263	470	4,918	4,779

(€ bn)	2016	2015	2016	2015	2016	2015	2016	2015
<b>Segment assets</b>	<b>48</b>	<b>49</b>	<b>22</b>	<b>30</b>	<b>14</b>	<b>18</b>	<b>84</b>	<b>97</b>

1) Including Net income from financial investments accounted for under the equity method.

2) Consolidation of the Loan loss provisions in the lending business and Hedging effect of credit derivative under the second loss guarantee.

3) Consolidation includes the effect from different accounting.

(€ m/%)	2016			2015		
	Other	Consolidation <sup>3)</sup>	Total Other and Consolidation	Other	Consolidation <sup>3)</sup>	Total Other and Consolidation
Net interest income	13	-70	-57	157	81	238
Net commission income	-8	-8	-16	-7	-	-7
Result from hedging	-	-4	-4	-	12	12
Net trading income	14	-59	-45	37	-238	-201
Net income from financial investments <sup>1)</sup>	-	4	4	-6	3	-3
<b>Total income</b>	<b>19</b>	<b>-137</b>	<b>-118</b>	<b>181</b>	<b>-142</b>	<b>39</b>
Loan loss provisions in the lending business incl. credit derivative under the second loss guarantee <sup>2)</sup>	-1	4	3	37	-1	36
Administrative expenses	22	-	22	9	5	14
Other operating income	-5	-1	-6	14	10	24
Expenses for bank levy and deposit guarantee fund	-10	-	-10	-8	-1	-9
<b>Net income before restructuring and privatisation</b>	<b>25</b>	<b>-134</b>	<b>-109</b>	<b>233</b>	<b>-129</b>	<b>104</b>
Net income from restructuring and privatisation	-	-110	-110	-	-31	-31
Expenses for government guarantees	-	-	-	-	-	-
<b>Net income before taxes</b>	<b>25</b>	<b>-244</b>	<b>-219</b>	<b>233</b>	<b>-160</b>	<b>73</b>
Cost/income ratio (CIR)	-	-	-	-	-	-
Return on equity before tax	-	-	-	-	-	-
Average equity	264	-1	263	474	-4	470

(€ bn)	2016			2015		
	Segment assets					
	<b>14</b>	<b>-</b>	<b>14</b>	<b>17</b>	<b>1</b>	<b>18</b>

1) Including Net income from financial investments accounted for under the equity method.

2) Consolidation of the Loan loss provisions in the lending business and Hedging effect of credit derivative under the second loss guarantee.

3) Consolidation includes the effect from different accounting.

Segment reporting is in accordance with the provisions of IFRS 8. The Group has five segments subject to a reporting requirement: four in the Core Bank, and the Non-Core Bank. The Core Bank segments result from the Bank's internal organisational structure which is based on product and customer groups and which corresponds to the delimitation for internal Group management purposes. The formation of the segments is intended to achieve the greatest possible homogeneity of customer groups with regard to a focused loan financing product range as well as other products and services.

HSH Nordbank's Core Bank consists of the segments Real Estate, Shipping, Corporate Clients and Treasury & Markets. The business activities of the Real Estate, Shipping and Corporate Clients customer departments focus on offering financing solutions in the lending business.

As at 31 December 2016, the Real Estate segment includes business with real estate clients, while the Shipping segment includes the business with shipping clients. The strategic focus of the Corporate Clients segment primarily lies on the Logistics & Infrastructure, Energy & Utilities, Healthcare, Commerce & Food and Industry & Services business fields. Another key area is the advising of wealthy private clients, institutions and non-profit organisations with regard to asset management. The Treasury & Markets segment supports the customer departments in their business by providing a tailored range of capital market-oriented product solutions and within the framework of syndications. At the same time, support is provided to the savings banks and institutional clients in the areas of issuance and deposits. This segment is also responsible for the central management of the liquidity and market price risks relating to the Bank's position and the Bank's function as an issuer.

The Non-Core Bank includes credit and capital market transactions that are not continued in the Core Bank. These are overall bank positions for which the Overall Management Board is responsible. The focus is on reducing the risk potential whilst minimising the effect on income. The Special Credit Management business unit is responsible for loan restructuring and workout and, as a result, also for the active winding down of the portfolio of impaired loan commitments.

The segment structure was adjusted in the second half of 2016. Up until the time of the adjustment, the Core Bank consisted of the following segments: Shipping, Project and Real Estate Financing (SPI), Corporates & Markets (CM) and the Corporate Center (CC). As part of the change in internal reporting, the SPI segment was split into the Real Estate and Shipping segments. The CM segment was split into two segments: Corporate Clients and Treasury & Markets. The CC segment is now showing, together with reconciliation effects, as a segment not subject to a reporting requirement under "Other and Consolidation". The segment previously known as the Restructuring Unit was renamed the Non-Core Bank in the second half of 2016. The figures for the previous year have been adjusted accordingly.

In connection with the adjustment of the segment structure, there were shifts in the portfolio between the Core Bank and the Non-Core Bank in the third quarter of 2016. Within this context, impaired loan portfolios in the amount of € 6.2 billion exposure at default (EaD), particularly from the Shipping recovery unit within the Core Bank, were transferred to the Non-Core Bank. These mainly relate to legacy burdens from the years before 2009, which are largely covered by the second loss guarantee of the federal state owners. In return, € 4.5 billion (EaD) relating mainly to cover pool portfolios was transferred from the Non-Core Bank to the Treasury & Markets segment of the Core Bank. This systematically splits the loan portfolio into activities to be continued in the Core Bank on the one hand, and impaired portfolios designated for risk reduction in the Non-Core Bank on the other. The figures for the previous year have been adjusted accordingly.

The expenses for the bank levy and deposit guarantee fund have been allocated to the segments based on the adjusted balance sheet volume since the 2016 year end. The figures for the previous year have been adjusted accordingly.

The management adjustment general loan loss provisions within loan loss provisions is shown in the segments in which it originated (previous year: in full in the CC segment). The amount reported for the previous year (€ -440 million) has been adjusted accordingly.

Loan loss provisions are shown in the segments in which they originated. For the loan loss provisions set up for the individual segments, the hedging effect of the second loss guarantee including the hedging effect of the credit derivative under the second loss guarantee is also shown in the corresponding segments, insofar as the loan exposures in question are hedged using the second loss guarantee.

By way of derogation from this principle, the guarantee fees are allocated to the segments based on the regulatory equity capital requirements for the guaranteed portfolio. Insofar as the guarantee fees would have been allocated based on the compensation effect in the reporting year, then the Core Bank would have had € 20 million (previous year: € 23 million) less to bear in guarantee fees, and the Non-Core Bank would have had to bear a higher amount accordingly.

The effects from the results of the loss settlements reported in the compensation item in the amount of € 430 million are shown in full in the Non-Core Bank. The share of the Core Bank for 2016 would come to 7%.

The compensation effect from the unwinding is also allocated to the Non-Core Bank in full. This would amount to € 7 million (previous year: € 12 million) for the Core Bank in 2016.

The Other column shows the contributions made by segments not subject to a reporting requirement and the contributions made by other business activities. These include the administration and service divisions and the Transaction Banking product division, which offers tailor-made services in the fields of payment transactions, account management and foreign trade for the customer departments, insofar as these activities were not allocated to the segments subject to a reporting requirement as part of the business management of the Bank.

The Consolidation column contains effects from different accounting methods between the parameters reported internally and the presentation in the Group financial statements. The reconciliation effects included are shown separately in the table above pursuant to IFRS 8.28 and are explained in further detail below.

Net interest income for the purpose of internal reporting to management is calculated in accordance with the Fund Transfer Pricing (FTP). The planned investment and financing profit is distributed among the business segments on the basis of economic capital committed. The transformation contribution is allocated to the segments on the basis of receivables. The calculation of the transformation contribution to be allocated was adjusted as at the reporting date so that only the results from the liquidity management of the banking book (liquidity account) are distributed among the segments. Compared with the previous allocation, a total amount of € 96 million (previous year: € 125 million), mainly the results from the money market business, remains in the Treasury & Markets segment. The previous year figures have been adjusted accordingly.

Reconciliation effects relating to net interest income in the amount of € –70 million are due largely to valuation differences. These are largely the result of the use of internal transactions within the framework of internal interest rate and liquidity management/the consideration of imputed interest rate margins (fund transfer pricing, FTP)) instead of gross interest in the lending business. Further reconciliation effects result, in particular, from the use of what are, in some cases, different calculation and amortisation methods within the context of internal reporting. In addition, in the internal management system, the measurement results of the hedging derivatives in hedge accounting are only shown in net interest income upon the disposal of AfS, LaR and LIA positions, whereas under the IFRS hedge accounting regulations, the hedge adjustments are continuously amortised within net interest income.

The reconciliation effects relating to net trading income in the amount of € 19 million (net) include differences resulting from the recognition

of capital market transactions between the internal management system and IFRS accounting, among other things resulting from different posting methods for foreign currency transactions and from changes in the credit rating of own issues that were not taken into account in internal management. This is offset by the valuation effects, taken into account in the internal reporting, resulting from the closure of derivatives in the amount of € –45 million, which were already taken into account in the fair value measurement in previous periods under the IFRS accounting. Net trading income of individual subsidiaries in the scope of consolidation in the amount of € 10 million is not taken into account in the internal management. Further differences result from the hedging of certain financial instruments in the amount of around € –35 million that are included in the portfolio fair value hedge in full in the internal recognition of the interest rate hedge transaction, whereas under the IFRS, they are not, or are only partly, included in the portfolio fair value hedge.

In addition, net income from restructuring and privatisation is also shown in full under Consolidation as an item for reconciliation with the internally managed values.

The business activities of HSH Nordbank lie predominantly in loan financing in Germany. As a result, there is no need to publish geographical information in accordance with IFRS 8.33.

The cost/income ratio (CIR) and return on equity (RoE) are not shown in the segment report for the Non-Core Bank segment. In the case of the Non-Core Bank, the segment involves business areas which are not strategic and are currently being wound down. This segment is not managed on the basis of these ratios.

Total income recognised in the segments is exclusively generated from business conducted with external customers.

The allocation key for the allocation of the average reported equity capital to the segments is the regulatory capital commitment due to its management relevance.

The CIR is calculated as the ratio of Administrative expenses to Total income plus Other operating income. Return on equity is the ratio of net income before taxes to average equity capital.

See Note 17 for comments on the depreciation of goodwill recognised in the segments. See Note 14 for comments on companies consolidated under the equity method recognised as part of Net income from financial investments.



## NOTES ON FINANCIAL INSTRUMENTS

### 52. CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS BY IAS 39 CATEGORY

#### CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS BY IAS 39 CATEGORY

(€ m)	LaR	AfS	DFV	HfT	LIA	No IAS 39 category	Total
<b>2016</b>							
<b>Assets</b>							
Cash reserve	3,373	118	-	-	-	-	3,491
Loans and advances to banks	4,108	84	-	-	-	-	4,192
Loans and advances to customers	49,430	61	1,321	-	-	-	50,812
Receivables under finance leases	-	-	-	-	-	98	98
Credit derivative under the second loss guarantee	-	-	-	199	-	-	199
Positive fair values of hedging derivatives	-	-	-	-	-	508	508
Value adjustments from the portfolio fair value hedge	-	-	-	-	-	403	403
Trading assets	-	-	-	5,433	-	-	5,433
Financial investments	1,498	12,441	1,554	-	-	-	15,493
Non-current assets held for sale and disposal groups	1,140	19	-	-	-	-	1,159
Other assets	50	-	-	-	-	-	50
<b>Total assets</b>	<b>59,599</b>	<b>12,723</b>	<b>2,875</b>	<b>5,632</b>	<b>-</b>	<b>1,009</b>	<b>81,838</b>
<b>Liabilities</b>							
Liabilities to banks	-	-	120	-	9,381	-	9,501
Liabilities to customers	-	-	1,331	-	38,841	-	40,172
Securitised liabilities	-	-	2,256	-	14,368	-	16,624
Negative fair value of hedging derivatives	-	-	-	-	-	290	290
Value adjustments from the portfolio fair value hedge	-	-	-	-	-	786	786
Trading liabilities	-	-	-	5,981	-	-	5,981
Liabilities relating to disposal groups	-	-	-	-	2	-	2
Subordinated capital	-	-	87	-	3,449	-	3,536
Other liabilities	-	-	-	-	812	-	812
<b>Total liabilities</b>	<b>-</b>	<b>-</b>	<b>3,794</b>	<b>5,981</b>	<b>66,853</b>	<b>1,076</b>	<b>77,704</b>

**CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS BY IAS 39 CATEGORY**

(€ m)	LaR	AfS	DFV	HfT	LIA	No IAS 39 category	Total
2015							
<b>Assets</b>							
Cash reserve	2,700	694	-	-	-	-	3,394
Loans and advances to banks	5,509	86	-	-	-	-	5,595
Loans and advances to customers	55,057	104	1,308	-	-	-	56,469
Receivables under finance leases	-	-	-	-	-	106	106
Credit derivative under the second loss guarantee	-	-	-	663	-	-	663
Positive fair values of hedging derivatives	-	-	-	-	-	783	783
Value adjustments from the portfolio fair value hedge	-	-	-	-	-	408	408
Trading assets	-	-	-	7,356	-	-	7,356
Financial investments	2,138	12,907	1,591	-	-	-	16,636
Non-current assets held for sale and disposal groups	5,081	-	-	-	-	-	5,081
Other assets	86	-	-	-	-	-	86
<b>Total assets</b>	<b>70,571</b>	<b>13,791</b>	<b>2,899</b>	<b>8,019</b>	<b>-</b>	<b>1,297</b>	<b>96,577</b>
<b>Liabilities</b>							
Liabilities to banks	-	-	148	-	14,250	-	14,398
Liabilities to customers	-	-	1,482	-	43,085	-	44,567
Securitised liabilities	-	-	3,029	-	15,587	-	18,616
Negative fair value of hedging derivatives	-	-	-	-	-	726	726
Value adjustments from the portfolio fair value hedge	-	-	-	-	-	872	872
Trading liabilities	-	-	-	6,758	-	-	6,758
Liabilities relating to disposal groups	-	-	-	-	1	-	1
Subordinated capital	-	-	87	-	3,365	-	3,452
Other liabilities	-	-	-	-	950	-	950
<b>Total liabilities</b>	<b>-</b>	<b>-</b>	<b>4,746</b>	<b>6,758</b>	<b>77,238</b>	<b>1,598</b>	<b>90,340</b>

### 53. RECLASSIFICATION UNDER IAS 39 (REV. 2008)

HSH Nordbank exercised the option of reclassifying assets under IAS 39 (rev. 2008) as LaR where they meet the relevant requirements, were not intended for short-term sale at the time of reclassification and are due to be held for the foreseeable future. The assets were reclassified in 2008 and 2009 due to the global financial market crisis and the consequences it has had on the measurement of securities portfolios. The reclassifications were performed in accordance with IAS 39.50D or IAS 39.50E respectively.

The reclassification as LaR measures fair value at the time of reclassification at cost or amortised cost, respectively. At the time of reclassification an effective interest rate was determined which is used for subsequent measurement

of the amortised acquisition cost. For reclassification of financial instruments from AfS to LaR the revaluation reserve recognised up to the point of reclassification is reversed through Net interest income on a pro rata temporis basis in accordance with IAS 39.54 a).

The financial instruments reclassified in 2008 fell due in 2015, meaning that they are not to be reported.

The reclassifications of assets in the second quarter of 2009 are shown in the table below:

(€ m)	Carrying amount as at the time of reclassification	2016		2015	
		Carrying amount	Fair value	Carrying amount	Fair value
Reclassified from AfS to LaR	6,336	623	733	945	1,059
<b>Total financial assets reclassified as LaR</b>	<b>6,336</b>	<b>623</b>	<b>733</b>	<b>945</b>	<b>1,059</b>

The effective interest rate applied in the case of financial instruments in the AfS category was between 0.87% and 5.00%. Anticipated repayments amounted to € 6,465 million.

The decrease in the carrying amounts and fair values of all reclassified financial instruments is due to extensive changes in holdings. Financial instruments that have been disposed of or fallen due since reclassification had a carrying amount of € 5,816 million in the AfS category at the time of the reclassification. The sales were carried out following the realignment of HSH Nordbank and were neither planned nor anticipated at the time of the restructuring.

Shown below is the impact the holdings reclassified to date that are still in the portfolio would have had on the income statement and

revaluation reserve if they had not been reclassified. For financial instruments reclassified from AfS in the 2009 financial year, the valuation result in the revaluation reserve for the current reporting period would have been € 12 million (previous year: € 5 million).

The actual impact of the holdings reclassified to date that are still in the portfolio on the income statement of the current reporting period are shown below. In the reporting period, the statement of income includes Net interest income of € 18 million (previous year: € 17 million), Net trading income of € 10 million (previous year: € 0 million) and Net income from financial investments of € 73 million (previous year: € 26 million).

#### 54. RESIDUAL MATURITY BREAKDOWN OF FINANCIAL INSTRUMENTS

When determining the residual maturities of financial liabilities for purposes of presenting liquidity risk, the contractually agreed maturity dates of non-discounted cash flows are used as the basis.

(€ m) 2016	Payable on demand	Up to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Total
<b>Liabilities</b>						
Liabilities to banks	1,681	1,213	827	4,169	1,873	9,763
Liabilities to customers	12,374	10,240	6,490	6,848	6,889	42,841
Securitised liabilities	–	517	3,017	10,109	4,610	18,253
Negative fair value of hedging derivatives	–	44	54	261	42	401
Trading liabilities	6	603	936	2,795	2,637	6,977
thereof: derivatives	6	603	936	2,795	2,637	6,977
Liabilities relating to disposal groups	–	–	2	–	–	2
Other liabilities	4	80	89	661	6	840
Subordinated capital	–	936	99	380	3,497	4,912
Contingent liabilities	2,189	–	–	–	–	2,189
Irrevocable loan commitments	6,654	–	–	–	–	6,654
<b>Total</b>	<b>22,908</b>	<b>13,633</b>	<b>11,514</b>	<b>25,223</b>	<b>19,554</b>	<b>92,832</b>

(€ m) 2015	Payable on demand	Up to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Total
<b>Liabilities</b>						
Liabilities to banks	982	6,948	874	4,078	2,067	14,949
Liabilities to customers	17,126	11,917	4,469	6,411	7,869	47,792
Securitised liabilities	2	1,406	2,173	12,065	5,818	21,464
Negative fair value of hedging derivatives	–	75	107	470	137	789
Trading liabilities	6	450	1,352	3,430	2,222	7,460
thereof: derivatives	6	450	1,352	3,430	2,222	7,460
Liabilities relating to disposal groups	–	–	1	–	–	1
Other liabilities	4	101	148	698	35	986
Subordinated capital	–	3	42	1,319	3,657	5,021
Contingent liabilities	2,833	–	–	–	–	2,833
Irrevocable loan commitments	6,370	–	–	–	–	6,370
<b>Total</b>	<b>27,323</b>	<b>20,900</b>	<b>9,166</b>	<b>28,471</b>	<b>21,805</b>	<b>107,665</b>

Interest rate swaps, cross currency interest rate swaps and equity swaps are presented on the basis of their future net payment obligations. Other derivatives are assigned to maturity bands by overall maturity at their carrying amount.

Liquidity management is described in detail in the Risk report section of the Group management report.

## 55. DISCLOSURE OF FAIR VALUE IN ACCORDANCE WITH IFRS 7 AND IFRS 13

### I. Fair values of financial instruments

The fair values of financial assets and financial liabilities are disclosed by classes of financial instruments and compared with the respective carrying amount below:

#### FAIR VALUES OF FINANCIAL INSTRUMENTS

##### ASSETS

(€ m)	2016			2015		
	Carrying amount	Fair value	Difference	Carrying amount	Fair value	Difference
Held for Trading (HfT)						
Trading assets	5,433	5,433	–	7,356	7,356	–
Credit derivative under the second loss guarantee	199	199	–	663	663	–
Designated at Fair Value (DFV)						
Loans and advances to customers	1,321	1,321	–	1,308	1,308	–
Financial investments	1,554	1,554	–	1,591	1,591	–
Available for Sale (AFS)						
Cash reserve	118	118	–	694	694	–
Loans and advances to banks	84	84	–	86	86	–
Loans and advances to customers	61	61	–	104	104	–
Financial investments <sup>1)</sup>	12,441	12,603	162	12,907	13,085	178
of which equity instruments measured at cost	203	–	–	211	–	–
Non-current assets held for sale and disposal groups	19	19	–	–	–	–
Loans and Receivables (LaR)						
Cash reserve	3,373	3,373	–	2,700	2,700	–
Loans and advances to banks	4,107	4,122	15	5,494	5,512	18
Loans and advances to customers	42,952	43,086	134	49,247	51,511	2,264
Financial investments	1,498	1,563	65	2,138	2,196	58
Non-current assets held for sale and disposal groups	907	910	3	2,679	2,679	–
Other assets	50	50	–	86	86	–
No IAS 39 category						
Positive fair value of hedging derivatives	508	508	–	783	783	–
Receivables under finance leases	98	98	–	106	106	–
Value adjustments from the portfolio fair value hedge	403	–	–403	408	–	–408
<b>Total assets</b>	<b>75,126</b>	<b>75,102</b>	<b>–24</b>	<b>88,350</b>	<b>90,460</b>	<b>2,110</b>

<sup>1)</sup> € 203 million (previous year: € 211 million) of the difference between the carrying amount and fair value is attributable to equity instruments measured at cost in accordance with IAS 39.46 (c). Another difference between the carrying amount and fair value of financial investments classified as AFS is attributable to the fact that the adjustment item recognised for these transactions from the portfolio fair value hedge is separately disclosed. It corresponds to the effective portion of the hedging relationship recognised through profit or loss and is therefore not included in the carrying amount.



The effective portions of the hedging relationship recognised through profit or loss are disclosed in the Value adjustments from the portfolio fair value hedge item, of which € 365 million is accounted for by financial investments classified as available for sale (AFS) (previous year: € 389 million) and € 38 million (previous year: € 19 million) by loans and advances to banks and customers classified as LaR.

## FAIR VALUES OF FINANCIAL INSTRUMENTS

### LIABILITIES

(€ m)	2016			2015		
	Carrying amount	Fair value	Difference	Carrying amount	Fair value	Difference
Held for Trading (HFT)						
Trading liabilities	5,981	5,981	–	6,758	6,758	–
Designated at Fair Value (DFV)						
Liabilities to banks	120	120	–	148	148	–
Liabilities to customers	1,331	1,331	–	1,482	1,482	–
Securitised liabilities	2,256	2,256	–	3,029	3,029	–
Subordinated capital	87	87	–	87	87	–
Other Liabilities (LIA)						
Liabilities to banks	9,381	9,387	6	14,250	14,276	26
Liabilities to customers	38,841	39,891	1,050	43,085	44,390	1,305
Securitised liabilities	14,368	14,138	–230	15,587	15,604	17
Liabilities relating to disposal groups	2	2	–	1	1	–
Other liabilities	812	812	–	950	950	–
Subordinated capital	3,449	2,948	–501	3,365	2,867	–498
No IAS 39 category						
Negative fair value of hedging derivatives	290	290	–	726	726	–
Value adjustments from the portfolio fair value hedge	786	–	–786	872	–	–872
<b>Total liabilities</b>	<b>77,704</b>	<b>77,243</b>	<b>–461</b>	<b>90,340</b>	<b>90,318</b>	<b>–22</b>

The carrying amounts of loans and advances to banks and loans and advances to customers classified as LaR are shown less the reported loan loss provisions, since fair value also reflects possible impairments.

## II. Fair value hierarchy for financial instruments measured at fair value

Assets and liabilities show the following breakdown by level in the fair value hierarchy under IFRS 13. For assets and liabilities recognised and measured at fair value, the fair values are broken down by class of financial instrument in the three levels in the hierarchy.

### HIERARCHY LEVELS, ASSETS

(€ m)	Assets recognised at fair value			Total
	Level 1	Level 2	Level 3	
<b>2016</b>				
<b>Balance sheet item/ category/ instrument type</b>				
Cash reserve				
Afs	-	118	-	118
of which debt instruments	-	118	-	118
Loans and advances to banks				
Afs	-	40	44	84
of which debt instruments	-	40	44	84
Loans and advances to customers				
Afs	-	-	61	61
of which debt instruments	-	-	61	61
DFV	-	48	1,273	1,321
of which debt instruments	-	48	1,273	1,321
Credit derivative under the second loss guarantee				
of which credit derivatives	-	-	199	199
Positive fair values of hedging derivatives				
of which interest rate derivatives	-	508	-	508
Trading assets (HFT)	161	4,826	446	5,433
of which debt instruments	161	307	9	477
of which interest rate derivatives	-	4,001	96	4,097
of which cross-currency interest rate derivatives	-	244	-	244
of which currency derivatives	-	108	29	137
of which credit derivatives	-	27	-	27
of which other derivatives	-	12	51	63
of which structured derivatives	-	114	261	375
of which other trading portfolios	-	13	-	13
Financial investments (excluding equity instruments measured at cost)				
Afs <sup>1)</sup>	9,968	2,241	29	12,238
of which debt instruments	9,913	2,239	-	12,152
of which equity and near-equity instruments	55	2	29	86
DFV	-	1,009	545	1,554
of which debt instruments	-	1,008	544	1,552
of which contractually linked instruments	-	1	-	1
of which equity and near-equity instruments	-	-	1	1
Non-current assets held for sale and disposal groups				
Afs	-	19	-	19
of which equity and near-equity instruments	-	19	-	19
<b>Total</b>	<b>10,129</b>	<b>8,809</b>	<b>2,597</b>	<b>21,535</b>

<sup>1)</sup> The difference between the total Afs financial investments in the asset hierarchy table and the fair value disclosures in Section I is attributable to effects in the item Value adjustments from the portfolio fair value hedge in the amount of € 365 million. These effects are not disclosed in the hierarchy table.

**HIERARCHY LEVELS, ASSETS**

(€ m)	Assets recognised at fair value			
	Level 1	Level 2	Level 3	Total
<b>2015</b>				
<b>Balance sheet item/ category/ instrument type</b>				
Cash reserve				
AFS	–	694	–	694
of which debt instruments	–	694	–	694
Loans and advances to banks				
AFS	–	42	44	86
of which debt instruments	–	42	44	86
Loans and advances to customers				
AFS	–	–	104	104
of which debt instruments	–	–	104	104
DFV	–	54	1,254	1,308
of which debt instruments	–	54	1,254	1,308
Credit derivative under the second loss guarantee				
of which credit derivatives	–	–	663	663
Positive fair values of hedging derivatives				
of which interest rate derivatives	–	783	–	783
Trading assets (Hft)	511	6,349	496	7,356
of which debt instruments	511	1,165	–	1,676
of which contractually linked instruments	–	85	–	85
of which equity and near-equity instruments	–	1	–	1
of which interest rate derivatives	–	4,362	150	4,512
of which cross-currency interest rate derivatives	–	221	–	221
of which currency derivatives	–	208	29	237
of which credit derivatives	–	30	–	30
of which other derivatives	–	46	17	63
of which structured derivatives	–	218	300	518
of which other trading portfolios	–	13	–	13
Financial investments (excl. equity instruments measured at cost)				
AFS <sup>1)</sup>	8,345	4,193	159	12,697
of which debt instruments	8,301	4,114	16	12,431
of which contractually linked instruments	–	59	–	59
of which equity and near-equity instruments	44	20	143	207
DFV	–	1,045	546	1,591
of which debt instruments	–	1,044	544	1,588
of which contractually linked instruments	–	1	–	1
of which equity and near-equity instruments	–	–	2	2
<b>Total</b>	<b>8,856</b>	<b>13,160</b>	<b>3,266</b>	<b>25,282</b>

<sup>1)</sup> The difference between the total AFS financial investments in the asset hierarchy table and the fair value disclosures in Section I is attributable to effects in the item Value adjustments from the portfolio fair value hedge in the amount of € 389 million. These effects are not disclosed in the hierarchy table.

**HIERARCHY LEVELS, LIABILITIES**

(€ m)	Liabilities recognised at fair value			<b>Total</b>
	Level 1	Level 2	Level 3	
<b>2016</b>				
Liabilities to banks				
DFV	-	11	109	120
of which debt instruments	-	11	109	120
Liabilities to customers				
DFV	-	313	1,018	1,331
of which debt instruments	-	313	1,018	1,331
Securitised liabilities				
DFV	-	1,762	494	2,256
of which debt instruments	-	1,762	494	2,256
Negative fair value of hedging derivatives	-	290	-	290
of which interest rate derivatives	-	290	-	290
Trading liabilities (Hft)	-	4,982	999	5,981
of which interest rate derivatives	-	4,171	583	4,754
of which cross-currency interest rate derivatives	-	396	-	396
of which currency derivatives	-	152	40	192
of which other derivatives	-	-	51	51
of which structured derivatives	-	263	325	588
Subordinated capital				
DFV	-	87	-	87
of which debt instruments	-	87	-	87
<b>Total</b>	<b>-</b>	<b>7,445</b>	<b>2,620</b>	<b>10,065</b>

**HIERARCHY LEVELS, LIABILITIES**

(€ m)	Liabilities recognised at fair value			
	Level 1	Level 2	Level 3	Total
2015				
Liabilities to banks				
DFV	-	28	120	148
of which debt instruments	-	28	120	148
Liabilities to customers				
DFV	-	316	1,166	1,482
of which debt instruments	-	316	1,166	1,482
Securitised liabilities				
DFV	-	2,385	644	3,029
of which debt instruments	-	2,329	644	2,973
of which contractually linked instruments	-	56	-	56
Negative fair value of hedging derivatives	-	726	-	726
of which interest rate derivatives	-	726	-	726
Trading liabilities (HFT)	-	5,873	885	6,758
of which interest rate derivatives	-	5,047	541	5,588
of which cross-currency interest rate derivatives	-	405	-	405
of which currency derivatives	-	124	40	164
of which credit derivatives	-	1	-	1
of which other derivatives	-	43	16	59
of which structured derivatives	-	253	288	541
Subordinated capital				
DFV	-	87	-	87
of which debt instruments	-	87	-	87
<b>Total</b>	<b>-</b>	<b>9,415</b>	<b>2,815</b>	<b>12,230</b>

Of the financial instruments allocated to level 3, € 2,101 million of assets (previous year: € 2,264 million) and € 2,068 million of liabilities (previous year: € 2,414 million) are in economic hedging relationships (at micro level), so that existing uncertainties and risk positions due to unobservable inputs offset each other at the level hedging relationships (at micro level) involved.



In the period under review financial instruments measured at fair value were transferred from one hierarchy level to another. These

transfers are shown below together with the carrying amounts at the time of transfer for each class of financial instruments.

#### TRANSFER, ASSETS

(€ m) 2016	Transfer to level 1	Transfer from level 1	Transfer to level 2	Transfer from level 2	Transfer to level 3	Transfer from level 3
Trading assets (HfT)	223	-86	87	-223	-	-1
of which debt instruments	223	-86	86	-223	-	-
Financial investments (excl. equity instruments measured at cost)						
AfS	3,770	-1,853	1,864	-3,770	-	-11
of which debt instruments	3,770	-1,853	1,864	-3,770	-	-11
<b>Total</b>	<b>3,993</b>	<b>-1,939</b>	<b>1,951</b>	<b>-3,993</b>	<b>-</b>	<b>-12</b>

#### TRANSFER, ASSETS

(€ m) 2015	Transfer to level 1	Transfer from level 1	Transfer to level 2	Transfer from level 2	Transfer to level 3	Transfer from level 3
Trading assets (HfT)	-	-139	194	-	-	-55
of which debt instruments	-	-139	139	-	-	-
of which interest rate derivatives	-	-	19	-	-	-19
of which structured derivatives	-	-	36	-	-	-36
Financial investments (excl. equity instruments measured at cost)						
AfS	2,414	-1,463	1,463	-2,425	11	-
of which debt instruments	2,414	-1,463	1,463	-2,425	11	-
<b>Total</b>	<b>2,414</b>	<b>-1,602</b>	<b>1,657</b>	<b>-2,425</b>	<b>11</b>	<b>-55</b>

There were no liability transfers in the reporting year.

#### TRANSFER, LIABILITIES

(€ m) 2015	Transfer to level 1	Transfer from level 1	Transfer to level 2	Transfer from level 2	Transfer to level 3	Transfer from level 3
Trading liabilities (HFT)	-	-	48	-	-	-48
of which interest rate derivatives	-	-	9	-	-	-9
of which structured derivatives	-	-	39	-	-	-39
<b>Total</b>	<b>-</b>	<b>-</b>	<b>48</b>	<b>-</b>	<b>-</b>	<b>-48</b>

IFRS 13 and IDW RS HFA 47 specify the principles to be applied in determining the fair value. They also include the guidelines for assigning input factors to the fair value hierarchy levels. HSH Nordbank uses prices obtained from pricing services such as Bloomberg or Reuters to measure interest-bearing securities, for which the OTC market is the relevant market. Average prices determined on the basis of binding offers or transaction-based prices are level 2 input factors within the meaning of IFRS 13 and IDW RS HFA 47. Interest-bearing securities were accordingly transferred from level 1 to level 2 or vice versa in the reporting period – depending on the prices used for measurement. Furthermore, significant transfers from level 3 to level 2 were also made in the reporting period for derivatives within the framework of regularly performed model validations, since it was possible to use observable inputs in the model now.

The following shows the reconciliation for all assets and liabilities recognised at fair value and assigned to level 3 in the fair value hierarchy. The data is presented by class of financial instrument from the start to the end of the period. The table takes into account all movements of assets and liabilities which were or are allocated to level 3 during the reporting period.

Income relating to liability items is shown with a negative sign and expenses are shown without a sign in the reconciliations below.

**RECONCILIATION, ASSETS**

(€ m)	Change in balance affecting income		
	1 January 2016	Realised net income (income statement)	Net income not recognised in profit or loss
<b>2016</b>			
<b>Balance sheet item/category/instrument type</b>			
Loans and advances to banks			
Afs	44	-	-1
of which debt instruments	44	-	-1
Loans and advances to customers			
Afs	104	-	-5
of which debt instruments	104	-	-5
DFV	1,254	47	-
of which debt instruments	1,254	47	-
Credit derivative second loss guarantee (Hft)	663	-464	-
of which credit derivatives	663	-464	-
Trading assets (Hft)	496	-62	-
of which debt instruments	-	-	-
of which interest rate derivatives	150	-55	-
of which currency derivatives	29	-	-
of which other derivatives	17	34	-
of which structured derivatives	300	-41	-
Financial investments (excluding equity instruments measured at cost)			
Afs	159	-	1
of which debt instruments	16	-	-
of which equity and near-equity instruments	143	-	1
DFV	546	24	-
of which debt instruments	544	24	-
of which equity and near-equity instruments	2	-	-
<b>Total</b>	<b>3,266</b>	<b>-455</b>	<b>-5</b>

	Quantitative change in balance			Transfers			Exchange rate changes	31 December 2016	Net income from assets held as at 31 December 2016
	Purchases	Sales	Settlements	From level 3	To level 3	Reclassification			
	-	-	-	-	-	-	-	-	-
	-	-	-	-	-	-	1	44	-
	-	-	-	-	-	-	1	44	-
	-	-	-39	-	-	-	1	61	-
	-	-	-39	-	-	-	1	61	-
	-	-29	-	-	-	-	1	1,273	42
	-	-29	-	-	-	-	1	1,273	42
	-	-	-	-	-	-	-	199	-464
	-	-	-	-	-	-	-	199	-464
	9	-	-	-1	-	-	4	446	-16
	9	-	-	-	-	-	-	9	-
	-	-	-	-	-	-	1	96	-43
	-	-	-	-	-	-	-	29	-
	-	-	-	-1	-	-	1	51	34
	-	-	-	-	-	-	2	261	-7
	-	-120	-5	-11	-	-	5	29	-
	-	-	-5	-11	-	-	-	-	-
	-	-120	-	-	-	-	5	29	-
	-	-1	-28	-	-	-	4	545	26
	-	-	-28	-	-	-	4	544	26
	-	-1	-	-	-	-	-	1	-
	<b>9</b>	<b>-150</b>	<b>-72</b>	<b>-12</b>	<b>-</b>	<b>-</b>	<b>16</b>	<b>2,597</b>	<b>-412</b>

**RECONCILIATION, ASSETS**

(€ m)	Change in balance affecting income		
	1 January 2015	Net income recognised in profit or loss	Net income not recognised in profit or loss
2015			
<b>Balance sheet item/category/instrument type</b>			
Loans and advances to banks			
Afs	45	-	-2
of which debt instruments	45	-	-2
DFV	49	1	-
of which debt instruments	49	1	-
Loans and advances to customers			
Afs	97	-1	2
of which debt instruments	97	-1	2
DFV	1,307	-53	-
of which debt instruments	1,307	-53	-
Credit derivative second loss guarantee (Hft)	3	660	-
of which credit derivatives	3	660	-
Trading assets (Hft)	733	-195	-
of which equity and near-equity instruments	-	-	-
of which interest rate derivatives	272	-108	-
of which currency derivatives	20	9	-
of which other derivatives	45	-28	-
of which structured derivatives	396	-68	-
Financial investments (excluding equity instruments measured at cost)			
Afs	152	-1	-7
of which debt instruments	14	-	1
of which equity and near-equity instruments	138	-1	-8
DFV	910	-10	-
of which debt instruments	558	-19	-
of which contractually linked instruments	336	6	-
of which equity and near-equity instruments	16	3	-
<b>Total</b>	<b>3,296</b>	<b>401</b>	<b>-7</b>



	Quantitative change in balance			Transfers			Exchange rate changes	31 December 2015	Net income from assets held as at 31 December 2015
	Purchases	Sales	Settlements	From level 3	To level 3	Reclassification			
									-
	-	-	-	-	-	-	1	44	-
	-	-	-	-	-	-	1	44	-
	-	-	-50	-	-	-	-	-	-
	-	-	-50	-	-	-	-	-	-
	-	-1	-	-	-	-	7	104	-
	-	-1	-	-	-	-	7	104	-
	-	-5	-	-	-	-	5	1,254	-53
	-	-5	-	-	-	-	5	1,254	-53
	-	-	-	-	-	-	-	663	660
	-	-	-	-	-	-	-	663	660
	7	-7	-	-55	-	-	13	496	102
	7	-7	-	-	-	-	-	-	-
	-	-	-	-19	-	-	5	150	62
	-	-	-	-	-	-	-	29	-9
	-	-	-	-	-	-	-	17	26
	-	-	-	-36	-	-	8	300	23
	-	-12	-	-	11	-	16	159	-
	-	-10	-	-	11	-	-	16	-
	-	-2	-	-	-	-	16	143	-
	-	-39	-300	-	-	-	-15	546	-20
	-	-	-	-	-	-	5	544	-19
	-	-21	-300	-	-	-	-21	-	-
	-	-18	-	-	-	-	1	2	-1
	<b>7</b>	<b>-64</b>	<b>-350</b>	<b>-55</b>	<b>11</b>	<b>-</b>	<b>27</b>	<b>3,266</b>	<b>689</b>

**RECONCILIATION, LIABILITIES**

(€ m)

	Change in balance affecting income		
	1 January 2016	Net income recognised in profit or loss	Net income not recognised in profit or loss
<b>2016</b>			
<b>Balance sheet item/category/instrument type</b>			
Liabilities to banks			
DFV	120	-6	-
of which debt instruments	120	-6	-
Liabilities to customers			
DFV	1,166	-45	-
of which debt instruments	1,166	-45	-
Securitised liabilities			
DFV	644	-39	-
of which debt instruments	644	-39	-
Trading liabilities (HfT)	885	112	-
of which interest rate derivatives	541	42	-
of which currency derivatives	40	-	-
of which other derivatives	16	34	-
of which structured derivatives	288	36	-
<b>Total</b>	<b>2,815</b>	<b>22</b>	<b>-</b>

	Quantitative change in balance				Transfers			Exchange rate differences	31 December 2016	Net income from assets held as at 31 December 2016
	Purchases	Sales	New business	Settlements	From level 3	To level 3	Reclassification			
	5	-	-	-10	-	-	-	-	109	7
	5	-	-	-10	-	-	-	-	109	7
	58	-7	-	-155	-	-	-1	2	1,018	67
	58	-7	-	-155	-	-	-1	2	1,018	67
	-6	-	12	-144	-	-	-	27	494	6
	-6	-	12	-144	-	-	-	27	494	6
	-	-	-	-	-	-	-	2	999	-164
	-	-	-	-	-	-	-	-	583	-48
	-	-	-	-	-	-	-	-	40	-
	-	-	-	-	-	-	-	1	51	-34
	-	-	-	-	-	-	-	1	325	-82
	<b>57</b>	<b>-7</b>	<b>12</b>	<b>-309</b>	<b>-</b>	<b>-</b>	<b>-1</b>	<b>31</b>	<b>2,620</b>	<b>-84</b>

**RECONCILIATION, LIABILITIES**

(€ m)	Change in balance affecting income		
	1 January 2015	Net income recognised in profit or loss	Net income not recognised in profit or loss
2015			
<b>Balance sheet item/category/instrument type</b>			
Liabilities to banks			
DFV	134	-3	-
of which debt instruments	134	-3	-
Liabilities to customers			
DFV	1,872	-69	-
of which debt instruments	1,872	-69	-
Securitised liabilities			
DFV	1,201	-29	-
of which debt instruments	1,201	-29	-
Trading liabilities (Hft)	1,096	-168	-
of which interest rate derivatives	656	-107	-
of which currency derivatives	27	13	-
of which other derivatives	41	-25	-
of which structured derivatives	372	-49	-
Subordinated capital			
DFV	16	-1	-
of which debt instruments	16	-1	-
<b>Total</b>	<b>4,319</b>	<b>-270</b>	<b>-</b>

Quantitative change in balance				Transfers			Reclassification	Exchange rate changes	31 December 2015	Net income from assets held as at 31 December 2015
Purchases	Sales	New business	Settlements	From level 3	To level 3					
4	-15	-	-	-	-	-	-	-	120	2
4	-15	-	-	-	-	-	-	-	120	2
41	-8	-	-665	-	-	-9	4	1,166	32	32
41	-8	-	-665	-	-	-9	4	1,166	32	32
-16	12	34	-613	-	-	-	55	644	18	18
-16	12	34	-613	-	-	-	55	644	18	18
1	-1	-	1	-47	-	-	3	885	154	154
1	-	-	-	-9	-	-	-	541	98	98
-	-	-	-	-	-	-	-	40	-13	-13
-	-	-	-	-	-	-	-	16	25	25
-	-1	-	1	-38	-	-	3	288	44	44
-	-	-	-15	-	-	-	-	-	-	-
-	-	-	-15	-	-	-	-	-	-	-
<b>30</b>	<b>-12</b>	<b>34</b>	<b>-1,292</b>	<b>-47</b>	<b>-</b>	<b>-9</b>	<b>62</b>	<b>2,815</b>	<b>206</b>	<b>206</b>



The following tables show the items containing realised and unrealised gains and losses in the income statement and equity (statement of comprehensive income).

#### NET INCOME ITEMS FROM RECONCILIATION, ASSETS

(€ m)

	Realised/unrealised net income (income statement)				Total
	Net interest income	Net trading income	Net income from financial investments	Hedging effect of credit derivative second loss guarantee	
<b>2016</b>					
<b>Balance sheet item/ category/ instrument type</b>					
Loans and advances to banks					
Afs	-	-	-	-	-
of which debt instruments	-	-	-	-	-
Loans and advances to customers					
Afs	-	-	-	-	-
of which debt instruments	-	-	-	-	-
DFV	-1	48	-	-	47
of which debt instruments	-1	48	-	-	47
Credit derivative second loss guarantee (HfT)	-	-	-	-464	-464
of which credit derivatives	-	-	-	-464	-464
Trading assets (HfT)	-10	-52	-	-	-62
of which interest rate derivatives	-5	-50	-	-	-55
of which other derivatives	-5	39	-	-	34
of which structured derivatives	-	-41	-	-	-41
Financial investments (excluding equity instruments measured at cost)					
Afs	-	-	-	-	-
of which debt instruments	-	-	-	-	-
of which equity and near-equity instruments	-	-	-	-	-
DFV	-1	25	-	-	24
of which debt instruments	-1	25	-	-	24
<b>Total</b>	<b>-12</b>	<b>21</b>	<b>-</b>	<b>-464</b>	<b>-455</b>

	Other net income for the period		Net income from assets still held as at 31 December 2016				Total	Other net income for the period
	Revaluation reserve	Net interest income	Net trading income	Net income from financial investments	Hedging effect of credit derivative second loss guarantee			
	-1	-	-	-	-	-	-1	
	-1	-	-	-	-	-	-1	
	-5	-	-	-	-	-	-7	
	-5	-	-	-	-	-	-7	
	-	-	42	-	-	42	-	
	-	-	42	-	-	42	-	
	-	-	-	-	-464	-464	-	
	-	-	-	-	-464	-464	-	
	-	4	-20	-	-	-16	-	
	-	1	-44	-	-	-43	-	
	-	-	34	-	-	34	-	
	-	3	-10	-	-	-7	-	
	1	-	-	-	-	-	-2	
	-	-	-	-	-	-	-1	
	1	-	-	-	-	-	-1	
	-	-	26	-	-	26	-	
	-	-	26	-	-	26	-	
	<b>-5</b>	<b>4</b>	<b>48</b>	<b>-</b>	<b>-464</b>	<b>-412</b>	<b>-10</b>	

## NET INCOME ITEMS FROM RECONCILIATION, ASSETS

(€ m)

	Realised/unrealised net income (income statement)				Total
	Net interest income	Net trading income	Net income from financial investments	Hedging effect of credit derivative second loss guarantee	
2015					
<b>Balance sheet item/ category/ instrument type</b>					
Loans and advances to banks					
Afs	-	-	-	-	-
of which debt instruments	-	-	-	-	-
DFV	-	1	-	-	1
of which debt instruments	-	1	-	-	1
Loans and advances to customers					
Afs	-1	-	-	-	-1
of which debt instruments	-1	-	-	-	-1
DFV	-	-53	-	-	-53
of which debt instruments	-	-53	-	-	-53
Credit derivative second loss guarantee (HfT)				660	660
of which credit derivatives	-	-	-	660	660
Trading assets (HfT)	7	-202	-	-	-195
of which interest rate derivatives	10	-118	-	-	-108
of which currency derivatives	-	9	-	-	9
of which other derivatives	-	-28	-	-	-28
of which structured derivatives	-3	-65	-	-	-68
Financial investments (excluding equity instruments measured at cost)					
Afs	-	-	-1	-	-1
of which debt instruments	-	-	-	-	-
of which equity and near-equity instruments	-	-	-1	-	-1
DFV	-	-10	-	-	-10
of which debt instruments	-	-19	-	-	-19
of which contractually linked instruments	-	6	-	-	6
of which equity and near-equity instruments	-	3	-	-	3
<b>Total</b>	<b>6</b>	<b>-264</b>	<b>-1</b>	<b>660</b>	<b>401</b>

	Other net income for the period		Net income from assets still held as at 31 December 2015					Other net income for the period
	Revaluation reserve	Net interest income	Net trading income	Net income from financial investments	Hedging effect of credit derivative second loss guarantee	Total		
	-2	-	-	-	-	-	-2	
	-2	-	-	-	-	-	-2	
	-	-	-	-	-	-	-	
	-	-	-	-	-	-	-	
	2	-	-	-	-	-	2	
	2	-	-	-	-	-	2	
	-	-	-53	-	-	-53	-	
	-	-	-53	-	-	-53	-	
	-	-	-	-	660	660	-	
	-	-	-	-	660	660	-	
	-	2	100	-	-	102	-	
	-	3	59	-	-	62	-	
	-	-	-9	-	-	-9	-	
	-	-	26	-	-	26	-	
	-	-1	24	-	-	23	-	
	-7	-	-	-	-	-	-7	
	1	-	-	-	-	-	1	
	-8	-	-	-	-	-	-8	
	-	-	-20	-	-	-20	-	
	-	-	-19	-	-	-19	-	
	-	-	-	-	-	-	-	
	-	-	-1	-	-	-1	-	
	<b>-7</b>	<b>2</b>	<b>27</b>	<b>-</b>	<b>660</b>	<b>689</b>	<b>-7</b>	

## NET INCOME ITEMS FROM RECONCILIATION, LIABILITIES

	Realised/unrealised net income (income statement)				Other net income for the period	Net income from liabilities still held as at 31 December 2016					
	Net interest income	Net trading income	Net income from financial investments	Total		Revaluation reserve	Net interest income	Net trading income	Net income from financial investments	Total	Other net income for the period
<b>2016</b>											
<b>Balance sheet item/ category/ instrument type</b>											
Liabilities to banks											
DFV	-	6	-	6	-	-	7	-	7	-	
of which debt instruments	-	6	-	6	-	-	7	-	7	-	
Liabilities to customers											
DFV	5	40	-	45	-	-1	68	-	67	-	
of which debt instruments	5	40	-	45	-	-1	68	-	67	-	
Securitised liabilities											
DFV	1	38	-	39	-	-	6	-	6	-	
of which debt instruments	1	38	-	39	-	-	6	-	6	-	
Trading liabilities (HfT)	5	-117	-	-112	-	-3	-161	-	-164	-	
of which interest rate derivatives	2	-44	-	-42	-	-	-48	-	-48	-	
of which other derivatives	-	-34	-	-34	-	-	-34	-	-34	-	
of which structured derivatives	3	-39	-	-36	-	-3	-79	-	-82	-	
<b>Total</b>	<b>11</b>	<b>-33</b>	<b>-</b>	<b>-22</b>	<b>-</b>	<b>-4</b>	<b>-80</b>	<b>-</b>	<b>-84</b>	<b>-</b>	



## NET INCOME ITEMS FROM RECONCILIATION, LIABILITIES

(€ m)	Realised/unrealised net income (income statement)				Other net income for the period	Net income from liabilities still held as at 31 December 2015					
	Net interest income	Net trading income	Net income from financial investments	Total		Revaluation reserve	Net interest income	Net trading income	Net income from financial investments	Total	Other net income for the period
2015											
<b>Balance sheet item/ category/ instrument type</b>											
Liabilities to banks											
DFV	-	3	-	3	-	-	2	-	2	-	
of which debt instruments	-	3	-	3	-	-	2	-	2	-	
Liabilities to customers											
DFV	10	59	-	69	-	2	30	-	32	-	
of which debt instruments	10	59	-	69	-	2	30	-	32	-	
Securitised liabilities											
DFV	-35	64	-	29	-	-1	19	-	18	-	
of which debt instruments	-35	64	-	29	-	-1	19	-	18	-	
Trading liabilities (HFT)	3	164	-	167	-	-	154	-	154	-	
of which interest rate derivatives	3	104	-	107	-	-	98	-	98	-	
of which currency derivatives	-	-13	-	-13	-	-	-13	-	-13	-	
of which other derivatives	-	25	-	25	-	-	25	-	25	-	
of which structured derivatives	-	48	-	48	-	-	44	-	44	-	
<b>Total</b>	<b>-22</b>	<b>290</b>	<b>-</b>	<b>268</b>	<b>-</b>	<b>1</b>	<b>205</b>	<b>-</b>	<b>206</b>	<b>-</b>	

### III. Fair value hierarchy for financial instruments not measured at fair value

The following tables show the distribution of fair values by asset and liability class to the individual levels of the fair value hierarchy as defined under IFRS 13 for financial instruments not measured at fair value on the balance sheet.

#### HIERARCHY LEVELS, ASSETS

(€ m)	Assets not recognised at fair value			Total
	Level 1	Level 2	Level 3	
<b>2016</b>				
<b>Balance sheet item/ category/ instrument type</b>				
Cash reserve (LaR)	–	3,373	–	3,373
Loans and advances to banks (LaR)				
of which debt instruments	–	4,070	52	4,122
Payable on demand	–	2,969	–	2,969
Other receivables	–	1,101	52	1,153
Loans and advances to customers (LaR)				
of which debt instruments	–	6,226	36,860	43,086
Retail customers	–	32	953	985
Corporate clients	–	2,379	35,407	37,786
Public authorities	–	3,815	500	4,315
Financial investments (LaR)	40	956	567	1,563
of which debt instruments	40	791	15	846
of which contractually linked instruments	–	165	552	717
Non-current assets held for sale and disposal groups (LaR)	–	7	903	910
of which debt instruments	–	7	903	910
Other assets (LaR)	–	50	–	50
of which debt instruments	–	50	–	50
<b>Total</b>	<b>40</b>	<b>14,682</b>	<b>38,382</b>	<b>53,104</b>

**HIERARCHY LEVELS, ASSETS**

(€ m) 2015	Assets not recognised at fair value			Total
	Level 1	Level 2	Level 3	
<b>Balance sheet item/ category/ instrument type</b>				
Cash reserve (LaR)	-	2,700	-	2,700
Loans and advances to banks (LaR)				
of which debt instruments	-	5,445	67	5,512
Payable on demand	-	3,462	-	3,462
Other receivables	-	1,983	67	2,050
Loans and advances to customers (LaR)				
of which debt instruments	-	6,564	44,947	51,511
Retail customers	-	44	1,332	1,376
Corporate clients	-	2,384	42,911	45,295
Public authorities	-	4,136	704	4,840
Financial investments (LaR)	44	1,605	547	2,196
of which debt instruments	44	1,194	24	1,262
of which contractually linked instruments	-	411	523	934
Non-current assets held for sale and disposal groups (LaR)	-	18	2,661	2,679
of which debt instruments	-	18	2,661	2,679
Other assets (LaR)	-	86	-	86
of which debt instruments	-	86	-	86
<b>Total</b>	<b>44</b>	<b>16,418</b>	<b>48,222</b>	<b>64,684</b>

**HIERARCHY LEVELS, LIABILITIES**

(€ m)	Liabilities not recognised at fair value			
	Level 1	Level 2	Level 3	Total
<b>2016</b>				
Liabilities to banks (LIA)	-	8,155	1,232	9,387
of which debt instruments	-	8,155	1,232	9,387
Liabilities to customers (LIA)	-	39,233	658	39,891
of which debt instruments	-	39,233	658	39,891
Securitised liabilities (LIA)	-	14,138	-	14,138
of which debt instruments	-	13,144	-	13,144
of which contractually linked instruments	-	994	-	994
Liabilities from disposal groups (LIA)	-	-	2	2
of which debt instruments	-	-	2	2
Subordinated capital (LIA)	-	2,862	86	2,948
of which debt instruments	-	2,862	86	2,948
Other liabilities (LIA)	-	812	-	812
of which debt instruments	-	812	-	812
<b>Total</b>	<b>-</b>	<b>65,200</b>	<b>1,978</b>	<b>67,178</b>

**HIERARCHY LEVELS, LIABILITIES**

(€ m)	Liabilities not recognised at fair value			
	Level 1	Level 2	Level 3	Total
<b>2015</b>				
Liabilities to banks (LIA)	-	12,411	1,865	14,276
of which debt instruments	-	12,411	1,667	14,078
of which contractually linked instruments	-	-	198	198
Liabilities to customers (LIA)	-	43,422	968	44,390
of which debt instruments	-	43,422	968	44,390
Securitised liabilities (LIA)	-	15,604	-	15,604
of which debt instruments	-	14,406	-	14,406
of which contractually linked instruments	-	1,198	-	1,198
Liabilities from disposal groups (LIA)	-	-	1	1
of which debt instruments	-	-	1	1
Subordinated capital (LIA)	-	2,160	707	2,867
of which debt instruments	-	2,160	707	2,867
Other liabilities (LIA)	-	950	-	950
of which debt instruments	-	950	-	950
<b>Total</b>	<b>-</b>	<b>74,547</b>	<b>3,541</b>	<b>78,088</b>

#### IV. Information on significant unobservable inputs

##### Quantitative information on significant unobservable inputs

The following overview contains quantitative information on significant unobservable inputs.

##### FAIR VALUE

(€ m)			Assets	Liabilities	Measurement procedures	Significant unobservable inputs (level 3)	Margin	(Weighted) average margin
<b>2016</b>								
<b>Loans and advances to banks</b>	AfS	Debt instruments	44	–	DCF method	Spread (bps)	54	54
<b>Loans and advances to customers</b>	AfS	Debt instruments	61	–	DCF method	Spread (bps)	700	700
	DFV	Debt instruments	1,273	–	Option pricing model	Price		
						Mean reversion	0% – 10%	2%
						Interest rate FX correlation	–32% – 16%	–16%
						Price	37 – 87	73
<b>Credit derivative under the second loss guarantee</b>	HfT	Credit derivatives	199	–	DCF method	Expected cash flow	–	–
<b>Trading assets/trading liabilities</b>	HfT	Debt instruments	9	–	Price	Price	100	100
		Interest rate derivatives	96	583	Option pricing model	Mean reversion	0% – 10%	2%
						Interest rate volatility	19% – 77%	31%
						Interest rate correlation	–51% – 100%	23%
						Interest rate FX correlation	–32% – 16%	–16%
		Currency derivatives	29	40	Option pricing model	FX correlation	35% – 66%	49%
		Other derivatives	51	51	Option pricing model	Shares FX correlation	–30% – 44%	–1%
		Structured derivatives	261	325	Option pricing model	Mean reversion	0% – 10%	2%
						Interest rate volatility	19% – 77%	31%
						Interest rate correlation	–51% – 100%	23%
						Interest rate FX correlation	–32% – 16%	–16%
						FX correlation	35% – 66%	49%



## FAIR VALUE

(€ m)			Assets	Liabilities	Measurement procedures	Significant unobservable inputs (level 3)	Margin	(Weighted) average margin
<b>2016</b>								
<b>Financial investments</b>	AFS	Equity and near-equity instruments	29	–	Price	Price	1 – 14,000	279
	DFV	Debt instruments	544	–	Option pricing model	Mean reversion	0% – 10%	2%
						Interest rate volatility	19% – 77%	31%
					Price	Price	7	7
<b>Liabilities to banks</b>	DFV	Equity and near-equity instruments	1	–	Price	Price	1 – 100	94
		Debt instruments	–	109	Option pricing model	Interest rate volatility	19% – 77%	31%
						Interest rate FX correlation	–32% – 16%	–16%
<b>Liabilities to customers</b>	DFV	Debt instruments	–	1,018	Option pricing model	Mean reversion	0% – 10%	2%
						Interest rate volatility	19% – 77%	31%
						Interest rate correlation	–51% – 100%	23%
						Interest rate FX correlation	–32% – 16%	–16%
<b>Securitised liabilities</b>	DFV	Debt instruments	–	494	Option pricing model	Mean reversion	0% – 10%	2%
						Interest rate volatility	19% – 77%	31%
						FX correlation	35% – 66%	49%
						Shares FX correlation	–30% – 44%	–1%
						Price	Price	62
			<b>2,597</b>	<b>2,620</b>				

## FAIR VALUE

(€ m)			Assets	Liabilities	Measurement procedures	Significant unobservable inputs (level 3)	Margin	(Weighted) average margin
2015								
<b>Loans and advances to banks</b>	AFS	Debt instruments	44	–	DCF method	Spread (bps)	84	84
<b>Loans and advances to customers</b>	AFS	Debt instruments	104	–	DCF method Price	Spread (bps) Price	27 78	27 78
	DFV	Debt instruments	1,254	–	Option pricing model	Mean reversion	0% – 10%	2%
						Interest rate volatilities	15% – 73%	26%
						Interest rate FX correlation	– 85% – 33%	– 12%
					Price	Price	80 – 100	94
<b>Credit derivative under the second loss guarantee</b>	HFT	Credit derivatives	663	–	DCF method	Expected cash flow	–	–
<b>Trading assets/trading liabilities</b>	HFT	Interest rate derivatives	150	541	Option pricing model	Mean reversion	0% – 10%	2%
						Interest rate volatility	15% – 73%	26%
						Interest rate correlation	– 49% to 99%	25%
						Interest rate FX correlation	– 85% – 33%	– 12%
		Currency derivatives	29	40	Option pricing model	FX correlation	24% – 56%	42%
		Other derivatives	17	16	Option pricing model	Securities FX correlation	– 47% – 16%	– 42%
		Structured derivatives	300	288	Option pricing model	Mean reversion	0% – 10%	2%
						Interest rate volatilities	15% – 73%	26%
						Interest rate correlation	– 49% – 99%	25%
						Interest rate FX correlation	– 85% – 33%	– 12%
						FX correlation	24% – 56%	42%
						Shares FX correlation	– 47% – 16%	– 42%

## FAIR VALUE

(€ m)			Assets	Liabilities	Measurement procedures	Significant unobservable inputs (level 3)	Margin	(Weighted) average margin
2015								
<b>Financial investments</b>	AfS	Debt instruments	16	–	Price	Price	86 – 106	101
		Equity and near-equity instruments	143	–	Price	Price	1 – 14,811	148
	DFV	Debt instruments	544	–	Option pricing model	Mean reversion	0% – 10%	2%
						Interest rate volatilities	15% – 73%	26%
					Price	Price	1	1
		Equity and near-equity instruments	2	–	Price	Price	1 – 100	94
<b>Liabilities to banks</b>	DFV	Debt instruments	–	120	Option pricing model	Interest rate volatilities	15% – 73%	26%
						Interest rate FX correlation	–85% – 33%	–12%
<b>Liabilities to customers</b>	DFV	Debt instruments	–	1,166	Option pricing model	Mean reversion	0% – 10%	2%
						Interest rate volatilities	15% – 73%	26%
						Interest rate correlation	–49% – 99%	25%
						Interest rate FX correlation	–85% – 33%	–12%
					Price	Price	80 – 96	91
<b>Securitised liabilities</b>	DFV	Debt instruments	–	644	Option pricing model	Mean reversion	0% – 10%	2%
						Interest rate volatilities	15% – 73%	26%
						FX correlation	24% – 56%	42%
						Shares FX correlation	–47% – 16%	–42%
					Price	Price	100	100
			<b>3,266</b>	<b>2,815</b>				

The correlation and volatility ranges shown for derivatives cover derivatives with different types of underlying, tenors and exercise prices.

The overview also includes financial instruments, whose change in value resulting from inputs unobservable in the market does not give rise to any P&L effect due to economic hedging relationships (at the micro level). Changes in value attributable to the respective relevant inputs are offset for these financial instruments by the changes in value of the hedging derivatives.

**Sensitivities of fair values in relation to unobservable inputs**

The following describes how the fair values of financial instruments can change as a result of fluctuations in significant unobservable inputs.

**Correlation**

Correlation can represent an important unobservable input for the measurement of derivatives. It is a measure of the degree to which two reference values move in relation to each other. Correlation is an important input for the model-based determination of the fair value of derivatives with more than one underlying. Financial instruments of this type include, for example, derivatives with several currencies (“FX basket”) or several shares as the underlyings (“equity basket” derivatives). Currency correlations describe the relationship between changes in value of several currencies. Share correlations express the relationship between yields on different shares. A high degree of correlation means that there is a high relationship between the changes in value of the respective underlyings.

Depending on the type of derivative changes in correlation can have a positive or negative effect on the fair value. For example, in the case of a “best of two” derivative, an increase in the correlation between two underlyings results in a decrease of the fair value of the derivative from the perspective of the purchaser.

**Volatility**

Volatility can also represent an important unobservable input for the measurement of options. It expresses how strongly the value of the underlying fluctuates over time. The amount of volatility depends on the type of the underlying, its tenor and the exercise price agreed for the option.

The fair value of options typically increases if volatility increases. The sensitivity of the fair value of options to changes in volatility can vary considerably. For example, the sensitivity of the fair value to changes in volatility is comparatively high, if the price of the underlying is close to the agreed exercise price (“at-the-money”). By contrast, sensitivity to changes in volatility is lower, if the price of the underlying is far from the exercise price (“far out-of-the-money” or “far in-the-money”).

**Price**

Prices can represent an important unobservable input for the measurement of financial instruments. These prices represent pricing information of third parties within the meaning of IFRS 13.93(d) sentence 4, whereby the Bank does not produce any quantitative, unobservable input factors for measuring the fair value of the respective financial instrument. More detailed quantitative information on these input factors is not required therefore. The fair value increases, if the price increases, and it falls, if the price declines.

**Reciprocal effects between unobservable inputs**

Reciprocal effects between unobservable inputs can exist in principle. If several unobservable inputs are used in determining fair value, the range of the possible characteristics for another unobservable input can be restricted or increased by the characteristic used for one of the relevant unobservable inputs.

**Effects of unobservable inputs**

If the measurement of a financial instrument is based partly on unobservable inputs, the fair value determined is the best estimated value in accordance with a discretionary decision made by the Bank. However, it remains subjective in that there may be alternative input selection options that cannot be refuted by observable market data. For many of the financial instruments included (such as derivatives) the unobservable inputs only represent a subset of the total inputs required for the measurement. The remaining inputs are observable inputs.

An alternative choice of inputs for the unobservable inputs depending on the limits of a possible range would have had the effect on the fair value of the financial instruments in question as set out in the following table. Advantageous and disadvantageous changes to fair value arise as a result of the recalculation of fair values based on possible alternative values to the relevant unobservable inputs. In doing so, interest rate volatilities were changed by +/-5%, all correlations by +/-20% (capped at +/-100%) and mean reversion by +/-0.5%. Furthermore, price parameters and spreads were also changed by +/-2% and +/-50 bp, respectively.

a) Financial instruments for which there are no economic hedging relationships in place (at the micro level)

### FAIR VALUE CHANGES LEVEL 3

(€ m)			2016		2015	
			advanta- geous	disadvanta- geous	advantageous	dis- advantageous
<b>Loans and advances to customers</b>	AfS	Debt instruments	3	3	–	–
<b>Credit derivative under the second loss guarantee</b>	HfT	Credit derivatives	9	10	25	23
<b>Trading assets/trading liabilities</b>	HfT	Interest rate derivatives	1	1	2	2
		Other derivatives	1	1	1	1
		Structured derivatives	2	2	1	1
<b>Financial investments</b>	AfS	Equity and near-equity instruments	1	1	3	3
			<b>17</b>	<b>18</b>	<b>32</b>	<b>30</b>
		thereof measured in profit or loss	13	14	29	27
		thereof not measured in profit or loss	4	4	3	3

There are no hedging derivatives in place for the financial instruments included in the above table that fully hedge the risk relating to changes in fair value caused by changes in unobservable inputs. However, there may be hedging derivatives in place that approximately hedge the changes in value.



b) Financial instruments for which there are economic hedging relationships in place (at the micro level)

### FAIR VALUE CHANGES LEVEL 3

(€ m)			2016		2015	
			advantageous	disadvantageous	advantageous	disadvantageous
<b>Loans and advances to customers</b>	DFV	Debt instruments	2	2	2	2
<b>Trading assets/trading liabilities</b>	HfT	Interest rate derivatives	1	1	1	1
		Structured derivatives	2	2	4	4
<b>Liabilities to banks</b>	DFV	Debt instruments	1	1	1	1
<b>Liabilities to customers</b>	DFV	Debt instruments	1	1	2	2
<b>Securitised liabilities</b>	DFV	Debt instruments	1	1	2	2
			<b>8</b>	<b>8</b>	<b>12</b>	<b>12</b>
thereof measured in profit or loss			8	8	12	12
thereof not measured in profit or loss			-	-	-	-

There are hedging derivatives in place for the financial instruments included in the above table that hedge the risk relating to changes in fair value caused by changes in unobservable inputs. The changes in value shown would not be reflected in the income statement as they are offset changes in fair value of the hedging derivatives.

### V. Day One Profit and Loss

The day one profit and loss reserve developed as follows:

(€ m)	2016	2015
Holdings as at 1 January	22	24
Additions not recognised in profit or loss	2	3
Reversals recognised in profit or loss	11	5
<b>Holdings as at 31 December</b>	<b>13</b>	<b>22</b>

The day one profit and loss reserve is solely attributable to financial instruments classified as HfT.

### VI. Equity instruments measured at cost

For equity instruments which are not listed and whose fair value cannot be determined reliably by other methods, subsequent meas-

urement takes place at cost in accordance with IAS 39.46 (c) in conjunction with IAS 39.A81. These are primarily equity instruments of unlisted companies for which no active market exists and reliable estimates of the parameters determining market value are not possible because future expectations are difficult to forecast.

The portfolio of shares and other non-interest bearing securities measured at cost amounts to € 125 million (previous year: € 137 million). Equity capital instruments accounted for at cost that relate to interests in affiliated companies and equity holdings in non-affiliated companies amount to € 78 million (previous year: € 75 million). There are currently no concrete intentions to dispose of these equity instruments.

Financial instruments accounted for at cost are disclosed as Financial investments under Assets measured at fair value (AfS).

In the year under review, equity instruments classified as AfS not measured at fair value with a carrying amount of € 26 million (previous year € 42 million) were disposed of. This resulted in a profit of € 0 million (previous year: € 6 million).

## 56. OFFSETTING OF FINANCIAL INSTRUMENTS

Financial assets and financial liabilities are netted and disclosed as a net amount on the balance sheet, if there is a legal entitlement to do so at the current point in time and there is the intention to settle the claims on a net basis or to settle the associated liability at the time the asset concerned is realised.

Set out below are the financial instruments on the balance sheet that were netted as at the reporting date as well as financial instruments, which are subject to a legally enforceable global netting agreement, irrespective of whether the financial instruments concerned are actually netted on the face of the balance sheet. ISDA master agreements and the Master Agreement for Financial Derivative Transactions (DRV) are the master agreements customarily used by HSH Nordbank for OTC transactions. These only provide for the netting of reciprocal claims and obligations in the event of the termination of all individual transactions under a master agreement that is

based on specific events and therefore do not permit netting of the assets and liabilities on the balance sheet. HSH Nordbank has entered into clearing agreements with brokers for certain OTC derivatives enabling the Bank to access central counterparties (clearing houses). The importance of these transactions for HSH Nordbank will probably increase in future with the gradual build up of this portfolio of transactions covered by these agreements. The contractual arrangements for these transactions include a legal right to set off financial assets and financial liabilities that can be enforced legally at any time and thereby result in the offsetting of positive and negative fair values of derivative financial instruments and of collateral provided and received in accordance with IAS 32.42.

The fair value of the collateral received or provided in this connection is also given in this table. This includes cash collateral as well as financial instruments received or provided as collateral.

### FINANCIAL ASSETS

(€ m)	Gross carrying amount	Gross carrying amount from netting	Net amount	Gross amount, netting criteria not met	Collateral received	Net amount after collateral
<b>2016</b>						
Loans and advances to banks	1	–	1	–	–	1
Loans and advances to customers	109	106	3	–	–	3
Derivatives	5,574	741	4,833	3,280	333	1,220

The netted amounts disclosed under Loans and advances to banks and Loans and advances to customers relate to genuine repo transactions.

Of the net amount of derivatives disclosed on the balance sheet positive market values of hedging derivatives account for € 506 million and trading assets for € 4,327 million.

### FINANCIAL LIABILITIES

(€ m)	Gross carrying amount	Gross carrying amount from netting	Net amount	Gross amount, netting criteria not met	Collateral provided	Net amount after collateral
<b>2016</b>						
Liabilities to banks	1,216	28	1,188	–	812	376
Liabilities to customers	338	70	268	–	25	243
Derivatives	7,005	749	6,256	3,280	2,816	160

The netted amounts disclosed under liabilities to banks and liabilities to customers relate to genuine repo transactions.

Of the net amount of derivatives disclosed on the balance sheet negative market values of hedging derivatives account for € 290 million and Trading liabilities for € 5,966 million.

**FINANCIAL ASSETS**

(€ m)	Gross carrying amount	Gross carrying amount from netting	Net amount	Gross amount, netting criteria not met	Collateral received	Net amount after collateral
2015						
Loans and advances to banks	5	–	5	–	–	5
Loans and advances to customers	40	31	9	–	–	9
Derivatives	6,050	457	5,593	3,609	384	1,600

The netted amounts disclosed under Loans and advances to banks and Loans and advances to customers exclusively concern current accounts.

Of the net amount of derivatives disclosed on the balance sheet positive fair value of hedging derivatives accounts for € 775 million and Trading assets for € 4,818 million.

**FINANCIAL LIABILITIES**

(€ m)	Gross carrying amount	Gross carrying amount from netting	Net amount	Gross amount, netting criteria not met	Collateral provided	Net amount after collateral
2015						
Liabilities to banks	1,585	45	1,540	–	1,404	136
Liabilities to customers	449	35	414	–	207	207
Derivatives	7,869	408	7,461	3,609	3,541	311

The netted amounts disclosed under Liabilities to banks and Liabilities to customers exclusively resulted from current account transactions.

Of the net amount of derivatives disclosed on the balance sheet negative market values of hedging derivatives account for € 725 million and Trading liabilities for € 6,736 million.

## 57. FINANCIAL TRANSACTIONS ENTERED INTO WITH SELECTED STATES

The following tables contain overviews of HSH Nordbank's exposure in European states where an increased economic risk is assumed. They present the risk directly attributable to the listed countries.

### ASSETS CLASSIFIED AS LAR

(€ m)	Gross carrying amount		Specific loan loss provisions		Fair value	
	2016	2015	2016	2015	2016	2015
<b>Portugal</b>	<b>193</b>	<b>194</b>	<b>7</b>	<b>6</b>	<b>190</b>	<b>203</b>
Public sector	171	169	-	-	176	186
Corporates/Other	22	25	7	6	14	17
<b>Italy</b>	<b>595</b>	<b>616</b>	<b>100</b>	<b>93</b>	<b>480</b>	<b>519</b>
Public sector	23	26	-	-	24	28
Banks	-	8	-	-	-	8
Corporates/Other	572	582	100	93	456	483
<b>Greece</b>	<b>1,442</b>	<b>1,094</b>	<b>268</b>	<b>88</b>	<b>1,100</b>	<b>1,007</b>
Corporates/Other	1,442	1,094	268	88	1,100	1,007
<b>Russia</b>	<b>44</b>	<b>94</b>	<b>-</b>	<b>17</b>	<b>44</b>	<b>78</b>
Corporates/Other	44	94	-	17	44	78
<b>Spain</b>	<b>1,244</b>	<b>1,297</b>	<b>108</b>	<b>87</b>	<b>1,152</b>	<b>1,214</b>
Public sector	151	156	-	-	159	165
Corporates/Other	1,093	1,141	108	87	993	1,049
<b>Cyprus</b>	<b>1,144</b>	<b>1,392</b>	<b>524</b>	<b>447</b>	<b>519</b>	<b>943</b>
Corporates/Other	1,144	1,392	524	447	519	943
<b>Croatia</b>	<b>99</b>	<b>104</b>	<b>-</b>	<b>-</b>	<b>101</b>	<b>103</b>
Corporates/Other	99	104	-	-	101	103
<b>Turkey</b>	<b>389</b>	<b>479</b>	<b>7</b>	<b>133</b>	<b>344</b>	<b>343</b>
Banks	10	10	-	-	10	10
Corporates/Other	379	469	7	133	334	333
<b>Total</b>	<b>5,150</b>	<b>5,270</b>	<b>1,014</b>	<b>871</b>	<b>3,930</b>	<b>4,410</b>

**FINANCIAL TRANSACTIONS ALLOCATED TO THE HOLDING CATEGORY**

(€ m)	HfT		Hedge		DFV		AfS	
	2016	2015	2016	2015	2016	2015	2016	2015
<b>Portugal</b>	-	-	-	-	<b>49</b>	<b>54</b>	-	<b>4</b>
Public sector	-	-	-	-	49	54	-	-
Banks	-	-	-	-	-	-	-	4
<b>Italy</b>	<b>6</b>	<b>17</b>	-	-	<b>402</b>	<b>418</b>	-	-
Public sector	-	-	-	-	402	418	-	-
Corporates/Other	6	17	-	-	-	-	-	-
<b>Greece</b>	<b>9</b>	<b>10</b>	-	-	-	-	-	-
Corporates/Other	9	10	-	-	-	-	-	-
<b>Russia</b>	<b>31</b>	<b>3</b>	-	-	-	-	-	-
Banks	2	3	-	-	-	-	-	-
Corporates/Other	29	-	-	-	-	-	-	-
<b>Spain</b>	<b>75</b>	<b>47</b>	<b>10</b>	<b>9</b>	-	-	-	<b>59</b>
Banks	37	11	10	9	-	-	-	-
Corporates/Other	38	36	-	-	-	-	-	59
<b>Cyprus</b>	<b>1</b>	<b>1</b>	-	-	-	-	-	-
Corporates/Other	1	1	-	-	-	-	-	-
<b>Croatia</b>	<b>1</b>	<b>1</b>	-	-	-	-	-	-
Corporates/Other	1	1	-	-	-	-	-	-
<b>Turkey</b>	-	<b>4</b>	-	-	-	-	-	-
Corporates/Other	-	4	-	-	-	-	-	-
<b>Total</b>	<b>123</b>	<b>83</b>	<b>10</b>	<b>9</b>	<b>451</b>	<b>472</b>	-	<b>63</b>

The cumulative measurement result recognised directly in equity for financial instruments held in the AfS category amounted to € 0 million for the selected countries (previous year: € - 3 million). A cumulative measurement result did not arise, as in the previous year.



## 58. CREDIT RISK ANALYSIS OF FINANCIAL ASSETS

### I. Credit quality of financial instruments which are neither impaired nor overdue

The table below gives information on the credit quality of financial instruments which were neither impaired nor overdue as of the reporting date. The table provides a breakdown of the financial instruments by category and rating class of the respective counterparty.

#### CREDIT QUALITY

(€ m)	1(AAA) to 1(AA+)		1(AA) to 1(A-)		2 to 5		6 to 9	
	2016	2015	2016	2015	2016	2015	2016	2015
Held for Trading (HfT)								
Trading assets	778	2,133	870	2,032	2,818	1,887	418	681
Credit derivative under the second loss guarantee	199	663	-	-	-	-	-	-
Designated at Fair Value (DFV)								
Loans and advances to customers	1,234	1,186	-	-	-	-	-	-
Financial investments	127	154	603	799	822	636	-	-
Available for Sale (AfS)								
Cash reserve	118	694	-	-	-	-	-	-
Loans and advances to banks	43	43	-	-	41	43	-	-
Loans and advances to customers	-	-	-	-	-	-	-	38
Financial investments	9,194	9,237	2,211	2,560	779	747	33	273
Non-current assets held for sale and disposal groups	15	-	3	-	1	-	-	-
Loans and Receivables (LaR)								
Cash reserve	3,373	2,700	-	-	-	-	-	-
Loans and advances to banks	1,463	1,819	1,440	2,084	1,167	1,553	27	39
Loans and advances to customers	4,227	4,399	4,646	4,434	12,459	14,171	10,533	14,645
Financial investments	527	535	251	399	149	44	350	304
Non-current assets held for sale and disposal groups	-	-	7	-	9	85	1	21
Other assets	-	-	-	-	-	-	-	-
No IAS 39 category								
Positive fair value of hedging derivatives	202	248	148	335	151	181	7	13
Receivables under finance leases	11	11	12	11	33	35	27	36
Value adjustments from the portfolio fair value hedge	160	129	118	175	120	94	5	7
<b>Total</b>	<b>21,671</b>	<b>23,951</b>	<b>10,309</b>	<b>12,829</b>	<b>18,549</b>	<b>19,476</b>	<b>11,401</b>	<b>16,057</b>

**CREDIT QUALITY**

(€ m)	10 to 12		13 to 15		16 to 18	
	2016	2015	2016	2015	2016	2015
Held for Trading (HfT)						
Trading assets	27	45	250	310	272	268
Credit derivative under the second loss guarantee	-	-	-	-	-	-
Designated at Fair Value (DFV)						
Loans and advances to customers	49	-	16	75	22	47
Financial investments	-	-	1	1	1	1
Available for Sale (AFS)						
Cash reserve	-	-	-	-	-	-
Loans and advances to banks	-	-	-	-	-	-
Loans and advances to customers	-	-	-	66	-	-
Financial investments	5	2	127	9	-	9
Loans and Receivables (LoR)						
Cash reserve	-	-	-	-	-	-
Loans and advances to banks	11	-	-	-	-	-
Loans and advances to customers	1,934	2,956	3,184	2,592	680	-
Financial investments	-	18	49	173	36	148
Non-current assets held for sale and disposal groups	7	62	6	6	254	-
Other assets	-	86	50	-	-	-
No IAS 39 category						
Positive fair values of hedging derivatives	-	6	-	-	-	-
Receivables under finance leases	5	7	8	6	2	-
Value adjustments from the portfolio fair value hedge	-	3	-	-	-	-
<b>Total</b>	<b>2,038</b>	<b>3,185</b>	<b>3,691</b>	<b>3,238</b>	<b>1,267</b>	<b>473</b>

## II. Carrying amounts of overdue but unimpaired financial assets

The table below shows the financial assets which were overdue but unimpaired as of the reporting date. The assets are broken down by category. Categories not shown have no overdue assets.

### CARRYING AMOUNTS OF OVERDUE BUT UNIMPAIRED FINANCIAL ASSETS

(€ m)	Overdue < 3 months		Overdue 3 to 6 months		Overdue 6 to 12 months		Overdue > 12 months	
	2016	2015	2016	2015	2016	2015	2016	2015
Loans and Receivables (LaR)								
Loans and advances to customers	859	464	643	86	185	113	395	353
of which hedged by the second loss guarantee	631	233	498	73	99	74	338	293
<b>Total</b>	<b>859</b>	<b>464</b>	<b>643</b>	<b>86</b>	<b>185</b>	<b>113</b>	<b>395</b>	<b>353</b>

Payments of € 4 million (previous year: € 33 million) on transactions with a carrying amount volume of € 96 million (previous year: € 231 million) were received up to ten days after the reporting date of 31 December 2016. Payments are regarded as being in arrears when they are one day overdue.

The overdue, unimpaired credit portfolio is offset by collateral in the form of real estate liens, ship mortgages, aircraft mortgages, assignments and transfers of ownership by way of security. The transfers by way of security mainly comprise physical assets.

### III. Impaired financial assets

The table below shows all impaired financial assets as of the reporting date. The financial assets are broken down by category.

#### IMPAIRED FINANCIAL ASSETS

(€ m)	Gross carrying amount of impaired financial assets		Impairment		Carrying amount of financial assets after impairment	
	2016	2015	2016	2015	2016	2015
Loans and Receivables (LaR)						
Loans and advances to banks	–	14	–	14	–	–
Loans and advances to customers	9,685	10,844	6,103	5,199	3,582	5,645
Financial investments <sup>1)</sup>	302	877	166	360	136	517
Non-current assets held for sale and disposal groups	856	4,908	233	2,402	623	2,506
Available for Sale (AfS)						
Loans and advances to customers	90	–	29	–	61	–
Financial investments <sup>1)</sup>	236	216	144	146	92	70
<b>Total</b>	<b>11,169</b>	<b>16,859</b>	<b>6,675</b>	<b>8,121</b>	<b>4,494</b>	<b>8,738</b>

<sup>1)</sup> Financial investments classified as LaR and AfS are shown net in the statement of financial position, i.e., at their carrying amounts less impairment.

The impaired credit portfolio is secured with collateral in the form of real estate liens, ship mortgages, aircraft mortgages, assignments and transfers of ownership by way of security. The transfers by way of security mainly comprise physical assets.

€ 9,634 million (previous year: € 15,354 million) of the total carrying amount of impaired financial assets of € 11,169 million (previous year: € 16,859 million) is hedged by the second loss guarantee, of which € 8,637 million is attributable to Loans and advances to customers (previous year: € 10,016 million), € 163 million to Financial investments in the LaR and AfS holding categories (previous year: € 631 million) as well as € 834 million to Non-current assets held for sale and disposal groups (previous year: € 4,707 million).

Further information regarding the guarantees received can be found in Note 3.

### IV. Credit risk exposure

With the exception of Loans and advances to banks and customers, credit risk exposure in accordance with IFRS 7.36 (a) as at the reporting date corresponds to the carrying amount of financial assets as presented in Note 52 as well as off-balance sheet liabilities as presented in Note 61.

In the case of Loans and advances to banks and customers, the credit risk exposure corresponds to the carrying amount after loan loss provisions as presented in Note 27. The maximum default risk of the

loans and advances designated at fair value (DFV) is not reduced by associated credit derivatives.

Collateral and other risk-reducing agreements are not reflected in these amounts.

### V. Collateral received

#### A) Collateral values of financial assets reducing default risk

The following information quantifies the extent to which the collateral retained and other loan collateralisation reduce the maximum default risk for financial instruments. The amount of risk reduction from the value of each form of collateral is indicated for each class of financial instruments.

The value of collateral received is determined directly on the basis of the objective market value, provided that such a value can be determined. The reliability of the collateral value is ensured by the fact that it is recognised as risk-reducing only up to the level of the applicable collateral-specific recovery ratio.

The following table shows the respective carrying amount for each class of financial instrument as well as the collateral value that reduces default risk.

**FINANCIAL ASSETS AND ASSOCIATED COLLATERAL**

(€ m)	Value of collateral received			
	Carrying amount	Real estate and registered liens	Sureties and guarantees	Other collateral
<b>2016</b>				
HfT				
Trading assets	5,433	398	23	516
Credit derivative under the second loss guarantee	199	–	–	–
DFV				
Loans and advances to customers	1,321	–	–	–
Financial investments	1,554	–	–	–
AFS				
Cash reserve	118	–	–	–
Loans and advances to banks	84	–	–	–
Loans and advances to customers	61	–	–	–
Financial investments	12,441	–	–	–
Non-current assets held for sale and disposal groups	19	–	–	–
LaR				
Cash reserve	3,373	–	–	–
Loans and advances to banks	4,108	10	27	34
Loans and advances to customers	49,430	16,301	742	1,659
Financial investments	1,498	–	–	–
Non-current assets held for sale and disposal groups	1,140	465	78	8
Other assets	50	1	–	1
No IAS 39 category				
Positive fair values of hedging derivatives	508	–	–	–
Value adjustments from the portfolio fair value hedge	403	–	–	–
Receivables under finance leases	98	–	–	–
Contingent liabilities	2,189	145	21	136
Irrevocable loan commitments	6,654	602	65	197
<b>Total assets</b>	<b>90,681</b>	<b>17,922</b>	<b>956</b>	<b>2,551</b>



**FINANCIAL ASSETS AND ASSOCIATED COLLATERAL**

(€ m)	Value of collateral received			
	Carrying amount	Real estate and registered liens	Sureties and guarantees	Other collateral
2015				
HfT				
Trading assets	7,356	470	47	560
Credit derivative under the second loss guarantee	663	-	-	-
DFV				
Loans and advances to customers	1,308	-	-	-
Financial investments	1,591	-	-	-
AfS				
Cash reserve	694	-	-	-
Loans and advances to banks	86	-	-	-
Loans and advances to customers	104	-	36	-
Financial investments	12,907	-	-	-
LaR				
Cash reserve	2,700	-	-	-
Loans and advances to banks	5,509	11	60	73
Loans and advances to customers	55,057	22,169	875	1,969
Financial investments	2,138	-	-	-
Non-current assets held for sale and disposal groups	5,081	1,917	2	1
Other assets	86	-	-	1
No IAS 39 category				
Positive fair values of hedging derivatives	783	-	-	-
Value adjustments from the portfolio fair value hedge	408	-	-	-
Receivables under finance leases	106	-	-	-
Contingent liabilities	2,833	311	8	126
Irrevocable loan commitments	6,370	754	64	217
<b>Total assets</b>	<b>105,780</b>	<b>25,632</b>	<b>1,092</b>	<b>2,947</b>

Above and beyond the collateral values shown in the table above, a sub-portfolio is secured by means of the guarantee facility provided by the Federal State of Schleswig-Holstein and the Free and Hanseatic City of Hamburg to HSH Nordbank AG and certain subsidiaries via HSH Finanzfonds AöR at the beginning of the realignment of the Bank (see Note 3). The same applies with regard to the protection provided by a synthetic securitisation transaction via the SPV "Horizon 2016 S.A." as part of a guarantee granted in 2016. Ultimately, reference is made to Note 3 II.

**B) Thereof collateral received for which there are no restrictions on disposal or realisation even if there is no default in payment**

HSH Nordbank has received collateral from counterparties with a total fair value of € 415 million (previous year: € 597 million). The collateral received is split up as follows: € 353 million (previous year: € 495 million) relate to OTC derivatives and structured transactions. The Group received collateral in the amount of € 62 million (previous year: € 102 million) within the framework of genuine repo transac-

tions where it acted as the lender. This includes cash collateral in the amount of € 320 million (previous year: € 448 million). Of the collateral received, an amount of € 34 million (previous year: € 50 million) was resold or pledged. There are no restrictions on disposal or realisation, HSH Nordbank is obliged to return all collateral resold or pledged to the guarantor without exception.

HSH Nordbank carries out securities repurchase and lending transactions as well as tri-party repo transactions under standard master agreements with selected counterparties. The same conditions and collateralisation methods apply as for collateral transferred and received.

**C) Other collateral received**

In the reporting period no assets were recognised from the realisation of collateral (previous year: € 0 million).

For information on the collateral transferred please refer to Note 64.

For further information regarding the guarantees received (incl. the cash collateral received in connection with the synthetic securitisation transaction), reference is made to the comments in Note 3.

**59. RESTRUCTURED OR MODIFIED LOANS**

The following table shows the gross carrying amounts of loans and loan commitments that have been restructured or whose contractual terms and conditions have been modified in order to place the debtor

in a position to continue to service or resume servicing its capital debt despite financial difficulties.

**FORBEARANCE EXPOSURE**

(€ m)	Core Bank		Non-Core Bank		Total
	Rating class 1-15	Rating class 16-18	Rating class 1-15	Rating class 16-18	
<b>2016</b>					
Loans and Receivables (LaR)	1,804	677	801	10,238	13,521
Loans and advances to customers	1,804	677	801	9,676	12,958
Non-current assets held for sale and disposal groups	-	-	-	563	563
Irrevocable and revocable loan commitments	75	23	33	422	552
<b>Total</b>	<b>1,878</b>	<b>700</b>	<b>834</b>	<b>10,660</b>	<b>14,073</b>

**FORBEARANCE EXPOSURE**

(€ m)	Core Bank		Non-Core Bank		Total
	Rating class 1-15	Rating class 16-18	Rating class 1-15	Rating class 16-18	
2015					
Loans and Receivables (LaR)	998	833	1,023	14,248	17,102
Loans and advances to banks	-	14	-	-	14
Loans and advances to customers	998	607	1,016	10,303	12,924
Non-current assets held for sale and disposal groups	-	212	7	3,945	4,164
Irrevocable and revocable loan commitments	45	23	29	147	244
<b>Total</b>	<b>1,043</b>	<b>856</b>	<b>1,052</b>	<b>14,395</b>	<b>17,346</b>

Loan loss provisions in the amount of € 5,098 million (previous year: € 6,442 million) were already created for the volume of receivables stated here to which forbearance measures have been applied. The

cover for the forbearance exposure by the Sunrise guarantee is about 83% (previous year: about 90%).

## 60. INFORMATION ON UNCONSOLIDATED STRUCTURED ENTITIES

### I. Interests in unconsolidated subsidiaries

HSH Nordbank maintains business relationships with unconsolidated structured entities, within the meaning of an interest pursuant to IFRS 12, if HSH Nordbank is exposed to variable returns based on equity, debt instruments, derivatives, guarantees, etc.

These unconsolidated structured entities relate to ABS conduits, securitisation and refinancing vehicles, investment funds and other structured entities.

#### INFORMATION ON THE SIZE OF UNCONSOLIDATED ENTITIES

Number	Total assets	
	2016	2015
ABS conduits	105	138
Investment funds	13	14
Securitisation and refinancing vehicles	14	16
Other	4	3
<b>Total</b>	<b>136</b>	<b>171</b>

Total assets	Number	
	2016	2015
32,210	105	138
2,071	13	14
845	14	16
172	4	3
<b>35,298</b>	<b>136</b>	<b>171</b>

HSH Nordbank uses ABS conduits for the purpose of risk diversification. ABS conduits are financed by the issuance of debentures. Furthermore these investments in ABS conduits are backed up by collateral. These companies are involved in the (revolving) purchase and securitisation of loan receivables, including refinancing with investors.

The function of refinancing and securitisation vehicles is to issue securities. These companies are involved in the (revolving) purchase and securitisation of receivables, including refinancing with investors. They are mainly financed through issuing debentures.

The main corporate purposes of investment funds are to finance assets, participate in non-listed companies and hold shares in real estate funds. The main activities of such investment funds are to carry out research for analysing markets, make decisions on investment and disinvestment in order to adjust portfolios and to attract investors. Investment funds raise their funds by the issuing of equity and debt instruments. The investment funds are funds launched by third parties, to which HSH Nordbank mainly grants loans.

HSH Nordbank has a business relationship within the meaning of an interest with a total of 136 unconsolidated structured entities (previous year: 171). The following table shows the accumulated total assets of the unconsolidated structured entities with which HSH Nordbank maintains a business relationship within the meaning of an interest:

### II. Risks from interests in unconsolidated structured entities

The following information concerning risk refers not just to the current reporting period but also to risks which result from business relationships with unconsolidated structured entities in earlier reporting periods.

The risks from unconsolidated structured entities are presented in the form of the maximum potential loss which may arise from these business relationships based on an interest within the meaning of IFRS 12. HSH Nordbank discloses the carrying amounts of these transactions as a maximum potential loss. In the case of irrevocable loan commitments and contingent liabilities, the carrying amount matches the par value.

There are no credit derivatives relating to unconsolidated structured entities as of the balance sheet date.

The following table shows the IFRS carrying amounts of exposures involving unconsolidated structured entities as of 31 December 2016 broken down into the items of financial position.

## TYPE OF BUSINESS RELATIONSHIP

(€ m) 2016	Investment funds	ABS	Refinancing and securitisation vehicles	Other structured entities	Total
Loans and advances to customers	148	-	185	7	340
Positive fair value of hedging derivatives	1	-	-	-	1
Trading assets	1	-	43	88	132
Financial investments	-	671	227	-	898
<b>Total assets</b>	<b>150</b>	<b>671</b>	<b>455</b>	<b>95</b>	<b>1,371</b>
Liabilities to customers	36	-	250	11	297
<b>Total equity and liabilities</b>	<b>36</b>	<b>-</b>	<b>250</b>	<b>11</b>	<b>297</b>

(€ m) 2015	Investment funds	ABS	Refinancing and securitisation vehicles	Other structured entities	Total
Loans and advances to customers	162	-	313	7	482
Trading assets	2	-	36	85	123
Financial investments	-	898	220	-	1,118
<b>Total assets</b>	<b>164</b>	<b>898</b>	<b>569</b>	<b>92</b>	<b>1,723</b>
Liabilities to customers	21	-	6	7	34
<b>Total equity and liabilities</b>	<b>21</b>	<b>-</b>	<b>6</b>	<b>7</b>	<b>34</b>

The above table contains the loans, debentures, deposits and derivatives in respect of unconsolidated structured entities.

In addition, there are maximum potential losses from irrevocable loan commitments amounting to € 0 million (previous year: € 19 million), € 0 million of which result from ABS (previous year: € 0 million) and € 0 million from refinancing and securitisation vehicles (previous year: € 19 million).

There are no business relationship risks based on an interest in unconsolidated structured entities as defined in IFRS 12, B26 that exceed the maximum potential loss, such as contractual terms under which HSH Nordbank would have to grant financial support, liquidity arrangements, guarantees extended or support provided by HSH Nordbank in the event of difficulties in refinancing unconsolidated structured entities.

Furthermore, HSH Nordbank has not entered into any loss-transfer agreements with unconsolidated structured entities. Mainly net interest income for granting loans and commission income were generated from business relationships with unconsolidated structured entities based on an interest within the meaning of IFRS 12.

### III. Sponsoring

HSH Nordbank has sponsor relationships within the meaning of IFRS 12 if HSH Nordbank is exposed to variable return flows, although there is no business relationship in the form of an interest within the meaning of IFRS 12. HSH Nordbank is a sponsor if it was involved in establishing an unconsolidated structured entity, if it stands to gain the main profit from the entity or is the main collateral taker, if HSH Nordbank provides implicit guarantees or if the name of HSH Nordbank is part of the name of the structured entity or of the products issued by such entity.

Details of sponsored entities are only shown, if they are not already included in the disclosures under II, (Risks from interests in unconsolidated structured entities). This requirement is satisfied in the case of two structured entities. These companies were sponsored by HSH Nordbank, but there is no interest within the meaning of IFRS 12.

During the reporting period HSH Nordbank sponsored a public fund, HSH Nordbank was involved in the establishment of this fund and provided the advisory investment committee during the reporting year. HSH Nordbank received an immaterial consultancy fee for this service.

HSH Nordbank has also been sponsoring a securitisation vehicle since December 2016. The transaction is based on the transfer of default risks. HSH Nordbank was involved in the establishment process and transferred default risks relating to a mezzanine tranche to the structured entity in the amount of € 235 million by way of a financial guarantee. Further information on this transaction can be found in Note 3.

#### IV. Provision of support

During the current reporting period HSH Nordbank has not supported any unconsolidated structured entity financially or in any other way without a contractual commitment to do so. HSH Nordbank has also no intention of granting financial support to any unconsolidated structured entity or helping to procure financial support from third parties.

### 61. CONTINGENT LIABILITIES AND IRREVOCABLE LOAN COMMITMENTS

#### CONTINGENT LIABILITIES

(€ m)	2016	2015
Contingent liabilities from guarantees and warranty agreements		
Loan guarantees	169	121
Letters of credit	358	258
Other warranties	–	–
Other guarantees	1,662	2,454
<b>Total</b>	<b>2,189</b>	<b>2,833</b>

#### IRREVOCABLE LOAN COMMITMENTS

(€ m)	2016	2015
Irrevocable loan commitments for		
Open account loans to banks	1	11
Open account loans to customers	6,496	6,209
Guarantees	63	59
Letters of credit	–	–
Other	94	91
<b>Total</b>	<b>6,654</b>	<b>6,370</b>

Information on collateral transferred is presented in Note 64.

For reasons of practicality no information in accordance with IAS 37.89 is disclosed.

Please refer to Note 43 and explanations set out in the Management of legal risks section in the Risk Report of the Management Report with respect to existing uncertainties regarding risks arising from legal disputes.

However, HSH Nordbank came to the conclusion in these cases, that the possibility of an outflow of resources is not remote within the meaning of IAS 37.28 in these cases and so has allowed for contingent liabilities. The financial impact of these contingent liabilities is estimated to be € 32 million (previous year: € 40 million).

There are contingent liabilities with regard to tax risks in connection with the tax audits that are ongoing at present. In particular, there is uncertainty surrounding how the tax authorities will interpret current trends in the court decisions made by the fiscal courts on various tax-related issues. The Bank, however, deems its legal positions to be correct, meaning that there is no need to set up corresponding provisions in this regard.

Please refer to the explanations set out in the Forecast of loan loss provisions section of the Forecast, Opportunities and Risks Report in the Management Report with regard to uncertainties relating to the determination of loan loss provisions.

The fair value of irrevocable loan commitments with a nominal volume of € 6,654 million (previous year: € 6,370 million) comes to € 12 million as at the balance sheet date (previous year: € 10 million).

With regard to future premium expense for the synthetic securitisation transaction, we refer to our statements in Note 3 II.



## OTHER DISCLOSURES

### 62. REPORT ON BUSINESS IN DERIVATIVES

Derivative financial instruments are used to a considerable degree in order to hedge risk efficiently, to take advantage of market opportunities and to cover special customer financing needs. The derivatives business of HSH Nordbank is predominantly transacted with banks based in OECD countries.

Positive and negative fair values are presented on the basis of gross values before offsetting in accordance with IAS 32.42.

#### I. Volumes

##### DERIVATIVE TRANSACTIONS WITH INTEREST RATE RISKS

(€ m)	Nominal values		Positive market values		Negative market values	
	2016	2015	2016	2015	2016	2015
Interest rate swaps	147,582	162,200	4,455	4,606	5,070	5,578
FRAs	-	-	-	-	-	-
Swaptions						
Long positions	2,847	3,381	149	131	24	31
Short positions	3,564	4,305	2	4	217	222
Caps, floors	7,738	7,822	40	54	27	36
Exchange-traded contracts	2,892	2,236	-	-	-	-
Other forward interest rate transactions	324	373	16	15	33	32
<b>Total</b>	<b>164,947</b>	<b>180,317</b>	<b>4,662</b>	<b>4,810</b>	<b>5,371</b>	<b>5,899</b>

##### DERIVATIVE TRANSACTIONS WITH INTEREST RATE AND FOREIGN EXCHANGE RISKS

(€ m)	Nominal values		Positive market values		Negative market values	
	2016	2015	2016	2015	2016	2015
Cross-currency interest rate swaps	15,417	20,362	244	221	396	405
<b>Total</b>	<b>15,417</b>	<b>20,362</b>	<b>244</b>	<b>221</b>	<b>396</b>	<b>405</b>

##### DERIVATIVE TRANSACTIONS WITH FOREIGN EXCHANGE RISKS

(€ m)	Nominal values		Positive market values		Negative market values	
	2016	2015	2016	2015	2016	2015
Forward exchange transactions	11,468	12,439	80	179	132	74
Currency options						
Long positions	579	706	57	59	-	-
Short positions	785	1,005	-	-	59	90
<b>Total</b>	<b>12,832</b>	<b>14,150</b>	<b>137</b>	<b>238</b>	<b>191</b>	<b>164</b>

**DERIVATIVE TRANSACTIONS WITH EQUITY AND OTHER PRICE RISKS**

(€ m)	Nominal values		Positive market values		Negative market values	
	2016	2015	2016	2015	2016	2015
Equity options						
Long positions	81	124	52	27	-	-
Short positions	60	91	-	-	51	23
Exchange-traded contracts	6	1	-	-	-	-
Equity/index-based swaps	84	-	11	-	-	-
Commodity-based transactions	-	10	-	36	-	36
<b>Total</b>	<b>231</b>	<b>226</b>	<b>63</b>	<b>63</b>	<b>51</b>	<b>59</b>

**CREDIT DERIVATIVES**

(€ m)	Nominal values		Positive market values		Negative market values	
	2016	2015	2016	2015	2016	2015
Guarantor position	96	135	1	1	-	-
Collateral taker position	170	187	26	29	-	-
<b>Total</b>	<b>266</b>	<b>322</b>	<b>27</b>	<b>30</b>	<b>-</b>	<b>-</b>

**CREDIT DERIVATIVE SECOND LOSS GUARANTEE**

(€ m)	Nominal values		Positive market values		Negative market values	
	2016	2015	2016	2015	2016	2015
Collateral taker position	1,107	2,723	199	663	-	-
<b>Total</b>	<b>1,107</b>	<b>2,723</b>	<b>199</b>	<b>663</b>	<b>-</b>	<b>-</b>

**DERIVATIVE TRANSACTIONS WITH STRUCTURED PRODUCTS**

(€ m)	Nominal values		Positive market values		Negative market values	
	2016	2015	2016	2015	2016	2015
Structured products	5,355	6,411	376	519	587	536
<b>Total</b>	<b>5,355</b>	<b>6,411</b>	<b>376</b>	<b>519</b>	<b>587</b>	<b>536</b>

**DERIVATIVE TRANSACTIONS IN FAIR VALUE HEDGE ACCOUNTING**

(€ m)	Nominal values		Positive market values		Negative market values	
	2016	2015	2016	2015	2016	2015
Fair value hedges						
Interest rate swaps	25,208	27,720	683	940	423	829
<b>Total</b>	<b>25,208</b>	<b>27,720</b>	<b>683</b>	<b>940</b>	<b>423</b>	<b>829</b>

## II. Counterparty classification

### COUNTERPARTY CLASSIFICATION

(€ m)	Nominal values		Positive market values		Negative market values	
	2016	2015	2016	2015	2016	2015
OECD banks	119,271	154,729	3,012	3,533	4,981	6,134
Non-OECD banks	88	215	3	4	-	-
Non-banks <sup>1)</sup>	99,084	88,470	2,895	3,048	1,573	1,351
Public authorities	6,920	8,817	481	899	465	407
<b>Total</b>	<b>225,363</b>	<b>252,231</b>	<b>6,391</b>	<b>7,484</b>	<b>7,019</b>	<b>7,892</b>

<sup>1)</sup>Including exchange-traded contracts

## III. Maturities

### MATURITIES

(€ m)	Positive market value of derivatives		Positive market value of derivatives from fair value hedging		Negative market value of derivatives		Negative market value of derivatives from fair value hedging	
	2016	2015	2016	2015	2016	2015	2016	2015
Residual maturity								
Up to 3 months	129	204	-	-	236	126	-	4
3 months to 1 year	378	173	35	26	375	369	6	15
1 year to 5 years	1,237	1,876	375	512	1,700	2,290	251	394
Over 5 years	3,964	4,291	273	402	4,285	4,278	166	416
<b>Total</b>	<b>5,708</b>	<b>6,544</b>	<b>683</b>	<b>940</b>	<b>6,596</b>	<b>7,063</b>	<b>423</b>	<b>829</b>

### 63. LEASE RECEIVABLES AND LIABILITIES

Operating leases where HSH Nordbank acts as a lessee serve the purpose of leasing technical facilities and equipment required to operate IT networks, among other purposes. In addition, HSH Nordbank is a lessee of real estate and motor vehicles.

In operating leases HSH Nordbank acts as lessor for aircraft and real estate.

In the case of finance leases on the US market HSH Nordbank acts as lessor under sale-and-lease-back leasing arrangements to finance photovoltaic installations.

For finance leases accumulated loan loss provisions in the amount of € 0 million (previous year: € 2 million) accrued.

#### I. Lessee under operating leases

##### MINIMUM LEASE PAYMENTS UNDER OPERATING LEASES

(€ m)	2016	2015
Minimum lease payments due		
Up to 1 year	31	34
1 year to 5 years	62	91
More than 5 years	5	5
<b>Total</b>	<b>98</b>	<b>130</b>

##### EXPENSES FOR LEASE PAYMENTS

(€ m)	2016	2015
Expenses for		
Minimum lease payments	32	36
<b>Total</b>	<b>32</b>	<b>36</b>

Expenses on assets used under operating leases are disclosed in Administrative expenses (cf. Note 16).

#### II. Lessor under operating leases

##### MINIMUM LEASE PAYMENTS TO BE EXPECTED UNDER OPERATING LEASES

(€ m)	2016	2015
Minimum lease payments to be received		
Up to 1 year	21	21
1 year to 5 years	39	10
More than 5 years	16	-
<b>Total</b>	<b>76</b>	<b>31</b>

Income from conditional leasing payments was neither recorded in the reporting period nor in the previous year.

#### III. Lessor under finance leases

##### FINANCE LEASES

(€ m)	2016	2015
Outstanding lease payments	71	80
+ Guaranteed residual values	15	15
= Minimum lease payments	86	95
+ Non-guaranteed residual values	19	18
= Gross investment	105	113
- Unearned finance income	7	7
= Net investment	98	106
- Net present value of non-guaranteed residual values	13	13
<b>= Net present value of minimum lease payments</b>	<b>85</b>	<b>93</b>

The gross investments amount and the net present value of the minimum lease payments break down by maturity as follows.

#### BREAKDOWN OF RESIDUAL MATURITIES

(€ m)	Gross investments in the lease		Net present value of the minimum lease payments	
	2016	2015	2016	2015
Minimum lease payments to be received				
Up to 1 year	12	11	11	11
1 year to 5 years	37	44	33	39
More than 5 years	56	58	41	43
<b>Total</b>	<b>105</b>	<b>113</b>	<b>85</b>	<b>93</b>

Income from conditional lease payments was neither recorded during the year nor in the previous year.

#### 64. DISCLOSURES ON COLLATERAL TRANSFERRED AND FINANCIAL ASSETS TRANSFERRED WITH RETENTION OF RIGHTS AND/OR OBLIGATIONS

##### I. Collateral transferred

As at 31 December 2016 HSH Nordbank had transferred assets as collateral which do not meet the requirements of derecognition under IAS 39. The assets transferred as collateral continue to be recognised in the Group statement of financial position as the interest rate risk, credit risk and other material risks as well as the prospects of appreciation and interest income largely reside with HSH Nordbank.

The following table mainly shows the collateral used to collateralise OTC derivative transactions and funds raised at central banks and other credit institutions. Notes on repurchase agreements are separately disclosed below. A small amount of collateral has been transferred in the course of securities lending business.

##### CARRYING AMOUNTS OF TRANSFERRED COLLATERAL

(€ m)	2016	2015
Loans and advances	8,555	11,804
Loans and advances to banks	3,218	3,634
Loans and advances to customers	5,337	8,170
Trading assets/Financial investments	10	1,830
Non-current assets held for sale and disposal groups	100	–
<b>Total</b>	<b>8,665</b>	<b>13,634</b>

Central Bank or other banks, but are assigned without this being disclosed. It is not possible to resell or pledge in the interim.

Money market borrowing generally involves pledging and transferring securities lodged with the European Central Bank. Promissory notes and other receivables from lending are not pledged to the European



In addition, HSH Nordbank concludes repurchase agreements under repo master agreements both on a national and international scale. The associated liabilities are recognised under Liabilities to banks or Liabilities to customers. At the end of the reporting period, the carrying amount of the securities transferred as collateral in the framework of repo transactions was € 949 million (previous year: € 1,144 million). The fair value amounts to € 899 million (previous year: € 1,086 million). The corresponding liabilities are recognised in the amount of € 833 million (previous year: 966 million) with the fair value corresponding to the carrying amount. A net position of € 66 million arose from the fair values of the assets transferred and the associated liabilities (previous year: € 120 million). Collateral transferred under repo transactions can be resold or repledged.

Repo and securities lending transactions are monitored by measuring transactions on a daily basis. If there is a shortfall in collateral the counterparty may require HSH Nordbank to provide additional securities to increase collateral. Where HSH Nordbank has provided collateral and the market situation changes such that the cover provided is excessive, it is entitled to require the counterparty to release collateral. The collateral provided is subject to a full transfer of rights, i.e. the party receiving collateral may act like an owner and in particular may transfer or pledge such collateral. In the case of securities collateral, securities of the same type and quality ('the same sort') must be delivered or returned unencumbered. Where collateral has been provided in the form of securities, it may not be returned in cash.

With regard to further collateral provided in the form of securities (under the "Financial investments" balance sheet item), reference is made to Note 3 II.

The above conditions and collateral modalities apply to tri-party repo transactions between HSH Nordbank and its counterparties accordingly. The transactions are executed via a tri-party agent.

## II. Financial assets transferred with retention of rights and/or obligations

HSH Nordbank has transferred assets to third parties outside the Group that meet the conditions for full derecognition. The rights and obligations retained under these transfers were of an overall immaterial nature. The risks become transparent by recognition of provisions and/or recording of contingent liabilities. There is a hypothetical repurchase option relating to the sale of an equity holding, which the Bank, however, can only exercise based on the occurrence of certain biometric events. The option has a time value of € 0; it entails no risk.

## 65. TRUST TRANSACTIONS

The table below shows the volume of trust transactions not recognised in the statement of financial position.

### TRUST TRANSACTIONS

(€ m)	2016	2015
Loans and advances to customers	5	7
<b>Trust assets</b>	<b>5</b>	<b>7</b>
Liabilities to customers	5	7
<b>Trust liabilities</b>	<b>5</b>	<b>7</b>

## 66. RELATED PARTIES

HSH Nordbank does business with related parties and companies.

These include HSH Beteiligungs Management GmbH, Hamburg; as the direct parent company and, at the same time, the top-level parent company of HSH Nordbank AG, which prepares Group financial statements, HSH Finanzfonds AöR as the top-level parent company of the Group, hsh portfoliomanagement AöR, as well as the Federal State of Schleswig-Holstein and the Free and Hanseatic City of Hamburg, which each hold a stake of 50% in the two aforementioned companies. Furthermore, business relations exist with subsidiaries which are controlled but not included in the Group financial statements for reasons of materiality, associates, joint ventures, individuals in key positions and their relatives and companies controlled by these individuals. Individuals in key positions comprise exclusively the members of the Management and Supervisory Boards of HSH Nordbank AG.

In the course of the normal business operations transactions are entered into at arm's length with companies and parties that are related parties. These transactions include loans, call and fixed-term deposits, derivatives and securities transactions.

### I. The parent company and companies with joint management or significant influence on the company

For transactions with HSH Beteiligungs Management GmbH and HSH Finanzfonds AöR as well as with the Federal State of Schleswig-Holstein and the Free and Hanseatic City of Hamburg, which each participate in HSH Finanzfonds AöR at 50%, the Bank makes use of IAS 24.25. Accordingly, HSH Nordbank is exempt from the disclosure requirement regarding public authorities, unless transactions are involved that have a significant impact on the Group financial statements.

The guarantee amount with regard to the guarantee facility provided by the Federal State of Schleswig-Holstein and the Free and Hanseatic City of Hamburg to HSH Nordbank AG and certain subsidiaries via HSH Finanzfonds AöR is identified as a significant transaction within the meaning of IAS 24. Please refer to Notes 3 and 20 for more details.

In addition, a loan portfolio was sold to the resolution institution (hsh portfoliomanagement AöR) formed by the federal states of Hamburg and Schleswig-Holstein as part of the implementation of the EU Commission's decision of 2 May 2016.

With effect from 30 June 2016, HSH Nordbank AG transferred a portfolio of non-performing shipping loans with a volume of € 5 billion (reporting date: 31 December 2015) to hsh portfoliomanagement AöR, which belongs to the federal states. Within this context, the Bank received the market price set by the EU Commission of € 2.4 billion from hsh portfoliomanagement AöR. The losses of € 2.6 billion

incurred were settled as part of the loss settlement under the guarantee. The transaction involved first of all transferring a portfolio of transactions from HSH Nordbank AG to hsh portfoliomanagement AöR by way of a cash sub-participation relating to the loans with a contractual trust agreement, including a cash flow pass through arrangement (known as a "synthetic transfer"). After this synthetic transfer, the in rem transfer is performed by way of partial universal succession as part of a spin-off pursuant to Section 123 (3) of the German Transformation of Companies Act (UmwG). In addition, a "guarantee and standstill agreement" was concluded between HSH Nordbank AG and hsh portfoliomanagement AöR for current accounts and derivatives in connection with the abovementioned loan portfolio. The "guarantee and standstill agreement" gives hsh portfoliomanagement AöR the option of making a decision on the assumption of current accounts and derivatives in connection with the abovementioned loan portfolio at a later date (purchase option). In return, any increases in risk at HSH Nordbank AG in the meantime are to be largely assumed and secured by hsh portfoliomanagement AöR. hsh portfoliomanagement AöR made use of its right under the guarantee and standstill agreement with regard to the current accounts with effect from 31 December 2016 and declared that it would not be exercising its purchase option.

There are also further service relationships set out in agreements between hsh portfoliomanagement AöR and HSH Nordbank AG, e.g. the servicing of the loans transferred and the provision of IT systems, for which standard market remuneration is paid.

### II. Subsidiaries

The transactions with unconsolidated subsidiaries are shown below:

#### SUBSIDIARIES - ASSETS

(€ m)	2016	2015
Loans and advances to customers	24	83
Loan loss provisions	-11	-23
Financial investments	1	-
<b>Total</b>	<b>14</b>	<b>60</b>

**SUBSIDIARIES - LIABILITIES**

(€ m)	2016	2015
Liabilities to customers	2	25
Provisions	-	22
Other liabilities	1	2
<b>Total</b>	<b>3</b>	<b>49</b>

**SUBSIDIARIES - INCOME STATEMENT**

(€ m)	2016	2015
Net interest income	1	2
Loan loss provisions	10	-4
Other operating income	4	4
<b>Total</b>	<b>15</b>	<b>2</b>

**III. Associates**

The following table shows the transactions with associates:

**ASSOCIATES - ASSETS**

(€ m)	2016	2015
Loans and advances to customers	-	53
Loan loss provisions	-	-40
<b>Total</b>	<b>-</b>	<b>13</b>

**ASSOCIATES - LIABILITIES**

(€ m)	2016	2015
Liabilities to customers	1	1
<b>Total</b>	<b>1</b>	<b>1</b>

**ASSOCIATES - INCOME STATEMENT**

(€ m)	2016	2015
Net interest income	-	1
Loan loss provisions	-	-1
Net income from financial investments	-2	2
Administrative expenses	-	-2
<b>Total</b>	<b>-2</b>	<b>-</b>

Other financial liabilities to associates amount to € 0 million (previous year: € 11 million).

**IV. Joint ventures**

The following tables show the transactions with joint ventures:

**JOINT VENTURES - ASSETS**

(€ m)	2016	2015
Loans and advances to customers	178	33
Trading assets	13	-
<b>Total</b>	<b>191</b>	<b>33</b>

**JOINT VENTURES - LIABILITIES**

(€ m)	2016	2015
Liabilities to customers	25	27
<b>Total</b>	<b>25</b>	<b>27</b>

**JOINT VENTURES - INCOME STATEMENT**

(€ m)	2016	2015
Net interest income	1	-
Loan loss provisions	-	-6
Net trading income	-4	-1
Net income from financial investments	-	1
<b>Total</b>	<b>-3</b>	<b>-6</b>

Irrevocable loan commitments to joint ventures amount to € 326 million (previous year: € 0 million).

**V. Other related parties and companies**

The following transactions had been entered into with individuals in key positions at HSH Nordbank AG and their close relatives or companies controlled by these individuals as at the balance sheet date:

(€ m)	2016	2015
Liabilities to customers	1	-
<b>Total</b>	<b>1</b>	<b>-</b>

## VI. Remuneration of persons in key management positions

In accordance with the decision of the EU Commission of 20 September 2011 concerning state aid the remuneration of the members of the Management Board of HSH Nordbank AG is limited for each board member to a maximum of € 500,000 per year (total fixed remuneration). Remuneration payable for secondary employment undertaken at the request of the Supervisory Board is set off against the remuneration entitlement set out in the employment contract. Furthermore, each board member receives pension benefits in the amount of 20% of the annual fixed income, as well as reasonable benefits in kind.

It is planned to add a variable remuneration component to the Management Board's remuneration system as soon as the Bank is able to pay dividends again and the reorganisation phase pursuant to the decisions of the EU Commission of 20 September 2011/2 May 2016 has been successfully completed.

The Bank does not offer additional long-term incentives such as share option schemes.

The following table shows the remuneration of persons in key management positions. Remuneration of the Supervisory Board consists of additions to provisions for the activities of the Supervisory Board carried out during the financial year excluding value-added tax.

### REMUNERATION OF PERSONS IN KEY MANAGEMENT POSITIONS

(€ k)	Management Board		Supervisory Board		Total	
	2016	2015	2016	2015	2016	2015
Short-term benefits	2,424	2,920	477	467	2,901	3,387
Termination benefits	1,004	-	-	-	1,004	-
Other long-term benefits	-	-	-	-	-	-
Post-employment benefits	600	500	-	-	600	500
<b>Total remuneration</b>	<b>4,028</b>	<b>3,420</b>	<b>477</b>	<b>467</b>	<b>4,505</b>	<b>3,887</b>

## VII. Additional disclosures under Section 315a HGB

HSH Nordbank is obliged to provide additional disclosures in its Group financial statements under Section 315a HGB. Several differences compared to the IFRS disclosures should be borne in mind in this regard: termination benefits payable are not included in the total remuneration of the active members of the Management Board. This remuneration is disclosed instead under total remuneration payable to former members of the Management Board.

As at 31 December 2016, a total amount of €k 57,833 (previous year: €k 53,820) was shown in provisions for pension obligations relating to former members of the Management Board and their surviving dependants.

As was the case in the previous year, there were no advances, loans and other liabilities to members of the Management Board as at 31 December 2016. For members of the Supervisory Board they amounted to €k 150 (previous year: €k 469). In the 2016 reporting year no new loans were granted to members of the Supervisory Board.

### REMUNERATION OF EXECUTIVE BODIES

(€ k)	2016	2015
<b>Total remuneration of all active members of executive bodies</b>		
Management Board	3,024	3,420
Supervisory Board	477	467
<b>Total</b>	<b>3,501</b>	<b>3,887</b>
<b>Total remuneration of former members of executive bodies and their surviving dependants</b>		
Management Board	3,708	2,751

The loans granted to members of the Supervisory Board relate to real estate financings. Loans to members of the Supervisory Board were granted with maturities from variable to final maturity in 2036. Loans to members of the Supervisory Board were at arm's length conditions with interest rates between 4.45% and 6.9%.

Collateral for loans is in the form of land charges for real estate financing. Repayments of loans by members of the Supervisory Board totalled €k 319 in total in 2016 (previous year: €k 30).

### VIII. Disclosure of Supervisory Board remuneration

The members of the Supervisory Board receive remuneration for their service during a financial year in an amount determined by the Annual General Meeting of the following year. The remuneration for the Supervisory Board for the 2015 financial year was therefore paid in the 2016 reporting period. Appropriate provisions have been recognised in the 2016 Annual Accounts for the 2016 reporting year.

The remuneration system is based on the requirements of the German Corporate Governance Code and is organised as follows after the resolution of the Annual General Meeting of HSH Nordbank AG on 23 May 2014 and applies to the term of office of the Supervisory Board that has started on 23 May 2014:

(in €)			
Executive body	Function	Fixed component	Attendance fee
Supervisory Board	Chair	25,000	250
	Deputy Chair	18,000	250
	Member	11,000	250
Risk Committee	Chair	15,000	250
	Member	7,000	250
Executive Committee	Chair	15,000	250
	Member	7,000	250
Audit Committee	Chair	15,000	250
	Member	7,000	250
Remuneration Monitoring Committee	Chair	12,000	250
	Member	5,000	250

The Mediation Committee to be formed under the German Co-determination Act of 1976 (*Mitbestimmungsgesetz*) does not receive any separate remuneration. Members of the Supervisory Board are also reimbursed for any value-added tax payable and for their expenses.

€k 550 of the amount provided for in the 2015 financial year (€k 556, thereof VAT: €k 89), were paid to the members of the Supervisory Board in the reporting period. This includes €k 82 of value-added tax.

€K 567 have been provided for activities of the Supervisory Board (thereof value-added tax: €k 91), which will be disbursed after the Annual General Meeting provided a corresponding resolution is passed by the Annual General Meeting 2017. Remuneration (excl. VAT) is expected to be distributed among the members of the Supervisory Board as follows:

(in €)	Fixed remuneration		Attendance fee		Total	
	2016	2015	2016	2015	2016	2015
<b>Members of the Supervisory Board</b>						
Dr Thomas Mirow, Chair	59,000	59,000	7,250	6,000	66,250	65,000
Olaf Behm, Deputy Chair	44,000	44,000	8,000	7,000	52,000	51,000
Stefanie Arp	18,000	18,000	2,750	3,250	20,750	21,250
Sabine-Almut Auerbach <sup>1)</sup>	2,712	11,000	500	2,250	3,212	13,250
Peter Axmann <sup>2)</sup>	18,000	7,540	3,000	1,500	21,000	9,040
Simone Graf	30,000	30,000	7,250	6,000	37,250	36,000
Silke Grimm	16,000	16,000	2,000	2,500	18,000	18,500
Torsten Heick <sup>3)</sup>	–	8,926	–	1,750	–	10,676
Cornelia Hintz <sup>4)</sup>	6,841	–	1,500	–	8,341	–
Stefan Jütte	26,000	26,000	3,250	3,000	29,250	29,000
Dr Rainer Klemmt-Nissen	30,000	30,000	7,250	6,000	37,250	36,000
Rieka Meetz-Schawaller	18,000	18,000	3,750	3,000	21,750	21,000
Dr David Morgan <sup>5)</sup>	25,000	25,000	5,250	4,500	30,250	29,500
Dr Philipp Nimmermann	30,000	30,000	6,500	5,250	36,500	35,250
Stefan Schlatermund	18,000	18,000	3,500	3,250	21,500	21,250
Klaus-Dieter Schwetscher <sup>5)</sup>	11,000	10,699	2,250	2,000	13,250	12,699
Elke Weber-Braun	26,000	26,000	3,500	3,250	29,500	29,250
Jörg Wohlers	25,000	24,118	5,750	4,750	30,750	28,868
<b>Total</b>	<b>403,553</b>	<b>402,283</b>	<b>73,250</b>	<b>65,250</b>	<b>476,803</b>	<b>467,533</b>

<sup>1)</sup> until 31 March 2016

<sup>2)</sup> from 14 July 2015

<sup>3)</sup> until 30 June 2015

<sup>4)</sup> from 18 May 2016

<sup>5)</sup> from 10 January 2015

<sup>6)</sup> Amounts before deduction of Supervisory Council tax and solidarity surcharge

The members of the Supervisory Board have again not provided any advisory or brokerage services or any other personal services to the

Bank in the year 2016. Accordingly no additional remunerations were granted.



## 67. OTHER FINANCIAL OBLIGATIONS

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The transactions listed below include payment obligations under pending contracts or continuing obligations that cannot be recognised in the balance sheet as well as other financial obligations that could have a material effect on the future financial position of HSH Nordbank.

There are shareholder liabilities of less than € 1 million for outstanding payments on subscribed nominal capital that have not yet been called in (previous year: € 11 million).

A new calculation methodology for determining target volumes in the guarantee scheme was approved as part of the implementation of the German Law on Deposit Insurance (EinSiG) that came into effect on 3 July 2015. The target amount to be calculated annually on the basis of the data as at 31 December of the previous year is to be raised by the member institutions by 3 July 2024 (build-up phase). The annual premium required for this is determined by 31 May of the current year by the German Savings Banks Association (DSGV) as the association responsible for the guarantee scheme. The premium is collected before 30 September of each year. HSH Nordbank AG contributed 30% of its premium obligation for 2016 (€ 4 million) as an irrevocable payment obligation. Special or additional contributions over and above those already paid may be levied, for instance, as part of a compensation case where support is provided. The obligation to pay contributions until 2024 and any special or additional contributions represent a risk with regard to HSH Nordbank AG's financial position.

With the transposition of the Bank Recovery and Resolution Directive (BRRD) into German law a new legal basis for determining the bank levy came into force as at 1 January 2015. The target amount of the EU-wide Single Resolution Fund (SRF) is to be achieved by 1 January 2024 through contributions paid by European banks. The current levy is determined by the supervisory authorities as at 31 May of each year and is payable by 30 June. Subsequent assessments are not provided for.

Obligations amounting to € 89 million (previous year: € 127 million) result from leasing agreements for IT services.

Long-term rental agreements for office space result in annual obligations of approximately € 5 million (previous year: € 8 million).

The sale of an equity holding results in obligations for the Bank to purchase fund units at the market price up to a nominal amount of € 8 million (previous year: € 8 million) and no obligation to provide indemnities (previous year: € 47 million).

The obligation to bear costs entered into by HSH Nordbank AG in connection with a loan restructuring arrangement expired in the financial year (previous year: € 8 million).

By way of a decision made on 24 June 2016, BVV Versicherungsverein des Bankgewerbes a.G. and BVV Versorgungskasse des Bankgewerbes e.V. reduced the pension payments to employees. By way of a decision made on 1 November 2016, the Management Board of HSH Nordbank AG decided to make additional pension plan contributions to BVV Versorgungskasse des Bankgewerbes e.V. in order to maintain the original benefit amount based on the individual pension commitments for these employees and prevent any pension gaps. This voluntary obligation is expected to result in additional annual contributions of less than € 1 million. As a result, the estimated payments made to BVV Versorgungskasse des Bankgewerbes e.V. amount to € 2 million.

As part of its former guarantor function the Bank also has a general liability towards Deka Bank Deutsche Girozentrale together with other former shareholders. It applies to liabilities entered into until 18 July 2001 regardless of their term.

For information on premium obligations resulting from the provision of guarantee facilities (second loss guarantee and synthetic securitisation transaction), we refer to our comments in Note 3.

There exist no material other financial obligations apart from those listed above.

## 68. LIST OF SHAREHOLDINGS

The following information is based on German commercial law.

## CONSOLIDATED SUBSIDIARIES WITH A SHARE OF VOTING RIGHTS OF THE BANK OF MORE THAN 50 %

Serial no.	Name/Place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
1	Avia Management S.à.r.l., Luxembourg, Luxembourg	100.00	100.00	EUR	-26,833.03	7,077.69
2	BINNENALSTER-Beteiligungsgesellschaft mbH, Hamburg	100.00	100.00	EUR	269,741.15	-7,349.50
3	Bu Wi Beteiligungsholding GmbH, Hamburg	100.00	100.00	EUR	17,887.96	958.40
4	CAPCELLENCE Dritte Fondsbeteiligung GmbH, Hamburg <sup>1)</sup>	100.00	100.00	EUR	8,051,161.30	1,700,761.48
5	CAPCELLENCE Erste Fondsbeteiligung GmbH, Hamburg <sup>1)</sup>	100.00	100.00	EUR	899,332.89	-408,301.65
6	CAPCELLENCE Holding GmbH & Co. KG, Hamburg <sup>1)</sup>	100.00	100.00	EUR	121,900,969.76	-629,838.96
7	Capcellence Vintage Year 06/07 Beteiligungen GmbH & Co. KG, Hamburg <sup>1)</sup>	83.33	99.91	EUR	305,542.03	-153,120.52
8	Capcellence Vintage Year 07/08 Beteiligungen GmbH & Co. KG, Hamburg <sup>1)</sup>	83.33	99.99	EUR	1,344,327.26	-321,407.48
9	CAPCELLENCE Vintage Year 11 Beteiligungen GmbH & Co. KG, Hamburg <sup>1)</sup>	83.33	99.99	EUR	15,450,701.68	369,579.05
10	CAPCELLENCE Vintage Year 13 Beteiligungen GmbH & Co. KG, Hamburg <sup>1)</sup>	83.33	99.47	EUR	1,156,481.58	-104,459.37
11	CAPCELLENCE Vintage Year 16 Beteiligungen GmbH & Co. KG, Hamburg <sup>1)</sup>	83.33	99.99	EUR	<sup>3)</sup>	<sup>3)</sup>
12	CAPCELLENCE Zweite Fondsbeteiligung GmbH, Hamburg <sup>1)</sup>	100.00	100.00	EUR	8,020,758.84	2,175,955.98
13	DEERS Green Power Development Company, S.L., Madrid, Spain <sup>1)</sup>	100.00	100.00	EUR	-32,004,545.00	-1,528,998.00
14	FSL Asset Management Pte. Ltd., Singapore, Singapore <sup>1)</sup>	100.00	100.00	USD	813,685.00	-111,083.00
15	FSL Holdings Pte. Ltd., Singapore, Singapore <sup>1)</sup>	100.00	100.00	USD	-2,664,602.00	1,975,821.00
16	FSL Trust Management Pte. Ltd., Singapore, Singapore <sup>1)</sup>	100.00	100.00	USD	1,716,341.00	1,216,817.00
17	GODAN GmbH, Hamburg	100.00	100.00	EUR	-1,124,839.50	-178,367.99
18	HSH Auffang- und Holdinggesellschaft mbH & Co. KG, Hamburg	100.00	100.00	EUR	37,551,389.69	1,186,800.93
19	HSH Care+Clean GmbH, Hamburg <sup>1) 4)</sup>	51.00	51.00	EUR	25,000.00	-3,389.30
20	HSH Facility Management GmbH, Hamburg <sup>2)</sup>	100.00	100.00	EUR	205,600.00	-39,202.31
21	HSH Gastro+Event GmbH, Hamburg <sup>1) 4)</sup>	100.00	100.00	EUR	25,000.00	-658,027.49
22	HSH Move+More GmbH, Kiel <sup>1) 4)</sup>	51.00	51.00	EUR	25,000.00	188,733.63
23	HSH N Finance (Guernsey) Limited, St. Peter Port, Guernsey	100.00	100.00	EUR	669,139.00	-85,811.00
24	HSH N Funding II, George Town, Cayman Islands	56.33	100.00	USD	654,305,988.00	36,276,800.00
25	HSH Nordbank Securities S.A., Luxembourg, Luxembourg	100.00	100.00	EUR	198,622,729.84	7,650,121.82
26	HSH N Residual Value Ltd., Hamilton, Bermuda	100.00	100.00	USD	3,576,064.00	-110,438.00
27	HSH Private Equity GmbH, Hamburg <sup>2)</sup>	100.00	100.00	EUR	550,000.00	-921,717.94
28	Ilex Integra GmbH, Hamburg <sup>1)</sup>	100.00	100.00	EUR	-20,976,000.01	-129,009.97
29	ISM Agency, LLC, New York, USA <sup>1)</sup>	100.00	100.00	USD	<sup>6)</sup>	<sup>6)</sup>

Serial no.	Name/Place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
30	Neptune Finance Partner S.à.r.l., Luxembourg, Luxembourg	100.00	100.00	USD	73,894.70	73,519.63
31	Neptune Finance Partner II S.à.r.l., Luxembourg, Luxembourg <sup>12)</sup>	100.00	100.00	USD	2,462,763.63	2,440,763.63
32	RESPARCS Funding Limited Partnership I, Hong Kong, Hong Kong <sup>1)</sup>	0.01	100.00	USD	-7,240,612.00	-1,225,325.00
33	RESPARCS Funding II Limited Partnership, St. Helier, Jersey <sup>1)</sup>	0.01	100.00	EUR	-	-683,677.00
					243,646,987.00	
34	Solar Holdings S.à.r.l., Luxembourg, Luxembourg	100.00	100.00	EUR	-	-4,640,871.13
					26,581,986.26	
35	Unterstützungs-Gesellschaft der Hamburgischen Landesbank mit beschränkter Haftung i.L., Hamburg	100.00	100.00	EUR	24,533.52	-921.07
36	2200 Victory LLC, Dover (Kent County), USA	100.00	100.00	USD	50,729,726.00	7,119,854.00

#### CONSOLIDATED SUBSIDIARIES WITH A SHARE OF VOTING RIGHTS OF THE BANK OF 50 % OR LESS

– of which subsidiaries due to a principal-agent relationship

Serial no.	Name/Place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
37	Amentum Aircraft Leasing No. Five Limited, Dublin, Ireland <sup>1)</sup>	49.00	49.00	USD	-	-3,127,784.00
					17,098,100.00	
38	Amentum Aircraft Leasing No. Seven Limited, Dublin, Ireland <sup>1)</sup>	49.00	49.00	USD	3,862,089.00	1,317,576.00
39	Amentum Aircraft Leasing No. Six Limited, Dublin, Ireland <sup>1)</sup>	49.00	49.00	USD	-	595,120.00
					10,141,899.00	
40	Mitco Real Estate A S.à.r.l., Canach, Luxembourg	0.00	0.00	EUR	-	924,571.72
					14,395,759.25	
41	Mitco Resolution 1 S.à.r.l., Canach, Luxembourg	0.00	0.00	EUR	-3,134,697.31	336,284.44
42	Mitco Resolution 2 S.à.r.l., Canach, Luxembourg	0.00	0.00	EUR	-8,711,353.56	-502,816.55
43	Mitco Resolution 3 S.à.r.l., Canach, Luxembourg	0.00	0.00	EUR	-1,495,344.96	-596,262.83
44	Mitco Resolution 4 S.à.r.l., Canach, Luxembourg	0.00	0.00	EUR	-2,010,045.03	-101,764.85
45	Mitco Resolution 5 S.à.r.l., Canach, Luxembourg	0.00	0.00	EUR	239,483.06	109,181.58
46	Next Generation Aircraft Finance 2 S.à.r.l., Findel, Luxembourg <sup>1)</sup>	49.00	49.00	EUR	-9,194,273.00	-2,510,795.00
47	Next Generation Aircraft Finance 3 S.à.r.l., Findel, Luxembourg <sup>1)</sup>	49.00	49.00	EUR	-	-2,442,221.00
					10,671,955.00	
48	RDM Limited, George Town, Cayman Islands	0.00	0.00	USD	-	-22,786,710.00
					177,194,229.00	

– of which subsidiaries due to contractual rights

Serial no.	Name/Place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
49	Adessa Grundstücksverwaltungsgesellschaft mbH & Co. Vermietungs KG, Mainz	0.00	0.00	EUR	-483,785.80	40,080.67
50	Castellum ABF S.A., Luxembourg, Luxembourg	0.00	0.00	EUR	22,253.00	0.00
51	GmbH Altstadt Grundstücksgesellschaft, Mainz <sup>1)</sup>	50.00	50.00	EUR	-65,200.16	107,696.20
52	Life Insurance Fund Elite LLC, New York, USA	0.00	0.00	USD	<sup>6)</sup>	<sup>6)</sup>
53	Life Insurance Fund Elite LLC, Minneapolis, USA	0.00	0.00	USD	<sup>6)</sup>	<sup>6)</sup>
54	OCEAN Funding 2013 GmbH, Frankfurt am Main	0.00	0.00	EUR	27,482.99	1,296.84
55	Senior Assured Investment S.A., Luxembourg, Luxembourg	0.00	0.00	EUR	31,000.00	0.00
56	Senior Preferred Investments S.A., Luxembourg, Luxembourg	0.00	0.00	EUR	31,000.00	0.00
57	Stratus ABF S.A., Luxembourg, Luxembourg	0.00	0.00	EUR	31,002.00	0.00

#### ASSOCIATES AND JOINT VENTURES CONSOLIDATED UNDER THE EQUITY METHOD

Serial no.	Name/Place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
58	Kontora Family Office GmbH, Hamburg <sup>14)</sup>	51.00	51.00	EUR	1,256,715.81	330,618.83
59	First Ship Lease Trust, Singapore, Singapore <sup>1)</sup>	25.19	25.19	USD	278,182,000.00	14,147,000.00

#### UNCONSOLIDATED SUBSIDIARIES WITH A SHARE OF VOTING RIGHTS OF THE BANK OF MORE THAN 50 %

Serial no.	Name/Place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
60	Asian Capital Investment Opportunities Limited, Hong Kong, Hong Kong <sup>1)</sup>	51.00	51.00	USD	115.00	0.00
61	Aviation Leasing OpCo France III, Paris, France <sup>1)</sup>	100.00	100.00	EUR	-140,320.00	-26,617.00
62	Aviation Leasing OpCo France IV, Paris, France <sup>1)</sup>	100.00	100.00	EUR	-39,145.00	-17,872.00
63	CAPCELLENCE Vintage Year 16 Beteiligungen GmbH (formerly: CAPCELLENCE Vintage Year 12 Beteiligungen GmbH), Hamburg <sup>1)</sup>	100.00	100.00	EUR	13,966.97	-1,850.45
64	European Capital Investment Opportunities Limited, St. Helier, Jersey <sup>1)</sup>	51.00	51.00	EUR	110.00	15.00
65	Grundstücksgesellschaft Porstendorf mbH & Co. KG, Hamburg	100.00	100.00	EUR	-2,020,716.09	-1,032.29
66	HSH N Structured Situations Limited, St. Helier, Jersey <sup>7)</sup>	100.00	100.00	USD	351,241.00	10,805.00
67	NORDIC BLUE CONTAINER V LIMITED, Majuro, Marshall Islands	100.00	100.00		<sup>6)</sup>	<sup>6)</sup>
68	PERIMEDES GmbH, Hamburg	100.00	100.00	EUR	26,253.53	3,204.83

**UNCONSOLIDATED SUBSIDIARIES WITH A SHARE OF VOTING RIGHTS OF THE BANK OF 50 % OR LESS**

– of which subsidiaries due to a principal-agent relationship

Serial no.	Name/Place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
69	AGV Irish Equipment Leasing No. 7 Limited, Dublin, Ireland <sup>1)</sup>	49.00	49.00	USD	76,804.00	4,813,588.00
70	Amentum Aircraft Leasing No. Ten Limited, Dublin, Ireland <sup>1) 9)</sup>	49.00	49.00	USD	–6,521,915.00	–2,858,784.00
71	Amentum Aircraft Leasing No. Three Limited, Dublin, Ireland <sup>1)</sup>	49.00	49.00	USD	–15,046,554.00	–1,175,030.00
72	TEAL FUNDING NO 1 LTD, Dublin, Ireland <sup>8)</sup>	0.00	0.00	GBP	–42,435.00	16,717.00

– of which subsidiaries due to contractual rights

Serial no.	Name/Place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
73	Lyceum Capital Fund 2000 (Number Five) GmbH & Co. KG, Stuttgart <sup>1)</sup>	80.00	0.00	EUR	–233,402.29	0.00

**UNCONSOLIDATED JOINT VENTURES**

Serial no.	Name/Place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
74	AGV Irish Equipment Leasing No. 4 Limited, Dublin, Ireland <sup>13)</sup>	100.00	100.00	USD	500.00	–17,382.00
75	Fosse Way Shipping Limited, London, Great Britain <sup>14)</sup>	58.85	58.85	EUR	–20,339,939.00	–145,973.00
76	Infrastructure Holding S.à.r.l., Luxembourg, Luxembourg <sup>9)</sup>	0.00	0.00	EUR	12,500.00	0.00
77	Lagan Viking Limited, Hong Kong, Hong Kong <sup>14)</sup>	58.85	58.85	EUR	–16,137,568.00	–63,756.00
78	Melody Holding Limited, Douglas, Isle of Man	0.00	0.00		<sup>3)</sup>	<sup>3)</sup>
79	Melody Shipping 1 Limited, Douglas, Isle of Man	0.00	0.00		<sup>3)</sup>	<sup>3)</sup>
80	Melody Shipping 2 Limited, Douglas, Isle of Man	0.00	0.00		<sup>3)</sup>	<sup>3)</sup>
81	Melody Shipping 3 Limited, Douglas, Isle of Man	0.00	0.00		<sup>3)</sup>	<sup>3)</sup>
82	Melody Shipping 4 Limited, Douglas, Isle of Man	0.00	0.00		<sup>3)</sup>	<sup>3)</sup>
83	Melody Shipping 5 Limited, Douglas, Isle of Man	0.00	0.00		<sup>3)</sup>	<sup>3)</sup>
84	Melody Shipping 6 Limited, Douglas, Isle of Man	0.00	0.00		<sup>3)</sup>	<sup>3)</sup>
85	Mersey Viking Limited, Hong Kong, Hong Kong <sup>14)</sup>	58.85	58.85	EUR	–15,710,100.00	–119,168.00
86	Watling Street Shipping Limited, London, Great Britain <sup>14)</sup>	58.85	58.85	EUR	–36,712,473.00	–126,682.00

**UNCONSOLIDATED ASSOCIATES**

Serial no.	Name/Place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
87	FSP CAPCELLENCE Beteiligungs GmbH, Hamburg <sup>1)</sup>	100.00	40.00	EUR	<sup>3)</sup>	<sup>3)</sup>
88	Global Format GmbH & Co. KG, Munich	28.57	28.57	EUR	1,821,428.72	300,491.75
89	HGA New Office Campus-Kronberg GmbH & Co. KG, Hamburg	56.44	56.44	EUR	10,329,220.34	–10,893,822.20
90	KAIACA LLC, New York, USA <sup>14)</sup>	55.30	55.30	USD	20,069.83	0.00
91	4Wheels Management GmbH, Düsseldorf <sup>1) 10)</sup>	68.75	40.00	EUR	13,733,996.12	–106,160.06

## EQUITY HOLDINGS IN NON-AFFILIATED COMPANIES

Serial no.	Name/Place	Share	Voting rights	Currency code	Equity capital in respective currency	Income/loss in respective currency
92	AKA Ausfuhrkredit-Gesellschaft mbH, Frankfurt am Main	1.33	1.33	EUR	212,967,103.15	16,035,000.00
93	Aprel Shipping (M) Inc., Majuro, Marshall Islands	15.00	15.00	USD	4,953,000.00	5,548,000.00
94	Arzel Shipping (M) Inc., Majuro, Marshall Islands	15.00	15.00	USD	14,343,000.00	6,258,000.00
95	Börse Düsseldorf AG, Düsseldorf	0.89	0.89	EUR	52,746,704.62	472,746.76
96	BRINKHOF Holding Deutschland GmbH, Erfurt <sup>1)</sup>	100.00	0.00	EUR	<sup>5)</sup>	<sup>5)</sup>
97	CapVis Equity III L.P., St. Helier, Jersey <sup>1)</sup>	2.50	0.00	EUR	408,156,000.00	43,738,000.00
98	Concardis GmbH, Eschborn	2.82	2.82	EUR	74,914,467.89	24,201,836.30
99	CVC European Equity Partners V (A) L.P., George Town, Cayman Inseln <sup>1)</sup>	0.45	0.00		<sup>6)</sup>	<sup>6)</sup>
100	Deutsche WertpapierService Bank AG, Frankfurt am Main	2.51	2.51	EUR	182,463,038.56	11,127,973.52
101	EURO Kartensysteme GmbH, Frankfurt am Main	2.82	2.82	EUR	329,788,080.07	65,637.36
102	GB Deutschland Fund GmbH & Co. KG, Hamburg <sup>1)</sup>	4.69	0.00	EUR	17,688,000.00	-6,517,000.00
103	GLB GmbH & Co. OHG, Frankfurt am Main	15.77	15.77	EUR	5,423,813.50	729,100.85
104	GLB-Verwaltungs-GmbH, Frankfurt am Main	15.80	15.80	EUR	49,752.16	2,263.60
105	Hamburgische Grundbesitz und Anlage GmbH & Co. Objekte Hamburg und Potsdam KG, Hamburg	5.15	5.16	EUR	9,999,359.85	1,059,994.97
106	Hapag-Lloyd Aktiengesellschaft, Hamburg	1.63	1.63	EUR	5,046,200,000.00	113,900,000.00
107	HCI Hammonia Shipping AG, Hamburg	6.60	6.60	EUR	1,864,000.00	1,768,000.00
108	HGA Objekt Frankfurt GmbH & Co. KG, Hamburg	5.97	5.97	EUR	16,071,951.06	14,471,536.75
109	HGA Objekt München GmbH & Co. KG, Hamburg	5.23	5.23	EUR	9,934,058.53	-1,468,807.32
110	HGA Objekt Stuttgart GmbH & Co. KG, Hamburg	7.25	7.26	EUR	10,169,843.94	471,406.64
111	HGA Objekte Hamburg und Hannover GmbH & Co. KG, Hamburg	5.10	5.09	EUR	4,832,393.52	4,613,393.42
112	Hines European Development Fund Limited Partnership, Houston, USA <sup>1)</sup>	9.90	9.90	EUR	65,879,000.00	152,574,000.00
113	Liquiditäts-Konsortialbank GmbH i.L., Frankfurt am Main <sup>11)</sup>	1.68	1.68	EUR	230,536,114.28	-5,996,151.33
114	RSU Rating Service Unit GmbH & Co KG, Munich	13.60	13.60	EUR	14,279,529.49	1,158,674.44
115	Scan Energy, Frederikshavn, Denmark	7.61	7.61		<sup>5)</sup>	<sup>5)</sup>
116	Society for Worldwide Interbank Financial Telecommunication (S.W.I.F.T. SCRL), La Hulpe, Belgium	0.04	0.04	EUR	387,876,000.00	19,498,000.00
117	True Sale International GmbH, Frankfurt am Main	7.69	7.69	EUR	4,763,001.53	70,864.16
118	UNI-ASIA HOLDINGS LIMITED, Grand Cayman, Cayman Islands	2.66	2.66	USD	140,174,000.00	3,520,000.00
119	Vofü-Fonds I Hamburgische Grundbesitz und Anlage GmbH & Co. KG, Hamburg	5.10	5.09	EUR	-802,385.90	1,223,488.33

<sup>1)</sup> Indirect holding.

<sup>2)</sup> A profit transfer agreement with the company is in place.

<sup>3)</sup> No information available due to newly established company.

<sup>4)</sup> There is a profit transfer agreement with HSH Facility Management GmbH.

<sup>5)</sup> No information available due to insolvency of the company.

<sup>6)</sup> No data available.

<sup>7)</sup> Only data as at 31 December 2010 is available.

<sup>8)</sup> Only data as at 30 November 2014 is available.

<sup>9)</sup> Only data as at 31 December 2014 is available.

<sup>10)</sup> Only data as at 31 July 2015 is available.

<sup>11)</sup> Only data as at 02 November 2015 is available.

<sup>12)</sup> Only data as at 09 December 2015 is available.

<sup>13)</sup> Joint control was explicitly agreed by contract, therefore the company is not a subsidiary despite a voting majority.

<sup>14)</sup> This is not a subsidiary due to the requirement for a qualified voting majority for important decisions.

## FOREIGN EXCHANGE RATES FOR € 1 AS AT 31/12/2016

Great Britain	GBP	0.8562
USA	USD	1.0541



## 69. OTHER DISCLOSURES IN ACCORDANCE WITH GERMAN COMMERCIAL LAW

### I. Basic principles

Under the terms of Section 315a (1) HGB, HSH Nordbank AG, which has its registered office in Hamburg (Hamburg commercial register number HRB 87366) and Kiel (Kiel commercial register number HRB 6127 KI) is required to observe the standards of the German Commercial Code in preparing and presenting the annual financial statements, as well as the IFRS standards. You may request the unabridged IFRS Group financial statements by following this link: [www.hsh-nordbank.com](http://www.hsh-nordbank.com). The complete list of equity holdings is set out in Note 68.

HSH Facility Management GmbH, Hamburg, makes use of the exemption from disclosure obligations in accordance with Section 264 (3) HGB.

### II. Number of employees

The average number of employees as of the reporting date is calculated on the basis of staff figures at quarter-end for all fully consolidated companies:

#### NUMBER OF EMPLOYEES

	2016			2015
	Male	Female	Total	Total
Full-time employees	1,311	490	1,801	1,984
Part-time employees	132	566	698	726
<b>Total</b>	<b>1,443</b>	<b>1,056</b>	<b>2,499</b>	<b>2,710</b>
Apprentices/trainees	21	15	36	37

### III. Corporate governance code

HSH Nordbank AG supports the aims of the German Corporate Governance Code and has recognised the Code's rules on a voluntary basis as an unlisted company. The Management Board and Supervisory Board of HSH Nordbank AG have given a declaration of conformity pursuant to Section 161 of the German Stock Corporation Act (AktG) that the recommendations of the German Corporate Governance Code Commission together with the restrictions have been complied with and will be complied with until the subsequent declaration is made. The declaration of conformity is published on HSH Nordbank AG's website and printed in the 2016 Annual Report.

Out of the provisions set up in the previous year for the auditor's fees, € 1 million was reversed in favour of other operating income.

### V. Seats on supervisory bodies

On the reporting date, the following seats are held by members of the Management Board on statutory supervisory bodies of major corporations or financial institutions:

#### Ulrik Lackschewitz

HSH Nordbank Securities S.A., Luxembourg  
Chairman of the Administrative Board

### IV. Auditor's fees

#### AUDITOR'S FEES

(€ m)	2016	2015
Audits KPMG AG	5	8
Other certification and valuation services provided by KPMG AG	2	2
Other services provided by KPMG AG	3	3
<b>Total</b>	<b>10</b>	<b>13</b>

## 70. NAMES OF BOARD MEMBERS AND DIRECTORSHIPS HELD

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### I. The Supervisory Board of the HSH Nordbank Group

#### **Dr Thomas Mirow, Hamburg**

Chair

Former President of the European Bank for Reconstruction and Development, London

#### **Olaf Behm, Hamburg**

Deputy Chair

Employee of HSH Nordbank AG

#### **Stefanie Arp, Norderstedt**

Employee of HSH Nordbank AG

#### **Sabine-Almut Auerbach, Neumünster**

(until 31 March 2016)

District secretary, ver.di Southern Holstein district

#### **Peter Axmann, Hamburg**

Employee of HSH Nordbank AG

#### **Simone Graf, Altenholz**

Employee of HSH Nordbank AG

#### **Silke Grimm, Reinbek**

Member of the Board of Euler Hermes Deutschland AG

#### **Cornelia Hintz, Dortmund**

(from 18 May 2016)

Federal state secretary ver.di district North Rhine-Westphalia

#### **Stefan Jütte, Bonn**

Former Chairman of the Management Board of Deutsche Postbank AG

#### **Dr Rainer Klemmt-Nissen, Hamburg**

Managing Director, HGV Hamburger Gesellschaft für Vermögens- und Beteiligungsmanagement mbH

#### **Rieka Meetz-Schawaller, Kiel**

Employee of HSH Nordbank AG

#### **Dr David Morgan, London**

Managing Director J.C. Flowers & Co. UK Ltd.

#### **Dr Philipp Nimmermann, Kiel**

Secretary of State at the Schleswig-Holstein Ministry of Finance

#### **Stefan Schlatermund, Hamburg**

Employee of HSH Nordbank AG

#### **Klaus-Dieter Schwetscher, Reinbek**

Representative of ver.di's federal management board

#### **Elke Weber-Braun, Hamburg**

Independent chartered accountant

#### **Jörg Wohlers, Rellingen**

Former Member of the Board of Hamburger Sparkasse AG and HASPA Finanzholding

**II. Members of the Risk Committee**

**Stefan Jütte**  
Chair

**Olaf Behm**

**Simone Graf**

**Dr Rainer Klemmt-Nissen**

**Rieka Meetz-Schawaller**

**Dr Thomas Mirow**

**Dr David Morgan**  
(until 31 December 2016)

**Dr Philipp Nimmermann**  
(from 1 January 2017)

**Stefan Schlatermund**

**III. Members of the Audit Committee**

**Elke Weber-Braun**  
Chair

**Stefanie Arp**

**Peter Axmann**

**Olaf Behm**

**Dr Philipp Nimmermann**

**Jörg Wohlers**

**IV. Members of the General/Nomination Committee****Dr Thomas Mirow**

Chair

**Olaf Behm****Simone Graf****Dr Rainer Klemmt-Nissen****Dr David Morgan****Dr Philipp Nimmermann****Jörg Wohlers****V. Members of the Remuneration Monitoring Committee****Dr Thomas Mirow**

Chair

**Olaf Behm****Simone Graf****Silke Grimm****Dr Rainer Klemmt-Nissen****Dr Philipp Nimmermann****VI. Members of the Mediation Committee****Dr Thomas Mirow**

Chair

**Olaf Behm****Dr Rainer Klemmt-Nissen****Rieka Meetz-Schawaller**

## **VII. The Management Board of the HSH Nordbank Group**

### **Stefan Ermisch**

Born in 1966

Chairman of the Management Board (since 10 June 2016)

Chief Financial Officer (until 30 June 2016)

### **Oliver Gatzke**

(from 1 July 2016)

Born in 1968

Chief Financial Officer

### **Ulrik Lackschewitz**

Born in 1968

Chief Risk Officer

### **Torsten Temp**

Born in 1960

Management Board member responsible for the Market divisions

### **Constantin von Oesterreich**

(until 9 June 2016)

Born in 1953

Chairman of the Management Board

### **Matthias Wittenburg**

(until 9 June 2016)

Born in 1968

Corporates & Markets

## ANNEX TO THE GROUP FINANCIAL STATEMENTS

### COUNTRY-BY-COUNTRY REPORTING 2016

#### Basic principles

The requirements for country-specific reporting, referred to as country-by-country reporting in Article 89 of the Directive 2013/36/EU (Capital Requirement Directive, CRD IV), have been transposed into German law in Section 26a (1) of the German Banking Act (KWG).

#### Disclosure at HSH Nordbank

HSH Nordbank country-by-country reporting includes the necessary information for all the subsidiaries fully consolidated in the Group financial statements as of this reporting date. Entities that were deconsolidated during the reporting year are not included in the figures presented. The geographical allocation is made on the basis of the location of a company's registered office. Branches are disclosed as independent companies. Representative offices are not listed. All accounting-related information is based on IFRS accounting.

In this report, HSH Nordbank defines the required size of turnover as the sum of total income as presented in the income statement and Other operating income (gross amounts before consolidation). The consolidated non-bank entities in particular report their turnover in Other operating income.

The profit or loss before tax disclosed in this report corresponds to the result before taxes of the individual entities presented. The tax position also corresponds to the definition under IFRS standards in the income statement.

HSH Nordbank has been granted a guarantee facility of € 10 billion by its owners. It is a second loss guarantee in which rating-induced actual payment defaults are secured. Please refer to Note 3 for more details.

The figure for the number of employees corresponds to the arrangement of Section 267 (5) of the German Commercial Code (HGB) for the entities still included in the Group financial statements as of the reporting date.

The information on the type of activities of the relevant companies is presented in line with the definitions used in Article 4 (1) CRR once the CRR came into effect.

The return on capital to be disclosed as at 31 December 2016, calculated as the quotient of net profit (Group net result after taxes) and total assets, is 0.08%.



## Reporting

## COUNTRY-SPECIFIC DETAILS OF TURNOVER, PROFIT OR LOSS AND TAXES AS WELL AS EMPLOYEE NUMBERS

<b>(€ m/number)</b>				
<b>2016</b>				
Country	Turnover	Profit or loss before tax	Tax on profit or loss	Number of employees
<b>EU</b>				
Germany	970	155	51	2,381
Luxembourg	118	61	7	67
Ireland	31	-32	-	-
Spain	5	-4	-	-
Greece	2	-	-	8
<b>Third countries</b>				
USA	8	1	-	-
Singapore	42	-27	-5	43
British Channel Islands	1	1	-	-
Hong Kong	1	1	-	-
Bermuda	1	1	-	-
Cayman Islands	38	33	-	-

## COUNTRY-SPECIFIC DETAILS OF THE HEDGING EFFECT OF THE SECOND LOSS GUARANTEE AS STATE AID RECEIVED

<b>(€ m)</b>	Country		
	EU		Third countries
	Germany	Luxembourg	Singapore
<b>2016</b>			
<b>Balance sheet amounts</b>			
Compensation under the second loss guarantee	7,102	538	214
Compensation under the credit derivative second loss guarantee	144	35	20

<b>(€ m)</b>	Country		
	EU		Third countries
	Germany	Luxembourg	Singapore
<b>2016</b>			
<b>P&amp;L amounts</b>			
Hedging effect of the second loss guarantee	2,071	153	60
Hedging effect of credit derivative under the second loss guarantee	-458	-6	-11
Expenses for government guarantees	-188	-22	-4

**NATURE OF ACTIVITIES AND GEOGRAPHICAL LOCATION OF THE BRANCHES AND FULLY CONSOLIDATED SUBSIDIARIES**

<b>Serial no.</b>	<b>Name of the company</b>	<b>City</b>	<b>Country</b>	<b>Nature of activities</b>
1	HSH Nordbank AG	Hamburg, Kiel	Germany	Bank
2	HSH Nordbank AG, Luxembourg branch	Luxembourg	Luxembourg	Bank
3	HSH Nordbank AG, Singapore branch	Singapore	Singapore	Bank
4	HSH Nordbank AG, Athens branch	Athens	Greece	Bank
5	Adessa Grundstücksverwaltungsgesellschaft mbH & Co Vermietungs KG	Mainz	Germany	Miscellaneous activities
6	Amentum Aircraft Leasing No. Five Limited	Dublin	Ireland	Miscellaneous activities
7	Amentum Aircraft Leasing No. Six Limited	Dublin	Ireland	Miscellaneous activities
8	Amentum Aircraft Leasing No. Seven Limited	Dublin	Ireland	Miscellaneous activities
9	Avia Management S.à.r.l.	Luxembourg	Luxembourg	Financial Institution
10	BINNENALSTER-Beteiligungsgesellschaft mbH	Hamburg	Germany	Financial Institution
11	Bu Wi Beteiligungsholding GmbH	Hamburg	Germany	Financial Institution
12	CAPCELLENCE Erste Fondsbeteiligung GmbH	Hamburg	Germany	Financial Institution
13	CAPCELLENCE Holding GmbH & Co. KG	Hamburg	Germany	Financial Institution
14	Capcellence Vintage Year 06/07 Beteiligungen GmbH & Co. KG	Hamburg	Germany	Financial Institution
15	Capcellence Vintage Year 07/08 Beteiligungen GmbH & Co. KG	Hamburg	Germany	Financial Institution
16	CAPCELLENCE Vintage Year 11 Beteiligungen GmbH & Co. KG	Hamburg	Germany	Financial Institution
17	CAPCELLENCE Vintage Year 13 Beteiligungen GmbH & Co. KG	Hamburg	Germany	Financial Institution
18	CAPCELLENCE Vintage Year 16 Beteiligungen GmbH & Co. KG	Hamburg	Germany	Financial Institution
19	CAPCELLENCE Zweite Fondsbeteiligung GmbH	Hamburg	Germany	Financial Institution
20	CAPCELLENCE Dritte Fondsbeteiligung GmbH	Hamburg	Germany	Financial Institution
21	Castellum ABF S.A.	Luxembourg	Luxembourg	Miscellaneous activities
22	DEERS Green Power Development Company S.L.	Madrid	Spain	Miscellaneous activities
23	FSL Asset Management Pte. Ltd.	Singapore	Singapore	Provider of ancillary services
24	FSL Holdings Pte. Ltd.	Singapore	Singapore	Financial Institution
25	FSL Trust Management Pte. Ltd.	Singapore	Singapore	Provider of ancillary services
26	GmbH Altstadt Grundstücksgesellschaft	Mainz	Germany	Financial Institution
27	GODAN GmbH	Hamburg	Germany	Financial Institution
28	HSH Auffang- und Holdinggesellschaft mbH & Co. KG	Hamburg	Germany	Financial Institution

<b>Serial no.</b>	<b>Name of the company</b>	<b>City</b>	<b>Country</b>	<b>Nature of activities</b>
29	HSH Care+Clean GmbH	Hamburg	Germany	Miscellaneous activities
30	HSH Facility Management GmbH	Hamburg	Germany	Provider of ancillary services
31	HSH Gastro+Event GmbH	Hamburg	Germany	Miscellaneous activities
32	HSH Move+More GmbH	Kiel	Germany	Miscellaneous activities
33	HSH N Finance (Guernsey) Limited	St. Peter Port	Guernsey	Financial Institution
34	HSH N Funding II	George Town	Cayman Islands	Financial Institution
35	HSH N Residual Value Ltd.	Hamilton	Bermuda	Insurance company
36	HSH Nordbank Securities S.A.	Luxembourg	Luxembourg	Bank
37	HSH Private Equity GmbH	Hamburg	Germany	Financial Institution
38	Ilex Integra GmbH	Hamburg	Germany	Financial Institution
39	ISM Agency, LLC	New York	USA	Miscellaneous activities
40	Life Insurance Fund Elite LLC	New York	USA	Miscellaneous activities
41	Life Insurance Fund Elite Trust	Minneapolis	USA	Miscellaneous activities
42	Mitco Real Estate A S.a.r.l.	Canach	Luxembourg	Miscellaneous activities
43	Mitco Resolution 1 S.a.r.l.	Canach	Luxembourg	Miscellaneous activities
44	Mitco Resolution 2 S.a.r.l.	Canach	Luxembourg	Miscellaneous activities
45	Mitco Resolution 3 S.a.r.l.	Canach	Luxembourg	Miscellaneous activities
46	Mitco Resolution 4 S.a.r.l.	Canach	Luxembourg	Miscellaneous activities
47	Mitco Resolution 5 S.a.r.l.	Canach	Luxembourg	Miscellaneous activities
48	Neptune Finance Partner S.à.r.l.	Luxembourg	Luxembourg	Financial Institution
49	Neptune Finance Partner II S.à.r.l.	Luxembourg	Luxembourg	Financial Institution
50	Next Generation Aircraft Finance 2 S.à.r.l.	Findel	Luxembourg	Miscellaneous activities
51	Next Generation Aircraft Finance 3 S.à.r.l.	Findel	Luxembourg	Miscellaneous activities
52	OCEAN Funding 2013 GmbH	Frankfurt am Main	Germany	Miscellaneous activities
53	RDM Limited	George Town	Cayman Islands	Miscellaneous activities
54	RESPARCS Funding Limited Partnership I	Hong Kong	Hong Kong	Financial Institution
55	RESPARCS Funding II Limited Partnership	St. Helier	Jersey	Financial Institution
56	Senior Assured Investment S.A.	Luxembourg	Luxembourg	Miscellaneous activities
57	Senior Preferred Investments S.A.	Luxembourg	Luxembourg	Miscellaneous activities
58	Solar Holdings S.à.r.l.	Luxembourg	Luxembourg	Financial Institution
59	Stratus ABF S.A.	Luxembourg	Luxembourg	Miscellaneous activities
60	Unterstützungs-Gesellschaft der Hamburgischen Landesbank mit beschränkter Haftung i.L.	Hamburg	Germany	Provider of ancillary services
61	2200 Victory LLC	Dover	USA	Miscellaneous activities

**DATE OF RELEASE FOR PUBLICATION**

The Management Board of HSH Nordbank has prepared the Group financial statements on 14 March 2017 and released these for forwarding to the Supervisory Board. The Supervisory Board is responsible for reviewing the Group financial statements and approving of these.

Hamburg/Kiel, 14 March 2017

Stefan Ermisch

Oliver Gatzke

Ulrik Lackschewitz

Torsten Temp

## AUDITOR'S REPORT

We have audited the consolidated financial statements prepared by HSH Nordbank AG, Hamburg and Kiel, comprising the statement of financial position, the income statement, the statement of comprehensive income, the statement of changes in equity, the statement of cash flows and the notes, together with the group management report for the business year from 1 January to 31 December 2016. The preparation of the consolidated financial statements and the group management report in accordance with IFRSs, as adopted by the EU, and with the additional requirements of German commercial law pursuant to Section 315a (1) HGB [Handelsgesetzbuch "German Commercial Code"] are the responsibility of the company's Management Board. Our responsibility is to express an opinion on the consolidated financial statements and on the group management report based on our audit.

We conducted our audit of the consolidated financial statements in accordance with Section 317 HGB and German generally accepted standards for the audit of financial statements promulgated by the Institute of Public Auditors in Germany (IDW). Those standards require that we plan and perform the audit such that misstatements materially affecting the presentation of the net assets, financial position and results of operations in the consolidated financial statements in accordance with the applicable financial reporting framework and in the group management report are detected with reasonable assurance. Knowledge of the business activities and the economic and legal environment of the group and expectations as to possible misstatements are taken into account in the determination of audit procedures. The effectiveness of the accounting-related internal control system and the evidence supporting the disclosures in the consolidated financial statements and the group management report are examined primarily on a test basis within the framework of the audit. The audit includes assessing the annual financial statements of those entities included in consolidation, the determination of entities to be included in consolidation, the accounting and consolidation principles used and significant estimates made by the Management Board, as well as evaluating the overall presentation of the consolidated financial statements and group management report. We believe that our audit provides a reasonable basis for our opinion.

Our audit has not led to any reservations.

In our opinion, based on the findings of our audit, the consolidated financial statements comply with IFRSs, as adopted by the EU, with the additional requirements of German commercial law pursuant to Section 315a (1) HGB and give a true and fair view of the net assets, financial position and results of operations of the group in accordance with these requirements. The group management report is consistent with the consolidated financial statements, complies with the statutory provisions and as a whole provides a suitable view of the Group's position and suitably presents the opportunities and risks of future development.

Without qualifying this opinion, we refer to the discussion in the group management report in the paragraph "Opportunities and risks resulting from the formal decision in the EU state aid proceedings" as well as to Note 1 to the consolidated financial statements. It is stated there that the going concern assumption for accounting and measurement purposes and the assumption of the continued going concern of HSH Nordbank AG and significant group companies is based in particular on the following assumptions:

(i) the agreements required for the implementation of the decision taken by the EU Commission in the EU state aid proceedings on the replenishment of the second loss guarantee are entered into comprehensively and on a timely basis and that the decision will be implemented by HSH Nordbank AG and its shareholders in full and on a timely basis.

(ii) the operating company, HSH Nordbank AG, is sold at a positive sales price in an open, non-discriminatory, competitive and transparent process not involving state aid until 28 February 2018 and the EU Commission grants its approval for the acquisition following a viability assessment of the new corporate structure. Should the divestment procedure not lead to offers not requiring state aid with a positive price being offered before the expiry of the deadline or should the EU Commission in the course of its viability assessment come to the conclusion that the integration of the operating company into the new corporate structure will not lead to a viable business model that is profitable in the long term, the operating company will cease new business and manage its assets as far as legally permissible with the aim of a structured winding down of its business. In the event that the bank is wound down as a result of the above or for other reasons, or if its rating is downgraded or other adverse developments emerge during the privatisation period, it could trigger outflows of short-term funds and fundamentally restrict HSH Nordbank's funding options. In the case of major unexpected fund outflows, additional measures will need to be taken by the owners and/or third parties to strengthen the liquidity situation.

(iii) as part of the ongoing privatisation process of HSH Nordbank AG, HSH Nordbank AG will be sold in full as a whole bank, i.e. the shares in the Bank held by the seller will be disposed of, including all assets and liabilities, without any material early disposals of assets or sub-segments at prices below the carrying amount in the event of outstanding bids for an overall sale. If extensive sales of loan portfolios, particularly in the Non-Core Bank, are required, it could result in significant additional loan loss provision expenses that are not compensated for by the guarantee, and could require material depreciation of deferred taxes.

(iv) the minimum capital requirements at all regulatory levels can be adhered to in accordance with the corresponding SREP resolutions passed by the European Central Bank and the statutory provisions during the forecast period. If there is a need for significant additional loan loss provision expenses and material depreciation of deferred taxes (e. g. in the scenario described above) or if the recovery of the shipping market that has been assumed in the Bank's corporate planning does not materialise as planned, or the significant risk transfer for the second loss guarantee is no longer ensured from the perspective of the banking supervisory authority, it could put considerable pressure on the capital ratios and additional measures may need to be taken by the owners and/or third parties to strengthen the capital ratios in order to be able to adhere to the minimum capital requirements, particularly at the level of the financial holding group. If such measures are not taken, it could result in the winding down of HSH Nordbank.

It is further required that acceptance by market participants and other relevant stakeholders necessary for the successful implementation of

HSH Nordbank AG's business model and the requirements under the formal decision of the EU Commission is maintained or gained.

Hamburg, 15 March 2017

KPMG AG  
Wirtschaftsprüfungsgesellschaft

Leitz  
Wirtschaftsprüfer

Thiede  
Wirtschaftsprüfer



## RESPONSIBILITY STATEMENT BY THE MANAGEMENT

We hereby affirm that to the best of our knowledge the Group financial statements have been prepared in accordance with the applicable accounting principles and give a true and fair view of the net assets, financial position and results of operations of the HSH Nordbank Group and that the Group management report presents the course of business, including the results of the business and the HSH Nordbank Group's situation, in such a manner that it gives a true and fair view and describes the main opportunities and risks for the HSH Nordbank Group's foreseeable performance.

Hamburg/Kiel, 14 March 2017

Stefan Ermisch

Oliver Gatzke

Ulrik Lackschewitz

Torsten Temp

**INFO**

# FURTHER FORMATION

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# HSH NORDBANK ADVISORY BOARD

**HSH NORDBANK AG FORMED AN  
ADVISORY BOARD**

to provide the Management Board with expert advice on performing its duties and to foster contact with the business community and the savings banks as well as any other Groups of public life. The members of the Advisory Board are being appointed by the Management Board.



**MEMBERS OF THE ADVISORY BOARD**

**Ulrich Boike**

Deputy Chairman of the Board of Management  
Förde Sparkasse  
Kiel

**Reinhard Boll**

President  
of the Savings Banks Association of Schleswig-Holstein  
Kiel

**Thomas H. Eckelmann**

Chairman of the Group Management Board  
EUROKAI KGaA  
Hamburg

**Michael Eggenschwiler**

Chairman of the Management Board  
Flughafen Hamburg GmbH  
(since 01.07.2016)

**Jutta Humbert**

Managing Partner  
NORD DRIVESYSTEMS Gruppe  
Bargteheide

**Jan Christoph Kersig**

Managing Director  
Kersig GmbH & Co. KG  
Kiel

**Dr. Johann Killinger**

Managing Partner  
Buss Group GmbH & Co. KG  
Hamburg

**Jochen Klösges**

Chief Executive Officer  
E.R. Capital Holding GmbH & Cie. KG  
Hamburg

**Max-Arnold Köttgen**

Member of the Board of Management  
REMONDIS SE & Co. KG  
Hamburg  
(since 01.05.2016)

**Angela Krüger-Steinhoff**

Managing Partner  
Steinhoff Familienholding GmbH  
Westerstede

**Dirk Lütje**

Managing Director  
CITTI Handelsgesellschaft mbH & Co. KG  
Kiel  
(until 04.05.2016)

**Fritz Horst Melsheimer**

President of the Hamburg Chamber of Commerce  
Hamburg

**Dr. Claus-Georg Nette**

Member of the Board of Management  
Marquard & Bahls AG  
Hamburg

**Dr. Arend Oetker**

Managing Partner  
Dr. Arend Oetker Holding GmbH  
Berlin

**Prof. Dr. med. Jens Scholz**

Chairman of the Board  
University Hospital Schleswig-Holstein  
Kiel  
(since 03.06.2016)

**Frank Schumacher**

Chairman of the Board of Management  
Sparkasse zu Lübeck AG  
Lübeck

**Katharina Strümpell**

Partner and Authorized Officer (Prokuristin)  
Linnhoff Schiffahrt GmbH & Co. KG  
Buxtehude  
(until 31.12.2016)

**Dr. Fritz Süverkrüp**

Honorary President  
Kiel Chamber of Industry and Commerce  
Kiel

**Egbert Tölle**

Member of the Board of Management  
REMONDIS SE & Co. KG  
Lünen  
(until 30.04.2016)

**Prof. Dr. Henning Vöpel**

Director  
Hamburg Institute of International Economics  
Hamburg  
(since 04.07.2016)

**Dr. Harald Vogelsang**

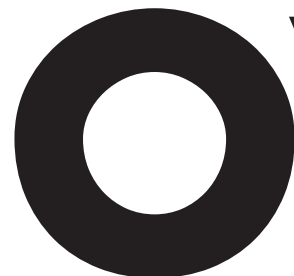
Speaker of the Board of Management  
Hamburger Sparkasse AG  
Hamburg  
(until 31.12.2016)

**Pieter Wasmuth**

Chairman of the Management Board  
Vattenfall Wärme Hamburg GmbH  
Chairman  
Vattenfall Europe Nuclear Energy GmbH  
General Executive (Generalbevollmächtigter)  
of Hamburg and Northern Germany of Vattenfall GmbH  
Hamburg  
(since 09.06.2016)

**Johannes Züll**

Chairman of the Management Board  
Studio Hamburg GmbH  
Hamburg  
(since 02.07.2016)





# MULTI- YEAR VERVIEW

HSH NORDBANK GROUP 2012 - 2016	2016	FOLLOWING ADJUSTMENT			
		2015	2014	2013	2012
<b>INCOME STATEMENT (€ M)</b>					
Net income before restructuring	445	954	883	- 48	160
Net income before taxes	121	450	287	- 518	- 185
Group net result for the year	69	98	160	- 769	- 124
<b>BALANCE SHEET (€ M)</b>					
Equity	4.950	4.885	4.672	4.579	5.272
Total assets	84.365	96.973	110.082	109.111	130.606
Business volume	93.208	106.176	119.880	118.729	138.515
<b>CAPITAL RATIOS<sup>1)</sup> (%)</b>					
Tier 1 capital ratio	18,7	16,4	14,4	15,3	12,3
Regulatory capital ratio	24,8	20,6	18,7	23,8	19,1
<b>EMPLOYEES<sup>2)</sup></b>					
Total	2.613	2.838	3.072	3.391	3.750
Germany	2.497	2.702	2.897	3.150	3.411
Abroad	116	136	175	241	339

<sup>1)</sup> After having established the annual financial statements 2016

<sup>2)</sup> Headcount

# CONTACT

HSH Nordbank AG  
Gerhart-Hauptmann-Platz 50  
20095 Hamburg, Germany  
Phone +49 40 3333-0  
Fax +49 40 3333-34001

Martensdamm 6  
24103 Kiel, Germany  
Phone +49 431 900-01  
Fax +49 431 900-34002

info@hsh-nordbank.com  
www.hsh-nordbank.de

## INVESTOR RELATIONS

Phone +49 40 3333-11500/-25421  
investor-relations@hsh-nordbank.com

## PRESS RELATIONS

Phone +49 40 3333-12973  
Fax +49 40 3333-34224  
presse@hsh-nordbank.com

## MARKETING & DIGITAL MEDIA

Phone +49 40 3333-14136  
Fax +49 40 3333-34224  
marketing@hsh-nordbank.com

# IMPRINT

## PRODUCTION

Inhouse produced with FIRE.sys

## PRINTED BY

HSH Facility Management GmbH, Hamburg

## NOTE

If at times only the masculine form is used for certain terms relating to groups of people, this is not meant in a gender-specific manner, but occurs exclusively for the sake of better readability. This Annual Report was published on 30 March 2016 and is available at [www.annualreport2016.hsh-nordbank.com](http://www.annualreport2016.hsh-nordbank.com). This is an English translation of the original German version of the Annual Report.

## FORWARD-LOOKING STATEMENTS

This Annual Report includes certain forward-looking statements. These statements are based on our beliefs and assumptions as well as on conclusions drawn from information currently available to us from sources which we consider to be reliable. A forward-looking statement involves information that does not simply reflect historical facts, including information relating to possible or anticipated future growth and future economic development.

Such forward-looking statements are based on a number of assumptions concerning future events and are subject to uncertainties, risks, and other factors, many of which are beyond our control. Therefore actual events may differ considerably from those forecast in the forward-looking statements. In view of this, you are advised never to rely to an inappropriate degree on forward-looking statements. We cannot accept any liability for the accuracy or completeness of these statements or for the actual realisation of forecasts made in this Annual Report. Furthermore, we are not obliged to update the forward-looking statements following publication of this information. In addition, information contained in this Annual Report does not represent any kind of offer for the acquisition or sale of any type of securities of HSH Nordbank AG.

