The European Banking Authority (EBA) published the results from the EU-wide stress test on July 15 and market participants have been busy analyzing the outcomes. HSH Nordbank has received several inquiries from market participants and we would like to share our thoughts on the results.

Summary of core findings:

1. The stress test assumes a static balance sheet as of December 31, 2010 which then stood at €151 billion. This assumption neglects the bank’s restructuring plan as implemented in March 2009 and runs counter to our obligation to deleverage as contractually agreed with our shareholders and the German SoFFin authority.

2. Using the static balance sheet assumption as of December 31, 2010, our core Tier 1 (CT1) ratio in the adverse scenario 2012 comes to 5.5 percent. However, taking into account the actual size of €139 billion at March 31, 2011 and the further balance sheet reductions as contractually agreed, the bank’s CT1 ratio would be 9.1 percent.

3. The EBA’s decision not to count approximately €1.8 billion of silent participations as core Tier 1 capital prevents HSH Nordbank’s CT1 ratio from exceeding 10 percent.

4. The disclosure templates publish the country exposures of the 91 participating banks. HSH Nordbank has limited exposure to troubled European sovereigns and financial institutions and would be minimally affected by a debt restructuring.

Detailed Discussion:

1. Following the outbreak of the financial market crisis HSH Nordbank quickly concluded a €3.2 billion capital increase in combination with a €10 billion second loss guarantee provided by the bank’s two majority shareholders, Hamburg and Schleswig-Holstein. We simultaneously committed to drastically reduce the balance sheet size as an obligation under the capital raise. Since March 2009 we have reduced our total assets from €208 billion to €139 billion as of first quarter 2011 and we are committed to further balance sheet reductions in the coming years. This is also a requirement of the EU-state aid proceedings agreed in Brussels on June 12, 2011 between the Finance Minister of the Federal Republic of Germany and EU-commissioner in charge. Formal approval by the EU-commission is expected for late September 2011.

2. The fact that the EU-commission had not formally approved the mitigating measures by April 30, 2011, has not been accounted for in the EBA stress test calculation. The stress test only acknowledged mitigat-
ing measures which had been publicly announced and committed prior to such date. Thus, HSH Nordbank was tested on the erroneous assumption utilizing a constant balance sheet size of €151 billion. The guideline assumes that we would replenish maturing assets with new assets of like quality and tenor. This assumption does not reflect reality and runs counter to our contractual obligations to our shareholders and measures imposed by EU. As such, the CT1 ratio of **5.5 percent is not a relevant figure for HSH Nordbank.** It makes more sense to assess the bank on the basis of the planned mitigating measures given how close they are to being finalized. The resulting core Tier 1 ratio of **9.1 percent more accurately reflects the Bank’s resilience to external shocks.** Such a CT1 ratio would rank HSH Nordbank above many competitors, even when also considering their planned or already implemented mitigating measures.

3. HSH Nordbank’s outstanding silent participation capital instruments total approximately €1.8 billion. Such hybrid Tier 1 instruments have not been accepted as core Tier 1 capital in the EBA stress test despite being loss absorbing on a going-concern basis. Basel III regulations acknowledge silent participations as CT1 through 2018. Including silent participations HSH Nordbank’s CT1 ratio would exceeded 10 percent in the adverse scenario 2012.

4. The disclosure templates of the 91 participating banks provide details about each bank’s country exposure. It shows that HSH Nordbank ranks among the banks least exposed to sovereign borrowers. Even assuming drastic restructuring measures currently discussed in the press, the impact on HSH Nordbank would be marginal. Fitch Ratings has stressed the EBA results and applied haircuts of 50% for Greek sovereign and financial institutions exposure, 25% on the Portuguese sovereign and financial institutions, and 25% on the Irish sovereign risk. As a result our CT1 ratio in the adverse scenario 2012 would drop only 0.1 percentage points.

Having concluded the EU state aid investigations and with final approval by the EU commission expected shortly, HSH Nordbank has reached safe waters following the turbulent financial market crisis. We now have a reliable basis for planning our future and focusing on our core business, i.e. serving our customers in their financing needs in markets where we are acknowledged experts with a proven track record.

We will be in touch with you. Give us a call if you have questions on the EBA stress tests.