DIRECTORS' REPORT

For the six months ended June 30, 2018

Corporate Governance

HSH N Funding II (the "Company"), was incorporated on May 26, 2005 as an exempted company with limited liability under the laws of the Cayman Islands. The Company is a wholly owned subsidiary of HSH Nordbank AG (the "Bank"). The financial results of the Company are consolidated within the Bank's financial statements. The Company does not have any employees. Its day-to-day administration is delegated to MaplesFS Limited, an independent service organization, which also provides two directors to the Company from its employees for a fixed annual fee.

The Directors of the Company who held office during the period are as follows:

Cleveland Stewart (independent) (appointed September 3, 2008)
Laura Chisholm (independent) (appointed January 29, 2013).

The Directors held no interests in the Company as at June 30, 2018.

Activities and Review of the Development of the Business

The business of the Company is principally limited to the issuance of two classes of preference shares and the investment of the proceeds thereof. The terms of the Company's asset classes are similar to the terms of the Class A Preference Shares and Class B Preference Shares issued and as a result, all cash flows received are passed through or attributed to the holders of those preference shares. The value of both classes of preference shares in issue as at June 30, 2018 amounted to US$885,409,000 (June 30, 2017: US$1,054,776,324)

The principal risks the Company faces include (i) credit risk within the various asset classes, mainly the counterparty risk associated with the Bank, and (ii) liquidity risk because an illiquid secondary market could have an adverse effect on the value of the Company's assets and consequently the holders of preference shares. The direct exposure to market risk including changes in interest rates and foreign exchange rates is not significant.

The Company earned US$18,138,400 (June 30, 2017: US$18,138,400) as scheduled interest income from its asset classes during the period and paid dividends on the Class B Preference Shares of NIL (June 30, 2017: NIL).

It is not intended that the business of the Company will diversify. The Company does not engage in the field of research and development.

Impairment of financial assets

On February 6, 2013, an announcement was made by HSH Nordbank relating to financial planning which will result in net losses for the business years 2013 and 2014. The financial results from the years 2015 to 2017 will then be used to write up hybrid instruments to par value. Therefore in the Company's opinion, no such loss events have occurred during the year ended December 31, 2014 or subsequently and the reductions in the nominal amount of the Silent contribution are not considered to be permanent. Also the non-payment of coupons is not considered to be an impairment trigger as there is no obligation to pay such coupons in the event that HSH Nordbank has insufficient distributable profits. Accordingly, no impairment is required to be recognised on the Company's investment in the Silent contribution.

On February 28, 2018, a share purchase agreement was signed whereby the shares of the Bank were sold to a consortium of private equity investors. As part of the restructuring the Bank has incurred a one-time negative effect with regards to the valuation of its loan portfolio. In light of this as well as other effects of the privatization, the Bank will not be able to make distributions in respect of the Participation Agreement for the fiscal year 2019 as originally expected but at the earliest from the fiscal year 2024 for the fiscal year 2023.

Following the adoption of IFRS 9 on January 1, 2018, the Company recognised an initial impairment adjustment of US$13,870,371 on its loan receivable. For the period ended June 30, 2018, the Company recognised a further impairment adjustment of US$1,246,918.

Going Concern

Due to the limited recourse nature of the Company's contractual arrangements, the Directors of the Company are of the opinion that the Company will be able to pay its debts as they fall due. Therefore, the financial statements have been prepared on a going concern basis, notwithstanding the current financial position of the Company and the carrying values of the Company's asset classes which were predominantly issued by the Bank.

Results and Allocation

The Company reported a profit for the period of US$16,887,367 (June 30, 2017: US$15,567,595) and issued NIL Class A Preference Shares.

All potential profit or losses which may crystallize as a result of the Company holding or realizing its asset classes will be attributed to the holders of the preference shares and not to the Company itself.

Management's Statement of Responsibility for Financial Reporting

The financial statements of the Company have been prepared by management. Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards. This responsibility includes: designing, implementing and maintaining internal controls relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error, selecting and applying appropriate accounting policies or making accounting estimates that are reasonable in the circumstances.

Statement on True and Fair View

The Directors of the Company state that, to the best of their knowledge:
- the unaudited financial statements dated as at June 30, 2018, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Company; and

- this report gives a true and fair view of the state of affairs of the Company as at the reporting date and of the course of affairs during the financial period of the Company together with a description of the principal risks the Company faces.

For and on behalf of the Board of Directors of the Company on 20 Sept, 2018

Cleveland Stewart, Director

Financial Statements of

HSH N FUNDING II

June 30, 2018

(compiled without audit or review)

HSH N FUNDING II

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HSH N FUNDING II

Statement of Financial Position

June 30, 2018 and December 31, 2017 *(compiled without audit or review)*
(stated in United States dollars)

	Note	Jun 30, 2018	Dec 31, 2017
Assets			
Silent Contribution	3,7,8	240,724,493	260,413,608
Loan receivable	4,7,8	537,882,711	553,000,000
Interest receivable	4,7,8	9,069,200	9,069,200
Cash and cash equivalents	7,8	18,341,994	203,594
Total assets	US$	**806,018,398**	**822,686,402**
Liabilities and Equity			
Liabilities			
Class B preference shares	5,8	240,375,000	321,955,951
Other liabilities		1,528	1,528
		240,376,528	321,957,479
Equity			
Share capital	6	10,000	10,000
Class A preference shares	6	645,034,000	645,034,000
Revaluation reserve	2(d)(viii)	-	(178,203,088)
Retained (accumulated loss)/earnings		(79,402,130)	33,888,011
		565,641,870	500,728,923
Total liabilities and equity	US$	**806,018,398**	**822,686,402**

See accompanying notes to financial statements.

Approved on ~~behalf~~ of the Board of Directors on 17 Sept., 2018

________________Director Cleveland Stewart

L Chisholm________Director Laura Chisholm

HSH N FUNDING II

Statement of Comprehensive Income

For the six months ended June 30, 2018 and 2017 *(compiled without audit or review)*
(stated in United States dollars)

	Note	2018	2017
Income			
Net change in revised discounted cash flows (Silent Contribution)	2(d)(viii),3	-	11,406,797
Interest income on loan	4,7	18,138,400	18,138,400
Net change in fair value of financial liabilities		19,685,000	-
		37,823,400	29,545,197
Finance costs			
Net change in revised discounted cash flows (Class B preference shares)	2(d)(viii),5	-	13,977,602
Impairment on loan receivable		1,246,918	-
Net change in fair value of financial assets		19,689,115	-
		20,936,033	13,977,602
Net income for period	US$	16,887,367	15,567,595
Other comprehensive loss			
Net change in fair value of available-for-sale financial assets	2(d)(viii),3	-	(997,845)
		-	(997,845)
Comprehensive income for the period	US$	16,887,367	14,569,750

See accompanying notes to financial statements.

HSH N FUNDING II

Statement of Changes in Equity

For the six months ended June 30, 2018 and 2017 *(compiled without audit or review)*
(stated in United States dollars)

		Note	Share Capital	Class A Preference Shares	Revaluation Reserve	Retained Earnings/ (Accumulated losses)	Total
Balance at January 1, 2017	US$		10,000	645,034,000	(361,508,238)	(3,390,511)	280,145,251
Net income for period			-	-	-	15,567,595	15,567,595
Net change in fair value of available-for-sale financial assets		3	-	-	(997,845)	-	(997,845)
Balance at June 30, 2017	US$		10,000	645,034,000	(362,506,083)	12,177,084	294,715,001
Net income for period			-	-	-	57,987,727	57,987,727
Class A dividend paid		6(a)i	-	-	-	(36,276,800)	(36,276,800)
Net change in fair value of available-for-sale financial assets		3	-	-	184,302,995	-	184,302,995
Balance at December 31, 2017	US$		10,000	645,034,000	(178,203,088)	33,888,011	500,728,923
Adjustments on adoption of IFRS 9			-	-	-	48,025,580	48,25,580
Transfer to Retained Earnings/(Accumulated losses)*		3	-	-	178,203,088	(178,203,088)	-
Adjusted balance at January 1, 2018			10,000	645,034,000	-	(96,289,497)	548,754,503
Net income for period			-	-	-	16,887,367	16,887,367
Balance at June 30, 2018	US$		10,000	645,034,000	-	(79,402,130)	565,641,870

* Due to the change in classification of the Silent Contribution from available-for-sale financial assets to financial assets measured at fair value through profit or loss, the Revaluation reserve amount of US$178,203,088 was transferred to accumulated losses.

See accompanying notes to financial statements.

HSH N FUNDING II

Statement of Cash Flows

For the six months ended June 30, 2018 and 2017 *(compiled without audit or review)*
(stated in United States dollars)

	2018	2017
Cash provided by/(applied in):		
Operating activities		
Net income for period	16,887,367	15,567,595
Add/(deduct) net changes in non-cash operating balances:		
Net change in revised discounted cash flows (Class B preference shares)	-	13,977,602
Net change in revised discounted cash flows (Silent Contribution)	-	(11,406,797)
Impairment on loan receivable	1,246,918	-
Net change in fair value of financial assets	19,689,115	-
Net change in fair value of financial liabilities	(19,685,000)	-
Increase in cash and cash equivalents during period	18,138,400	18,138,400
Cash and cash equivalents at beginning of period	203,594	9,272,794
Cash and cash equivalents at end of period	US$ 18,341,994	27,411,194
Supplementary information on cash flows from operating activities:		
Interest received	18,138,400	18,138,400

1. Incorporation and background information

HSH N Funding II ("the Company") was incorporated on May 26, 2005 as an exempted company with limited liability under the laws of the Cayman Islands for the purpose of carrying on business as an investment company. The Company is a wholly owned subsidiary of HSH Nordbank AG (the "Bank"). The financial results of the Company are consolidated by the Bank.

The objectives for which the Company has been established are limited by the Memorandum of Association to entering into transaction documents and exercising its rights and performing its obligations in connection therewith. The Company issued 500,000 Class B preference shares in the aggregate nominal amount of US$500,000,000 to Banque de Luxembourg, a société anonyme incorporated in Luxembourg (the "Fiduciary") and used the proceeds to acquire a silent capital interest in the commercial enterprise (*Handelsgewerbe*) (the "Participation") of the Bank in the form of a *Stille Gesellschaft* pursuant to an agreement providing for an asset contribution to the Bank in the amount of US$500,000,000 (the "Silent Contribution") and dated June 17, 2005 (the "Participation Agreement").

The Fiduciary financed the purchase of Class B preference shares with proceeds from issuance of US$500,000,000 HSH Nordbank Silent Participation Hybrid Equity Regulatory (SPHERE) Securities in the denomination of US$1,000 (the "SPHERE Securities") on a fiduciary basis at 100% of the principal amounts. The Fiduciary acquired the Class B preference shares at the sole risk of the holders of the SPHERE Securities. The SPHERE Securities are listed on the Euronext Amsterdam Exchange. The Bank has entered into a support undertaking agreement with the Fiduciary that the Company will at all times be in a position to meet its dividend obligations under the Class B preference shares if and when due as contemplated in the Company's Memorandum and Articles of Association.

Going concern

The ability of the Company to continue as a going concern is directly linked to the same assumption being applicable at the Bank level. The financial accounting and measurement in these financial statements are based on the assumption that the Bank is a going concern.

With regard to the going concern assumption, the section entitled "Forecast, opportunities and risks report" in the interim Group management report shows that the going concern assumption for accounting and measurement purposes, as well as the continued survival of the Bank and major group companies is based, in particular, on the share purchase agreement concluded on 28 February 2018, in which with the HSH Beteiligungsmanagement GmbH sold 94.9 % of the shares in the Bank to various funds of Cerberus European Investments LLC, J.C. Flowers & Co. LLC, Golden Tree Asset Management L.P., Centaurus Capital LP and BAWAG P.S.K. AG (hereinafter referred to as the "bidders") being closed and implemented.

1. Incorporation and background information (continued)

Going concern (continued)

After the competition authorities in Germany and Austria have granted their approval, the approval of the federal state parliaments in Hamburg and Schleswig-Holstein has been obtained and HSH Finanzfonds AöR has submitted a final settlement report on the full settlement of the second loss guarantee granted by HSH Finanzfonds AöR, the closing of the share purchase agreement requires that:

- the competent banking supervisory authority (European Central Bank (ECB)), German Federal Financial Supervisory Authority (BaFin) and Commission de Surveillance du Secteur Financier (CSSF Luxembourg) grants the necessary approvals,

- the European Commission approves the proposed new corporate structure after performing a viability review,

- the extension of the Bank's membership of the guarantee scheme of the German Savings Banks Finance Group (SFG) beyond the two years stipulated in the articles of association, namely for an additional third year following the closing of the share purchase agreement, is confirmed,

- the bidders pay the portion of the purchase price attributable to them on the closing date.

If any of the conditions set out above for the closing of the share purchase agreement are not met, and if no agreement can be reached between the parties involved in each case, in particular if the EU Commission reaches the conclusion, in the course of its viability review, that the planned new corporate structure will not lead to a business model that is profitable in the long term, then the Bank 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, then this could trigger outflows of short-term funds and fundamentally restrict the Bank'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.

It is further required that the acceptance by market participants and other relevant stakeholders necessary for the successful implementation of the Bank's future business model is maintained or gained.

2. Significant accounting policies

These financial statements are prepared in accordance with International Financial Reporting Standards ("IFRSs"). The accounting policies have been applied consistently by the Company. Significant accounting policies and their effect on the financial statements are as follows.

(a) Adoption of IFRS 9 - 'Financial Instruments: Classification and Measurement'

The Company has applied the provisions set out in IFRS 9 for the first time in these financial statements.

IFRS 9 deals with recognition, derecognition, classification and measurement of financial assets and financial liabilities. Its requirements represent a significant change from the existing requirements in IAS 39 Financial Instruments, 'Recognition and Measurement'. The initial application of IFRS 9 results in changes in the carrying amounts between the closing balance sheet in accordance with IAS 39 as at 31 December 2017 and the opening balance sheet in accordance with IFRS 9 as at 1 January 2018. The changes relate to financial instruments and are based on the new classification, measurement and impairment provisions set out in IFRS 9. Retrospective application is required but comparative information is not compulsory.

Upon adoption of IFRS 9, the classification of the Silent Contribution changed from available-for-sale financial assets to financial assets measured at fair value through profit or loss and the classification of the Class B preference shares changed from financial liabilities measured at amortised cost to financial liabilities measured at fair value through profit or loss. The Class B preference shares are designated as financial liabilities measured at fair value through profit or loss in order to eliminate or significantly reduce the measurement inconsistency that would otherwise arise from measuring the Silent Contribution at fair value through profit or loss whilst measuring the Class B preference shares at amortised cost. The loan receivable is assessed for any impairment upon adoption of IFRS 9.

In accordance with the option provided for in IFRS 9.7.2.15, the Company has opted not to adjust the comparative figures in the statement of financial position and has prepared a reconciliation for the reclassified items from the closing balance sheet in accordance with IAS 39 as at 31 December 2017 to the opening balance sheet in accordance with IFRS 9 as at 1 January 2018.

The below reconciliation has been prepared in accordance with the requirements set out in IFRS 7.42L to IFRS 7.42O. The balance sheet carrying amounts in the closing balance sheet as at 31 December 2017 in accordance with IAS 39 are reconciled to the balance sheet carrying amounts of the opening balance sheet as at 1 January 2018 in accordance with IFRS 9. The information is provided using two tables for each reclassified item containing financial instruments. For the reconciliation of impairment allowances in accordance with IAS 39 to impairment allowances in accordance with IFRS 9, a further table was also prepared in line with the requirements of IFRS 7.42P.

(stated in United States dollars)

2. Significant accounting policies (continued)

(a) Adoption of IFRS 9 - 'Financial Instruments: Classification and Measurement' (continued)

Reconciliation of measurement categories and carrying amounts of financial instruments from IAS 39 to IFRS 9

	IAS 39 measurement category	IAS 39 carrying amount	IFRS 9 measurement category	IFRS 9 carrying amount
Asset				
Silent Contribution	Available-for-sale assets measured at fair value	260,413,608	Fair value through profit or loss	260,413,608
Loan receivable	Loans and receivables measured at amortised cost	553,000,000	Amortised cost	539,129,629
Interest receivable	Assets measured at amortised cost	9,069,200	Amortised cost	9,069,200
Cash and cash equivalents	Assets measured at amortised cost	203,594	Amortised cost	203,594
Liability				
Class B preference shares	Liabilities measured at amortised cost	321,955,951	Fair value through profit or loss	260,060,000
Other liabilities	Liabilities measured at amortised cost	1,528	Amortised cost	1,528

(stated in United States dollars)

2. Significant accounting policies (continued)

(a) Adoption of IFRS 9 - 'Financial Instruments: Classification and Measurement' (continued)

Reconciliation of carrying amounts from IAS 39 to IFRS 9 based on the categories of financial instruments under IFRS 7

		31-Dec-17			1-Jan-18
		IAS 39 carrying amount	Reclassification	Remeasurement	IFRS 9 carrying amount
Silent Contribution					
From	Available-for-sale	260,413,608			
To	Fair value through profit or loss		260,413,608	-	260,413,608
Loan receivable					
From	Amortised cost	553,000,000			
To	Amortised cost		553,000,000	(13,870,371)	539,129,629
Interest receivable					
From	Amortised cost	9,069,200			
To	Amortised cost		9,069,200	-	9,069,200
Cash and cash equivalents					
From	Amortised cost	203,594			
To	Amortised cost		203,594	-	203,594
Class B preference shares					
From	Amortised cost	(321,955,951)			
To	Fair value through profit or loss		(321,955,951)	61,895,951	(260,060,000)
Other liabilities					
From	Amortised cost	1,528			
To	Amortised cost		1,528	-	1,528

Due to the change in classification of the Silent Contribution from available-for-sale financial assets to financial assets measured at fair value through profit or loss, the Revaluation reserve amount of US$178,203,088 was transferred to Accumulated loss.

(stated in United States dollars)

2. Significant accounting policies (continued)

(a) Adoption of IFRS 9 - 'Financial Instruments: Classification and Measurement' (continued)

Reconciliation of impairments in accordance with IFRS 7.42P. - financial assets

		31-Dec-17			1-Jan-18
		IAS 39 amount	Reclassification	Remeasurement	IFRS 9 amount
Impairment on loan receivable					
From	Amortised cost	-			
To	Amortised cost		-	(13,870,371)	(13,870,371)

The initial application of IFRS 9 requires the amount of changes in the fair value that is attributable to changes in the credit risk of the Class B preference shares to be presented in other comprehensive income. In cases where the stated accounting treatment would create or enlarge an accounting mismatch, the fair value changes shall be presented in profit or loss.

The silent participation and Class B preference shares are financial instruments with similar characteristics and are economically related such that their fair value movements mainly offset each other. Therefore, in order to avoid an accounting mismatch, the fair value movements of both financial instruments, including the movements attributable to changes in credit risk, are presented through profit and loss.

The below table has been prepared in accordance with the requirements set out in IFRS 7.10A and IFRS 7.11, showing the amount of change, during the period and cumulatively, in the fair value of the Class B preference shares that is attributable to changes in the credit risk of this liability:

	For the six months ended June 30, 2018	
	Cumulatively	During the period
Changes in fair value of the Class B preference shares attributable to changes in credit risk	355,836,873	(10,921,755)

The Company compares market quotes with a calculated fair value that uses the historical credit spread of the Class B preference shares to determine the changes in credit risk. The difference between these two prices represents the cumulatively change in fair value due to changes in credit risk.

The Class B preference shares are a perpetual financial instrument with no contractual maturity date.

2. Significant accounting policies (continued)

(b) Use of estimates

The preparation of financial statements in accordance with IFRSs requires management to make estimates and assumptions that affect the application of accounting policies and the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amount of income and expenses during the period. Actual results could differ from those estimates. The disclosures in accordance with IAS 1.125 are made (additionally to the information provided in this note) in notes 3, 4, 5, 8 and 9.

(c) Profit participation under the Participation Agreement, interest income, Class B dividends and Class A dividends

Profit participation under the Participation Agreement and interest income are recognised on an accruals basis. Class A and Class B dividends are recognised in accordance with the Article of Association.

(d) Financial instruments

(i) Classification

A financial asset is any asset that is cash, a contractual right to receive cash or another financial asset, or to exchange financial instruments with another enterprise under conditions that are potentially favorable or an equity instrument of another enterprise. Financial assets comprise cash and cash equivalents, interest receivable, Silent Contribution and loan receivable.

A financial liability is any liability that is a contractual obligation to deliver cash or another financial asset or to exchange financial instruments with another enterprise under conditions that are potentially unfavorable. Financial liabilities comprise Class B preference shares and other liabilities.

Financial assets that are classified as loans and receivables include cash and cash equivalents and loan receivable.

IFRS 9 replaces the provisions of IAS 39 that relate to the recognition, classification and measurement of financial assets and liabilities, derecognition of financial instruments, impairment of financial assets and hedge accounting.

2. Significant accounting policies (continued)

(d) Financial instruments (continued)

(i) Classification (continued)

Upon adoption of IFRS 9 on January 1, 2018 the Company changed the classification of its investments in Silent Contribution from available-for-sale to financial assets measured at fair value through profit or loss. The investments in Silent Contribution are not held for trading purposes. All other financial assets are classified as financial assets measured at amortized cost. The classification of the Class B preference shares changed from financial liabilities measured at amortised cost to financial liabilities measured at fair value through profit or loss. All other financial liabilities are classified as financial liabilities measured at amortized cost. The Company classifies financial instruments issued as financial liabilities or equity instruments in accordance with the substance of the contractual terms of the instruments.

(ii) Recognition

The Company recognizes financial assets and financial liabilities on the date it becomes a party to the contractual provisions of the instrument.

(iii) Measurement

Financial instruments are measured initially at cost which is the fair value of the consideration given or received.

All recognised financial assets that are within the scope of IFRS 9 are required to be subsequently measured at amortised cost or fair value on the basis of the entity's business model for managing the financial assets and the contractual cash flow characteristics of the financial assets.

Debt investments that are held within a business model whose objective is to collect the contractual cash flows, and that have contractual cash flows that are solely payments of principal and profit on the principal amount outstanding, are subsequently measured at amortised cost.

All financial instruments classified as fair value through profit or loss are measured at fair value. IFRS 9 requires that the changes in the fair value of the financial liability that is attributable to changes in the credit risk of that liability be presented in other comprehensive income, unless the recognition of the effects of changes in the liability's credit risk in other comprehensive income would create or enlarge an accounting mismatch in profit or loss. Changes in fair value attributable to a financial liability's credit risk are not subsequently reclassified to profit or loss, but are instead transferred to retained earnings when the financial liability is derecognised.

2. Significant accounting policies (continued)

(d) Financial instruments (continued)

(iii) Measurement (continued)

Financial liabilities that are not held for trading and are not designated as at fair value through profit or loss are measured at amortised cost using the effective interest method. Amortised cost is calculated by taking into account any discount or premium on settlement.

The related net income or expense is recognized in the statement of comprehensive income (see notes 3 and 5).

(iv) Determination of Fair Values

The determination of fair values for certain financial instruments is for the sole purpose to present the respective information in note 8 of these financial statements.

Fair Value is defined in accordance with IFRS 9 as the price at which a financial instrument can be traded between two informed, willing and independent parties who are under no obligation to deal.

The fair value of financial instruments is determined on the basis of the listed prices on an active market (mark-to-market), or if this is not possible on the basis of recognized valuation techniques and models (mark-to-matrix or mark-to-model).

The mark-to-market method is used if a market price is available at which a transaction could be performed or has been performed. This is generally the case for securities traded on liquid markets. The mark-to-matrix method is used to determine fair value where no market price is available under the mark-to-market method. If a fair value cannot be determined from the market or transaction prices of a financial instrument, either it is derived from the prices of comparable financial instruments or a model valuation is conducted with parameters that are almost completely observable in the market. This method has been applied to measure the fair value of the Class B Shares as well as the fair value of the Silent Contribution. These financial instruments are linked to the listed SPHERE securities, which are listed on the Stock Exchange in Amsterdam.

The fair value is determined by the mark-to-model valuation using a suitable model if a valuation cannot be derived, either of adequate quality or at all, using the mark-to-market or mark-to-matrix method.

The fair value of the loan receivable is determined by discounting contractual cash flows taking into account rating-related spreads.

2. Significant accounting policies (continued)

(d) Financial instruments (continued)

(v) Derecognition

The Company derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset are transferred or in which the Company neither transfers nor retains substantially all of the risks and rewards of ownership and does not retain control of the financial asset.

The Company uses the specific identification method to determine gains or losses on derecognition for financial assets that are sold.

(vi) Loan loss provisions and Impairment of financial assets

The introduction of IFRS 9 will replace the current model used to calculate loan loss provisions/impairments under IAS 39, which is based primarily on incurred losses, with a model based on the expected credit losses. The scope of the new model consistently includes all financial assets that are recognised at amortised cost.

For all financial instruments that fall under the scope of the loan loss provisions model under IFRS 9.5.5.1, the basic principle involves setting up loan loss provisions depending on the change in the credit quality of the financial instrument concerned. This model only applies to financial instruments which are not impaired at the time of initial recognition. At the time of initial recognition, these financial instruments are assigned to level 1, which is explained below. Depending on the extent of the change in credit quality, the financial instrument is assigned to one of the following three levels as part of the subsequent measurement process:

a. Level 1: No significant increase in the loan default risk, 12-month expected loss

   For financial instruments whose loan default risk is not significantly increased, the impairment is recognised in the amount of the anticipated 12-month credit losses.

b. Level 2: Significant increase in the loan default risk, lifetime expected loss

   For financial instruments whose loan default risk has increased significantly since the time of initial recognition, expected credit losses are recognised over the entire remaining term of the financial instrument.

c. Level 3: Financial assets that are credit-impaired, lifetime expected loss

Financial instruments for which one or more events have occurred after the time of initial recognition that have an adverse impact on the expected future cash flows are assigned to level 3. The expected credit losses over the entire remaining term to maturity of the financial instrument are recognised for these financial instruments as well.

2. Significant accounting policies (continued)

(d) Financial instruments (continued)

(vi) Loan loss provisions and Impairment of financial assets (continued)

The Company 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)

With regards to the loan agreement the Company has entered into with the Bank, the external rating of the Bank is mapped onto the internal credit risk models of HSH Nordbank which – where necessary – are adjusted for the purposes of IFRS 9 are taken as a basis in this regard. The rating models used by the Bank have been developed based on the definition of "default" set out in Art. 178 CRR and are validated in this respect on a regular basis.

Any necessary adjustments/expansions of the existing models relate primarily to the use of methods for multiannual estimates. Within this context, the Company 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 loan agreement is used to project the gross carrying amount forward over the multiannual period.

In addition, the credit risk parameters are expanded to include additional macroeconomic information relating to the future – if necessary.

The lifetime expected loss is calculated as the sum product of the period-specific credit risk parameters determined during the term. Discounting to the reporting date is based on the effective interest rate in each case.

The loan loss provisions are generally calculated at the level of the individual financial instrument.

A financial instrument is transferred (back) from level 2 to level 1 if the loan default risk is no longer significantly increased based on the rating. In cases involving modified financial instruments, however, a good conduct period set, during which the financial instrument remains in level 2. This corresponds to the good conduct period for forbearance.

2. Significant accounting policies (continued)

(d) Financial instruments (continued)

(vi) Loan loss provisions and Impairment of financial assets (continued)

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 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.

On February 6, 2013, an announcement was made by the Bank relating to financial planning which will result in net losses for the business years 2013 and 2014. The financial results from the years 2017 to 2020 will then be used to write up hybrid instruments to par value. Therefore in the Company's opinion, the reductions in the nominal amount of the Silent contribution are not considered to be permanent. Also the non-payment of coupons is not considered to be an impairment trigger as there is no obligation to pay such coupons in the event that the Bank has insufficient distributable profits. Accordingly, no impairment is required to be recognised on the Company's investment in the Silent contribution. On June 8, 2017, the Bank announced that the next coupon payments on Silent Contributions will only take place in the year 2020 for the fiscal year 2019. On February 28, 2018, a share purchase agreement was signed whereby the shares of the Bank were sold to a consortium of private equity investors. As part of the restructuring the Bank has incurred a one-time negative effect with regards to the valuation of its loan portfolio. In light of this as well as other effects of the privatization, the Bank will not be able to make distributions in respect of the Participation Agreement for the fiscal year 2019 as originally expected but at the earliest from the fiscal year 2024 for the fiscal year 2023.

2. Significant accounting policies (continued)

(d) Financial instruments (continued)

(vii) Fair value disclosures

IFRS 7 outlines disclosures to be made with respect to fair value measurements within the financial statements. All financial instruments designated at fair value are categorised with a three-level hierarchy that reflects the significant of inputs used in measuring fair values. The fair value hierarchy is as follows:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: inputs other than quotes prices included with Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3: inputs for the asset or liability that are based on observable market data (unobservable inputs).

Specific disclosures are required when fair value measurements are categorised as Level 3 in the fair value hierarchy. Furthermore, changes in valuation techniques from one period to another, including the reasons therefore, are required to be disclosed for each class of financial instruments.

(viii) Specific instruments

Cash and cash equivalents
For the purposes of the statement of cash flows, cash and cash equivalents include current accounts with original maturities of three months or less.

Silent Contribution
Upon adoption of IFRS 9 on January 1, 2018 the Company changed the classification of its investments in Silent Contribution from available-for-sale to financial assets measured at fair value through profit or loss. The investments in Silent Contribution are not held for trading purposes.

It is measured initially at cost which is the fair value of the consideration given and subsequently measured at and presented in the statement of financial position at fair value. The Silent Contribution is adjusted in accordance with the requirements of IFRS 9. Accrued profit participations and the net result from the application of IFRS 9 are recognized in the statement of comprehensive income. The inputs for the calculation of the Silent Contribution are based upon observable market data and accordingly the asset is categorized as a level 2 investment in the fair value hierarchy.

2. Significant accounting policies (continued)

(d) Financial instruments (continued)

(viii) Specific instruments (continued)

Silent Contribution (continued)
Pursuant to the EU Commission's requirements, the Bank is not permitted to make any payouts on profit participation capital and silent partnerships due to the Bank's net loss or balance sheet loss. In case of a successful completion of the privatization procedure, the Bank expects to pay dividends as well as distributions under the hybrid capital instruments. On June 8, 2017, the Bank announced that the next coupon payments on Silent Contributions will only take place in the year 2020 for the fiscal year 2019. However, the next coupon date is now expected to take place in the year 2024 for the fiscal year 2023.

Loan receivable
Loan receivable is subsequently measured at amortized cost, being the amount at which the loan receivable is measured at initial recognition minus principal repayments, and minus any write down for impairment or uncollectibility. The loan receivable is interest bearing with interest income being recognized in the statement of comprehensive income.

Class B preference shares
Class B preference shares are classified as a financial liability according to IAS 32.11 (a) and measured at fair value through profit or loss (note 2(c)(iii)). Dividends on Class B preference shares and the net result from the application of IFRS 9 are recognised as interest expense in the statement of comprehensive income as accrued.

According to IFRS 9, embedded derivatives shall not be separated from the host contract and accounted for as a derivative if the value of the derivative would change in response to a non-financial variable that is specific to a party. The value of the Class B preference shares vary in response to a non-financial variable linked to the performance of the Bank.

(e) Offsetting

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when a signed agreement clearly defines the enforceable right of the Company and another party to settle on a net basis or realize the asset and settle the liability simultaneously.

3. Silent Contribution

The Company acquired a silent capital interest in the aggregate amount of US$500,000,000 (2017: US$500,000,000) in the commercial enterprise of the Bank in the form of the Participation pursuant to the Participation Agreement dated June 17, 2005, providing for an asset contribution to the Bank in the amount of US$500,000,000 (2017: US$500,000,000).

(stated in United States dollars)

3. Silent Contribution (continued)

The Participation Agreement has no fixed redemption date and may only be redeemed when terminated by the Bank. The Bank may, if tax or regulatory changes occur, terminate the Participation Agreement only after providing two years notice thereof and approval therefore has been given by the German Banking Supervisory Authority. The Company shall be entitled to Profit Participations on the nominal contribution amount at a fixed rate of 7.25% p.a.

Pursuant to terms of the Participation Agreement profit participations will accrue on the principal amount for each fiscal year of the Bank or part thereof. No profit participations accrue to the extent payment thereof would lead to or increase an annual balance sheet loss, if there has occurred a reduction which has not yet been fully restored, in the case of regulatory interventions or if the termination date falls within such period.

The Company may share in the losses of the Bank after allocation to/from its reserves and retained earnings up to the principal amount of the Silent Contribution. Any such losses will reduce the principal amount of the Silent Contribution. If at any time, the principal amount of the Silent Contribution is reduced on account of a loss, the principal amount of the Silent Contribution will be re-credited in the years subsequent in which profits are recorded, provided that at no time shall the principal amount of the Silent Contribution be more than the principal amount of the Silent Contribution on the date of the Participation Agreement.

At June 30, 2018 the fair value of the level 2 investments, comprising solely of the Silent Contribution, was US$240,724,493 (2017: US$260,413,608).

	Silent contribution USD	Accrued profit participation USD	Net results from revised discounted cash flows USD	Fair value adjustments USD	Total USD
Balance at January 1, 2017	500,000,000	92,034,722	(116,887,305)	(361,508,238)	113,639,179
AG.8 and fair value movements	-	-	(36,530,721)	183,305,150	146,774,429
Balance at December 31, 2017	500,000,000	92,034,722	(153,418,026)	(178,203,088)	260,413,608
Fair value movements	-	-	-	(19,689,115)	(19,689,115)
Balance at June 30, 2018	500,000,000	92,034,722	(153,418,026)	(197,892,203)	240,724,493

(stated in United States dollars)

4. Loan receivable

On June 17, 2005 the Company entered into a term loan agreement, (the "Loan Agreement") with the Bank under which the Company has made a US$553,000,000 term loan facility in the form of a German law governed *Schuldscheindarlehen* available to the Bank.

At June 30, 2018 the balance of the loan receivable was US$537,882,711 (2017: US$553,000,000) comprising the initial term loan facility of US$553,000,000, current period net adjustments due to impairment of US$1,246,918 and net adjustments due to impairment of US$13,870,371 following adoption of IFRS 9 on January 1, 2018 (2017: US$Nil).

The below table has been prepared in accordance with the requirements set out in IFRS 7.35H, showing the reconciliation from the opening balance to the closing balance of the loss allowance/impairment:

Impairment on loan receivable	For the six months ended June 30, 2018
Balance as at December 31,2017	-
Remeasurement following adoption of IFRS 9	13,870,371
Balance as at January 1, 2018	13,870,371
Additions during the period	1,246,918
Balance as at June 30, 2018	15,117,289

The impairment on loan receivable amounting to a total of US$15,117,289 as at June 30, 2018 was attributable to Level 2.

Interest is charged on the loan at a rate of 6.56% p.a. and the loan will mature on December 31, 2036. At June 30, 2018 the balance of interest receivable was US$9,069,200 (2017: US$9,069,200).

5. Class B preference shares

The Company issued 500,000 Class B preference shares to the Fiduciary. The purchase was funded from the issuance of US$500,000,000 SPHERE Securities.

At June 30, 2018 the balance of the Class B preference shares was US$240,375,000 (2017: US$321,955,951) comprising the initially issued amount of US$500,000,000, net cumulative results from revised discounted cash flows of US$(178,044,049) (2017: US$(178,044,049)) until December 31, 2017 in accordance with IAS 39.AG8, net adjustments due to IFRS 9 of US$(61,895,951) (2017: US$Nil) following adoption of IFRS 9 on January 1, 2018 and fair value movements of US$(19,685,000) (2017: US$Nil).

(stated in United States dollars)

5. Class B preference shares (continued)

	Class B preference shares	Net results from revised discounted cash flows	Fair value movements	Total
	USD	USD	USD	USD
Balance at January 1, 2017	500,000,000	(104,234,806)	-	395,765,194
Result of revised discounted cash flows for the year	-	(73,809,243)	-	(73,809,243)
Balance at December 31, 2017	500,000,000	(178,044,049)	-	321,955,951
Adjustments following adoption of IFRS 9	-	-	(61,895,951)	(61,895,951)
Adjusted balance at January 1, 2018	500,000,000	(178,044,049)	(61,895,951)	260,060,000
Fair value movements	-	-	(19,685,000)	(19,685,000)
Balance at June 30, 2018	500,000,000	(178,044,049)	(81,580,951)	240,375,000

Rights attaching to Class B preference shares:

i. Each Class B preference shareholder has a right to receive an annual dividend on each Class B preference share held, calculated, declared and paid based on the specification in the Articles of Association. Dividends are paid in cash.

ii. On winding–up of the Company or other return of capital (other than purchase or redemption of Class B preference shares), the Class B preference shareholders will be entitled to share in the Company's rights to interest accrued under the Loan Agreement, repayment amount under the Participation Agreement, interest on the repayment amount and the Company's rights to funding of the Luxembourg gross-up amount (the "Class B Ring-Fenced Assets"). No other holders of shares in the Company will be entitled to the Class B Ring-Fenced Assets. If the value of claims of the Company's creditors exceed the Company's assets (minus the Class A Ring-Fenced Assets and the Class B Ring-Fenced Assets), the rights of the Class B preference shareholders in the assets of the Company will rank junior to the rights of Class A preference shareholders up to an amount equal to the sum of the loan repayment amount under the Loan Agreement (plus amounts which have actually been received thereunder and minus amounts which have been received and passed on to Class A preference shareholders), but senior to the holders of other shares in the Company up to an amount equal to the Class B Ring-Fenced Assets (plus amounts which have actually been received thereunder and minus amounts which have been received and passed on to Class B preference shareholders).

(stated in United States dollars)

5. Class B preference shares (continued)

Rights attaching to Class B preference shares(continued):

iii. The Class B preference shareholders shall be entitled to receive notice of general meetings of the Company but shall not be entitled to attend and vote thereat.

iv. The Company will, forthwith upon becoming aware that the Class B preference shares will be redeemed, notify the Class B preference shareholders of (A) the date on which they will be redeemed, and (B) the amount of payment in cash.

v. The Company shall make all payments to the Class B preference shareholders pursuant to terms of the Articles of Association without any tax deduction, unless a tax deduction is required by law.

6. Share capital

		2018	2017
Authorised:			
10 Ordinary Shares of US$1,000 each		10,000	10,000
1,050,000 Class A preference shares of US$1,000 each		1,050,000,000	1,050,000,000
	US$	1,050,010,000	1,050,010,000
Issued and fully paid:			
10 Ordinary Shares of US$1,000 each	US$	10,000	10,000

During the period ended June 30, 2018 and 2017, there were no changes to issued and fully paid Ordinary Shares.

Rights attaching to Ordinary shares:

i. Income: Each Ordinary Shareholder has right to receive such profits of the Company available for distribution as determined by the Directors after the payment to the Preference Shares of their dividends.
ii. Capital: On a winding-up or other return of capital, the holder of each Ordinary Share shall be entitled, following payment to the holders of the Preference Shares, to repayment of the nominal amount of the capital paid-up thereon and thereafter any surplus then remaining shall be distributed pari passu among the holders of the Ordinary Shares.
iii. Voting: Each Ordinary Shareholder has right to receive notice of general meetings of the Company and to attend and to vote thereat either in person or proxy.

(stated in United States dollars)

6. Share capital (continued)

Issued and fully paid Class A preference shares:

	2018 Number of shares	2018 US$	2017 Number of shares	2017 US$
Balance at beginning of period	645,034	645,034,000	645,034	645,034,000
Balance at end of period	645,034	645,034,000	645,034	645,034,000

Rights attaching to Class A preference shares:

i. Each Class A preference shareholder has a right to receive annual interim and final dividends on each Class A preference share held calculated based on the Articles of Association. Interim dividends are not paid by cash but by issue of such number of Class A preference shares, the aggregate par value of which equals the amount of such declared interim dividend. Final dividends are paid in cash.

ii. On winding–up of the Company or other return of capital (other than purchase or redemption of Class A preference shares), the Class A preference shareholders will be entitled to share in the Company's rights to the loan repayment amount under the Loan Agreement (the "Class A Ring-Fenced Assets"). No other holders of shares in the Company will be entitled to the Class A Ring-Fenced Assets. If the value of claims of the Company's creditors exceed the Company's assets (minus the Class A Ring-Fenced Assets and the Class B Ring-Fenced Assets), the rights of the Class A preference shareholders in the assets of the Company will rank senior to the rights of holders of other shares in the Company, up to an amount equal to the Class A Ring-Fenced Assets (plus amounts which have actually been received there under and minus amounts which have been received and passed on to Class A preference shareholders).

iii. The Class A preference shareholders shall be entitled to receive notice of general meetings of the Company and shall be entitled to vote thereat.

iv. Class A preference shares may only be redeemed contemporaneously with redemption of the Class B preference shares or after the Class B preference shares have been redeemed. Class A preference shares may be redeemed at the option of the Class A preference shareholder or the Company by notice to the other. The Class A preference shares will be redeemed in an amount equal to the loan repayment amount under the Loan Agreement and aggregate profit participations under the Participation Agreement. The Company may set off its obligation to pay cash dividends in accordance with the terms of the Articles of Association against obligations owing to the Company by the Class A preference shareholder in respect of interest accrued and due but unpaid under the Loan Agreement.

(stated in United States dollars)

7. Related party balances and transactions

The Company is controlled by the Bank, which is considered as related party.

The following transactions and balances with the bank are disclosed below:

	Note	2018	2017
Statement of Financial Position:			
Silent Contribution	3	240,724,493	260,413,608
Loan receivable	4	537,882,711	553,000,000
Interest receivable	4	9,069,200	9,069,200
Cash and cash equivalents		18,341,994	203,594
Statement of Comprehensive Income:			
Interest income on loan	4	18,138,400	36,276,800

The Bank's audited financial statements for the year end December 31, 2017 and 2016 contain an emphasis of matter paragraph in the audit opinion regarding the Bank's ability to continue as a going concern.

8. Disclosure of Fair Values in Accordance with IFRS 7

For each financial asset and liability, the fair values are disclosed and compared with the respective carrying amount (IFRS 7.25):

June 30, 2018	Note	Carrying Amount	Fair Value	Difference
Silent Contribution	3	240,724,493	240,724,493	-
Loan receivable	4	537,882,711	684,998,971	147,116,260
Interest receivable	4	9,069,200	9,069,200	-
Cash and cash equivalents		18,341,994	18,341,994	-
Class B preference shares	5	240,375,000	240,375,000	-
Other liabilities		1,528	1,528	-

(stated in United States dollars)

8. Disclosure of Fair Values in Accordance with IFRS 7 (continued)

December 31, 2017	Note	Carrying Amount	Fair Value	Difference
Silent Contribution	3	260,413,608	260,413,608	-
Loan receivable	4	553,000,000	708,396,234	155,396,234
Interest receivable	4	9,069,200	9,069,200	-
Cash and cash equivalents		203,594	203,594	-
Class B preference shares	5	321,955,951	260,060,000	(61,895,951)
Other liabilities		1,528	1,528	-

9. Credit, liquidity and market risk

The Company's investment activities expose it to various types of risk that are associated with the financial instruments and markets in which they invest. The most significant type of financial risk to which the Company is exposed is credit risk.

The nature and extent of the financial instruments outstanding at the date of the statement of financial position and the risk management policies employed by the Company are discussed below:

Credit risk

Credit risk is the risk that a counterparty to a financial instrument will fail to discharge an obligation or commitment that it has entered into with the Company. Credit risk is generally higher when a non-exchange traded financial instrument is involved because the counterparty for non-exchange traded financial instruments is not backed by an exchange clearing house.

The Company is potentially exposed to credit risk on the Silent Contribution, loan receivable and interest receivable and from its exposure on its cash and cash equivalents.

The counterparty of these items is solely the Bank. The carrying amounts of financial assets best represent the maximum credit risk exposure at the statement of financial position date.

(stated in United States dollars)

9. Credit, liquidity and market risk (continued)

Credit risk (continued)

As at June 30, 2018 and December 31, 2017 the Company's financial assets exposed to credit risk amounted to the following:

	Note	2018	2017
Silent Contribution	3	240,724,493	260,413,608
Loan receivable	4	537,882,711	553,000,000
Interest receivable	4	9,069,200	9,069,200
Cash and cash equivalents		18,341,994	203,594
	US$	806,018,398	822,686,402

The Class B preference shareholders bear the risk of the Silent Contribution and the Class A preference shareholders bear the credit risk of the loan and its interest receivable. The balance of the Silent Contribution comprises of a current year fair value adjustment of US$(30,218,924) and a revised discounted cash flows adjustment of US$10,529,809 (2017: US$183,305,150 and US$(36,530,721) respectively).

Liquidity risk and refinancing risk

Liquidity risk is the risk that the Company will encounter difficulties in meeting obligations associated with financial liabilities. The timing and terms of cash inflows from Silent Contribution and loan receivable are similar to cash outflows on accounts of Class A preference shares and Class B preference shares. As such, the Company is deemed to have insignificant exposures to liquidity risk and refinancing risk.

Market risk

Market risk is the risk that the value of a financial instrument will fluctuate as a result of changes in market, whether those changes are caused by factors specific to the individual instrument or factors affecting all instruments in the market.

Market risk represents the potential loss that can arise as a result of adverse changes on market positions. Relevant for the Company are interest rates and credit spreads (interest rate risk). The Company is not exposed to foreign exchange risks, stock prices, indices and fund prices or commodity prices. As explained in Note 1 the limited purpose of the company as an investment company is to provide funding to the Bank.

9. Credit, liquidity and market risk (continued)

Market risk (continued)

The terms of the Loan Agreement and Participation Agreement are similar to terms of Class A preference shares and Class B preference shares. All proceeds received from the Bank under the loan receivable and the Silent Contribution are distributed to Class A and Class B Shareholders. Hence, the entire market risk of loan receivable and Silent Contribution are passed onto Class A preference shares and Class B preference shares. As such, the Company is deemed to have insignificant exposures to interest rate or credit spread risk. Changes in interest rates or credit spread risk do not have any significant impact on profit or loss and equity of the Company.

10. Taxation

There are no taxes on income or gains in the Cayman Islands and the Company has received an undertaking from the Governor in Cabinet of the Cayman Islands exempting it from all local income, profits and capital taxes until 2025 should such taxes be enacted. Accordingly, no provision for income taxes is included in these financial statements.

11. New pronouncements

New Accounting Standards, amendments to existing Accounting Standards and/or interpretations of existing Accounting Standards (separately or together, "New Accounting Requirements") adopted during the current period

The Company has assessed the impact, or potential impact, of all New Accounting Requirements. In the opinion of the Company, there are no mandatory New Accounting Requirements applicable in the current period that had any material effect on the reported performance, financial position, or disclosures of the Company other than those listed below. The Company has not adopted any New Accounting Requirements that are not mandatory.

11. New pronouncements (continued)

Standards and amendments to existing standards effective from January 1, 2018

IFRS 9 'Financial Instruments: Classification and Measurement'

IFRS 9 deals with recognition, derecognition, classification and measurement of financial assets and financial liabilities. Its requirements represent a significant change from the existing requirements in IAS 39 Financial Instruments, 'Recognition and Measurement'. The initial application of IFRS 9 results in changes in the carrying amounts between the closing balance sheet in accordance with IAS 39 as at 31 December 2017 and the opening balance sheet in accordance with IFRS 9 as at 1 January 2018. The changes relate to financial instruments and are based on the new classification, measurement and impairment provisions set out in IFRS 9. Retrospective application is required but comparative information is not compulsory.

The Company has applied the provisions set out in IFRS 9 for the first time in these financial statements. Refer to note 2 – Significant accounting policies for further details.

There were no other standards, interpretations or amendments to existing standards that are effective during 2018 that have a significant impact on the Company.

New standards, amendments and interpretations issued but not effective for the financial year beginning January 1, 2018 and not early adopted

There are no standards, interpretations or amendments to existing standards that are not yet effective that would be expected to have a significant impact on the Company.

12. Subsequent events

There are several events directly affecting the Bank and indirectly the Company which are disclosed in the Notes 1 and 2. There have been no other material subsequent events up until the date this report was authorised.

The financial statements were approved and authorised for issue by Directors on________2018.

Business development – Significant developments and events in the first half of 2018

Satisfactory business development

In the run-up to the closing

After the federal state owners sold their shares to renowned private investors timely on 28 February 2018, the key prerequisite for the successful conclusion of the ongoing privatisation process has been met. Since then, individual conditions leading up to the closing of the share purchase agreement have been fulfilled step by step. From the Bank's point of view, the transition of the Bank from the guarantee scheme of the German Savings Banks Finance Group (Sparkassen-Finanzgruppe) to the guarantee scheme of private banks will result in delays, meaning that it will not be possible to close the transaction in the middle of the year, as the Bank had originally hoped. Instead, the Bank does not expect the closing of the transaction until the fourth quarter. This will also delay the implementation of the transformation process. In this complex process, the Bank is supporting all of the stakeholders involved to the best of its ability in order to bring the agreed change of ownership to a successful conclusion as quickly as possible and, in doing so, lay the necessary foundation for the upcoming optimisation of the business model.

The following developments are particularly worthy of mention as at 30 June 2018:

- **Fulfilment of the closing conditions is progressing:** Following approval by the responsible competition authorities and the federal state parliaments in Schleswig-Holstein and Hamburg, the Deutsche Sparkassen- und Giroverband (DSGV) amended its articles of association in June 2018, opening up the fundamental option of extending membership in the guarantee scheme of the German Savings Banks Finance Group for an additional third year after the closing. At the same time, the Bank has applied for admission to the guarantee schemes of private banks. From today's perspective, the Bank is confident that the outstanding approvals will be granted. Nevertheless, the Bank expects that it will be possible to finalise the completion of the privatisation process, including all approvals issued by the banking supervisory authorities, in the fourth quarter in view of the delays that have occurred.

- **Transformation focusing on earnings and cost initiatives:** The bank-wide transformation project Reset & Go bundles all activities associated with the Bank's realignment. In the period leading up to the closing, the Bank will be focusing on developing and implementing profitable and risk-oriented growth strategies. Within this context, measures are being taken to improve the interrelationship between client wishes and banking products, as well as the associated processes. This includes internal improvements and the reorganisation of existing processes, as well as investments in new products, services and digitalisation topics. In addition, key topics identified with a view to optimising cost structures are being intensively prepared and developed further in order to enable implementation as quickly as possible after closing.

Business development – Significant developments and events in the first half of 2018 (continued)

Satisfactory business development (continued)

In the run-up to the closing (continued)

- **Satisfactory business development overall:** Key earnings and cost ratios are in line with expectations, key management indicators relating to capital and liquidity exceed defined ambition levels. The positive development of the risk ratios is consistent with the strategic realignment. New business activities are characterised by slightly improved new business margins and new business profitability that is developing as planned. While the volume of new business, in an environment that is competitive overall, with real estate customers is growing in line with expectations, the development is restrained in the corporate customer segment in particular.

Privatisation process on the home stretch

The federal state owners and Sparkassen- und Giroverband für Schleswig-Holstein concluded a share purchase agreement for all of their indirectly held HSH shares (a total of 94.9 %) on 28 February 2018, and therefore agreed the first successful privatisation of a Landesbank in Germany. At the same time, an agreement was reached within the context of the privatisation to relieve HSH Nordbank of large parts of the non-performing legacy loans, as well as to cancel the second loss guarantee prematurely. The closing of the share purchase agreement, the portfolio transaction and the cancellation agreement for the second loss guarantee are still subject to the following conditions, taking the approval that has already been granted into account:

- the European Commission's viability review of the future bank,
- the approval of the banking supervisory authorities (ECB, BaFin and CSSF in Luxembourg),
- confirmation of the extension of HSH Nordbank AG's membership in the guarantee scheme of the German Savings Banks Finance Group (Sparkassen-Finanzgruppe, SFG) beyond the two years stipulated in the articles of association, namely for an additional third year following the closing of the share purchase agreement.

The Bank currently assumes that the privatisation process will be completed as quickly as possible and, in particular, that the coordination between the guarantee schemes (DSGV and BdB), which is naturally a highly complex matter due to this transition being the first of its kind, meaning that there are no corresponding regulations in place, can be finalised as soon as possible. Due to the ongoing privatisation of HSH Nordbank AG, the Bank has to move from the guarantee scheme of the German Savings Banks Finance Group to the guarantee scheme of private banks, consisting of the Compensation Scheme of German Banks (EdB) and the voluntary deposit guarantee fund (ESF), collectively referred to as BdB; the aim is to achieve a seamless transition between these guarantee schemes. The Deutsche Sparkassen- und Giroverband (DSGV) has taken the first step in this direction by laying the necessary foundation in its articles of association.

Business development – Significant developments and events in the first half of 2018 (continued)

Privatisation process on the home stretch (continued)

Closing in the near future would support the ongoing and necessary restructuring process within the Bank and, as a result, the successful and sustainable realignment of the business model. To this end, the Bank is supporting all of the stakeholders involved to the best of its ability, doing everything in its power to contribute to the successful conclusion of the privatisation process.

Further details on the privatisation process, the portfolio transaction, the cancellation agreement for the second loss guarantee and the related opportunities and risks can be found in the Group Management Report for the 2017 financial year, in particular in the "Forecast, opportunities and risks report" in the section entitled "Forecast report including opportunities and risks".