

# After the Fall

The rise and fall of Hamburg shipping lender HSH Nordbank mirrors the turbulent history of German maritime finance. Now the takeover of HSH by private equity firms opens a new chapter, reports **Nicholas Brautlecht**.

The story of HSH Nordbank, once the world's largest ship financing bank, has everything that a gripping drama set in the financial world needs. Greedy bankers, naive politicians, billions of lost money and, as a bonus feature: ships.

Now, that drama has reached a new chapter: The state owners of HSH sold the bank to a group of buyout firms, an act that only months ago most observers deemed highly unlikely. After two state rescues, the European Union had ordered that HSH must be privatized to comply with its aid rules or be wound down, putting 2.000 jobs at HSH at risk. The deadline was on February 28.

At the start of the sales process last year, observers doubted that HSH owners, the regional states of Hamburg and Schleswig-Holstein, would find a buyer. The bank was crippled by billions of euros in faulty shipping loans and the deepest shipping sector slump on record. Still, within months a number of financial investors threw their hat into the ring, offering some glimmer of hope for employees.

But it was not until 11 hours before D-Day that employees could finally heave a sigh of relief: A consortium of financial investors led by Cerberus, J. C. Flowers and GoldenTree on the morning of February 28 signed a deal to pay around a billion euros for HSH, marking the first successful privatisation of a federal state bank in Germany.

Torsten Temp, HSH board member

'It's a huge relief that we all still have jobs and that the bank is not going to be wound down,' Torsten Temp, as HSH board member in charge of markets including shipping, said at a Hamburg maritime conference in February. Employees took the afternoon of the last February day off to celebrate the news. A smaller circle continued to have drinks through the night. 'The last colleagues left the party at 03.30 the next morning,' said Temp, who worked as global shipping head at Unicredit Bank before joining the HSH board eight years ago.

Even though the sale still needs approvals including from state parliaments and the EU, HSH staff have good reasons to be upbeat. Not only saved the US funds HSH from collapse, but they also stripped the bank from nearly all toxic assets: €6.5bn in non-performing loans (NPL), mainly from ship finance, are shifted to a separate vehicle steered by units of the new owners. 'That's a totally new situation for HSH and a ship finance bank and – we still are a ship finance bank,' said Temp.

HSH's history started in 2003 when the city of Hamburg and neighbouring province Schleswig-Holstein merged their regional banks and named it Hamburgische Schleswig-Holsteinische, or HSH. Local politicians joined the supervisory board and supported the management's strategy to internationalise the bank beyond its roots as a regional lender. Instead of focussing on funding local companies, HSH also entered global capital markets including the US housing market.

The merger and aggressive funding inflated HSH's shipping loan book to €40bn. China's entry to the WTO triggered double-digit gains in trade in the early 2000s, so new ship orders were seen as a safe bet. Germany became home to the world's biggest container shipping fleet (which it still is today). The banks based in Europe's biggest economy dominated


maritime finance, focussing on container ships and bulkers.

More than half of Germany's merchant fleet also received funding from private investors: Doctors, lawyers and grandmothers heard from bank advisors that single-ship partnerships are the perfect pension scheme. Helping to fuel the private shipping investment boom in Germany were flat taxes based on vessel capacity rather than revenue, while banks including HSH, Commerzbank, DVB and Norddeutsche Landesbank (NordLB) often backed the ventures with loans.

But the collapse of Lehman Brothers in 2008 changed everything: The US housing market, which HSH heavily invested in, was in turmoil. The ensuing euro crisis propelled the shipping industry into a slump: Charter and freight rates sank, as vessels ordered before the crisis kept entering the fleet. Hundreds of single-vessel firms went bankrupt, burning billions of euros invested by private would-be shipping barons.

HSH and its German peers are forced to write off billions of euros in credits to shipping companies and boost loan loss provisions amid increased pressure from European banking regulators. Commerzbank in 2012 announced its complete exit from ship finance. It has since cut its maritime loan book to around €3bn. NordLB today still runs a shipping loan book of around €13bn, but aims to shrink it to €10bn in the mid-term, it said in November. The package includes loans formerly managed by Bremer Landesbank (BLB), another German state lender based in the port city of Bremen. BLB was taken over by NordLB in a rescue mission last summer after it struggled under the weight of toxic shipping loans.

While German lenders curbed or halted lending to the industry throughout the near-decade long shipping downturn, new competitors including Asian banks and export agencies, supporting regional shipyards, as well as private equity firms expanded funding to the maritime sector. Some of the investment firms new to shipping burned their fingers as they bet on an earlier market upturn.

While the industry still sees capacity rising with large vessels entering the fleet, it now finally shows some signs of a recovery. Demand is seen to grow as much as 4.5% this year, while the fleet will expand by 3.9%, according to BIMCO. The IMF significantly lifted its 2018 and 2019 GDP forecast for advanced economies, which signals solid container shipping demand, BIMCO chief shipping analyst, Peter Sand, said in a note.

The improved outlook may ease access to funding for the maritime sector. Having shed nearly all toxic loans from the pre-financial crisis era and with new owners on board, HSH will stay committed to the industry, said Temp, whose contract on the HSH board runs till April 2019. He emphasised that his first act on the morning after the sale was to approve a shipping loan.

While the bank will be renamed as its private shareholders settle in in the coming months, HSH aims to still manage a loan book of between €4-6bn in the future, said Temp. Learning from past mistakes, the bank won't again 'put too many eggs in one basket' and instead diversify its portfolio, while planning to increase corporate lending, he said.

'German ship finance won't go back to where it was in the past, neither to the extent nor the size of the loans,' Temp said. Instead, Chinese leasing companies and capital markets are likely to play a bigger role in filling some of the funding gaps left by the banks, he added.

If HSH should still steer into trouble again in the future, at least German tax payers would be off the hook. They will still be busy, licking their wounds. The two HSH state bailouts led to as much as €15bn in losses for the North German residents. That's enough drama, for now. ●