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Corporate Communications
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HSH Nordbank

Report



**HSH NORDBANK**

US economy shrugs off high oil prices

Notwithstanding the renewed rise in the price of oil, the US economy is expected to expand at a rate of approximately 3.5 % in the current quarter. This will be ensured by the strong momentum seen in consumer spending early in the quarter; July retail sales were up 1.8 % on top of a clear increase recorded in June. Even allowing for a certain backswing in August, private consumption is still likely to grow at just under 3.5%. However, the rate of expansion is set to slow down as from the autumn.

Oil prices boosting consumer prices

Consumer prices rose by 0.5 % in July, reflecting the surge in oil prices. The year-on-year rate climbed to 3.2 %. August's renewed increase in the price of oil will be instrumental in keeping the consumer prices in the region of 3 % until well into next spring. Having said this, we believe that the oil price-induced inflation momentum will wane in the medium term, given that we do not expect oil prices to continue their advance. We therefore do not see a noticeable rise in the core rate, expecting 3 % annual average consumer price growth for 2005, softening to 2.5 % in 2006. Against this background the Fed will stick to its current policy and raise its key rates to 4.25 % by the beginning of next year.

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Burgeoning recovery in Euroland

There have been growing indications of a slightly more dynamic economy within the EMU zone, particularly in manufacturing industry. Both incoming orders and industrial output, especially in Germany, have lately pointed to a pickup in activity, with industrial sentiment indicators equally moving upwards by appreciable margins compared to the previous months. However, the by now substantial rise in the price of oil and the continuing pessimism on the part of consumer households combine to dampen the economic momentum. This is why we are sceptical whether the favourable development in the corporate sector will translate into higher capital spending any time soon. Our medium-term expectations also assume that exports will weaken in the face of slower growth in the USA and in Asia and a slightly strengthening euro. As a result, the temporary acceleration, modest as it is, will probably be over in about a year. At the bottom line, we continue to forecast 1.25 % growth for this year and set our 2006 forecast at 1.5 %.

Remarkably stable inflation rates

While oil prices surged in the wake of hurricane Katrina, they will merely cause a spike in the inflation rate without raising inflationary concerns. The core rate, i.e. adjusted for changes in energy and food prices, has meanwhile settled clearly below the 2 % mark, and prices are not bound to be stimulated in the moderate economic environment.

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USA			
	2004	2005*	2006*
Real GDP ¹⁾	4,2	3,5	3,1
Private Consumption ¹⁾	3,9	3,6	3,1
Fixed Investment ¹⁾	11,9	5,2	4,1
Exports ¹⁾	8,4	7,7	6,5
Unemployment Rate (%)	5,5	5,0	4,7
Consumer Prices ¹⁾	2,7	3,0	2,5

¹⁾ % change, year on year, * Forecast

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Euro area			
	2004	2005*	2006*
Real GDP ¹⁾	2,0	1,3	1,5
Private Consumption ¹⁾	1,4	1,1	1,4
Fixed Investment ¹⁾	1,3	0,7	0,7
Exports ¹⁾	6,0	3,1	4,1
Unemployment Rate (%)	8,9	8,7	8,6
Consumer Prices ¹⁾	2,2	2,0	1,9

¹⁾ % change, year on year, *Forecast

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US interest rates remain pointed upwards

The devastation caused in New Orleans has given rise to calls for the Fed to slow down the pace of its tightening policy while the momentum in US economy is slightly slowing down. Nevertheless, the Fed will stick to its policy and raise its rates to 4.25 % by the beginning of the next year in order to prevent inflation from accelerating. Once the 4.25 % level has been reached, the Fed under its new chairman will then wait and see what the effects of the 325 bp tightening since the summer of 2004 will be. In the face of waning economic momentum, the markets will become increasingly susceptible to speculation about an initial rate cut from the summer of 2006 onwards.

Interest Rates USA and Euro area			
	Date	Forecast	Forecast
	12.09.2005	3M	6M
Fed-Funds Rate	3,50 %	4,25 %	4,25 %
3-Months-US-Libor	3,85 %	4,35 %	4,35 %
10 y Treasuries	4,12 %	4,65 %	4,65 %
ECB-Main refinancing	2,00 %	2,00 %	2,00 %
3-Months-Euribor	2,13 %	2,15 %	2,15 %
10y Bunds	3,07 %	3,60 %	3,60 %

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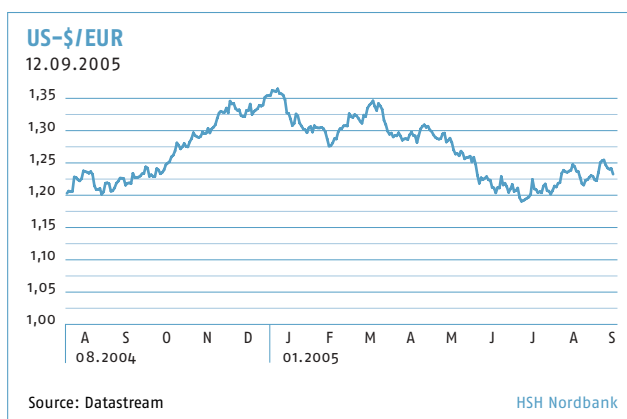
Euro-zone yields in decline

Euro-zone treasuries have lately been going from strength to strength. Temporary concerns about the economy have pushed the yields on 10-year Bunds towards a historic low near the 3 % mark. As growth prospects have meanwhile improved again, we believe that this downward movement will not continue and that yields will gradually tend to normalise again. Having said this, we do not anticipate a real reversal of this trend, given that the ECB will keep its rate unchanged well into next year against the background of the lacklustre economy and stable prices; we do not expect the ECB's monetary policy to change due to the devastation in the Gulf of Mexico. All of which means that US bond market developments will remain the key source of stimulation for European rates.

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"Katrina" leaves mark on the US dollar

The greenback has come under pressure in the wake of "Katrina". Faced with the devastation left behind by the hurricane, many market players felt that the Fed might suspend its rate-raising policy at its September 20 meeting. Most recently the dollar has regained some confidence, even though the real impact of the storm will become visible only in the economic data of the coming quarters. Turning our attention to developments in Europe and Germany, we



note that the euro is suffering from the political stalemate situation which has become more likely in the light of the most recent pre-election polls in Germany. All told, USD/EUR is set to remain within a trading range of 1.21 to 1.26 through September.

Exchange rates				
		Date	Forecast	Forecast
		12.09.2005	3M	6M
USA	USD	1,241	1,23	1,26
UK	GBP	1,675	0,70	0,71
Japan	JPY	135,350	129	129
Switzerland	CHF	1,544	1,55	1,55

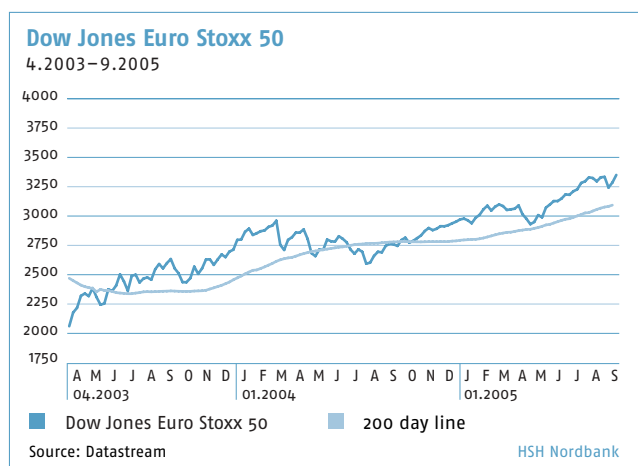
Exchange rates in foreign currency per EUR (1 EUR = x US-\$)

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Capital Markets FX Trading

Stock markets continue to head upwards

The bright sentiment prevailing in the stock markets in recent days has mainly been due to factors related to the devastating hurricane. First the disaster drove the oil price to record highs beyond US\$ 70 per barrel, followed by the release of strategic reserves entailing a softening in the price by a good 10%. Assuming that the devastation may dent US economic growth, many market players expect the Fed to announce a pause in its tightening cycle following its September 20 meeting. Stock prices have also been boosted by takeover speculation particularly in the energy sector (takeover of Endesa by Gas Natural in Spain, Eon's takeover plans for Scottish Power). Add to this the gratifying quarterly reporting season which saw the majority of companies present upbeat outlooks which bear out additional potential for rising stock prices. In contrast, the oil price development remains a key risk to the global economy and to the worldwide stock markets. As for the short term, Germany's upcoming elections on September 18 continue to fuel the DAX. Even though the index has already climbed considerably in the run-up to election day, a change in government might give it further momentum. From a technical perspective, 5,150 or even 5,400 points seem possible. Conversely, a different election outcome would most likely weigh on the index for a short while and entail an interim consolidation. In this case, we see strong technical support at 4,650 points. As for the medium to longer term, we see potential in European equities. Our view is mainly based on a PER of 13, additional takeover speculation and high dividend yields. Averaging 3.3%, these are clearly superior to the yields on 10-year Bunds which are at an historic low at 3.05% p.a. (and are comparatively less favourable in tax terms).



Private-Equity: Investing in ideas for tomorrow

Prospects of attractive returns have stimulated interest in private equity investments on the part of both institutional and private investors. Private equity is a form of investing in non-listed companies which require medium or long-term funding in an important phase of their development. Until recently, private equity investments were possible mainly through closed-end funds and umbrella funds; both of which require high minimum investments which tend to deter private investors. This is all changing now thanks to a new type of private equity investment certificate enabling private investors to invest in this promising and lucrative segment of the market which has so far been the exclusive domain of major insurance companies and pension funds. The new LPX Major Market Index Certificate gives investors exposure to a well diversified private equity index. The underlying LPX Major Market Index comprises 15 leading private equity companies. To ensure effective risk diversification, the index is subject to 6-monthly adjustments which limit each company's weight in the index at 10% of the total market capitalisation of the index. The LPX Major Market Index is a performance index and 75% of the dividends are reinvested.

ABN Amro's LPX Private-Equity Open End certificate offers allure for investors interested in private equity in that it provides diversified exposure to the share price development of the fifteen biggest listed private equity companies. In contrast to classical private equity funds, these certificates can be bought and sold in the markets at any time. The past performance also speaks for itself – since 1998 the LPX index has clearly outperformed such high-profile indexes as the MSCI World, Nasdaq Composite and the DAX. In addition, this private equity instrument only exhibits a low correlation with stock market and bond market indices. The bottom line: the LPX certificate is a liquid instrument allowing investors to optimise the risk/reward structure of their portfolios and buffer their downside risks. Your account manager will be pleased to provide you with further information.

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Port of Hamburg holds a pre-eminent position in Sino-European trade

China has emerged as the European Union's number two trading partner, second only to the USA. The Port of Hamburg has been a clear beneficiary of the dynamic growth in China's foreign trade activity. Building on its traditional links with China, Hamburg has been able to expand its good market position among Europe's ports in the past two decades. In fact, the port not only supplies the German market but also serves as a central hub for trade between China and Germany's North-East European neighbours.

Almost half of Europe's container transshipment volume is handled in the biggest six ports making up the so-called Northern Range, namely Rotterdam, Antwerp, Bremen, Zeebrugge, Le Havre and Hamburg. Over the past two decades Hamburg has steadily expanded its position within this group; while the Hanseatic port accounted for only 14 % of total container transshipment in 1986, this share had risen to roughly 25 % by 2004. This growth has been driven by Hamburg's dominant position in Sino-European trade as well as by its function as a hub for the Baltic Sea nations. A regional specialisation can be observed among the major European ports. For example, China trade accounts for a quarter of Hamburg's container throughput, compared to just under 15 % in Rotterdam.

Remarkably, the Asian share of Hamburg's total transshipment volume has not risen further as a result of the buoyant trade with China; the Asian routes have accounted for a good half of the port's container transshipment volume already for 15 years. Even though trade with the other Asian economies did not contract in absolute volume terms, the extraordinary expansion of Chinese trade handled in Hamburg has resulted in lower market shares for China's Asian neighbours who have seen their combined share decline from 40 % to 28 % since 1989, with China's share rising from 13 % to 24 % during the same period.

Providing a hub for Chinese trade in the Baltic Sea region

Apart from Asia, the Baltic Sea is the second most important cruising area for the container ships docking in Hamburg, accounting for 25 % of the total volume handled. The past 15 years have seen trade with the dynamic Baltic Sea region grow at an average rate of 12.9 % yoy, i.e. almost as fast as trade with China (13.9 %). A good half of the EU's total ex-

ports to China come from countries bordering on the Baltic Sea, that is Germany, Scandinavia, Poland and the Baltic Republics. This is partly due to the good position of German and Scandinavian manufacturers of industrial goods in the world market and also reflects the strong demand for these products in the industrialising Middle Kingdom. A considerable portion of the goods trade between China and the Baltic Sea region runs through the port of Hamburg and feeds into its transit statistics. According to estimates by Hafen Hamburg Marketing e.V., roughly 50 % of the Far Eastern cargo arriving in Hamburg is transhipped. Almost one third of Hamburg's total Asian trade volume either originates in, or is absorbed by, the Baltic Sea region.

Outlook

A considerable portion of the buoyant investment in China has been directed to the country's export sectors in recent years. Therefore, the next two years are likely to see a continuation of the present trends, i.e. strongly expanding Chinese exports and relatively slower growth in Chinese demand for imported capital goods. While demand for consumer goods is set to rise at the same time, German and Scandinavian exporters will benefit from this trend only in smaller measure. Sino-European trade will nevertheless continue to gain in importance because even after a certain cooling the pace of growth of China's foreign trade will still be faster than in most other regions. Against this background, Hamburg is well placed to leverage its traditional links with the Middle Kingdom also in the future.

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In our next issue: Poland, Russia and Balticum

From Hamburg to Sylt – powered by HSH Nordbank and AGV all down the line

With a little stretch of the imagination, trips from Hamburg to the stylish resort of Sylt may soon qualify as “work-related travel” for the employees of HSH Nordbank and the AGV Group. In any case, the trains to be operated on the “Sylt-Express” line from December are owned by a leasing company that is a member of the AGV Group and, hence, of the HSH Nordbank Group.

This great success was achieved by HSH Nordbank and its 40 % subsidiary AGV Group on June 30 and is considered to be the largest transaction in Germany’s local public rail transport sector to date. Two operating leases for 90 railroad cars and four electric locomotives were signed with Nord-Ostsee-Bahn (NOB), Kiel. The agreements were drafted and negotiated by HSH N Nordic Finance AB, a wholly-owned subsidiary of AGV, in coordination with HSH Nordbank. The lessors are two Swedish leasing companies of HSH N Nordic Finance AB. The total investment volume amounts to some EUR 126 million. This highly important transaction marks a milestone in the German rail transport market in more respects than just one:

1. The State of Schleswig-Holstein’s involvement in the leasing model has been shaped in such a way as to ensure efficient competition on this particular route in the long term (i.e. even after a renewed tender for the operation of the line).
2. For NOB, which is a member of the Connex Group, the leases qualify as operating leases to International Financial Reporting Standards (IFRS). Connex focuses on the operation of the route and avoids property risks.
3. HSH N Nordic Finance AB has customised this cross-border leasing transaction to the client’s specific requirements.

But how was the transaction initiated in the first place and what obstacles had to be overcome?

The client: Nord-Ostsee-Bahn

The operator, NOB, is part of the Connex Group, Germany’s largest private railway company. NOB has gained experience in operating lines in and around Kiel, e.g. to Neumünster and Husum, for two years. According to a survey, both the number of travellers and their satisfaction with the service offered have increased noticeably. For the maintenance of

the Sylt Express trains, a workshop has been purpose-built in Husum, where NOB will do the daily maintenance. Regular major inspections will be performed by the manufacturer, Bombardier. NOB will hire 100 new employees, including 70 engine drivers and conductors.

NOB wins the “Marschbahn” tender

A private Kiel-based railway company wins a major contract in Schleswig-Holstein’s local railway transport market? This would have been inconceivable a few years ago. But thanks to Germany’s railway reform, it is now possible. Ever since the railway sector was reformed, more and more regional routes have been put to tender by the transport sponsors (usually the Transport Ministries of the federal states). The percentage of private operators beside Deutsche Bahn AG (DB) has increased to over 10 % and will soon reach approx. 40 % in Schleswig-Holstein – a percentage which puts the state in the number one position in Germany.

The first operators have already tried to engage in long-distance traffic, with varied success. In 2002, Kiel-based NOB won the much-travelled Hamburg-Westerland medium distance route, which required the purchase of high-quality rail coaches as this route cannot be travelled with the two-to-four-segment Diesel Multiple Units typically used for short distances. NOB will operate the Hamburg-Westerland route from December 11, 2005 for an initial period of 10 years. However, there is still dispute about the rail infrastructure use. DB Netz AG (the incumbent operator of the rail network) is refusing to let NOB use the route to Hamburg’s central station, claiming that it has always been used by DB trains (“grandfathering”) and that there is no room for the NOB trains left. Unless the court fails to take a decision in favour of NOB before December 2005, the trains will initially end in Hamburg-Altona.

The manufacturer: Bombardier

Already back in 2003, Connex ordered 90 high-quality coaches suitable for long-distance travel plus four electric engines to extend the passenger trains to Berlin and the Rhineland. The contract was awarded to Bombardier Transportation, the world’s largest manufacturer of rail vehicles. The comfortable coaches are air-conditioned and feature notebook ports. Their maximum speed is 200 km/h – on suitable routes. Between Westerland and Hamburg, they will travel at a maximum speed of 140 km/h, pulled by large 4,000 bhp diesel engines built by Vossloh AG, Kiel. The coaches are built in

Henningsdorf near Berlin, while the Bombardier locomotives are built in Kassel.

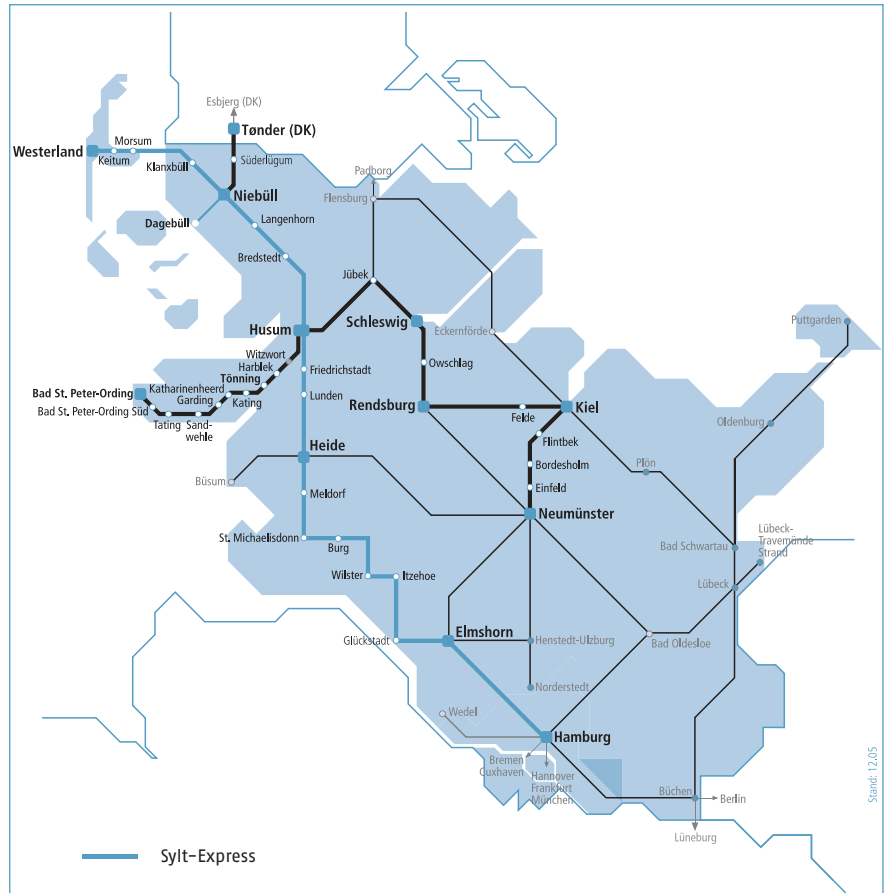
To lease or not to lease

While Connex had selected, configured and ordered the trains and engines, they wanted to finance them off balance sheet and limit the related investment and property risks to the term of the transport agreement. Thus a leasing or rental solution was needed and the obvious decision was to call in the HSH Nordbank, AGV and HSH N Nordic Finance team. After all, the partners had jointly completed not only numerous real estate leasing transactions but also big ticket leases for rail coaches, container ships and regional aircraft for many years.

The project teams on both sides jointly structured an overall concept for Connex and a Term Sheet was finalised in late 2004. But that did not mean that the transaction was complete. Right on the contrary, it merely marked the launch of a complex documentation, structuring and negotiation phase. The political turbulence in the State of Schleswig-Holstein during the first half of the year was only one of the obstacles that had to be overcome.

The solution

Under the leasing structure, NOB rents or leases the trains from a Swedish leasing company. The leasing company will initially step into the delivery contract with Bombardier, fund the down payments, monitor the months-long delivery process and finally make the fleet available to NOB for operation of the Sylt Express network. Financing of the project, from the first payment to Bombardier to providing long-term finance, is managed by HSH Nordbank`s Transport CC. HSH Nordbank is the underwriter of the project and may syndicate out parts of the large volume.



Conclusion

This shared success was made possible by the structured railway finance expertise and leasing know-how for big ticket and cross-border transactions of HSH Nordbank and its partners.

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