German Ship Finance Forum

Case study:
The combination of CSAV’s container shipping activities with Hapag-Lloyd

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Introduction
Introduction – The Merger Parties (pre-closing)

Hapag-Lloyd

• One of the leading global container carriers
• 154* modern container vessels with a capacity of 777,469 TEU
• Extensive network with 101 services around the globe
• Global presence with more than 330 sales offices in 112 countries
• 6,971 employees

*including chartered vessels

CSAV

• One of the world’s oldest and Latin America’s largest container shipping line
• 53 container vessels*
• 30 trades worldwide
• Presence in more than 80 countries; 85 % of the turnover generated by own agencies
• 4,211 employees
Introduction - The Combined Entity

- **200 container vessels** with a capacity of **app. 1m TEU**
- Annual **transport volume** of **7.5m TEU**
- **Turnover** of **€ 9bn**
- Corporate seat and headquarters in **Hamburg**
- Regional headquarters in **Valparaíso, Chile, Piscataway, Singapore**
- Creating the **world’s fourth largest container shipping line**
## Introduction – The 20 Largest Shipping Lines

<table>
<thead>
<tr>
<th>Rank</th>
<th>Shipping Line</th>
<th>TEU</th>
<th>Market Share</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>APM-Maersk</td>
<td>2,603,323</td>
<td>14.5%</td>
</tr>
<tr>
<td>2</td>
<td>Mediterranean Shg Co</td>
<td>2,387,317</td>
<td>13.3%</td>
</tr>
<tr>
<td>3</td>
<td>CMA CGM Group</td>
<td>1,505,728</td>
<td>8.4%</td>
</tr>
<tr>
<td>4</td>
<td>Hapag-Lloyd / CSAV</td>
<td>1,003,498</td>
<td>5.6%</td>
</tr>
<tr>
<td>5</td>
<td>Evergreen Line</td>
<td>876,013</td>
<td>4.9%</td>
</tr>
<tr>
<td>6</td>
<td>COSCO Container L.</td>
<td>772,751</td>
<td>4.3%</td>
</tr>
<tr>
<td>7</td>
<td>Hapag-Lloyd</td>
<td>738,406</td>
<td>4.1%</td>
</tr>
<tr>
<td>8</td>
<td>APL</td>
<td>651,531</td>
<td>3.6%</td>
</tr>
<tr>
<td>9</td>
<td>Hanjin Shipping</td>
<td>601,785</td>
<td>3.4%</td>
</tr>
<tr>
<td>10</td>
<td>CSCL</td>
<td>582,632</td>
<td>3.3%</td>
</tr>
<tr>
<td>11</td>
<td>MOL</td>
<td>552,638</td>
<td>3.1%</td>
</tr>
<tr>
<td>12</td>
<td>Hamburg Süd Group</td>
<td>473,222</td>
<td>2.6%</td>
</tr>
<tr>
<td>13</td>
<td>NYK Line</td>
<td>466,737</td>
<td>2.6%</td>
</tr>
<tr>
<td>14</td>
<td>OOCL</td>
<td>461,140</td>
<td>2.6%</td>
</tr>
<tr>
<td>15</td>
<td>Yang Ming Marine Transport Corp.</td>
<td>369,105</td>
<td>2.1%</td>
</tr>
<tr>
<td>16</td>
<td>Hyundai M.M.</td>
<td>363,763</td>
<td>2.0%</td>
</tr>
<tr>
<td>17</td>
<td>PIL (Pacific Int. Line)</td>
<td>355,844</td>
<td>2.0%</td>
</tr>
<tr>
<td>18</td>
<td>K Line</td>
<td>354,131</td>
<td>2.0%</td>
</tr>
<tr>
<td>19</td>
<td>Zim</td>
<td>328,218</td>
<td>1.8%</td>
</tr>
<tr>
<td>20</td>
<td>UASC</td>
<td>275,834</td>
<td>1.5%</td>
</tr>
<tr>
<td></td>
<td>CSAV Group</td>
<td>265,092</td>
<td>1.5%</td>
</tr>
</tbody>
</table>
The Transaction
The Transaction - Structure

- **Carve out of the container shipping activities ("CCS Activities") of CSAV in 47 jurisdictions**
- **CCS Activities contributed to a German interim holding company ("CC Co")**
- **Contribution by CSAV of CC Co to HL resulting in CSAV becoming a new anchor shareholder of HL** in addition to HGV (holding company of the City of Hamburg) and Kühne

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<table>
<thead>
<tr>
<th>Controlling Shareholder Group</th>
</tr>
</thead>
<tbody>
<tr>
<td>CSAV</td>
</tr>
<tr>
<td>HGV</td>
</tr>
<tr>
<td>Kühne</td>
</tr>
<tr>
<td>TUI</td>
</tr>
<tr>
<td>Minority Shareholders¹</td>
</tr>
<tr>
<td>Car Carriers &amp; Others</td>
</tr>
</tbody>
</table>

Hapag-Lloyd

CC Co (CCS Activities)
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Minority Shareholders¹: HGV, Car Carriers & Others, TUI, Kühne
The Transaction – Structure (cont’d)

- **Post-closing:**
  - CSAV subscribed € 259m of a € 370m capital increase, (the remaining € 111m were subscribed by Kühne)
  - Thereby, CSAV increased its shareholding in the combined entity to 34%
  - IPO planned in the near future (late 2015/2016)
  - Further € 370m capital increase in the course of the IPO
  - In addition to its shareholding in the Combined Entity, CSAV continues to operate **car carriers, reefers and bulkers** ("Retained Activities")
The Transaction – Strategic Rationale

• Hapag-Lloyd and CSAV as **strategic fit**

• **Financial**
  - Value enhancement through synergies
  - Optimization of capital structure and capital increases

• **Strategic**
  - Leadership in selected markets and economies of scale
  - Complementary trade routes
  - Expansion of customer base and strengthening of sales network

• **Operational**
  - Fleet expansion – larger, younger and more efficient vessels
  - State-of-the-art IT through leading, scalable HL systems

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Estimated synergies of US$ 300m p.a.
The Transaction – Timeline

MoU Negotiations

January 2014

MoU signing

Cross Due Diligence

March 2014

BCA Negotiations

May 2014

Global Carve-out

BCA signing

July 2014

Relevant Date Accounts

Merger control notifications and preparation of closing

November 2013

30 Sept. 2014

December 2014

Closing
The Challenges
(and how they were tackled)
The Challenges – Multitude of Shareholders

• Diverse group of shareholders with partially conflicting objectives and expectations requiring flexible solutions in respect of:
  - **Holding period/sales restrictions**: long-term investment vs. short-term exit/flexibility depending on market conditions
  - **Corporate governance**: different levels of participation of shareholders in corporate governance rights
    - Post-merger **joint control** by CSAV (Quiñenco/Luksic), HGV (holding company of the City of Hamburg) and Kühne Maritime
    - Minority shareholders (TUI, banks, insurance companies) with limited/tailored governance rights to ensure support from all relevant stakeholders
  
• Ensuring **transaction certainty** also in the event of new shareholders joining before closing (e.g. due to a pre-closing exit of existing shareholders)
  - (Limited) vote pooling agreements
  - Creation of an authorised capital
The Challenges – Complexity of the Transaction

• All relevant economic, legal and structural issues of the entire transaction agreed upfront in a comprehensive Business Combination Agreement (BCA)

• Carve-out of CSAV’s container shipping activities
  - App. 90% of CSAV’s activities
  - Reverse carve-out of non-container shipping activities (reefer, bulker, car carrier = “Retained Activities”) **not possible** as CSAV TopCo listed at the Santiago stock exchange
  - Detailed description of the transaction object in the BCA (comparable to asset deal, “completeness guarantee”)
  - Carve-Out Step Plan (numerous internal restructuring measures in 47 jurisdictions)
  - **Separation of economic and legal ownership of vessels** to avoid (i) taxation under German controlled foreign corporation (CFC) rules, (ii) re-flagging of ships, and (iii) need to re-negotiate ship finance loans and re-register ship mortgages
  - Numerous worldwide **transitional services**, negotiation of TSAs
  - Comprehensive agreement on the parties’ cooperation during the merger phase: **Carve Out Steering Committee** and **Core Carve Out Agreements**
The Challenges – Complexity of the Transaction (cont’d)

• Transfer of liner operations
  - **Transfer upon closing date not practical**, as transition takes several months (issuance of bills of lading by new carrier, duration of a round trip (“loop“) up to 8 weeks, required licences in certain ports of destination for new carrier)
  - **Solution**: All liner operations transferred pre-closing to CSAV’s subsidiary carrier “Norasia“; shares in Norasia contributed to HL at closing; liner operations to be transferred from Norasia to HL within the HL group post closing

• Cabotage service
  - **Cabotage** = maritime transport of passengers or goods between ports of the same country or confederation of countries (in this case Conosur: Brazil, Uruguay, Argentina, Chile, Peru)
  - Highly profitable, but **certain restrictions** apply: majority of share capital to be held by, and majority of board members of carrier must be Chilean nationals (further requirements: flag state, crewing, construction of vessels operated etc.)
  - **Solution**: Establishment of a cabotage company in which CSAV continues to hold the majority; appropriate structuring of by-laws
• **Due diligence exercise**
  - **Cross due diligence**: Review of HL by CSAV and review of CSAV by HL
  - Numerous internal and external interested parties: operational staff of merger parties, shipping experts, strategy and tax consultants, auditors, lawyers (including 42 local counsels)
  - App. **1500 persons in the (virtual) data room**
  - Definition of tailored materiality thresholds (experience from comparable transactions)
  - More than 10,000 questions and answers, steering via project management office
  - Further steering at the executive board level necessary to ensure focussed DD exercise
The Challenges – Valuation Issues and Timing

- **Determination of the relative valuation of HL and CSAV**
  - Difficulties to reach agreement on **valuation parameters** despite uniform IFRS accounting
    - Background: ships represent 90% of fixed assets; uncertainty as to possible realization of book value due to volatile and non-liquid market for container vessels
    - Future sustainable yields are prone to speculation in volatile markets and against background of restructuring going on for years
    - Substantial fleet investment program by CSAV

- **Time required for negotiating and implementing the transaction**
  - More than one year from the start of negotiations to closing
  - Adjustment mechanism required to determine the relative value of merger parties particularly in light of volatile markets: cash covenant and equity covenant (tailor made adjustment mechanism)
The Challenges – Valuation Issues and Timing (cont’d)

• **Time required for negotiating and implementing the transaction (cont’d)**
  - Comprehensive pre-closing covenants required to validate cash and equity covenants
    - Conduct of business in the ordinary course
    - Implementation of all budgeted investments
    - No leakage

• **Closing review** by HL and CSAV as of 30 September 2014 ("Relevant Date")
  - Compliance with pre-closing covenants
  - Compliance with cash covenant and equity covenant
  - Execution of carve out in accordance with the BCA
  - Audit
  - Additional mutual special purposes review
The Challenges – Merger Clearance and Antitrust Law

- Notification of proposed merger with **15 authorities in 14 jurisdictions** (Argentina, Brazil, Chile, China, Colombia, Costa Rica, Ecuador, EU, Mexico, South Africa, South Korea, Turkey, Ukraine, US (HSR and CFIUS))

- Transaction not only considered as merger of HL und CSAV, but also including controlling HGV, Kühne Maritime and Quiñenco (depending on jurisdiction)

- Container shipping is a fragmented market, but antitrust authorities focus on vessel sharing agreements and alliances/consortia
  - HL is a member of G6
  - China denied clearance of P3 (Maersk, MSC, CMA/CGM)

- “Education” of national antitrust authorities on economic significance of alliances/consortia (in contrast to mergers) required

- No binding timeline for merger clearance eg. in Chile and China

- **High priority of merger clearance work stream**; global coordination and good relationship with national antitrust authorities is key
Thank you for your attention!