European Financial Stability Facility

European Financial Stability Facility

August 2011

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Determined and coordinated action to safeguard financial stability

- **11 February 2010**, the Heads of State and Government of the Euro Area Member States ("EAMS") made it very clear that coordinated action will take place to safeguard the Euro Area
- **12 April 2010**: €110 billion for Greece (€ 80 billion EAMS, € 30 billion IMF)
- **10 May 2010**: €750 billion for European support package to secure stability within the Euro Area
- **7 June 2010**: As part of this package, ***The European Financial Stability Facility ("EFSF")*** was created
- **28 November 2010**: Agreement of financial assistance programme for Ireland (€85 billion)
- **25 January 2011: EFSF inaugural issue as part of programme for Ireland**
- **17 May 2011**: Agreement of financial assistance programme for Portugal (€78 billion)
- **15 June 2011: EFSF's first issue in support of programme for Portugal**
- **20 June 2011:** Agreement by euro zone and EU finance ministers to increase EFSF effective capacity, widen its scope of mandate and to finalise terms of permanent stability mechanism, the European Stability Mechanism (ESM)
- **22 June 2011: EFSF's second issue for Portugal**
- **21 July 2011**: Euro zone summit, second support package for Greece including Private Sector Involvement and increased scope for EFSF/ESM

A robust framework for crisis management …

€750bn Financial Stability Package

European Financial Stabilisation Mechanism "EFSM"

€60 bn

Available to all 27 EU member states

European Financial Stability Facility "EFSF"

€440 bn

(in guarantees by euro area Member States)

For euro area Member States

International Monetary Fund

€250 bn max

Up to half the amount drawn from EFSF and EFSM

… and a clear commitment to future financial stability

- **The Euro Plus Pact was adopted in March 2011. Open to all EU Member States, this pact aims to:**
  - Foster competitiveness
  - Enhance sustainability of public finances
  - Reinforce financial stability

  Member states will pursue these objectives with their own policy-mix taking into account their specific situation

- **On 24 June 2011, the European Council confirmed:**
  - To increase fiscal discipline by strengthening the Stability and Growth Pact
  - To broaden economic surveillance to tackle macro-economic imbalances
  - To set up a permanent crisis resolution mechanism - **European Stability Mechanism ("ESM"**) in 2013 supported by a limited treaty change

- **On 21 July 2011, the euro zone summit agreed** to further widen the scope of activity of EFSF/ESM

- **Measures have been taken to improve financial oversight:**
  - A "European Systemic Risk Board" (ESRB) to monitor high-level risks to the EU's financial system
  - Three supervisory authorities – EBA, EIOPA, ESMA – have been set up to oversee banking, insurance and securities markets

- **On 16 August 2011, President Sarkozy and Chancellor Merkel proposed:**
  - Reinforcing euro zone governance through bi-annual formal meetings, reinforcing the Eurogroup
  - Reinforcing the monitoring and integration of budget and economic policies
  - Harmonisation of business tax, introduction of a financial transaction tax

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EFSF: key features

Mandate: To safeguard financial stability in Europe by providing financial assistance to euro area Member States

- **Guaranteed by €440 billion commitments,** EFSF is an **emergency lending facility** available to all EAMS requesting financial support within a strict conditionality programme
- **Founded 7 June 2010**
- **Based in Luxembourg** (“société anonyme” under Luxembourgish law)
- **Shareholders are the euro area Member States**
- **Headed by Klaus Regling (CEO),** former Director-General for economic and financial affairs at the European Commission, has long-standing experience at the IMF, the German Ministry of Finance and within the private sector
- **Fully operational** since 4 August 2010
- **Tenure of 3 years -** up to June 2013, (after 2013, management and repayment of outstanding debt)

EFSF: AAA credit rating

STANDARD & POOR'S	AAA Stable
MOODY'S	Aaa Stable
FitchRatings	AAA Stable

The top rating and the long-term issuer rating reflect:

- Strong shareholder support
- Credit enhancements
- An organisation supported by the best expertise
- Conservative strategy of funding and investment

EFSF bonds are eligible as ECB collateral

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EFSF: Initial shareholders' contribution

Member States	Credit rating (S&P/Moodys/Fitch)	ECB Capital Subscription Key	Contribution Key	Maximum Guarantee Commitments (€m)	Adjusted Contribution Key
Austria	**(AAA/Aaa/AAA)**	**1.9%**	**2.8%**	**12,241**	**3.0%**
Belgium	(AA+/Aa1/AA+)	2.4%	3.5%	15,292	3.7%
Cyprus	(BBB+/Baa1/BBB)	0.1%	0.2%	863	0.2%
Finland	**(AAA/Aaa/AAA)**	**1.3%**	**1.8%**	**7,905**	**1.9%**
France	**(AAA/Aaa/AAA)**	**14.2%**	**20.4%**	**89,657**	**21.9%**
Germany	**(AAA/Aaa/AAA**	**18.9%**	**27.1%**	**119,390**	**29.1%**
Greece	(CC/Ca/CCC)	2.0%	2.8%	12,388	0.0%
Ireland	(BBB+/Ba1/BBB+)	1.1%	1.6%	7,002	0.0%
Italy	(A+/Aa2/AA-)	12.5%	17.9%	78,785	19.2%
Luxembourg	**(AAA/Aaa/AAA)**	**0.2%**	**0.3%**	**1,101**	**0.3%**
Malta	(A/A1/A+)	0.1%	0.1%	398	0.1%
Netherlands	**(AAA/Aaa/AAA)**	**4.0%**	**5.7%**	**25.144**	**6.1%**
Portugal	(BBB-/Ba2/BBB-)	1.8%	2.5%	11,035	0.0%
Slovakia	(A+/A1/A+)	0.7%	1.0%	4,372	1.1%
Slovenia	(AA/Aa2/AA)	0.3%	0.5%	2,073	0.5%
Spain	(AA/Aa2/AA+)	8.3%	11.9%	52,353	12.8%
Total		**100%**	**100%**	**440,000**	**100%**

In case a country steps out, contribution keys would be readjusted among remaining guarantors and the €440 guarantee committee amount would decrease accordingly

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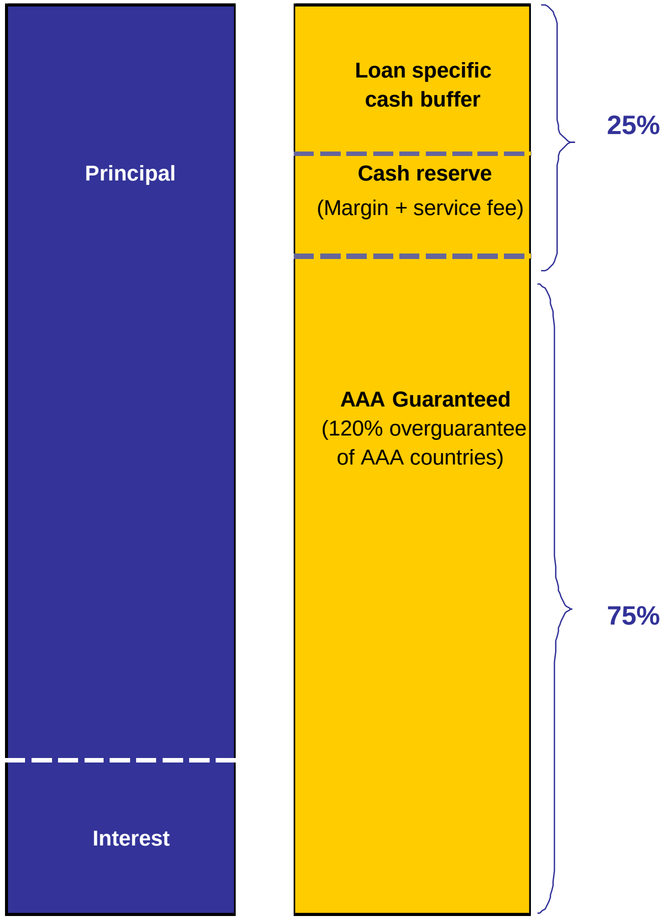
EFSF: credit enhancements

The credit enhancements are designed to **cover payments in case of any payment default from a borrower**. The guarantees cover both principal and interest.

- **Over-guarantee**
  - Each guarantor issues unconditional and irrevocable guarantees to the amount of
    - Contribution Key* x 120% x EFSF Obligations
- **Cash reserve raised from borrowers at inception (loss absorbing capital)**
  - One-off 0.5% Service Fee
  - PV of loan margin is retained by EFSF from loan upfront
  - Cash reserve to be distributed to Guarantors only after payment of all bonds issued by EFSF
- **Loan specific cash buffer (loss absorbing capital)**
  - EFSF can require borrowers to contribute additional amounts from loan advances to ensure a 100% AAA rating



* The contribution key is on a pro rata basis in accordance with EAMS' share in the paid-up capital of the European Central Bank

A solid and simple mechanism to ensure timely payments

- If a payment is missed by a borrower, the country programme could be interrupted and subsequently reviewed and the MoU renegotiated but the **conditionality would still exist**
- In order to allow timely processing of payments, the scheduled payment dates for loans are at least 14 days prior to the scheduled payment dates under the related funding instruments
- In the case of a missed payment by a borrower, EFSF would ensure that **each Guarantor remits its share of the shortfall** to the EFSF
- The shortfall would be covered by the:
  1. **Guarantees**
  2. **Grossing up of guarantees (120% over-collateralisation)**
  3. **Loan-specific cash buffer**
  4. **Cash reserve**
- All guarantors rank equally and ***pari passu*** amongst themselves

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EFSF

EFSF: a lean organisation supported by the best expertise

Board of Directors*

European Financial Stability Facility

CEO Klaus Regling +
about a dozen staff covering:
Operations:
- Funding strategy
- Lending
- Risk management

Research
Legal
Communication
Corporate governance,
Audit, accounting & admin

Federal Republic of Germany
Finance Agency GmbH

Finanzagentur (German DMO)

Front/Back office
debt issuance
cash management
risk management

European Investment Bank

European Investment Bank

Accounting
Documentation
Infrastructure (IT & Facility)
Procurement

ECB
(Account opened)

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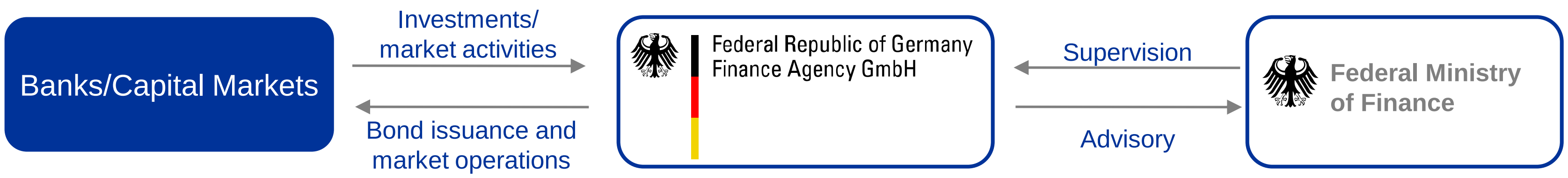
*The Board of Directors is composed of each Shareholder's representative in the Eurogroup Working Group (in most cases the respective Deputy Minister of Finance).

Supported by the German debt management office

Finanzagentur (German debt management office):
Europe's benchmark issuer (€338bn funding volume in 2010)

Services to EFSF
Front office:
debt issuance
cash management
risk management



Tasks and targets

- Managing the German federal governments issuance, activities, debt and liquidity
- Reduce interest costs and optimise funding conditions
- Ensure benchmark status of German government securities
- Providing advisory services related to the funding of the fiscal budget, the cash and debt management
- Market analysis, managing the debt portfolio, risk control, investor relations

Supported by the German debt management office

Roles and achievements

Benefits of Market Practices

- Support of liquidity for German government securities
- Market insight: identifying fair pricing levels exist, liquidity situation, identifying demand structures
- Broad picture of prevailing market situation
- Close cooperation with international banks and investors contribute to optimisation of funding conditions and issuance activities
- Collecting information for structuring issuance activities on a long-term horizon
- Placement of securities along investor demand

Achievements

- Successful funding across the years (bid/cover/ average of around 2)
- Establishment of new funding tools: building up a curve in inflation-linked bonds, rare issue of FX bonds
- Permanent Interest cost savings of around €500m annually
- Broader investor base
- Transparent and reliable market appearance

Supported by the German debt management office

Market practices

Permanent cooperation with the major international banks: Primary market auctions, secondary market activities, market analysis, investor activities, syndicated issues

Market practices German Finance Agency

Primary market	Secondary market	Management of the debt portfolio	Market analysis	Investor activities	Risk control and management	Corporate communications
▪ Multi price auctions (voluntary participation/web-based system) ▪ Annual and quarterly issuance calendar (€338bn in 2010) ▪ Bund issues auction group (33 international banks) ▪ Syndicated issues	▪ Market operations in German government securities ▪ Liquidity support ▪ Swaps ▪ Money market	▪ Structuring the annual issuance calendar ▪ Improving diversification by more funding tools ▪ Adjusting funds activities based on macro-economic analysis ▪ Reaching a target portfolio ▪ Implementing cost and risk preferences of the issuer	▪ Valuation of Bund curves ▪ Monitoring market indicators ▪ Analysing auctions ▪ Identifying issuance windows ▪ Analysing market segments for new funding tools (e.g. inflation linked bonds) ▪ Analysing peer markets	▪ Serving information to investors actively and on request ▪ Meeting investors globally ▪ Analysing investor demand and secondary market structures	▪ Monitoring counter-party and market risk permanently ▪ Arranging and checking limits ▪ Federal budget planning ▪ Accounting	▪ Reporting to press ▪ Serving information to press and media ▪ Arranging publications or interviews ▪ Answering requests on most recent or specific topics

How the EFSF works: loan disbursement and funding strategy

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EFSF: loan request procedure

Application for aid
EAMS makes **formal request** to other members

Support programme
European Commission negotiates stabilization programme – including **strong conditionality** - in cooperation with the IMF and in liaison with the ECB

Approval of loan terms
A common **MoU*** of loan terms is established between the EC, the IMF and beneficiary country and approved by Eurogroup and IMF Board

Loan disbursement
EFSF finalises **technical terms of loan:** term, redemption, schedule, interest rate.
On defined date, EFSF **makes loan available** to borrower

3 to 4 weeks

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EFSF

***** Memorandum of Understanding

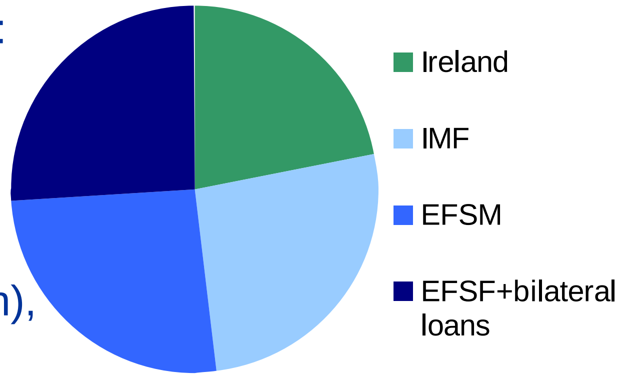
Financial assistance programme for Ireland

Objectives of the programme

- Immediate **strengthening and comprehensive overhaul of the banking sector** — €35 billion
- Ambitious **fiscal adjustment** to restore fiscal sustainability, **correction of excessive deficit by 2015** — €50 billion
- **Growth enhancing reforms**, in particular on the labour market, to allow a return to a robust and sustainable growth

Financing

- The total **€85 billion** of the programme will be financed as follows:
  - €17.5 bn contribution from Ireland (Treasury and NPRF*)
  - €67.5 bn external support
    - €22.5bn from IMF
    - €22.5bn from EFSM
    - €17.7bn from EFSF + bilateral loans from the UK (€3.8bn), Denmark (€0.4bn) and Sweden (€0.6bn)



Disbursements will be made over 3 years with an average loan maturity of 7½ years**

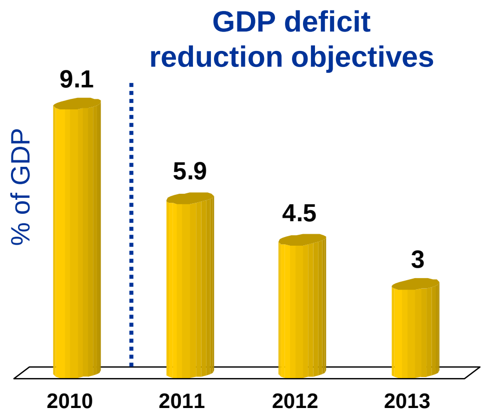
* National Pension Reserve Fund

** Maturity and lending costs are subject to revision following euro zone summit of 21 July (see slide 24)

Financial assistance programme for Portugal

Objectives of the programme

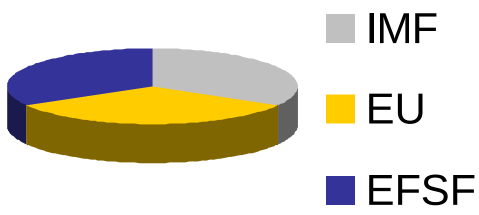
- Restore fiscal sustainability through ambitious fiscal adjustment
- Enhance growth and competitiveness via reforms and measures, i.e.
  - Freeze govt. sector wages until 2013, reduce pensions over €1500
  - Reform unemployment benefits and reduce tax deductions
  - Execute an ambitious privatisation programme (TAP, Caixa Seguros …)



- Improve liquidity and solvency of financial sector
  - Banking support scheme of up to €12 billion to provide necessary capital for banks to bring Tier 1 capital ratios to 10% by end 2012 in case market solutions cannot be found

Financing

- The total **€78 billion** of the programme will be financed as follows:
  - €26 billion from IMF
  - €26 billion from the EU (EFSM)
  - €26 billion from EFSF



Disbursements will be made over 3 years with an average loan maturity of 7½ years*

* Maturity and lending costs are subject to revision following euro zone summit of 21 July (see slide 25 and 26)

New financial support for Greece …

A second programme for Greece totalling €109 billion

- To be financed by euro zone (through the EFSF) and IMF
- Key elements to improve debt sustainability:
  - Lower interest rates (but above EFSF funding costs plus operational costs)
  - Extended maturities (from current average of 7.5 years to a minimum average of 15 years and up to 30 years with 10 year grace period)
- European Commission will create a task force to work with the Greek government to improve growth and competitiveness

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… with Private Sector Involvement

"Greece requires an exceptional and unique solution"
Statement by Euro zone summit – 21 July 2011

The Financing Offer for Greece offers a menu of new instruments to investors in order to mobilize voluntary participation.

In addition to the opportunity to participate in a debt buyback programme established by the Greek government, investors are offered the following four instruments:

1. A Par Bond Exchange into a 30 year instrument
2. A Par Bond offer involving rolling-over maturity Greek government bonds into 30 year instruments
3. A Discount Bond Exchange into a 30 year instrument
4. A Discount Bond Exchange into a 15 year instrument

All instruments will be priced to produce a 21% Net Present Value loss based on an assumed discount rate of 9%.

For instruments 1,2 and 3 the principal is fully collateralized by 30 year zero coupon AAA bonds. For instrument 4, the principal is partially collateralized through funds held in an escrow.

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EFSF issuance

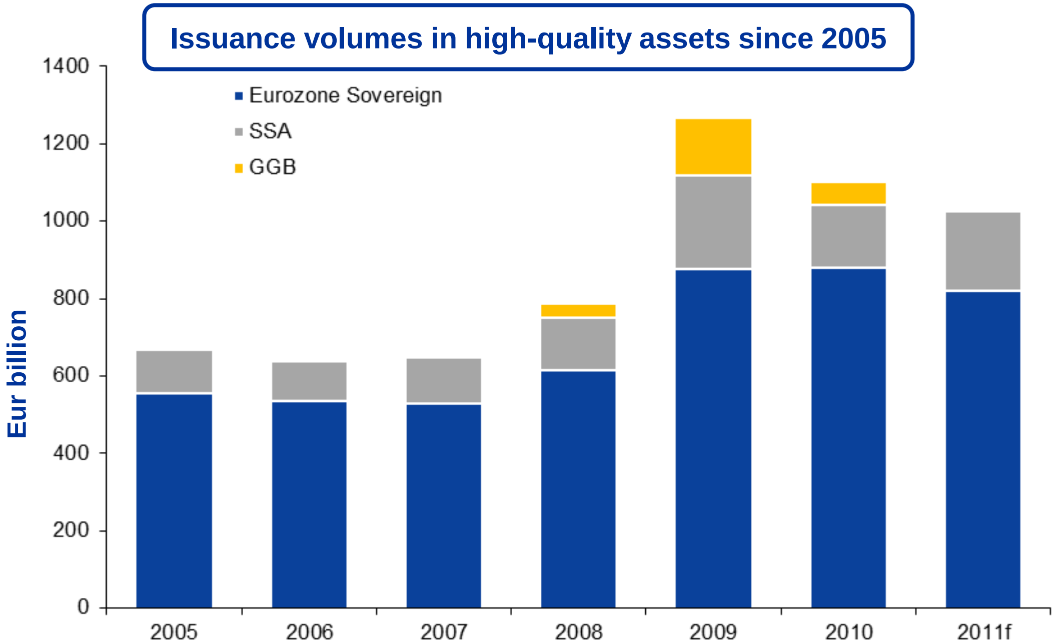
EFSF funding strategy

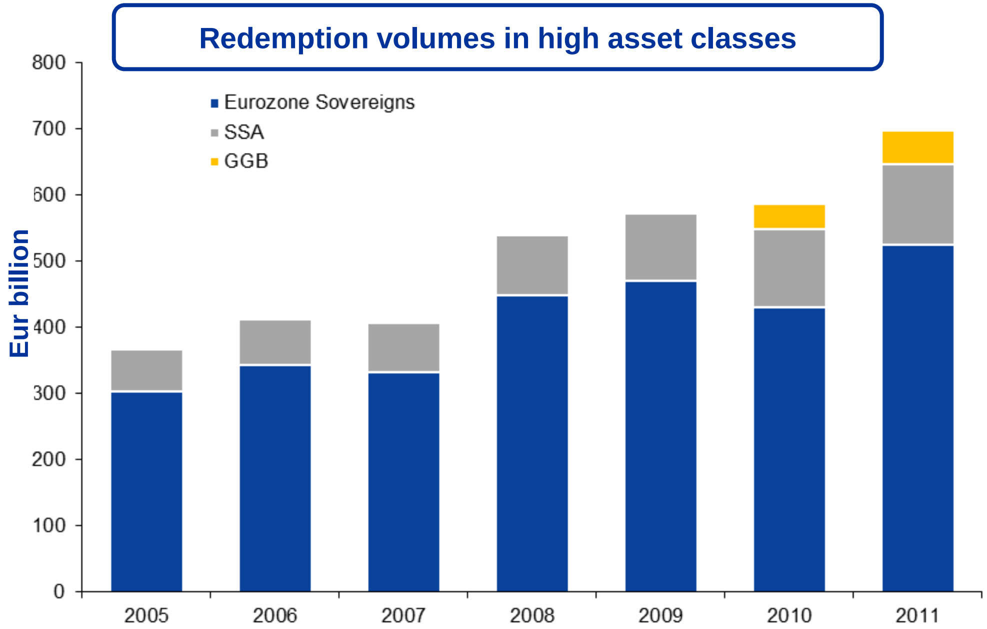
- EFSF does **not pre-fund** until a programme has been approved for a euro area Member State
- **Flexibility:** Funding instruments do not need to be “back to back” with lending operations, but shall have in general the same profile as the related loans to the country in difficulty
- **Size/Maturity:** EFSF strategy adapts to market conditions in order to meet investors requirements for **liquidity**
- **Currencies:** The EFSF does not have any currency limitation for its funding activities but it is expected that the majority of funds would be raised in euro. The EFSF would in all likelihood need to swap the proceeds back into euro
- **Issuance method:** Syndications and auctions, private placements, new lines and tap issues
- In addition to the financing instruments already mentioned, **short-term instruments** would be used to insure the needed continuity in financing

  The funding strategy should be described as SSA (Sovereign, Supranational, Agency) type through **benchmark issuance**, with focus on a high standard of liquidity. This would permit volumes and pricing to be in line with what is expected from the EFSF mission and is in line with the ECB classification

Strong market demand for EFSF issues

- Euro-denominated sovereign or quasi-sovereign issuance **volumes grew significantly** in 2008 and 2009, boosted by higher EGB and SSA volumes, but also by the **emergence of the government-guaranteed bank** (GGB) asset class
- Net **issuance fell in 2010 and will be even lower in 2011**. Redemption is likely to be reinvested in assets of similar credit, offering **better funding conditions to high quality issuers**
- The new **Basel III** regulation will require banks to be invested more in high quality and most liquid fixed income products





Source: Deutsche Bank and Dealogic, 30/06/2011

EFSF issuance calendar for Ireland and Portugal

	2011	After 2011
Ireland	**Up to €15 billion** 3 benchmark bonds of €3-5 billion per transaction. (including first €5 bn bond issued on 25 January)	**Up to €10 billion**
Portugal	**Up to €18 billion** 4 benchmark bonds of €3-5 billion per transaction (including €5 bn bond issued on 15 June and €3bn bond issued on 22 June)	**Up to €17 billion**

EFSF may complement their funding needs by smaller bond issues, through taps or targeted issues

Data is preliminary and can change due to market developments. Actual funding and disbursements will be subject to Portugal's and Ireland's requirements and to quarterly reviews by the Commission in cooperation with the IMF and in liaison with the ECB.

Due to its structure of over guarantee and cash buffer, EFSF, under its current structure, needs to raise an amount above that of its disbursements.

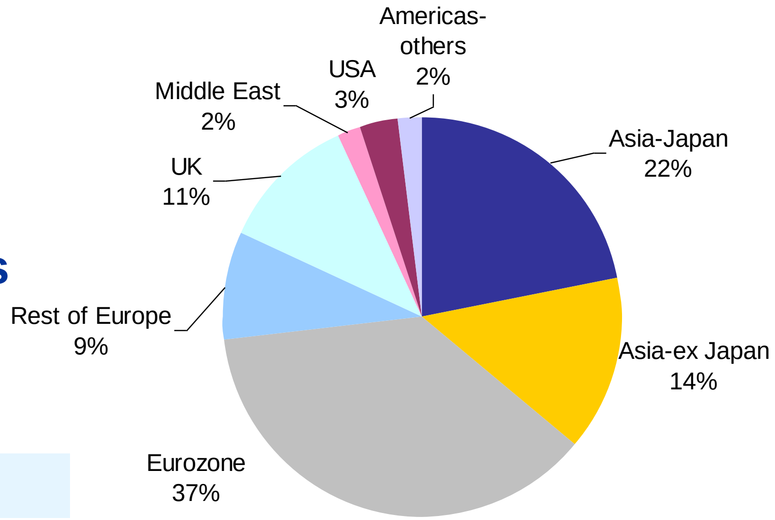
EFSF inaugural issue : record breaking investor demand

On **25 January 2011**, EFSF placed its inaugural issue in support of Ireland.

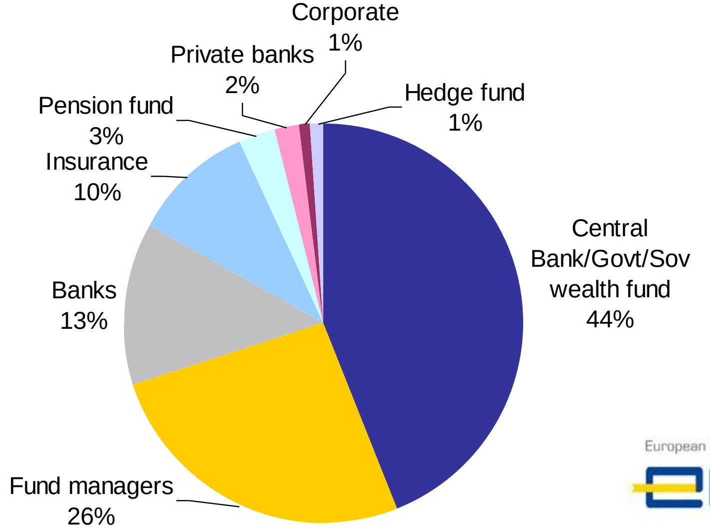
- Record breaking order book of **€44.5 bn**
- Orders received from over **500 investors**

Amount placed	€5 billion
Maturity	18/07/2016
Coupon	2.75%
Initial pricing	Mid swap +6bp
Reoffer yield	2.892%
Reoffer price	99.302%
Settlement date	1 February 2011
Lead managers	Citi, HSBC, Société Générale
Effective lending cost	5.9%
Amount transferred to Ireland	€3.6 billion

Geographical breakdown



Breakdown by investor type



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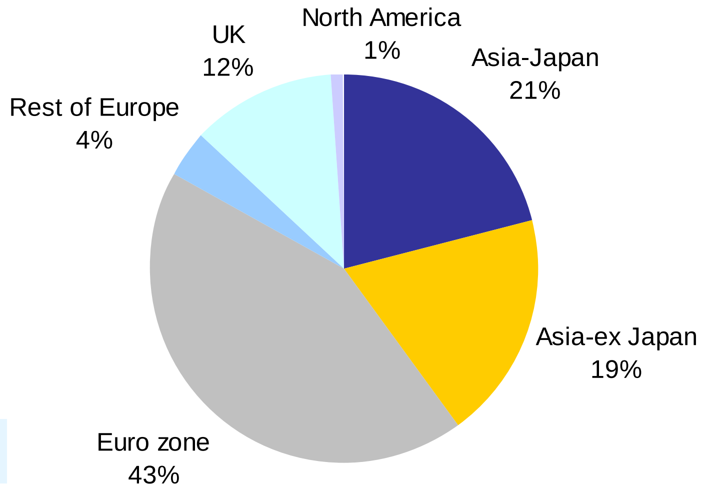
First issue for Portugal

On **15 June 2011**, EFSF placed its first issue in support of the Portuguese programme

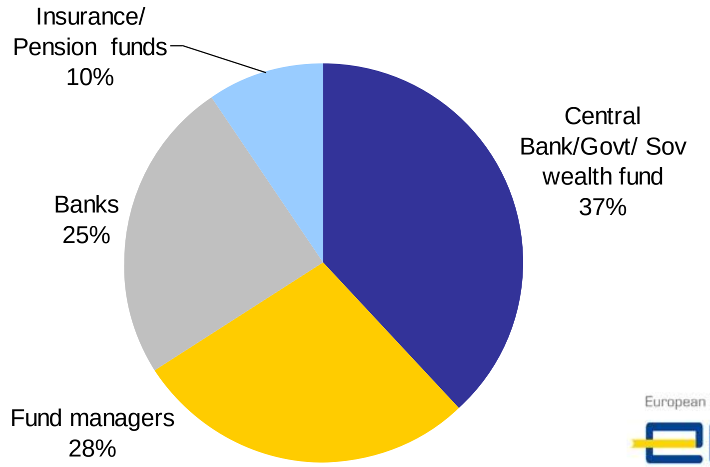
- **10 year maturity**
- Orders received from over **100 investors**

Amount placed	€5 billion
Maturity	05/07/2021
Coupon	3.375%
Initial pricing	Mid swap +17bp
Reoffer yield	3.493%
Reoffer price	99.013%
Settlement date	22 June 2011
Lead managers	Barclays, Deutsche Bank, HSBC
Effective lending cost	6.08%
Amount transferred to Portugal	€3.7 billion

Geographical breakdown



Breakdown by investor type



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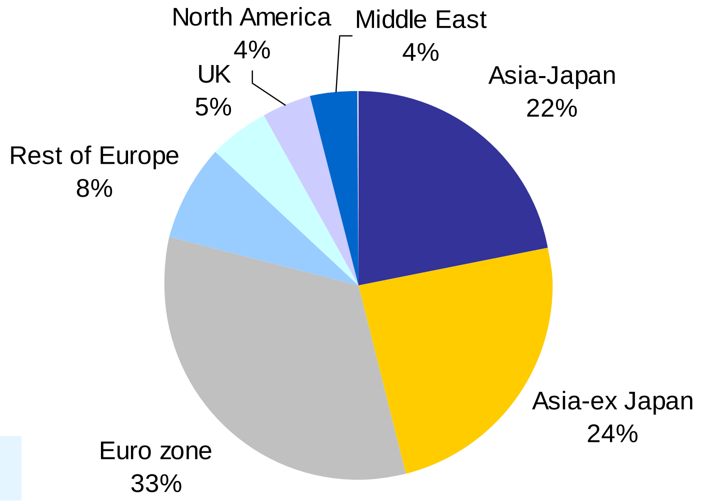
Second issue for Portugal

On **22 June 2011**, despite volatile market conditions, EFSF placed its second issue in support of the Portuguese programme

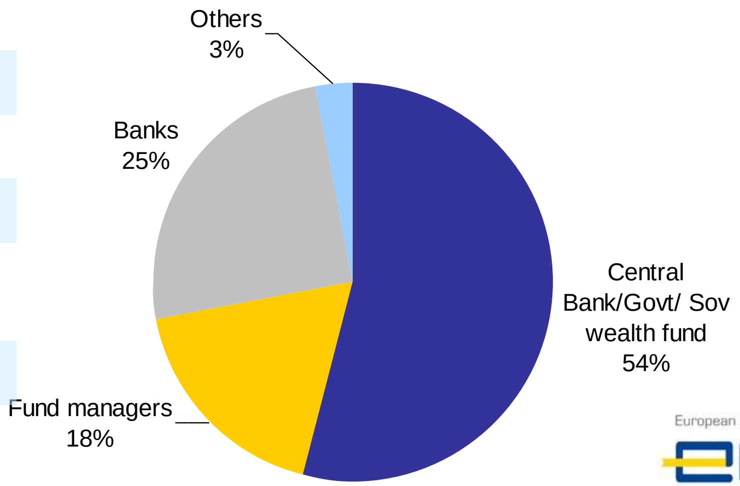
- **€3 billion issue** with a **5 year maturity**
- Order book in excess of €7 billion

Amount placed	€3 billion
Maturity	05/12/2016
Coupon	2.750%
Initial pricing	Mid swap +6bp
Reoffer yield	2.825%
Reoffer price	99.636%
Settlement date	29 June 2011
Lead managers	BNP Paribas, Goldman Sachs, RBS
Effective lending cost	5.32%
Amount transferred to Portugal	€2.2 billion

Geographical breakdown



Breakdown by investor type



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Going forward

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Going forward: amended EFSF…

With the objective of raising EFSF's effective lending capacity and efficiency, it has been agreed to:

- **Increase maximum guarantee commitments to €780 billion**
- **revise the credit enhancement structure**
  - **Credit enhancement of up to 165% over-guarantee** to cover payments in case of any payment default from a borrower. The guarantees cover both principal and interest.

Cash reserve, loan specific cash buffer and service fee no longer required

- authorise EFSF to exceptionally **intervene in the debt primary market** only within a programme with strict conditionality

Estonia will become EFSF's 17th shareholder

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EFSF

…and additional tasks for the EFSF

To improve effectiveness, the euro zone summit of 21 July agreed to authorise the EFSF and future ESM to:

- Act on the basis of a precautionary programme
- Finance recapitalisation of financial institutions through loans to governments including in non programme countries
- Intervene in the secondary markets on the basis of an ECB analysis recognizing the existence of exceptional financial market circumstances and risks to financial stability and on the basis of a decision by mutual agreement of EFSF/ESM Member States to avoid contagion

All amendments to the EFSF Framework Agreement will be effective following national ratification or approval procedures in all Euro area countries

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Going forward: amended EFSF shareholder contribution

Member States	Credit rating (S&P/Moodys/Fitch)	Original EFSF maximum guarantee Commitments (€m)	Amended EFSF maximum guarantee Commitments (€m)	Amended EFSF contribution key (%)
Austria	**(AAA/Aaa/AAA)**	**12,241**	**21,639**	**2.98**
Belgium	(AA+/Aa1/AA+)	15,292	27,031	3.72
Cyprus	(BBB+/Baa1/BBB)	863	1,525	0.21
Estonia	(AA-/A1/A+)	-	1,994	0.28
Finland	**(AAA/Aaa/AAA)**	**7,905**	**13,974**	**1.92**
France	**(AAA/Aaa/AAA)**	**89,657**	**158,487**	**21.83**
Germany	**(AAA/Aaa/AAA**	**119,390**	**211,045**	**29.07**
Greece	(CC/Ca/CCC)	12,388	21,897	0.00
Ireland	(BBB+/Ba1/BBB+)	7,002	12,378	0.00
Italy	(A+/Aa2/AA-)	78,785	139,267	19.18
Luxembourg	**(AAA/Aaa/AAA)**	**1,101**	**1,946**	**0.27**
Malta	(A/A1/A+)	398	704	0.10
Netherlands	**(AAA/Aaa/AAA)**	**25,144**	**44,446**	**6.12**
Portugal	(BBB-/Ba2/BBB-)	11,035	19,507	0.00
Slovakia	(A+/A1/A+)	4,372	7,727	1.06
Slovenia	(AA/Aa2/AA)	2,073	3,664	0.51
Spain	(AA/Aa2/AA+)	52,353	92,543	12.75
Total		**440,000**	**779,783**	**100**

In case a country steps out, contribution keys would be readjusted among remaining guarantors and the guarantee committee amount would decrease accordingly. Greece, Ireland and Portugal have become Stepping-Out Guarantors. This means that as of the Effective Date of the Amendments the aggregate of the active Guarantee Commitments is EUR 726,000 million

European Financial Stability Facility

Going forward: creation of a permanent crisis mechanism

The creation of the **European Stability Mechanism (ESM)**

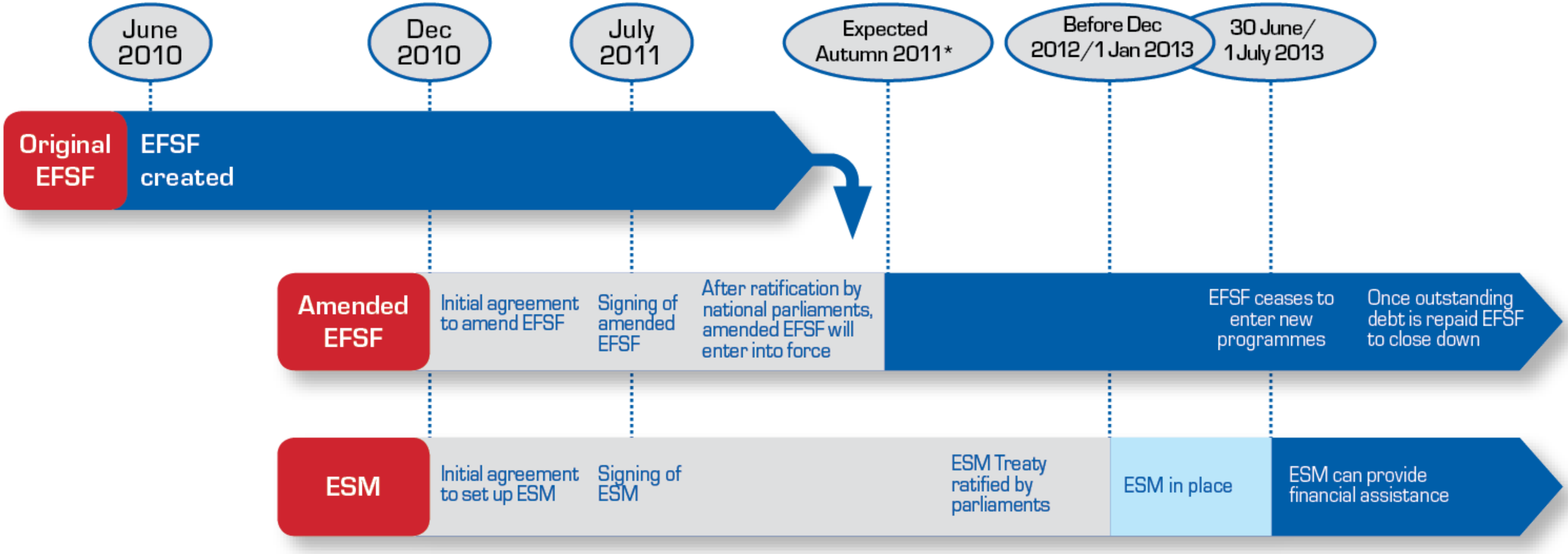
- an **intergovernmental organisation** under public international law, operational from mid-2013
- ESM will provide financial assistance to euro area Member States, and may also exceptionally **intervene in debt primary market**, within a programme with strict conditionality
- ESM will take over **all the features** of the amended EFSF
- **effective lending capacity of €500 billion**
- **total subscribed capital of €700 billion**, with paid-in capital (€80 billion) and committed callable capital and guarantees (€620 billion)
- **private sector involvement**
  - Case-by-case based on debt sustainability analysis
  - Following established IMF policies
  - ESM will claim preferred creditor status (except for countries under a European financial assistance programme in June 2011)
  - Standardized and Collective Action Clauses (CACs) will be included for all new euro area government bonds from June 2013

ESM treaty to be ratified by euro zone country parliaments.

European Financial Stability Facility

EFSF

Going forward: EFSF / ESM timeline



* Transfer to Amended EFSF depends upon national ratification procedures and therefore the timeline may change

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European Financial Stability Facility

EFSF

EFSF: issuance

Bond issue	Issue date	Maturity	Amount issued	Issued at MS	Programme
EU000A1G0AA6	25/01/2011	18/07/2016	€5,000,000,000	+6bp	Ireland
EU000A1G0AB4	15/06/2011	5/07/2021	€5,000,000,000	+17bp	Portugal
EU000A1G0AC2	22/06/2011	05/12/2016	€3,000,000,000	+6bp	Portugal