

European Financial Stability Facility (EFSF)

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Section A – EFSF general questions

➤ A1 - What is the EFSF?

The European Financial Stability Facility (EFSF) is a company which was agreed by the countries that share the euro on 9 May 2010 and incorporated in Luxembourg under Luxembourgish law on 7 June 2010¹. The EFSF's objective is to preserve financial stability of Europe's monetary union by providing temporary financial assistance to euro area Member States if needed.

On June 24, the Head of Government and State agreed to increase EFSF's scope of activity and increase its guarantee commitments from €440 billion to €780 billion which corresponds to a lending capacity of €440 billion and on July 21, the Heads of Government and State agreed to further increase EFSF's scope of activity²

Following the conclusion of all necessary national procedures, these amendments to the EFSF Framework came into force on 18 October 2011³.

➤ A2 - What is the EFSF's scope of activity?

In order to fulfil its mission, the EFSF is authorised to:

- issue bonds or other debt instruments on the market to raise the funds needed to provide loans to countries in financial difficulties.
- intervene in the debt primary market
- intervene in the debt secondary markets
- act on the basis of a precautionary programme

¹ See http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/misc/114977.pdf

² See http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/123979.pdf

³ For further information on the original EFSF before the amendments came into force, please see Annex 1.

- finance recapitalisations of financial institutions through loans to governments including in non-programme countries

All financial assistance to Member States is linked to appropriate conditionality.

➤ **A3 – How are EFSF issues backed?**

EFSF issues are backed by guarantees given by the euro area Member States for €724.47 billion in accordance with their share in the paid-up capital of the European Central Bank (see table below)

	EFSF amended contribution key* (%)
Austria	2.9869
Belgium	3.7313
Cyprus	0.00
Estonia	0.2754
Finland	1.9289
France	21.8762
Germany	29.1309
Greece	0.00
Ireland	0.00
Italy	19.2233
Luxembourg	0.2687
Malta	0.0972
Netherlands	6.1350
Portugal	0.00
Slovakia	1.0666
Slovenia	0.5058
Spain	12.7739
Total	100.00

As of 30 April 2013

* The amended contribution key takes into account the stepping out of Greece, Ireland, Portugal and Cyprus.

➤ **A4 - Where is the EFSF headquartered?**

The EFSF is located at 6a, Circuit de la Foire Internationale, L-1347 Luxembourg.

➤ **A5 – How big is the EFSF?**

The EFSF is a lean organisation, with a staff of around 110 people.

➤ **A6 - Who manages the EFSF?**

The Chief Executive Officer is Klaus Regling, a former Director General of the European Commission's Directorate General for Economic and Financial Affairs who also worked at the International Monetary Fund (IMF) and the German Ministry of Finance and has professional experience of working in financial markets.

➤ **A7 - Who oversees the EFSF?**

The board of the EFSF comprises high level representatives of the 17 euro area Member States

i.e. Deputy Ministers or Secretaries of State or director generals of national treasuries. The European Commission and the European Central Bank (ECB) each have observers on the EFSF board. The EFSF board is headed by the Chairman of the EU's Economic and Financial Committee.

➤ A8 - Does the European Parliament have an oversight role?

Although there is no specific statutory requirement for accountability to the European Parliament, EFSF has a close relationship with the relevant committees.

➤ A9 - Is the EFSF a preferred creditor?

No. Unlike the IMF the EFSF has the same standing as any other sovereign claim on the country (*pari passu*). Private investors would be reluctant to provide loans to the country concerned if there were too many preferred creditors.

➤ A10 - Are EFSF bonds eligible for ECB repo facilities?

EFSF debt instruments are eligible as collateral in European Central Bank refinancing operations⁴.

EFSF as an "Agency – non-credit institution" falls under liquidity category II of the Eurosystem collateral approach. Talks with other Central Banks and regulators (*inter alia* FSA, SEC) for EFSF eligibility and classification are ongoing.

➤ A11 - What rating does the EFSF have?

The EFSF has been assigned an AA rating by Standard & Poor's, an Aa1 rating by Moody's and an AA+ by Fitch Ratings.⁵

EFSF has been assigned the highest possible short-term rating from all three major credit rating agencies – Standard and Poor's (A-1+); Moody's (P-1) and Fitch Ratings (F1+).

➤ A12 - Would the EFSF default if one of its borrower countries defaulted?

The guarantee mechanism under the Framework Agreement is designed to exclude such a situation. If a country were to default on its payments, guarantees would be called in from the guarantors. The shortfall would be covered by the:

- Guarantees
- Grossing up of guarantees (up to 165% over-collateralisation)

If a guarantor did not respect its obligations, guarantees from others could be called in to cover the shortfall. All guarantors rank equally and *pari passu* amongst themselves.

➤ A13 – Are the guarantees provided by euro area Member States unlimited?

No guarantor is required to issue guarantees which would result in it having a guarantee exposure in excess of its aggregate guarantee commitment, as stated in the EFSF Framework Agreement.

➤ A14 – Do the guarantees vary between series of bonds?

Guarantees would vary between bonds that were issued under the original EFSF and bonds that

⁴ The ECB List of eligible marketable assets can be consulted using the following link:
<http://www.ecb.europa.eu/mopo/assets/assets/html/index.en.html>
https://mfi-assets.ecb.int/query_EA.htm

⁵ See http://www.efsf.europa.eu/investor_relations/rating/index.htm
9 December 2013

will be issued under the amended EFSF due to the change in the credit enhancement structure of the amended EFSF.

Furthermore, the composition of the list of guarantors and their respective Guarantee Contribution Key % may vary between different bonds by reason either of a Guarantor becoming a Stepping-Out Guarantor or the adherence of a new euro area Member State to EFSF. Such adjustments do not change the composition of the list of Guarantors or their Guarantee Contribution Key % for Notes already issued but only for the bonds issued after the relevant event.

➤ **A15 - Can countries step down from a guarantee already made?**

No – guarantees are “irrevocable and unconditional”

➤ **A16 – Can the EFSF recapitalise banks?**

The EFSF is authorised to provide loans to Member States which then use the funds to recapitalise their financial institutions.

This may occur within a macro-economic adjustment programme as was the case for Ireland when it was agreed that Ireland would use funds to stabilise the banking sector. €35 billion out of the total €85 billion of the Irish programme has been allocated to the banking sector.

Following the agreement of the Heads of Government and State on 21 July, EFSF may provide assistance to a Member State which is not within a programme to enable it to recapitalise financial institutions.

➤ **A17 – What is the current status of the EFSF?**

As of 1 July 2013, the EFSF may no longer engage in new financing programmes or enter into new loan facility agreements. This is in accordance with the EFSF Framework Agreement signed by the 17 euro area Member States, and the EFSF Articles of Incorporation. From that date, the European Stability Mechanism (ESM) is the sole and permanent mechanism for responding to new requests for financial assistance by euro area Member States.

The EFSF will remain active in financing the ongoing programmes for Portugal, Ireland and Greece. The EFSF will be dissolved and liquidated when all financial assistance provided to euro area Member States and all funding instruments issued by the EFSF have been repaid in full.

More information on the ESM is available at <http://www.esm.europa.eu/>.

Section B – Funding

➤ **B1 – What is the EFSF's funding strategy?**

Initially the EFSF used a simple back-to-back funding strategy. In November 2011, a diversified funding strategy was adopted using a liquidity buffer as a key component. As part of this strategy, EFSF has introduced a short term bill programme and since the end of last year, we have held regular auctions of 3-month and 6-month bills, all of which have met with strong demand from the investor community.

One consequence of our diversified strategy is that funds raised are no longer attributed to a particular country. The funds are pooled and then disbursed to programme countries.

➤ **B2 – Which banks may act as lead managers?**

The lead managers are mandated from the 46 international institutions that make up the EFSF

Market Group⁶. The lead managers are chosen following a rigorous and transparent selection process.

➤ B3– Who are the main investors in EFSF bonds?

Investors in EFSF bonds are predominantly institutional investors such as banks, pension funds, central banks, sovereign wealth funds, asset managers, insurance companies and private banks. The investor base is varied geographically with interest from around the world.

Detailed information showing geographical breakdown and breakdown by investor type for each issue is available on the EFSF website (please see http://www.efsf.europa.eu/investor_relations/issues/index.htm).

➤ B4 - Can EFSF and EFSM⁷ be in the market at the same time?

As the Irish and the Portuguese programmes show, the issuance calendar is closely coordinated between EFSF and EFSM. This ensures smooth market operations over the entire duration of the support programmes while both mechanisms are in the market.

➤ B5 – Does EFSF issue in euros only?

EFSF does not have any general currency limitation for its funding activities. However, it is currently expected that the funds would be raised in euro.

➤ B6 – Are EFSF bonds listed on the stock exchange?

Yes, they are listed on the Luxembourg Stock Exchange. However, the vast majority of trading volume takes place through over-the-counter trading platforms. EFSF bills are only traded OTC.

➤ B7 – Is EFSF part of the main indices for SSA investors?

EFSF is included in the following indices: Barcap Euro Aggregate Index, iBoxx Euro Sub-Sovereigns, JP Maggie, Citi EuroBig Index and ML EMU Board Market Index.⁸

➤ B8 – Which EFSF issues can be tapped?

Issues of notes by EFSF made prior to 13 February 2012 cannot be tapped, because the guarantee structure has changed twice since EFSF started to issue notes in January 2011, and notes issued after the last set of changes to the guarantee structure in February 2012 would, therefore, not be fungible with those issued before then.

Section C – Questions related to lending within a macro-economic adjustment programme

➤ C1 - Is the EFSF's support linked to conditions?

Yes, financial assistance provided to beneficiary countries is linked to strict policy conditions which are set out in a Memorandum of Understanding (MoU) between the country in need and the European Commission. For example, conditions for the Irish programme include strengthening and overhaul of the banking sector, fiscal adjustment including correction of excessive deficit by 2015 and growth enhancing reforms, in particular of the labour market.

⁶ See http://www.efsf.europa.eu/attachments/efsf_market_group_en.pdf

⁷ See http://ec.europa.eu/economy_finance/eu_borrower/efsm/index_en.htm

⁸ See http://www.efsf.europa.eu/investor_relations/indices-platforms/index.htm

Decisions about the maximum amount of a loan, its margin and maturity, and the number of instalments to be disbursed are taken unanimously by the euro area Member States' finance ministers.

➤ C2 - What happens if a country in difficulty fails to meet the conditions?

The loan disbursements and the country programme would be interrupted until the review of the country programme and the MoU is renegotiated. In such cases the conditionality still exists.

➤ C3 – Does the EFSF still have any lending capacity?

As the ESM is now the sole mechanism for responding to new requests for financial assistance, the EFSF can only disburse the remaining amounts of assistance committed to Portugal and Greece.

➤ C4 - What is the maturity of EFSF loans and bonds?

The Framework Agreement does not contain any maturity limitations for the loans nor for the funding instruments. They will be defined on a case-by-case basis. However, at the euro zone summit 21 July 2011, it was agreed that maturities would be extended from the current average of 7.5 years to a minimum average of 15 years and up to 30 years.

➤ C5 – How does the EFSF assess what maturity it will issue and will it swap issuance?

The choice of maturity for a specific bond depends on the prevailing market conditions at the time of a planned issue. EFSF does not intend to use derivatives for the time being.

➤ C6 - What is the interest rate of EFSF loans?

EFSF's on-lending costs are funding costs plus operational costs.

➤ C7 - Do non-euro area Member States participate in EFSF support activities?

There is no binding agreement with Member States outside the euro area. However, for the Irish programme, the UK, Denmark and Sweden have pledged bilateral loans for a combined total of €4.8 billion.

➤ C8 - Does EFSF support countries outside the euro area?

No. For Member States outside the euro area other European Union support mechanisms exist. For Member States that are not members of the euro area there is the Balance of Payments facility⁹; for countries outside the EU there is the Macro-Financial Assistance programme¹⁰. Furthermore, the EFSM could support all European Union Member States.

Section D – EFSF financial assistance instruments

Bank recapitalisations¹¹

➤ D1 –What is the objective of the EFSF's participation of recapitalisation of financial institutions?

The objective is to limit contagion of financial stress by ensuring capacity of a government

⁹ See http://ec.europa.eu/economy_finance/financial_operations/balance/index_en.htm.

¹⁰ See http://ec.europa.eu/economy_finance/financial_operations/market/third_countries/index_en.htm.

¹¹ See EFSF Guideline on Recapitalisation of Financial Institutions

http://www.efsf.europa.eu/attachments/efsf_guideline_on_recapitalisation_of_financial_institutions.pdf

(typically those with “small country, large financial sector problem”) to finance recapitalisation of financial institution(s) at sustainable borrowing costs.

➤ D2 - Which countries may benefit from this assistance?

It applies to Member States which are not under a macro-economic adjustment programme. For those under a programme, an amount has already been designated within the programme for the recapitalisation of the financial sector (€12 billion for Portugal, €35 billion for Ireland).

➤ D3 – Can the EFSF make loans directly to financial institutions?

No, the EFSF may only provide financial assistance to euro area Member States.

➤ D4 - How is eligibility decided?

A three step approach is applied. First of all, the private sector (shareholders) will participate followed by participation on a national level (government) and then finally on a European level via the EFSF.

➤ D5 – Will conditions be attached?

Yes, the planned restructuring/resolution of financial institutions will be the sine qua non condition for EFSF assistance for recapitalisation. In addition, as this type of assistance is considered as state aid, it will therefore have to comply with European state aid rules. Finally, additional conditionality should also be envisaged in the domains of financial supervision, corporate governance and domestic laws relating to restructuring/resolution.

Precautionary Programmes¹²

➤ D6 –What is the objective of EFSF’s precautionary programmes?

The EFSF precautionary programme is a credit line to a non-programme country to overcome external temporary shocks and to prevent a crisis from occurring. The objective is to support sound policies and prevent crisis situations by encouraging countries to secure EFSF assistance before they face difficulties in the capital markets (and avoid negative connotation of being a programme country).

➤ D7 –What sort of credit lines will be available?

In line with IMF’s credit lines, three types of credit line will be available:

- Precautionary conditioned credit line (PCCL) – Access limited to a euro area Member State whose economic and financial situation is fundamentally sound, as determined by respecting eligibility criteria (sustainable public debt, respect of SGP and EIP commitments, track record of access to capital markets on reasonable terms)
- Enhanced conditions credit line (ECCL) – Access open to all euro area Member States whose general economic and financial situation remains sound but faces moderate vulnerabilities that preclude access to a PCCL. Beneficiary must adopt, after consultation with EC and ECB, corrective measures aimed at addressing weaknesses.
- Enhanced conditions credit line with sovereign partial risk protection (ECCL+) – An ECCL can be provided in the form of sovereign partial risk protection to primary bonds. The Partial Protection Certificate (PPC) gives the holder of the certificate a

¹² See EFSF Guideline on Precautionary programmes
http://www.efsf.europa.eu/attachments/efsf_guideline_on_precautionary_programmes.pdf

fixed amount of credit protection equal to a percentage of the principal amount of the sovereign bond. Access to the ECCL+ corresponds, as a basis, to the same criteria and conditionality as that of the ECCL, while reflecting the specific circumstances requiring the issuance of a PPC.

➤ D8 –What would be the size and duration of EFSF credit lines?

The typical size of an EFSF credit line would be 2 to 10% of GDP of a beneficiary country. In terms of duration, it would be 1 year renewable for 6 months twice.

Primary market intervention¹³

➤ D9 - What is the objective of primary market intervention by EFSF?

The main objective is to allow a Member State to maintain or restore its relationship with the dealer / investment community and therefore reduce the risk of a failed auction. It would also serve to increase efficiency of EFSF lending.

➤ D10 – Which countries could benefit from EFSF primary market intervention?

Bond purchase operations in the Primary Market could be made in complement to regular loans under a macroeconomic adjustment programme or to drawdown of funds under a precautionary programme. This instrument would be used primarily towards the end of an adjustment programme to facilitate a country's return to the market.

➤ D11 –Would conditionality be attached?

Conditions would be those of the macroeconomic adjustment programme or precautionary programme.

➤ D12 –What is the relation between the EFSF's primary market intervention and the ECB's Outright Monetary Transactions (OMT)?

As announced by ECB President Mario Draghi on 6 September 2012, Outright Monetary Transactions, i.e. is the purchase of euro area sovereign bonds on the secondary market by the ECB, will be considered for future cases of EFSF/ESM macroeconomic adjustment programmes or precautionary programmes, provided that they include the possibility of EFSF/ESM primary market purchases. OMT may also be considered for Member States currently under a macroeconomic adjustment programme when they will be regaining bond market access.

➤ D13 –Would there be a limit to the amount purchased?

Any primary market purchases by the EFSF would be limited to no more than 50% of the final issued amount. However, this restriction would not apply if loans or payments made under a precautionary programme are extended by way of primary market purchases of CIFs.

➤ D14 –What would EFSF do with the bonds purchased?

Once purchased by EFSF, securities could be either

- resold to private investors when market conditions have improved
- held until maturity
- sold back to country

¹³ See EFSF Guideline on Primary Market Purchases
http://www.efsf.europa.eu/attachments/efsf_guideline_on_primary_market_purchases.pdf

- used for repos with commercial banks to support EFSF's liquidity management

Secondary market intervention¹⁴

➤ D15 - What is the objective of secondary bond market intervention by EFSF?

Secondary bond market intervention by EFSF has a twofold objective. First, it serves to support the functioning of the debt markets and appropriate price formation in government bonds in exceptional circumstances where the limited liquidity of markets threaten financial stability and push sovereign interest rates towards unsustainable levels. Secondly, EFSF intervention could serve the purpose of a market making to ensure some liquidity in debt markets and giving incentives to investors to further participate in the financing of countries.

➤ D16 – Which countries could benefit from EFSF secondary market intervention?

Secondary market bond intervention could be provided for countries within a programme and also for non-programme countries.

➤ D17 –Would conditionality be attached?

For countries under a programme, the conditionality of that programme applies. For those not in a programme, conditionality refers to a) ex-ante eligibility criteria as defined in the context of the European fiscal and macro-economic surveillance framework and b) appropriate policy reforms (defined in MoU)

➤ D18 –What would be the procedure to activate secondary market purchases?

The procedure would be initiated by a request from a Member State to the Eurogroup President. However, in exceptional circumstances, ECB could issue an early warning to the Euro Working Group. In all cases, it will be subject to an ECB report identifying risk to euro area and assessing need for intervention. The procedure should take 2-3 days.

➤ D19 –What would EFSF do with the bonds purchased?

As with purchases in the primary bond market, securities purchased by EFSF on the secondary bond markets could be either resold to private investors when market conditions have improved, held until maturity, sold back to the beneficiary country or used for repos with commercial banks to support EFSF's liquidity management

➤ D20 –How will EFSF buy on the secondary markets?

The European Central Bank (ECB) will act as Fiscal Agent for the EFSF (and future ESM)

➤ D21 –For the ECB to intervene on behalf of the EFSF would you need a country request?

Yes.

➤ D22 –Would you need a Memorandum of Understanding?

Yes.

¹⁴ See EFSF Guideline on interventions in the secondary market
http://www.efsf.europa.eu/attachments/efsf_guideline_on_interventions_in_the_secondary_market.pdf

- D23 – Will the EFSF take over bonds previously bought by the ECB?

This is not intended at this stage.

- D24 – Could the Co-Investment Fund take over bond previously bought by the ECB?

This is not intended at this stage.

Section E - Maximising the EFSF's lending capacity¹⁵

- E1 – Why is there a need to leverage?

In 2011 the sovereign debt markets of some Member States were under pressure. The EFSF exists to help under such circumstances and the recently created set of new instruments can be used for this purpose. However, EFSF resources are limited compared to the size of the debt markets. Therefore we will use the capacity of EFSF more efficiently by leveraging its resources.

- E2 – How will EFSF be leveraged?

Two approaches will be used to enlarge EFSF's capacity. These two approaches respect the EU-Treaty and are compatible with the EFSF Framework Agreement and its guidelines.

- Option 1 - Partial risk protection. EFSF would provide a partial protection certificate to a newly issued bonds of a Member State. After initial issue, the certificate could be traded separately. It would give the holder an amount of fixed credit protection of 20-30% of the principal amount of the sovereign bond. The partial risk protection is to be used primarily under precautionary programmes and is aimed at increasing demand for new issues of Member States and lowering funding costs. A partial protection certificate would entitle the holder to claim their entitlement against this loss in EFSF bonds and cash under the condition that the certificate holder also holds an underlying bond.
- Option 2 - Co-Investment Fund (CIF). The creation of one or more Co-Investment Funds would allow the combination of public and private funding. A CIF would provide funding directly to Member States through the purchase of bonds in the primary and secondary markets, this funding could, inter alia, be used by Member States for bank recapitalisation. The CIF would comprise a first loss tranche which would be financed by EFSF.

- E3 – By how much can EFSF leverage?

- The degree of leverage depends on the exact structure of the new instrument, market conditions, investor response to the new measures and the soundness of the countries benefiting from EFSF support facilities. Improved credibility is expected to reduce the amount of EFSF resources needed, because investors will ask for less risk protection and will be willing to put up more capital complementing EFSF.
- Therefore it is difficult to give precise figures at this stage on the leverage. It can only be determined after further discussions with investors and assessments from rating agencies. The two approaches have been developed so as to be attractive to the international investor community. They cover different investor needs to unfold the maximum impact. We firmly believe that the two approaches chosen provide a robust strategy which attracts investors.

¹⁵ Please see Terms of Reference Maximising the capacity of EFSF
http://www.efsf.europa.eu/attachments/efsf_terms_of_reference_maximising_the_capacity.pdf

- The EFSF has the flexibility to use these two options simultaneously to increase the robustness of the financing strategy.

➤ E4 – Can the EFSF start intervening on primary and secondary markets immediately?

The instruments agreed in July are now operationalized through the guidelines which were adopted. EFSF has now set up all practical arrangements. It has broadened its funding strategy and has set up the necessary infrastructure.

➤ E5 – Will the EFSF cooperate more closely with the IMF?

IMF involvement has always been an important element of our crisis resolution framework. EFSF has asked the Eurogroup, the Commission and the EFSF now to contact the IMF and look into available options of closer cooperation with the EFSF support packages. The IMF has indicated that it would be ready to also support the policy monitoring outside its standard programme setup. So far the joint financing of programme countries has worked very well and underscored the usefulness of closer financial cooperation. EFSF would invite the IMF to explore any other options of co-financing or attracting capital.

➤ E6 – Would assistance under these options be linked to conditionality?

Financing under both options would be linked to a Memorandum of Understanding (MoU) entailing policy conditionality and appropriate monitoring and surveillance procedures.

➤ E7 - How will these options reduce the cost of issuance for the member state?

EFSF is providing loss protection for investors in newly-issued Member State bonds and thus the risk profile of these bonds for investors is reduced; this will be reflected in pricing.

Option 1 – Credit enhancement

➤ E9 - What will be the scope of the protection under option 1?

The partial protection certificate will cover a portion of the principal value of a bond. The precise amount will depend on market conditions and the country circumstances but it will be in the range of 20 to 30% of the principal of the bond.

➤ E10 - How will the event of default be defined?

The certificate gives rise to a claim in the event of a Member State credit event under the full ISDA definition, which covers

- (i) Failure by the Issuer to make full and timely payments of amounts scheduled to be due in respect of one or more bonds, subject to grace periods; or
- (ii) Repudiation or moratorium; or
- (iii) Restructuring

These losses will be determined based on the ISDA procedures

➤ E11 - How and when will the partial protection certificates pay out?

Following a default event, the incurred loss per bond will be determined. The certificate will entitle the holder of the partial protection certificate to claim their entitlement against this loss in EFSF bonds under the condition that the certificate holder also holds an underlying bond.

➤ E12 - Will the certificate cover both principal and interest of the underlying bond?

The intention is that it will cover part of the principal value of the underlying bond.

➤ E13 - Will the certificate cover more than one country?

No.

➤ E14 - Why should an investor participate in the scheme rather than buy a plain vanilla bond issued by the Member State?

Whilst existing member state market yields are higher than the coupon under the scheme, investors holding the partial protection certificate will enjoy a degree of credit protection provided by EFSF bond collateral.

➤ E15 - Who are the likely users of the scheme?

Institutional investors willing to detain European Sovereign with credit enhancement.

➤ E16 - How will EFSF ensure a liquid market for the certificates?

This will be a relevant consideration for the EFSF in deciding how to activate the scheme in relation to a particular country, and EFSF will engage closely with relevant market participants.

➤ E17 - How will negative pledge clauses relating to existing Member State obligations affect the scheme?

This will be determined through due diligence in relation to the circumstances of any specific country before the EFSF decides to implement the scheme in relation to that country.

➤ E18 - Will this scheme increase the headline debt figure of the Member State?

Any statistical effect of this sort will be determined in discussion with Eurostat.

➤ E19 – Has EFSF had direct conversations with investors and what were their reactions?

Initial conversations have been held with a number of investors; these have provided information on the design of the scheme.

Option 2 – Co-Investment Fund (CIF)

➤ E20 – What is the structure of such a CIF?

One or more special purpose vehicles (CIF) would be established; each dedicated CIF would have a mandate to facilitate funding of Member States, and invest in sovereign bonds of a specific country or multi countries in the primary and/or secondary markets. This vehicle could be funded by different instruments with distinctive risk/return characteristics. The instruments could include a senior debt instrument and a participation capital instrument, both of which would be freely traded instruments. In addition there would have to be an EFSF investment channelled through the Member State which will absorb the first proportion of losses incurred by the vehicle.

The mechanisms to implement this approach will be compatible with the operational model of EFSF.

The CIF structure should be set up so as to attract a broad class of international public and private investors. For that purpose, the senior debt instrument could be credit rated and targeted at traditional fixed income investors. The participation capital instrument could be junior to the senior debt instrument but rank ahead of the EFSF investment. This might attract Sovereign Wealth Funds, risk capital investors and potentially some long-only institutional investors. This tranche will potentially share with EFSF any upside generated by the investments.

- E21 - What will be the investment policy of a vehicle?

Each vehicle will have a clearly stated investment mandate.

- E22 - How will EFSF manage any conflict of interest/ governance issues for investors given the CIF will be controlled by EFSF?

There would be no conflict of interest as they have the same mission.

- E23 – Will the vehicle have a focus on primary or secondary purchases and what will the percentage split be?

In principle, either. This will be determined in the light of EFSF's assessment of what is likely to be most effective in the circumstances of the relevant country and depending on investor demand.

- E24 - How will a CIF reduce the cost of issuance of a member state?

The additional investment capacity that the vehicle is designed to attract to the market should have a positive effect on market prices.

- E25 - Which investors are expected to participate in the participating tranche?

A wide range of potential investors could be attracted, including risk capital investors, Sovereign Wealth Funds and long-only institutional investors.

- E26 - Can investors from outside the euro area participate?

Yes

- E27 - Will profits be distributed and if so, how?

The participation capital tranche could carry a modest coupon and it would benefit from net gains achieved when the bonds are redeemed. The senior debt tranche could carry a fixed coupon, but would receive no share in any upside. The EFSF could share some gains, or derive interest on its tranche, but this is yet to be determined.

- E28 - What is the ratio you expect between the EFSF first loss tranche, participation capital and senior bonds?

This will be decided by the EFSF in the circumstances of each CIF in a way that maximizes the effectiveness of EFSF resources and in the light of investor appetite

- E29 - What is the expected nature and size of the senior tranche?

The senior tranche will consist of traditional senior debt carrying a fixed coupon and is expected to be investment-grade.

- E30 - What is the expected size of the CIF portfolio?

This will depend on market circumstances and investor demand. In the first wave, large investors have committed €60 billion to the CIF.

- E31 - What would be the loss EFSF would have to take?

The CIF would be set up with a 2- or 3-tier capital structure, where the EFSF would invest in the first loss tranche. Under the Framework Agreement, EFSF needs to have recourse against the

Member State for any loss on the EFSF first loss tranche, as if it were EFSF funding to the Member State. The maximum loss would depend on the size of the first loss tranche. The relative sizes of the three tranches, would all vary depending on investor participation.

- E32 - What kind of eligibility criteria and policy conditionality would be attached to primary and secondary market purchases?

Policy conditionality will be required in relation to any country receiving support through the scheme according to EFSF guidelines.

- E33 - Is the CIF covered by guidelines for new instruments

Both options rely on a transfer of funds from the EFSF to the beneficiary Member State and thus, given the EFSF Framework Agreement, they have to be covered by the guidelines for the new instruments. Financing under both options would be linked to a MoU entailing policy conditionality and appropriate monitoring and surveillance procedure and based on a Financial Assistance Facility Agreement.

- E34 - How long would it take to set up the CIF?

The introduction of the CIF was agreed by euro area Finance Ministers on 29 November. EFSF will now implement this approach to be ready early in 2012.

Section F – The programme for Ireland (concluded on 8 December 2013)

- F1 – Why did Ireland need financial assistance?

The Irish economy has suffered as a consequence of a devastating boom-bust cycle in the housing market. House prices increased four-fold from 1997 to 2007, when the bubble burst. As the property boom was financed through aggressive lending by Irish banks, the decline in property prices and the collapse in construction activity resulted in severe losses in the Irish banking system. The government of Ireland responded by injecting public funds into banks to restore their solvency (over €60 billion). This led to a huge increase in Ireland's public debt, while the sharp decline in economic activity caused GDP to fall and unemployment to rise. At that time the Irish government was not able to resolve the situation on its own, and therefore requested financial assistance from the euro area countries, the EU and the IMF.

- F2 – How was the decision to grant financial assistance to Ireland taken?

On 28 November 2010, the ECOFIN Council (i.e. finance ministers of the EU) concurred with the European Commission and the ECB that providing financial assistance to Ireland was warranted to safeguard the financial stability in the euro area and the EU as a whole. The IMF Executive Board approved the arrangement on 16 December 2010.

- F3 – Who contributed to the financial assistance package?

The programme for Ireland was financed as follows:

- €67.5 billion in external support including
 - €17.7 billion from EFSF (this was the EFSF's first financial assistance programme);
 - €22.5 billion from EFSM (European Financial Stabilisation Mechanism – an EU facility funded through bonds issued by the European Commission);
 - €22.5 billion from IMF;
 - €4.8 billion in bilateral loans from the UK (€3.8 billion), Sweden (€0.6 billion) and Denmark (€0.4 billion);
- €17.5 billion contribution from Ireland (from the Treasury and the National Pension Fund Reserve)

➤ F4 – What were the policy conditions that the Irish government had to implement in order to receive financial assistance?

- A financial sector strategy comprising fundamental downsizing and reorganisation of the banking sector (including recapitalisation and deleveraging);
- A strategy to restore fiscal sustainability (expenditure restraint, tax system reform, generation of additional revenue);
- A structural reform package to underpin growth, focusing on competitiveness and job creation.

➤ F5 – How were the funds used by the Irish government?

The majority of total programme amount was used for budget financing needs and a substantial component was assigned for the purpose of recapitalisation of banks.

➤ F6 – Has Ireland achieved the objectives of its macroeconomic adjustment programme?

According to a statement issued in November 2013 by the European Commission, ECB and IMF following the 12th and final review of Ireland's economic adjustment programme, the implementation of the programme has been rigorous and effective. Growth prospects are strengthening, unemployment has been declining. The fiscal deficit target for 2013 (7.5% of GDP) will be met comfortably, and the target of 4.8% for 2014 is more ambitious than the deficit ceiling of 5.1% set under the Excessive Deficit Procedure. The overall health of the Irish banking sector has also significantly improved and Irish banks have enjoyed better funding conditions and improved market access.

➤ F7 – What is the significance of the fact that Ireland is now able to issue long-term bonds again?

Ireland's return to long-term bond issuance means that financial markets have a positive assessment of the country's creditworthiness, which in turn stems from favourable prospects for the Irish economy and the ability to service debt. Ireland will no longer have to rely on external assistance to meet its financing needs, and the Irish people deserve recognition for their efforts under difficult circumstances.

➤ F8 – When will Ireland have to repay the loans?

Ireland will repay the principal of the loan tranches starting from 2029, and the repayment is scheduled to end in 2042. Initially, the average maturity of loan tranches was up to 15 years, but this period was extended in April 2013 by members of the Eurogroup by 7 years.

➤ F9 – Has the Irish government requested a precautionary programme from the ESM?

No, in November 2013 the Irish government announced that it would exit the 3-year financial assistance programme without seeking precautionary financial assistance (a line of credit) from the ESM. This decision was fully supported by other euro area Member States, as well as by the European Commission, ECB and IMF.

➤ F10 – Will the Irish economy be subject to surveillance now that the financial assistance programme is over?

Yes. The "Two-Pack" regulation introduced a new system of post-programme monitoring for Member States emerging from adjustment programmes or precautionary assistance.¹⁶ Euro area countries will remain subject to post-programme monitoring until they have paid back a minimum of 75% of the assistance received. The European Commission (in liaison with the ECB) will carry

¹⁶ See Article 14 of Regulation (EU) No 472/2013 of 21 May 2013 "on the strengthening of economic and budgetary surveillance of Member States in the euro area experiencing or threatened with serious difficulties with respect to their financial stability"

out missions twice a year to assess the economic, fiscal and financial situation of the post-programme country. The European Commission is required to communicate its assessment to the European Parliament, the EFC, the parliament of the Member State concerned and will assess, in particular, whether corrective measures are needed.

In order to ensure timely loan repayments by Ireland, EFSF will continue to work closely with the Irish authorities and participate in post-programme missions when appropriate.

Section G - The programme for Portugal

➤ G1 – How much is the programme for Portugal?

Following the formal request for financial assistance made by the Portuguese authorities on 7 April 2011, the Eurogroup and ECOFIN Ministers agreed to grant financial assistance on 17 May. The financial package of the programme will cover financing needs up to €78 billion.

➤ G2 - How will the programme be financed?

The programme will be shared equally (€26 billion each) amongst: (i) the European Financial Stabilisation Mechanism, (ii) the EFSF, and (iii) the IMF.

➤ G3 -What are the conditions of the programme?

The three year programme joint EU/IMF programme is both ambitious and frontloaded. It will be based on three pillars:

- An ambitious fiscal adjustment to restore fiscal sustainability, including through the correction of the excessive deficit by 2013 respecting the original deadline set by the Council. Fiscal sustainability will be supported by (i) a strengthening of the budgetary processes, including enhanced monitoring and reporting, more efficient revenue administration and better control over Public-Private-Partnerships and State-Owned Enterprises; (ii) reforms of the health system and of public administration; (iii) an ambitious privatisation programme
- Growth and competitiveness enhancing reforms of the labour market, the judicial system, network industries and housing and services sectors, to foster sustainable and balanced growth and the unwinding internal and external macroeconomic imbalances
- Measures to ensure a balanced and orderly deleveraging of the financial sector and to strengthen the capital of banks, including adequate support facilities (€12 billion designated).

➤ G4 -What is the EFSF's issuance calendar for Portugal?

In 2011, EFSF issued €8 billion in support of Portugal through 2 benchmark issues. The first issue, a €5 billion benchmark bond with a 10 year maturity, was placed on 15 June. The second issue, a €3 billion bond with a 5 year maturity was placed on 22 June. From the two issues, a total of €5.9 billion was disbursed to Portugal. A further €1 billion was disbursed through EFSF's short term funding programme.

In 2012, EFSF placed a 3-year €3 billion issue of which €1.73 billion was disbursed to Portugal on 12 January 2012.

➤ G5 – What are the details of the first issue made for Portugal?

The first issue made by EFSF in support of the Portuguese programme was placed on 15 June 2011. Details are as follows:

Amount issued:	€5 billion
Maturity	05/07/2021
Issuance spread:	Mid swap +17 bp
Coupon:	3.375%
Reoffer yield:	3.493%

Reoffer price:	99.013%
Settlement date:	22 June 2011
Effective lending cost to Portugal	6.08%
Amount transferred to Portugal	€3.7 billion

➤ G6 – And the details of the second issue made for Portugal?

The second issue made by EFSF in support of the Portuguese programme was placed on 22 June 2011. Details are as follows:

Amount issued:	€3 billion
Maturity	05/12/2016
Issuance spread:	Mid swap +6 bp
Coupon:	2.750%
Reoffer yield:	2.825%
Reoffer price:	99.636%
Settlement date:	29 June 2011
Effective lending cost to Portugal	5.32%

Amount transferred to Portugal €2.2 billion

For details on subsequent issues, please consult the EFSF website
http://www.efsf.europa.eu/investor_relations/issues/index.htm

Section H – The second programme for Greece

➤ H1 – What is the second programme for Greece? ¹⁷

At the euro zone summit held on 26 October 2011, euro zone Heads of State or Government agreed to a second financial assistance programme for Greece. The details of this programme were agreed by the Eurogroup on 21 February 2012¹⁸.

➤ H2 – How much is the new Greek programme?

The details and amount of the new Greek programme are outlined in the table below.

Disbursement	Amount (bn)
Total Greek Package (including bank recap, undisbursed GLF – 24.4 bn and IMF contribution)	172.6*
of which	
PSI	Up to 30
Accrued interest	Up to 5.5
IMF contribution to the 2 nd Greek programme	28 (of which 8.2 after 2014)
EFSF contribution to the 2 nd Greek programme including:	109.1
Bank recap	up to €48
Undisbursed GLF	24.4
New GLF	36.7

¹⁷ The first financial support programme for Greece (April 2010) involved bilateral loans from euro area Member States amounting to €80 bn, and a €30 bn loan from the IMF. It did not involve the EFSF.

¹⁸ http://www.consilium.europa.eu/media/1440478/statement_on_greece_21_february_2012.pdf

* The financing needs until end 2014 are covered by the amount of 164.4 bn, while the 8.2 bn will be disbursed by the IMF subsequently.

➤ H3 – What are the details of the Private Sector Involvement (PSI)?

The public offer for the PSI was launched by the Hellenic Republic on 24 February and closed on 8 March. On 9 March, it was announced that bondholders holding 85.8% of Greece's Greek law-bonds agreed to the bond swap¹⁹. The activation of Collective Action Clauses lifted the participation rate to 95.7%. This led to a 53.5% reduction in the nominal face value of Greek debt held by private investors which corresponds to a reduction in the debt stock of approximately €107 billion for Greece.

➤ H4 – What is the objective of PSI?

The objective is to secure the decline of the Greek debt to GDP ratio with an objective of reaching 120% by 2020. Due to the high take up of the bond swap, Greece's debt is expected to fall below 120% of GDP in 2020, reaching 117%.

➤ H5 – How will the EFSF contribute to the second assistance programme for Greece?

The second Greek Programme is envisaged to cover the financing needs of Greece until the end of 2014 and it includes the undisbursed contribution from the Greek Loan Facility. EFSF will have to provide these amounts minus the contribution of the IMF. The second programme has a bank recapitalisation component of up to €48 billion (including an initial €25 billion in the PSI package).

The other elements which require financing by the EFSF are:

- PSI Contribution (€29.7 billion at end April): as part of the voluntary debt exchange, Greece offered investors EFSF bonds (1 and 2 years). These EFSF bonds, provided to holders of bonds under Greek law, will subsequently be rolled over into longer maturities. Maturities for the refinancing will be decided according to market demand and in order to ensure a well-diversified EFSF portfolio covering the entire yield curve. Once the debt exchange offer has also been completed on Greek sovereign bonds, issued under foreign law, and Greek corporate and municipal bonds, guaranteed by the Greek state, the amount of the PSI contribution could increase to a total of €30 billion.
- Accrued interest (€4.82 billion at April): to enable Greece to repay accrued interest on outstanding Greek sovereign bonds under Greek law which will be included in the PSI. Greece has given investors EFSF 6-month bills. The bills will be subsequently rolled over into longer maturities to ensure smooth market operations. Once the debt exchange offer has been completed on Greek sovereign bonds, issued under foreign law, and Greek corporate and municipal bonds, guaranteed by the Greek state, the amount of accrued interest could increase up to €5.5 billion.
- Buy-Back for Eurosystem (€35 billion): to enable Greece to finance a buy-back offer, whereby Greece, acting through the ECB as its agent, offers to buy back from Eurosystem national central banks (NCBs) bonds issued or guaranteed by Greece, which are held by NCBs as collateral for Eurosystem monetary policy operations and in respect of which a monetary policy counterparty defaults. The buy-back offer is available for the period commencing on the date on which one or more of each of the three main credit rating agencies, as a result of the debt exchange, a default, selective default or restrictive default rating with respect to Greece or any bond issued or guaranteed by

¹⁹ Further details are available on <https://www.bondcompro.com/greeceexchange/genDocuments.asp>

Greece. The buy-back offer will end 60 calendar days after the default, selective default or restrictive default triggered by the debt exchange is lifted by all three credit rating agencies, but no later than maximum ten months after the signature of the facility agreement. The objective of the buy-back offer scheme is to allow the continuing eligibility of bonds issued or guaranteed by Greece as collateral for Eurosystem monetary policy operations in this context. Greece received 1-year EFSF bonds for this operation and, if not used for buy-back, they will be returned and cancelled before their maturity.²⁰

- The €35 billion for the buy-back for the Eurosystem will be on top of the new Greek package.

➤ **H6 – How will EFSF fund these amounts?**

EFSF will use a flexible, diversified funding strategy to ensure that amounts to be funded are spread over the entire length of the programme. This also means that EFSF will be able to take advantage of the best possible market conditions.

The PSI contribution, accrued interest and loan programme (excluding the amount earmarked for bank recapitalisations) is financed through the markets. The collateral enhancement for the Eurosystem is a cashless operation. This is also expected to be the case for the recapitalisation of Greek banks which has been financed by the provision of EFSF bonds.

➤ **H7 – What will happen to the first Greek programme agreed in May 2010?**

The first Greek programme has been discontinued. The remaining amount to be contributed by the euro area (€24.4 billion) will now be disbursed by the EFSF. The remaining €10 billion from the IMF from the first Greek programme has been transferred to the new Greek programme.

➤ **H8 – What decisions were taken by the Eurogroup on 13 December 2012?**

Following an assessment by the European Commission, ECB and IMF that Greece had in a satisfactory manner implemented all the previously agreed policy reforms, the Eurogroup formally approved the second disbursement under the second economic adjustment programme for Greece.

The Eurogroup noted that the outlook for the sustainability of Greek government debt had worsened compared to March 2012 when the second programme was concluded, mainly due to a deteriorated macro-economic situation and delays in programme implementation. Therefore, the Eurogroup approved a set of measures (first proposed on 27 November 2012) designed to ease Greece's debt burden and bring its public debt back on a sustainable path, so that a level of debt-to-GDP of 124% could be achieved in 2020. These measures included:

- **Reduction of the Greek Loan Facility (GLF – bilateral loans to Greece) interest margin:** A lowering by 100 basis points of the interest rate charged to Greece on the loans provided under the GLF (Member States under a full financial assistance programme are not required to participate in the lowering of the GLF interest rates for the period in which they receive themselves financial assistance). This measure is estimated to lower the financing needs of the country by €1.9 billion by 2016.
- **Cancellation of the EFSF guarantee commitment fee** (conditional upon the continued implementation of reforms by Greece): Cancellation of the guarantee commitment fee, amounting 10 basis points, paid by Greece on the EFSF loans. This measure is estimated to save a total of € 2.7 billion over the entire period of EFSF lending to Greece.
- **Maturity extension of GLF and EFSF loans*:** Even though the maturities of both loans by

²⁰ These bonds were returned to the EFSF on 25 July 2012 and were cancelled on 3 August 2012.

* Applies only to loans under EFSF Master Financial Assistance Facility Agreement, i.e. does not apply to 9 December 2013

the GLF and the EFSF are long-term, this still creates an amortisation hump for Greece in 2020s, which could have hampered the country's return to market financing. An extension of the maturities of the bilateral and EFSF loans by 15 years does not per se have an impact on the reduction of debt by 2020 or beyond, but significantly improves the country's debt profile and improves conditions for a return to market financing.

- **Deferral of EFSF interest rate payments*:** A deferral of interest payments on EFSF loans by 10 years will allow Greece to reduce substantially its financing needs. This operation will not create additional costs for the EFSF since Greece will have to pay interest charges on the deferred interest. This measure is estimated to lower the financing needs of the country by a total of €12.9 billion by 2016.
- **SMP Income:** A commitment by Member States to pass on to Greece's segregated account an amount equivalent to the income on the ECB's Securities Markets Programme (SMP) portfolio accruing to their national central bank as from budget year 2013 (Member States under a full financial assistance programme are not required to participate in this scheme for the period in which they receive themselves financial assistance).
- **Foregoing the previously programmed decline in the stock of T-Bills:** The decisions made by policymakers envisage maintaining a T-Bill stock of €15 billion through the end of the programme, thus reducing the financing needs of the country by €9 billion in the period 2012-2014 (or 1% of GDP).
- **Postponing part of the Treasury cash buffer build-up:** The March programme had foreseen a build-up of the Treasury cash buffer by €5 billion to provide some flexibility to the Greek treasury. Decisions taken in Eurogroup meetings suggest that the cash buffer build-up is partially postponed after the expiration of the programme. Over the 2012-2014 period, the cash buffer build-up is now reduced to €1.5 billion, and it is set to increase by an additional €2 billion in 2015-2016.
- **Other contingent measures:** Greece and other euro area Member States will consider further measures and assistance, including inter alia lower co-financing in structural funds and/or further reduction of the interest rate on the Greek Loan Facility, if necessary, to ensure that Greece can reach a debt-to-GDP ratio of 124% in 2020, and in 2022 a debt-to-GDP ratio substantially lower than 110%. This is contingent on Greece reaching an annual primary surplus, as envisaged in the current MoU and full implementation of all conditions contained in the programme.

The Eurogroup also stressed that the benefits of the above-mentioned measures would accrue to Greece in a phased manner and conditional upon the continued implementation of agreed reforms.

➤ [H9 – How were these measures related to the buy-back of Greek debt?](#)

Final approval for the above measures was conditional upon the success of a debt buy-back operation conducted by the Greek government. The buy-back applied to the new Greek sovereign bonds (NGGBs) issued in the context of the Private Sector Initiative (PSI) operation of March 2012. It was conducted through a tender operation open to all market participants holding NGGBs of any outstanding series. The debt buy-back (announced by the Greek Ministry of Finance on 3 December and completed on 11 December 2012) reduced the amount of the country's nominal debt by approximately €21 billion (in net terms).

➤ [H10 – How is the debt buy-back financed?](#)

PSI Facility or Bond Interest Facility

The EFSF is providing a loan, within the envelope of the second financial assistance programme to Greece, to finance the buy-back operation. For this purpose, the EFSF issued six-month notes for a total nominal amount of €11.3 billion, which were transferred to the Greek government on December 19, 2012.

- H11 – What are the other components in the current disbursement of financial assistance to Greece?

The EFSF will provide funds to the Greek government for the Hellenic Financial Stability Fund (HFSF) to finance the recapitalization and resolution costs of selected banks. In addition, the EFSF will provide funds to the Greek government for its budgetary financing needs.

- H12 – Are there any specific transferability restrictions on the EFSF notes disbursed in the context of bank recapitalisation?

No. In what concerns the EFSF notes disbursed in the context of bank recapitalizations, there are no specific transferability restrictions upon note holders other than those generally applicable pursuant to the terms and conditions of any notes issued under the EFSF Debt Issuance Programme.

The EFSF may only impose additional transferability restrictions on the basis of contractual agreements in place between the EFSF and a note holder which then would restrict only such note holder.

In case a market participant acquires legal title to EFSF notes – for example, in the context of a repo transaction with a recapitalised bank – and in the absence of an additional contractual arrangement, only the terms and conditions of such EFSF notes would apply.

- H13 – What are the amounts to be disbursed to Greece in December 2012 and the first quarter of 2013?

The disbursement will be made in several tranches. Overall, over this period Greece will receive €49.1 billion from the EFSF. This amount is part of the EFSF contribution of €109.1 billion agreed by the Eurogroup under the second Greek programme in February 2012. The details of the current disbursement by the EFSF are as follows:

December 2012	€ billion
for bank recapitalisation and resolution (EFSF notes)	16.0
for debt buy-back (EFSF notes)	11.3
for budgetary financing (cash)	7.0
Total	34.3
January – March 2013	
for bank recapitalisation and resolution (EFSF notes)	7.2
for budgetary financing (cash)	7.6
Total	14.8

Total EFSF disbursements	49.1
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Source: EFSF

Annex

Initial EFSF FAQs before amendment of Framework Agreement.

➤ 1 – What was the initial lending capacity of EFSF

At the establishment of EFSF in May, the total guaranteed commitments were agreed to be €440 billion.

➤ 2 – What was the corresponding guarantee commitment per country?

The country contribution key is in accordance with each country's share in the paid-up capital of the European Central Bank (ECB). The initial guarantee commitment per country was as follows:

	EFSF Guarantee Commitments (€m)	EFSF contribution key (%)
Austria	12,241	2.78
Belgium	15,292	3.48
Cyprus	863	0.20
Finland	7,905	1.79
France	89,657	20.38
Germany	119,390	27.13
Greece	12,388	2.82
Ireland	7,002	1.59
Italy	78,785	17.91
Luxembourg	1,101	0.25
Malta	398	0.09
Netherlands	25,144	5.71
Portugal	11,035	2.51
Slovakia	4,372	0.99
Slovenia	2,073	0.47
Spain	52,353	11.9
Total	440,000	100

➤ 3 – What is the credit enhancement structure?

In order to ensure the highest possible credit rating, various credit enhancements were put into place:

- an over-guarantee of 120 per cent on each issue.
- an up-front cash reserve which equals the net present value of the margin of the EFSF loan.
- a loan specific cash buffer

Together these credit enhancements ensure that all loans provided by EFSF are backed by

guarantees of the highest quality and sufficient liquid resource buffers. The available liquidity is invested in securities of the best quality.

➤ 4 - What is the interest rate of EFSF loans?

The interest rate is the fixed annual rate which accrues on the net loan amount during each interest period which is equal to the sum of EFSF's cost of funding (excluding any negative carry component which has been deducted on the disbursement date) and the margin, irrespective of maturity, applicable to such net loan amount. Currently the margin for Ireland stands at 247 basis points, the margin for Portugal is 208 basis points following the conclusions of the March European Council for lower interest rates.

Following the euro zone summit of 21 July, interest rates would be lowered to an equivalent of those of the Balance of Payments facility, close to, without going below, the EFSF funding cost.

➤ 5 - Can EFSF invest proceeds to manage excess liquidity?

Funds raised by EFSF will be provided as loans to the euro area Member States who have requested financial support. However the cash reserve and the loan-specific cash buffer, which is retained by EFSF, are invested in very safe and liquid assets. Asset-liability management is currently conducted by the German Debt Management Office.

➤ 6 – Could EFSF be considered as a Collateralized Debt Obligation (CDO)?

No, EFSF is not a CDO. The essential difference between EFSF and a CDO is that EFSF debt has no tranche structure. There is no seniority and all investors have exactly the same rights. Secondly, EFSF bonds are covered by the guarantees from the euro area countries. However, a triple-AAA rating from all three leading credit rating agencies is not assigned lightly. EFSF has put into place additional credit enhancements through the use of a cash reserve and loan specific cash buffer which are immediately deducted from the loan made to a borrowing country in order to provide additional reassurance to investors. Consequently, all claims on the EFSF are 100% covered by AAA guarantors and cash.

