ESM & EFSF
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## EFSF & ESM – Similarities and differences

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<th>EFSF and ESM</th>
</tr>
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<tr>
<td>Mission</td>
<td>Safeguard financial stability within the eurozone</td>
</tr>
<tr>
<td>Scope of activity</td>
<td>Provide loans to members in financial difficulties</td>
</tr>
<tr>
<td></td>
<td>Intervention in primary and secondary bond markets</td>
</tr>
<tr>
<td></td>
<td>Act on the basis of a precautionary program</td>
</tr>
<tr>
<td></td>
<td>Finance bank recapitalizations through loans to governments, including non-program countries</td>
</tr>
<tr>
<td>Shareholders</td>
<td>17 eurozone countries</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Differences</th>
<th>EFSF</th>
<th>ESM</th>
</tr>
</thead>
<tbody>
<tr>
<td>Legal structure</td>
<td>Private company under Luxembourg law</td>
<td>Inter-governmental institution under international law</td>
</tr>
<tr>
<td>Duration</td>
<td>Temporary (June 2010 - June 2013)</td>
<td>Permanent institution</td>
</tr>
<tr>
<td>Capital structure</td>
<td>Guarantees of eurozone countries</td>
<td>Subscribed capital of EUR 700bn, of which EUR 80bn paid-in and EUR 620bn committed callable capital</td>
</tr>
<tr>
<td>Guarantee structure</td>
<td>Program countries step out of guarantee structure</td>
<td>No stepping out</td>
</tr>
<tr>
<td>Maximum lending capacity</td>
<td>EUR 440bn</td>
<td>EUR 500bn</td>
</tr>
<tr>
<td>Claims to loans</td>
<td>Pari passu</td>
<td>Preferred creditor status with the one-off exception that the assistance for the Spanish bank recap will be pari passu</td>
</tr>
</tbody>
</table>

Source: EFSF, ESM, UniCredit Research
EFSF & ESM - Timeline

- **EFSF:**
  - October 2012: EFSF ceases to enter new programs.
  - January 2013: EUR 192bn already committed for Ireland, Portugal and Greece.

- **ESM:**
  - ESM inaugurated 8 October.
  - Paid-in capital 1st and 2nd Tranche EUR 32bn 2H12.

- **Overall lending capacity:**
  - EUR 248bn.
  - EUR 500bn*.

---

*Up to July 2013 EFSF may engage in new programs in order to ensure a full fresh lending capacity of EUR 500bn. EUR 500bn lending capacity can be reached through accelerated capital payments, if needed. Source: ESM, UniCredit Research*
## ESM & EFSF – Lending capacity

<table>
<thead>
<tr>
<th>EFSF lending capacity</th>
<th>EUR bn</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total lending capacity of the EFSF</td>
<td>440.0</td>
</tr>
<tr>
<td>Lending committed to Ireland, Portugal and Greece (including EUR 3.7bn cash buffer from EFSF 1.0 support structure)</td>
<td>192.0</td>
</tr>
<tr>
<td>of which:</td>
<td></td>
</tr>
<tr>
<td>Ireland</td>
<td>17.7</td>
</tr>
<tr>
<td>Portugal</td>
<td>26.6</td>
</tr>
<tr>
<td>Greece (excluding EUR 35bn from the buyback for Eurosystem/ECB collateral from the total official figure of EUR 179.6bn for the Greek program)</td>
<td>144.6</td>
</tr>
</tbody>
</table>

| Remaining lending capacity of the EFSF | 248.0 |

### ESM lending capacity

| Total lending capacity of the ESM on top of EFSF lending capacity* | 500.0 |

### Spain

Support package for bank recap of up to EUR 100bn**

---

*Up to July 2013 EFSF may engage in new programs in order to ensure a full fresh lending capacity of EUR 50bn. EUR 500bn lending capacity can be reached through accelerated capital payments, if needed.

**The amount provided to Spain for bank recapitalization will be transferred from the EFSF to the ESM. The combined EFSF-ESM lending capacity of EUR 700bn will be maintained. Source: EFSF, UniCredit Research
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ESM – A profile

**Profile:** The European Stability Mechanism (ESM) is a permanent crisis resolution mechanism for the countries of the euro area. The ESM was inaugurated on 8 October 2012 following ratification by all 17 euro area member states.

**Mission:** The mission of the ESM is to provide stability support through a number of financial assistance instruments to ESM member states. For this purpose, the ESM is entitled to raise funds by issuing financial instruments or by entering into financial or other agreements with ESM members, financial institutions or other third parties.

**The ESM may provide stability of support in the same form as the EFSF:**
- Provide loans to euro area member states in financial difficulties
- Intervene in the primary and secondary bond markets
- Act on the basis of a precautionary program
- Finance recapitalization of financial institutions through loans to governments including in non-program countries

All financial assistance to member states is linked to appropriate conditionality.

**Legal Form:** The ESM is an intergovernmental organization under international law, headquartered in Luxembourg.

**Legal Basis:** The legal basis of the ESM is "The Treaty Establishing the ESM" ([Link](#)), which entered into force on 27 September 2012.
ESM – A profile

- **Lending capacity**: The effective lending capacity of the ESM is EUR 500bn. Given that the EFSF will continue to fund the existing programs for Portugal, Ireland and Greece, the combined lending capacity of the EFSF/ESM is EUR 700bn.

- **Preferred creditor status**: ESM loans under a macroeconomic adjustment program and recapitalization facilities enjoy preferred credit status, junior only to the IMF. The decision to forego preferred creditor status in the case of the recapitalization of Spanish banks was one-off in nature, as the program was negotiated by the EFSF. The Spanish program will be transferred to the ESM with rights and obligations, including the EFSF’s pari passu status.

- **Instruments**: For details on the instruments used by the ESM, please see section "EFSF – Instruments".
ESM – Governance

- **Board of Governors:** The ESM is governed by a board of governors consisting of the ministers of finance of the euro area member states (as voting members), while the European commissioner for economic and monetary affairs and the ECB president may participate as observers.

- **Unanimity:** The most important decisions taken by the board of governors require mutual consent (unanimity). These include decisions to provide stability support to an ESM member; the choice of instruments, conditions and terms of such support; calling in authorized unpaid capital (with the exception of emergency capital calls); changing the authorized capital stock and adapting the maximum lending volume.

- **Qualified Majority:** In a number of areas the board of governors take decisions by qualified majority (defined in the ESM Treaty as 80% of the votes cast, with voting rights equal to the number of shares allocated to each country). These areas include setting out the detailed terms of accession of a new member to the ESM, appointing the managing director, and approving the annual accounts of the ESM.

- **Board of Directors:** The ESM also has a board of directors. Each euro area country appoints one director and one alternate director. As in the case of the board of governors, the European Commission and ECB may appoint a non-voting observer.

- **Managing Director:** The board of governors appoints a managing director responsible for the day-to-day management of the ESM. The managing director chairs the board of directors, as well as the management board, which assists the managing director in conducting the current business of the ESM.
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ESM – Capitalization

- The total subscribed capital is EUR 700bn provided by eurozone members, of which
  - EUR 80bn is paid-in capital, and
  - EUR 620bn callable capital.

- Thus, given a maximum lending capacity of EUR 500bn, **subscribed capital will exceed the lending capacity by 40%**. **Paid-in capital will be 11.4% of subscribed capital.** Moreover, the paid-in capital will not be available for on-lending but will be mainly invested in high-quality liquid assets in order to serve as loss-absorbing capital.

- **The level of capitalization of the ESM is very strong compared to other supranationals.** For example, the European Investment Bank (EIB; Aaan/AAAn/AAAn), which has a similar structure of capitalization with 27 members, has total subscribed capital of EUR 242bn (after the capital increase), of which EUR 21.6bn is paid-in (8.9% of subscribed capital).

- **Paid-in capital:** The first two tranches were transferred in October 2012 (total EUR 32bn). Two more tranches will be transferred in 2013 (total EUR 32bn) and a final tranche in 1H14 (EUR 16bn). During the transitory phase, members have to accelerate their paid-in shares in order to maintain a minimum 15% ratio between paid-in capital and the outstanding amount of ESM issuances. (Finland pays in all capital immediately given its Greek collateral agreement).

- Article 8.4 of the ESM Treaty states that **"ESM members hereby irrevocably and unconditionally undertake to provide their contribution to the authorized capital stock"**.

- Should the ESM require additional capital beyond the paid-in amount, the ESM (by simple majority) may call in authorized unpaid capital **"at any time"** (Art. 9 of the ESM Treaty). **"ESM Members hereby irrevocably and unconditionally undertake to pay on demand any capital call made on them [...] within seven days of receipt."**
ESM – Capitalization

- Each ESM member will only be liable for its share of the capital of the ESM.

- However, if an ESM member fails to meet the required payment under a capital call, a revised increased capital call shall be made to all members with a view to ensuring that the ESM receives the total amount of paid-in capital needed. When an ESM member settles its debt with the ESM, the excess capital shall be returned to the other members.

- Moreover, there is no stepping-out mechanism for countries receiving financial assistance, as is the case for the EFSF.

→ ESM capitalization will be very strong compared to other supranationals.

Art. 8.5 of the Treaty: "The liability of each ESM Member shall be limited, in all circumstances, to its portion of the authorized capital stock at its issue price. No ESM Member shall be liable, by reason of its membership, for obligations of the ESM. The obligations of ESM Members to contribute to the authorized capital stock in accordance with this Treaty are not affected if any such ESM Member becomes eligible for, or is receiving, financial assistance from the ESM."
ESM – Callable capital mechanism

Callable capital mechanism

- **General capital calls**: This type includes the payment of initial capital and any adjustment of paid-in capital, for example due to a revision of lending capacity. To initiate a call, the managing director would make a proposal to the board of governors outlining the objective, amounts and payment schedule. The board of governors, acting by mutual agreement, may call in capital at any time.

- **Capital calls to replenish paid-in capital**: This type would be used to restore the level of paid-in capital due to non-payment by a beneficiary country or to maintain a 15% threshold of paid-in capital to maximum lending volume. The managing director would make a proposal to the board of directors, which can then decide by simple majority. If a state fails to meet the required capital call, a revised increased call would be made to all ESM members by increasing their contributions on a pro-rata basis. Once the country having previously failed to meet the call finally settles its debt to the ESM, the excess capital is returned to the other members.

- **Emergency capital calls**: This type is used to avoid an ESM payment default. In this case, the managing director makes a direct call to ESM members without any approval requirements. ESM members have irrevocably and unconditionally undertaken to pay on demand such capital within seven days. In case a member fails to meet the call, the above-mentioned mechanism using a revised call applies.
## ESM – Contribution keys and subscription to the capital stock

<table>
<thead>
<tr>
<th>ESM Member</th>
<th>ESM contribution key</th>
<th>Number of shares</th>
<th>Capital subscription (EUR bn)</th>
<th>Paid-in capital (EUR bn)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Austria</td>
<td>2.78%</td>
<td>194,838</td>
<td>19.5</td>
<td>2.23</td>
</tr>
<tr>
<td>Belgium</td>
<td>3.48%</td>
<td>243,397</td>
<td>24.3</td>
<td>2.78</td>
</tr>
<tr>
<td>Cyprus</td>
<td>0.20%</td>
<td>13,734</td>
<td>1.4</td>
<td>0.16</td>
</tr>
<tr>
<td>Estonia</td>
<td>0.19%</td>
<td>13,020</td>
<td>1.3</td>
<td>0.15</td>
</tr>
<tr>
<td>Finland</td>
<td>1.80%</td>
<td>125,818</td>
<td>12.6</td>
<td>1.44</td>
</tr>
<tr>
<td>France</td>
<td>20.39%</td>
<td>1,427,013</td>
<td>142.7</td>
<td>16.31</td>
</tr>
<tr>
<td>Germany</td>
<td>27.15%</td>
<td>1,900,248</td>
<td>190.0</td>
<td>21.72</td>
</tr>
<tr>
<td>Greece</td>
<td>2.82%</td>
<td>197,169</td>
<td>19.7</td>
<td>2.25</td>
</tr>
<tr>
<td>Ireland</td>
<td>1.59%</td>
<td>111,454</td>
<td>11.1</td>
<td>1.27</td>
</tr>
<tr>
<td>Italy</td>
<td>17.91%</td>
<td>1,253,959</td>
<td>125.4</td>
<td>14.33</td>
</tr>
<tr>
<td>Luxembourg</td>
<td>0.25%</td>
<td>17,528</td>
<td>1.8</td>
<td>0.20</td>
</tr>
<tr>
<td>Malta</td>
<td>0.07%</td>
<td>5,117</td>
<td>0.5</td>
<td>0.06</td>
</tr>
<tr>
<td>Netherlands</td>
<td>5.72%</td>
<td>400,190</td>
<td>40.0</td>
<td>4.57</td>
</tr>
<tr>
<td>Portugal</td>
<td>2.51%</td>
<td>175,644</td>
<td>17.6</td>
<td>2.01</td>
</tr>
<tr>
<td>Slovakia</td>
<td>0.82%</td>
<td>57,680</td>
<td>5.8</td>
<td>0.66</td>
</tr>
<tr>
<td>Slovenia</td>
<td>0.43%</td>
<td>29,932</td>
<td>3.0</td>
<td>0.34</td>
</tr>
<tr>
<td>Spain</td>
<td>11.90%</td>
<td>833,259</td>
<td>83.3</td>
<td>9.52</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>100.00%</strong></td>
<td><strong>7,000,000</strong></td>
<td><strong>700.0</strong></td>
<td><strong>80.0</strong></td>
</tr>
</tbody>
</table>

Note that the ESM level is based on the ECB capital contribution key. Member states with a GDP per capita less than 75% of the EU average benefit from a temporary correction for 12 years after their entry into the eurozone according to the formula, ESM share = ECB key share - 0.75*(ECB key share-GNI share). The downwards compensation is redistributed among all other countries according to the ECB key share. GNI and GDP per capita as of 2010. Source: EFSF Treaty, UniCredit Research
ESM: Paid-in capital instalments

Total EUR 80bn paid-in capital (EUR 32bn already paid in)

Source: ESM, UniCredit Research
## SELECTED ARTICLES OF THE TREATY ESTABLISHING THE ESM

<table>
<thead>
<tr>
<th>Article</th>
<th>Description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Article 8.4</td>
<td>&quot;ESM members hereby irrevocably and unconditionally undertake to provide their contribution to the authorized capital stock […]. They shall meet all capital calls on a timely basis in accordance with the terms set out in this Treaty.&quot;</td>
</tr>
<tr>
<td>Article 8.5</td>
<td>&quot;The liability of each ESM Member shall be limited, in all circumstances, to its portion of the authorized capital stock at its issue price. No ESM Member shall be liable, by reason of its membership, for obligations of the ESM. The obligations of ESM Members to contribute to the authorized capital stock in accordance with this Treaty are not affected if any such ESM Member becomes eligible for, or is receiving, financial assistance from the ESM.&quot;</td>
</tr>
<tr>
<td>Article 9.3.</td>
<td>&quot;ESM Members hereby irrevocably and unconditionally undertake to pay on demand any capital call made on them […] within seven days of receipt.&quot;</td>
</tr>
<tr>
<td>Article 25.2.</td>
<td>&quot;If an ESM Member fails to meet the required payment under a capital call […], a revised increased capital call shall be made to all ESM Members with a view to ensuring that the ESM receives the total amount of paid-in capital needed.”</td>
</tr>
<tr>
<td>Article 25.3.</td>
<td>“When an ESM Member settles its debt to the ESM[…], the excess capital shall be returned to the other ESM Members in accordance with rules to be adopted by the Board of Governors.”</td>
</tr>
</tbody>
</table>

Source: Treaty establishing the ESM, UniCredit Research
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ESM – Investment Policy

**Investment Policy**: The investment policy of the ESM defines the framework for the ESM to carry out its investment management. It refers to the management of the Investment Portfolios, which consist of the investment of the proceeds from
1) the paid-in capital (EUR 80bn) and
2) the reserve fund (net income generated by the ESM operations, financial sanctions received from ESM members).

**Objectives of the Investment Portfolios**

1) **Constant availability of the ESM's maximum lending volume**: The investment policy must ensure that the investment portfolios' market value amounts to a minimum of 15% of the maximum lending volume of the ESM. Based on the current maximum lending capacity of EUR 500bn, the market value of the investment portfolios must equal to at least EUR 75bn.

2) **Liquidity**: The investment portfolios are used to cover losses arising from ESM operations (Art. 25 of the ESM Treaty), and specifically any shortfall due to a non-payment by a beneficiary ESM member.

3) **ESM creditworthiness**: The investment of the investment portfolios follow a prudent Investment Policy, in order to preserve the ESM's highest creditworthiness (Art. 22). To achieve this, an amount equivalent to 15% of the targeted maximum lending volume of the ESM is invested in assets of the highest creditworthiness, as defined by the "General Eligible Asset List". The remaining part of the investment portfolios can be invested in assets defined by the "Enlarged Eligible Asset List".

4) **Return**: The ESM is entitled to use part of the return on the investment portfolios to cover its operating and administrative costs (Art. 22). Investment return can be retained as reserves or distributed as a dividend to the ESM Members "if the amount of paid-in capital and the reserve fund exceeds the level required to maintain the lending capacity of the ESM and proceeds from the investment are not required to avoid a payment shortfall to creditors" (Art. 23).
ESM – Investment Policy

- **Portfolio Structure**: The investment portfolios are divided into a short-term tranche and a medium/long-term tranche. The size of the short-term tranche is determined by the future payments due from program countries over at least the next 6 months (minimum EUR 5bn). The medium/long-term tranche has a capital preservation objective over a three-year horizon and a maximum loss of 2% over a one-year horizon to ensure the financial strength of the ESM.

- **Liquidity**: The ESM holds liquidity sufficient to cover any due payments arising from its liabilities in the next 12 months. In order to enable the ESM to meet these liabilities, if not already covered by the "Available Funds" (the aggregate of the short-term tranche plus 50% of the medium/long term tranche invested in the general eligible assets), the difference between the Available Funds and the due payments arising from ESM liabilities in the next 12 months shall be prefunded. The prefunding of the needs shall be invested in a liquidity buffer.
# ESM – General Eligible Asset List

## List of General Eligible Assets

<table>
<thead>
<tr>
<th>Investment Instruments</th>
<th>Debt securities (mainly bonds, bills, covered bonds and commercial papers, certificates of deposit)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Secured deposits with eligible counterparties (repurchase agreements where the ESM receives securities collateral as a guarantee of a placement)</td>
</tr>
<tr>
<td></td>
<td>Unsecured deposits with eligible counterparties (placement in money market instruments with no collateral)</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Issuers</th>
<th>Central banks</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Sovereigns and their related debt management offices</td>
</tr>
<tr>
<td></td>
<td>Euro area government-related agencies</td>
</tr>
<tr>
<td></td>
<td>Supranational institutions</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Rating criteria</th>
<th>Minimum rating for all debt securities:</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>For each rating agency, a short or long-term rating that is equal to or higher than at least AA or equivalent for short-term assets</td>
</tr>
</tbody>
</table>

Source: ESM, UniCredit Research
# ESM – Extended Eligible Asset List

## List of Extended Eligible Assets

### Investment Instruments
- Debt securities (mainly bonds, bills, covered bonds and commercial papers, certificates of deposit)
- Secured deposits with eligible counterparties (repurchase agreements where the ESM receives securities collateral as a guarantee of a placement)
- Unsecured deposits with eligible counterparties (placement in money market instruments with no collateral)

### Issuers
- Central banks
- Sovereigns and their related debt management offices
- Government-related agencies
- Supranational institutions
- Financial institutions

### Rating criteria
- Minimum rating for all debt securities issued outside the euro area, or by non-sovereign entities:
  - For each rating agency, a short or long-term rating that is equal to or higher than at least AA or equivalent for short-term assets

Source: ESM, UniCredit Research
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EFSF – A profile

The EFSF was created in June 2010 as part of a stabilization package agreed on by the eurozone members including:

- the European Union: EUR 60bn (EFSM program),
- the European Financial Stability Facility: EUR 440bn,
- the International Monetary Fund: EUR 250bn, and
- the ECB, which purchases sovereign bonds in the secondary market.

The EFSF’s mandate: To safeguard financial stability of Europe’s monetary union by providing temporary financial assistance to euro area member states.

Temporary institution: The EFSF has been created as a temporary institution.

No preferred creditor status: EFSF loans to a eurozone member rank pari passu with the eurozone member’s senior unsecured bonds. In contrast to most other supranationals, the EFSF does not enjoy preferred-creditor status.

There is strong support for the EFSF from its shareholders as well as from the international political community.
EFSF – Legal structure & scope of activity

- **EFSF – limited liability company incorporated under Luxembourg law.**

- 17 **shareholders** – the 17 eurozone members.

- From a credit perspective, the **EFSF is a supranational issuer** as it is backed by more than one sovereign state.

- **Scope of activity** - In order to fulfill its mission, the EFSF is authorized to:
  - Provide loans to euro area member states in financial difficulties
  - Intervene in the primary and secondary bond markets
  - Act on the basis of a precautionary program
  - Finance recapitalizations of financial institutions through loans to governments including in non-program countries
  - All financial assistance to member states is linked to strict conditionality.
## EFSF – Lending by country

### EFSF lending by country (EUR bn)

<table>
<thead>
<tr>
<th>Country</th>
<th>Already disbursed</th>
<th>Pending disbursement</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ireland</td>
<td>12.0</td>
<td>5.7</td>
<td>17.7</td>
</tr>
<tr>
<td>Portugal</td>
<td>17.4</td>
<td>8.6</td>
<td>26.0</td>
</tr>
<tr>
<td>Greece</td>
<td>73.9</td>
<td>70.7</td>
<td>144.6</td>
</tr>
<tr>
<td><strong>PSI participation</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>34.5</td>
<td>0</td>
<td>35.5</td>
</tr>
<tr>
<td>of which</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>- PSI sweetener</td>
<td>29.7</td>
<td>0</td>
<td>30.0</td>
</tr>
<tr>
<td>- Accrued interest</td>
<td>4.8</td>
<td>0</td>
<td>5.5</td>
</tr>
<tr>
<td><strong>Second program</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>75.7</td>
<td>24.4</td>
<td>109.1</td>
</tr>
<tr>
<td>of which</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>- Bank recapitalization</td>
<td>41.0</td>
<td>9.0</td>
<td>48.0</td>
</tr>
<tr>
<td>- Rest of program</td>
<td>34.7</td>
<td>24.4</td>
<td>59.1</td>
</tr>
</tbody>
</table>

Data as of 7 February 2013. Source: EFSF, UniCredit Research
Loan details – Ireland and Portugal

### Ireland - Current average maturity 12.47Y

<table>
<thead>
<tr>
<th>Date of disbursement</th>
<th>Amount disbursed</th>
<th>Maturity of loan</th>
</tr>
</thead>
<tbody>
<tr>
<td>1/2/2011</td>
<td>3.6</td>
<td>18/07/2016</td>
</tr>
<tr>
<td>10/11/2011</td>
<td>3.0</td>
<td>4/2/2022</td>
</tr>
<tr>
<td>15/12/2011</td>
<td>1.0</td>
<td>23/08/2019</td>
</tr>
<tr>
<td>12/1/2012</td>
<td>1.2</td>
<td>04/02/2015</td>
</tr>
<tr>
<td>19/01/2012</td>
<td>0.5</td>
<td>19/07/2041</td>
</tr>
<tr>
<td>3/4/2012</td>
<td>2.7</td>
<td>3/4/2037</td>
</tr>
</tbody>
</table>

*Interim Financing, to be rolled over. The final maturity (provided to be a max. average of 15Y) will be known once the long-term funding has been performed. Source: EFSF, UniCredit Research

### Portugal - Current average maturity 14.66Y

<table>
<thead>
<tr>
<th>Date of disbursement</th>
<th>Amount disbursed</th>
<th>Maturity of loan</th>
</tr>
</thead>
<tbody>
<tr>
<td>22/06/2011</td>
<td>3.7</td>
<td>5/7/2021</td>
</tr>
<tr>
<td>29/06/2011</td>
<td>2.2</td>
<td>5/12/2016</td>
</tr>
<tr>
<td>20/12/2011</td>
<td>1.0</td>
<td>23/08/2025</td>
</tr>
<tr>
<td>12/1/2012</td>
<td>1.7</td>
<td>04/02/2015</td>
</tr>
<tr>
<td>19/01/2012</td>
<td>1.0</td>
<td>19/07/2026</td>
</tr>
<tr>
<td>30/05/2012</td>
<td>5.2</td>
<td>30/05/2032</td>
</tr>
<tr>
<td>17/07/2012</td>
<td>2.6</td>
<td>17/07/2038</td>
</tr>
<tr>
<td>3/12/2012</td>
<td>0.8</td>
<td>3/12/2028</td>
</tr>
<tr>
<td>7/2/2013</td>
<td>0.8</td>
<td>7/02/2022</td>
</tr>
</tbody>
</table>

*Interim Financing, to be rolled over. The final maturity (provided to be a max. average of 15Y) will be known once the long-term funding has been performed. Source: EFSF, UniCredit Research
# Loan details – Greece

Greece - Current average maturity 29.66Y

<table>
<thead>
<tr>
<th>Second Greek program</th>
<th>Date of disbursement</th>
<th>Amount disbursed</th>
<th>Maturity of loan</th>
</tr>
</thead>
<tbody>
<tr>
<td>Loan – Installment 1 - Tranche 1</td>
<td>19/03/2012</td>
<td>5.9</td>
<td>19/03/2047</td>
</tr>
<tr>
<td>Loan - Installment 1 - Tranche 2</td>
<td>10/04/2012</td>
<td>3.3</td>
<td>10/04/2041</td>
</tr>
<tr>
<td>Loan - Installment 1 - Tranche 3 (Bank recapitalization)</td>
<td>19/04/2012</td>
<td>25.0</td>
<td>19/04/2046</td>
</tr>
<tr>
<td>Loan - Installment 1 - Tranche 4</td>
<td>10/05/2012</td>
<td>4.2</td>
<td>10/05/2042</td>
</tr>
<tr>
<td>Loan - Installment 1 - Tranche 5</td>
<td>28/06/2012</td>
<td>1.0</td>
<td>28/06/2040</td>
</tr>
<tr>
<td>Loan - Installment 2 - Tranche 1</td>
<td>17/12/2012</td>
<td>11.291</td>
<td>17/06/2042</td>
</tr>
<tr>
<td>Loan - Installment 3 - Tranche 1</td>
<td>7/12/2012</td>
<td>7.0</td>
<td>17/12/2046</td>
</tr>
<tr>
<td>Loan - Installment 3 - Tranche 2 (Bank recapitalization)</td>
<td>19/12/2012</td>
<td>16.0</td>
<td>***</td>
</tr>
<tr>
<td>Loan - Installment 3 - Tranche 3</td>
<td>31/01/2013</td>
<td>2.0</td>
<td>31/01/2043</td>
</tr>
</tbody>
</table>

**PSI participation**

<p>| | | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>PSI sweetener</td>
<td>various dates *</td>
<td>29.7</td>
</tr>
<tr>
<td>Accrued interest</td>
<td>various dates **</td>
<td>4.8</td>
</tr>
</tbody>
</table>

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EFSF – Support mechanisms

- There are several support mechanisms in place for the EFSF.

- In the first instance, EFSF bonds are serviced by loan repayments from the borrowing eurozone members.
  - The borrower is required to deposit loan repayments with the European Central Bank (ECB) 14 business days before the due date.

- Should a borrower fail to make a loan repayment, there are additional credit enhancements, which are divided into:
  
  - EFSF 1.0 (the initial EFSF structure) and
  
  - EFSF 2.0 (the amended EFSF structure).
Support mechanism: EFSF 1.0 (initial structure)

The initial structure included:

- **Guarantees from the eurozone member states**: The eurozone member states provide explicit, unconditional, and irrevocable guarantees for the EFSF's bond issues (EUR 440bn). Each member state guarantees up to 120% of its own share of the bonds issued by the EFSF ("over-guarantee"). The share is determined by their paid-in capital contribution to the ECB, adjusted for the shares of those sovereigns that have stopped acting as guarantors. All guarantors rank equally and pari passu among themselves. As Greece, Ireland and Portugal have "stepped out" as guarantors for EFSF bonds, the remaining euro member states' contribution keys have been readjusted. If a guaranteeing member state were to "step out" after a bond has already been issued, it would still be responsible for the guarantees already provided for previous bonds (e.g. Portugal will still have to honor its guarantee for the inaugural EFSF 2.75% 07/16 bond although it has "stepped out" as guarantor in the meantime).

- **Extensive liquidity reserves**: They are designed in such a way that any loan is covered either by AAA/AA+ guarantees, and/or by liquidity reserves. The EFSF’s operational policies state that the cash reserve as well as the cash buffer must be invested in AAA-rated securities. There are two components in the liquidity reserve:
  - **Cash reserve**: It is generated by deducting: 1. an upfront service fee of 50bp on the principal amount, and 2. a percentage equal to the net present value of the interest margin from loan disbursements to a borrowing sovereign. The cash reserve will ultimately provide remuneration for the guarantors (after repayment of all funding instruments), but will initially be retained by the EFSF as loss-absorbing capital.
  - **Loan-specific cash buffer**: All of EFSF's funding instruments are matched by the sum of: 1. guarantees from AAA/AA+ rated sovereigns, 2. the cash reserve, and 3. the loan-specific buffer itself. The loan-specific cash buffer is the residual to make sure that any EFSF loan is fully covered by AAA/AA+ guarantees and/or liquidity reserves.

The first three bonds by the EFSF have been issued under this structure: **EFSF 2.75% 07/16 (issued in January 2011)**, **3.375% 07/21 (issued in June 2011)**, and **2.75% 12/16 (issued in June 2011)**.
Support mechanism: EFSF 2.0 (amended structure)

- Bonds issued by the EFSF after 13 October 2011 are supported by the amended guarantee structure.

- Each member state guarantees up to 165% of its own share of the bonds issued by the EFSF ("over-guarantee").
  - The over-guarantee was increased from 120% to 165% compared to the initial structure.
  - The share is determined by a member state's paid-in capital contribution to the ECB, adjusted for the shares of those sovereigns that have stopped acting as guarantors (Ireland, Portugal and Greece).
  - All guarantors rank equally and pari passu among themselves.
  - The liquidity buffers that existed under the initial structure are no longer required.

- The guarantees for the EFSF's bond issues are explicit, unconditional, and irrevocable.

- The total guarantee commitments were increased to EUR 780bn under the amended structure. The effective lending capacity of the EFSF is therefore EUR 440bn, which is explained by the over-guarantee of 165%.
EFSF – Guarantee structure without Ireland, Greece, and Portugal

Adjusted contribution keys

Maximum guarantee commitments (EUR mn)

Note that GR, IE, and PT have become stepping-out guarantors. Their contribution keys are readjusted among the remaining guarantors and the guarantee commitment is reduced.

Source: EFSF, UniCredit Research
EFSF 1.0 and 2.0 – credit enhancements

Credit enhancements of EFSF 1.0

Credit enhancements of EFSF 2.0

Source: EFSF, UniCredit Research
Liquidity test under EFSF 2.0

- **Liquidity test:** Under the new structure, the EFSF will conduct a liquidity test ten days prior to any debt payment coming due to ensure that there are sufficient funds available. If there is a shortfall, guarantors are required to provide the EFSF with additional funds no later than three days prior to the due date. If there is still a shortfall because of a failure of one or more guarantors to remit the requested amount, the guarantors will be required to provide additional funds up to 165% of their share subject to the ceiling on their guarantee commitment as specified in the amended Framework Agreement.

<table>
<thead>
<tr>
<th>Test: Are available funds at least equal to guarantees from non-AAA guarantors?</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Yes:</strong> Additional test made on T-3</td>
</tr>
<tr>
<td><strong>No:</strong> Guarantees are called for funds to be received on T-3; Second test to be undertaken on T-3</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Test: Are cash and bank deposits at least equal to scheduled payment of debt service?</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Yes:</strong> No call on guarantors</td>
</tr>
<tr>
<td><strong>No:</strong> Guarantors are called, including over-guarantees</td>
</tr>
</tbody>
</table>

Source: Fitch, UniCredit Research
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Instruments of the EFSF - Overview

- The EFSF is authorized to use additional instruments (in addition to providing loans to euro area member states):
  - Intervene in the primary bond markets
  - Intervene in the secondary bond markets
  - Act on the basis of a precautionary program
  - Finance recapitalizations of financial institutions through loans to governments including in non-program countries

- In the following slides, we have summarized the EFSF guidelines for these four instruments.
**Instruments: Guidelines for primary market purchases**

- **Objective and activation:** Primary market purchases (PMP) are complementary to regular loans under a macroeconomic adjustment program or to draw-downs of funds under a precautionary program. The EFSF's participation would reduce the risk of a failed auction or of not raising the required fund amount. Furthermore, this instrument should encourage states to return to the financial markets.

- **Timing:** A complementary tool that would primarily be used towards the end of an adjustment program to facilitate the return of a beneficiary country to the market, or as an alternative to the draw-down of funds under a precautionary program (while the possibility of using PMP at an earlier stage should not be fully excluded).

- **Participation in auctions:**
  - The EFSF should participate at the weighted average price to minimize the impact on the auction result.
  - The amount of purchases should be limited to no more than 50% of the final issued amount. If there are insufficient market bids at acceptable levels to sell 50% or more of the targeted amount, the EFSF will buy the balance between the amount which can be sold to the market and 50% of the targeted issuing amount. Thus, the outstanding amount is at least half of the originally targeted amount.

- **Participation in syndicated transactions:**
  - The EFSF will purchase securities at the re-offer price.
  - The amount of purchases should be limited to no more than 50% of the final issued amount. If the order book does not allow the sale of at least 50% of the targeted amount, the EFSF will buy the balance between the amount that can be sold to investors and 50% of the targeted issuing amount. The remaining 50% must be taken up by the syndicate.

- **Management of the portfolio of bonds:**
  - Four strategies: Sell the bonds back to the market; Hold bonds to maturity; Keep bonds as available-for-sale and sell bonds back to the country; or use bonds for repos with commercial banks to support liquidity management of the EFSF.

Source: EFSF [Link](#)
**Objective:** Secondary market purchases (SMP) serve to support the functioning of debt markets and appropriate price formation of government bonds.

SMP of EUR-denominated bonds of euro area member states can be activated immediately subject to the EFSF capacity available, on the basis of ECB analysis recognizing an exceptional market situation and contagion risk that could threaten the financial stability of the euro area as a whole and its member states, and compliance with the acceptance procedure. The ECB will provide an expert analysis of financial market disruptions and contagion risk. In addition, it is able – in an advisory capacity – to provide recommendations regarding the volumes and types of assets to be purchased.

**Conditions:** Access to an SMP facility will imply appropriate policy reform efforts to be specified in a Memorandum of Understanding (MoU). For program countries, compliance with the macroeconomic policy conditions is clearly a requirement. Countries benefiting from such interventions outside a macroeconomic adjustment program would have to comply with ex-ante eligibility conditions as defined in the context of the European fiscal and macroeconomic surveillance framework and take corrective action.

**Procedure:** The procedure is initiated by a request from a member state. The Commission, in liaison with the ECB, would prepare an MoU within 1-2 days specifying the availability period, the fiscal adjustment and the structural reforms needed for support. The intervention envelope will be equal to the remaining lending capacity of the EFSF. The technical sub-committee will also set pro-tempore intervention caps. The guarantee amount needed to finance the envelope will be approved, where necessary, by restricted committees in National Parliaments under a fast track procedure.

The SMP allows to buy all marketable debt instruments if they are a) denominated in EUR, b) either (i) issued by central governments or public entities of the member states whose currency is the euro, or (ii) issued by other entities incorporated in the euro area and meeting the asset eligibility criteria of ECB collateral rules for repo operations. The EFSF secondary market intervention will have a more limited scope, being directed towards EUR-denominated securities issued by the public sector of a euro area member state.

**Management of the portfolio of bonds:**
- Four strategies: Sell the bonds back to the market; hold bonds to maturity; keep bonds as available-for-sale and sell bonds back to the country; or use bonds for repos with commercial banks to support liquidity management of the EFSF.

Source: EFSF ([Link](#))
Instruments: Guidelines for precautionary programs

**Objective:** The objective is to support sound policies and prevent crisis situations, by encouraging countries to secure the possibility to access EFSF assistance before they face difficulties raising funds in the capital markets. This serves as a "reserve type" instrument to overcome external temporary shocks. This instrument is activated upon request by a member state.

**Activation:** Upon request by member state.

**Types of credit lines:** There are three types of credit lines available:
- a precautionary credit line (PCCL)
- an enhanced conditions credit line (ECCL)
- an enhanced conditions credit line offering partial risk protection (ECCL+)

**Conditions:** See table on next slide. There is a global assessment with respect to a number of criteria, including the fulfillment of the Stability and Growth Pact (SGP) commitments, debt sustainability, access to capital markets, the external balance, etc. before a credit line is granted.

**Enhanced surveillance:** A member state receiving assistance under a precautionary program is placed under enhanced surveillance by the European Commission. It will vary according to the nature of risks to financial stability or imbalances to address.

**IMF:** IMF involvement is actively sought.

**Procedure:** The state has the flexibility to request the draw-down of funds or a primary market intervention at any time during the availability period, according to the agreed terms. It shall inform the EFSF at least a week in advance of its intention to draw funds. The maximum size of a tranche or primary market purchase shall be set in the initial decision to grant a credit line. The lending conditions will be the same as for regular EFSF loans.

**Conditionality:** In case of deviation from policy conditions, the credit line may be closed. The state will then be expected to request regular support under a full adjustment program.

Source: EFSF (Link)
Instruments: Guidelines for precautionary programs

### Types of credit lines

<table>
<thead>
<tr>
<th></th>
<th>Precautionary conditioned credit line (PCCL)</th>
<th>Enhanced conditions credit line (ECCL)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Access</strong></td>
<td>Countries with robust policy frameworks and very strong track records in economic performance</td>
<td>Countries with sound policies and fundamentals, but with some vulnerabilities that preclude using the PCCL</td>
</tr>
<tr>
<td><strong>Benchmark</strong></td>
<td>IMF’s FCL</td>
<td>IMF’s PCL</td>
</tr>
<tr>
<td><strong>Ex-ante conditions</strong></td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td><strong>Ex-post conditions</strong></td>
<td>No</td>
<td>Yes – adopt corrective measures</td>
</tr>
<tr>
<td><strong>Cap</strong></td>
<td>No upfront cap</td>
<td>No upfront cap</td>
</tr>
<tr>
<td><strong>Typical size</strong></td>
<td>2%-10% of GDP</td>
<td>2%-10% of GDP</td>
</tr>
<tr>
<td><strong>Information exchange</strong></td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td><strong>Duration</strong></td>
<td>1Y, renewable for 6 months twice</td>
<td>1Y, renewable for 6 months twice</td>
</tr>
</tbody>
</table>

**ECCL+**: The third type of credit line available is the ECCL+. It is an enhanced conditions credit line that is provided with sovereign partial risk protection to primary bonds. Access to the ECCL+ corresponds to the same criteria and conditionality as that to the ECCL, while reflecting the specific circumstances requiring the issuance of a PCCL. The MoU will detail the corrective measures to be adopted during the availability period and the commitment to comply with the eligibility criteria for the duration of the credit line.

Source: EFSF ([Link](#))
Instruments: Guidelines for FI recapitalization via loans to non-program countries

**Objective:** The objective is to provide financing to member states in order to specifically support financial institutions against appropriate conditionality, i.e. not necessarily in the context of a macroeconomic adjustment program but under another more focused form of conditionality. The ability of the beneficiary country to reimburse the loan granted should nevertheless be ensured by a sound macroeconomic policy framework and the existence of an otherwise resilient financial sector. The capital injected as part of such a public recapitalization is expected to be of the highest possible quality.

- **Financing is channeled through the state.**

**Eligibility:** Pecking order of financing of the recapitalization:
- Private sector contribution (financed by shareholders)
- National governments (possibly through national schemes for the recapitalization or resolution of the financial institutions in distress [deposit guarantee scheme-type or resolution frameworks])
- Last-resort instrument: EFSF.

A candidate for recapitalization will have to be a distressed financial institution, which is either systemically relevant or posing a threat to financial stability. In addition, a beneficiary country will have to demonstrate that it has a sound fiscal policy record and sufficient capacity to reimburse the EFSF loan even in cases where such a beneficiary country would not be able to recover the capital injected according to the timing agreed in the state-aid decision. The size of the loan should not threaten the fiscal position of the beneficiary member state.

**Two forms of conditionality:**
- EU law related, institution-specific conditionality to comply with EU state aid rules. As a general rule, every beneficiary institution will be subject to a restructuring plan commensurate with the extent of the financial support received.
- Horizontal conditionality including structural reform of the domestic financial sector

**Procedure:** Request from a national government, which will ultimately bear the liability of the loan. This is followed by an independent assessment covering the origin and degree of distress of an institution, the need to restore viability, and systemic relevance. An MoU is prepared while compliance is verified by the European Commission. Should a profit be realized from the recapitalization, this would be used for early repayment of the loan upon request of the EFSF.
Leveraging the EFSF

- **Two options to leverage the EFSF**: The options aim at providing immediate and credible support, they are always linked to appropriate conditionality and seek co-operation with the IMF.

- **There are two options:**

  - **Option 1 – Partial sovereign risk protection**
    Aimed at increasing demand for new issues of member states’ sovereign bond programs and lowering the member state’s funding costs, thereby supporting the sustainability of public finances.

  - **Option 2 – Co-Investment Funds (CIF)**
    Allows the combination of public and private funding to enlarge the resources available to EFSF’s financial assistance instruments.

- **Guidelines**: Financing will be linked to a Memorandum of Understanding entailing policy conditionality appropriate for the financial instrument chosen, and monitoring and surveillance procedures as specified in the EFSF guidelines.

  - Option 1 will be applied under the guidelines for precautionary programs or under regular programs.

  - Option 2 will follow the guidelines on primary and secondary market purchases.

- **ESM**: ESM member states are considering extending these options to maximize the capacity of the ESM.

Source: EFSF (Link)
Leveraging the EFSF: Option 1 – Partial sovereign risk protection

Option 1 - Partial sovereign risk protection

The approach of partial risk protection is to be used primarily under precautionary programs and is aimed at increasing demand for new issues from member states and lowering funding costs. Under this option, the EFSF provides a partial protection certificate to a newly issued sovereign bond. Both would have the same maturity. Thus, the sovereign bond and the certificate are initially offered together, but after the initial issue, the bond and the certificate will be detachable and can be traded separately. The partial protection certificate gives the holder fixed credit protection of 20-30% (to be determined) of the principal amount of the sovereign bond to which it was initially attached. The certificate is issued by an SPV in Luxembourg, which is not legally connected to the EFSF or member states.

According to the terms, 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 of 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. The SPV shall finance the payments due by receipt of drawings made under a financial assistance facility agreement (FFA). The claim will be settled by delivering cash or EFSF bonds. As such, the claim is unfunded until the time of a call. Upon investors’ request, it could be considered that claims would be funded at the outset. Investors will be required, at time of claim or settlement, to demonstrate that they hold outstanding sovereign bonds of at least the same principal value as the original bond covered by the certificate.

Source: EFSF (Link)
Leveraging the EFSF: Option 2 – Co-Investment Funds (CIF)

**Option 2 – Co-Investment Funds (CIF)**

The creation of one or more Co-Investment Funds (CIF) to allow the combination of public and private funding. The CIF would aim to create additional liquidity and to enhance market capacity to fund loans. It would purchase bonds in the primary and/or secondary markets, which as a rule will be held to maturity but could also be sold earlier in pre-defined circumstances. The CIF will have one or more compartments. Each compartment could either be dedicated to a single member state or to several. The CIF will be a subsidiary of the EFSF in Luxembourg, and have a predefined lifetime. The CIF will have three layers: a first-loss tranche (financed by the EFSF), a participating tranche – freely tradable – and potentially a third layer of a rated senior debt tranche, also freely tradable.

The details with respect to each tranche of a CIF are as follows:

- **The first loss tranche will be financed by the EFSF.** A coupon of the first loss tranche will be set to cover the all-in funding and related operational costs of the EFSF. The tranche is made available to the CIF after the EFSF enters into a financial assistance facility agreement with the relevant member state and the signing of a Memorandum of Understanding specifying conditionality. At maturity of the CIF, or earlier in the case of any sale of underlying bonds, the first loss tranche will be redeemed from disposal proceeds, after redemption of the capital of any senior tranche, the participating tranche, but prior to any gains. The EFSF funding for the first loss tranche will be guaranteed by the member states.
Leveraging the EFSF: Option 2 – Co-Investment Funds (CIF)

- **Option 2 – Co-Investment Funds (CIF) protection – Details on the tranches ctd.**

  - **A participating tranche will be sold to investors:** these units will be tradable. The tranche ranks ahead of the first loss tranche in any distribution of gains from the CIF, after repaying the capital contribution from both the first loss tranche and the capital of the participating tranche. The tranche would be funded in pre-agreed drawdowns and any undrawn commitments would be supported by acceptable commitments. It will receive a coupon from the cash flows being generated by the CIF. This may rank either above, or after, the coupon due on the first loss tranche. The coupon due on any senior bond tranche will rank ahead of both these tranches. At maturity of the CIF, or earlier in the case of the sale of the underlying bonds, the participating tranche will be redeemed pro-rata from disposal proceeds, ahead of the first loss tranche but prior to distribution of any gains. The majority or all of the gains made on investments at termination of the CIF will be allocated to this tranche, after repayment of all senior tranches and the EFSF's first loss capital.

  - **Senior debt tranche (optional):** The CIF can issue rated fixed-income senior bonds, ranking ahead of the participating tranche and the first loss tranche. The bonds will have a target rating of AA/A, dependent on the underlying securities purchased.

Source: EFSF (Link)
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Funding strategies – An overview

- **EFSF**
  - **Instruments**: Benchmark bonds, T-Bill stopped since replaced by ESM bill program in Jan 2013
  - **Currencies**: So far only EUR, others possible
  - **Longest outstanding benchmark**: April 2037 (EUR 2.5bn), issued in June 2012
  - **Total bonds outstanding**: EUR 137bn
  - **2013 funding**: EUR 58bn (2012: 44.8bn, 2011: EUR 16bn); 2014: EUR 34.5bn

- **ESM**
  - **Instruments**: Benchmark bonds (1-30Y), T-Bills, taps, promissory/registered notes
  - **Currencies**: Initial focus on building a EUR-benchmark curve, diversification into other currencies possible
  - **Timing**: Inaugural bond is expected for 2H13. T-Bill program started in Jan 2013.
ESM – Funding strategy

- **EFSF and ESM funding will be managed in parallel by one team.**

- **The ESM will apply a diversified funding strategy using a variety of instruments**, including capital market instruments with maturities of 1-30Y, and money market instruments including bills, unsecured market transactions, liquidity lines and credit lines.

- In terms of size and maturity, the ESM strategy will adapt to market conditions in order to meet investor demand. The main funding currency is EUR, but the ESM may diversify by issuing in other currencies in the future.

- The ESM will initially focus on establishing a benchmark curve denominated in EUR.

- **The funding strategy uses a liquidity buffer as a key component: funds are pooled and then disbursed to program countries when required.**

- In order to avoid discrimination among beneficiary countries, an ESM base rate will be calculated as the daily average interest rate resulting from the funding pooling, such that all countries pay the same rate on the same day and accrue in accordance with their specific loan maturities.

- The ESM may hold its own bonds for a limited amount of time. This offers the possibility to raise additional funding either by selling the bonds in the secondary market or by using them as collateral in the secured money market.
EFSF – Funding strategy

- The EFSF adopts a **diversified funding strategy**, including medium-to-long-term bonds.

- EFSF’s debt issuance program is sized EUR 241bn.

- Given this approach, the funds raised by the EFSF are **no longer attributed to a particular country**, but are instead pooled and then disbursed. As such, a common lending rate is applied to all countries.

- Funding does not need to be **back-to-back** with lending operations, although the EFSF aims to ensure the same profile as the underlying loans.

- The German Finanzagentur provides both front and back-office functions of debt issuance, cash and risk management.

- Strategy with respect to size and maturity **adapts to market conditions in order to meet investor requirements for liquidity.** In terms of issuance method, the EFSF may use syndications, auctions, private placements and taps.

- No restriction with regard to currencies, but the majority of funds are likely to be raised in EUR.

- The EFSF’s debt obligations carry a **0% Basel II risk weighting** (under the Standardized Approach). The bonds are included in the **iBoxx Sub-Sovereigns - Supranationals.**
EFSF
Ireland, Portugal & Greece's macroeconomic adjustment programs

**Ireland:** Package of EUR 85bn for 2010-2013 agreed on at end-November 2010

- **EUR 17.7bn EFSF**
- **EUR 22.5bn EU (EFSM)**
- EUR 4.8bn bilateral loans from the UK, Denmark, and Sweden
- **EUR 22.5bn IMF**
- **EUR 17.5bn from Ireland itself**

**Portugal:** Package of EUR 78bn for 2011-2014 agreed on in May 2011

- **EUR 26bn EFSF**
- **EUR 26bn EU (EFSM)**
- **EUR 26bn IMF**

**Greece:** Package of EUR 172.6bn during 2012-2014 agreed in February 2012

- **EUR 144.6bn EFSF** (excluding EUR 35bn for temporary ECB collateral)
- **EUR 28bn IMF** (of which EUR 8.2bn after 2014)
### Greek package

**Greek financial assistance program (EUR bn)**

<table>
<thead>
<tr>
<th>2012-2014</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Total Greek package</strong></td>
<td>172.6</td>
</tr>
<tr>
<td>of which</td>
<td></td>
</tr>
<tr>
<td>PSI</td>
<td>30.0</td>
</tr>
<tr>
<td>Accrued interest</td>
<td>5.5</td>
</tr>
<tr>
<td>IMF contribution</td>
<td>28.0 (of which 8.2 after 2014)</td>
</tr>
<tr>
<td>Bank recap</td>
<td>up to 48.0</td>
</tr>
<tr>
<td>Undisbursed first bilateral facility</td>
<td>24.4</td>
</tr>
<tr>
<td>New loan facility</td>
<td>36.7</td>
</tr>
</tbody>
</table>

Source: EFSF, UniCredit Research
## EFSF preliminary funding plan

### Preliminary funding plan of the EFSF (EUR bn)

<table>
<thead>
<tr>
<th>Country</th>
<th>1Q13</th>
<th>2Q13</th>
<th>3Q13</th>
<th>4Q13</th>
<th>Total 2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>Ireland</td>
<td>0.80</td>
<td>1.40</td>
<td>1.40</td>
<td>1.20</td>
<td>4.80</td>
</tr>
<tr>
<td>Portugal</td>
<td>0.80</td>
<td>0.00</td>
<td>1.90</td>
<td>1.90</td>
<td>4.60</td>
</tr>
<tr>
<td>Greece</td>
<td>7.60</td>
<td>3.20</td>
<td>0.60</td>
<td>5.10</td>
<td>16.50</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th>1Q13</th>
<th>2Q13</th>
<th></th>
<th>3Q13</th>
<th>4Q13</th>
<th>Total 2013</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total lending requirements</td>
<td>10.00</td>
<td>4.60</td>
<td>3.90</td>
<td>8.20</td>
<td>25.90</td>
<td></td>
</tr>
<tr>
<td>Long-term funding</td>
<td>16.50</td>
<td>16.50</td>
<td>13.00</td>
<td>12.00</td>
<td>58.00</td>
<td></td>
</tr>
<tr>
<td>Short Term Funding (end of period)</td>
<td>18.00</td>
<td>17.00</td>
<td>11.00</td>
<td>4.20</td>
<td>-</td>
<td></td>
</tr>
</tbody>
</table>

Data as of 7 February 2013. Source: EFSF, UniCredit Research
The first financial assistance was provided by the ESM in December in the form of two bills and three floating rate notes for a total amount of close to EUR 39.5bn for the Spanish bank recapitalization. For 2013, the ESM will finance the rollover of the two aforementioned bills for an amount of EUR 8.968bn. The ESM bill program is expected to cover funding needs for the first half of 2013 with an inaugural bond issuance expected for the second half. In addition, the ESM will be responsible for the financing of future macroeconomic assistance programs.
EFSF & ESM maturity profile

Source: ESM as at 21 Jan 2013, UniCredit Research
European Supras – Spread development

ASW spread development: 3Y maturity bracket

Data as of 7 February 2013
Source: UniCredit Research
European Supras – Spread development

ASW spread development: 10Y maturity bracket

Data as of 7 February 2013
Source: UniCredit Research
European Supras – Credit curves over time

Data as of 7 February 2013
Source: UniCredit Research
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ESM – Rating agencies' view

Ratings of ESM

<table>
<thead>
<tr>
<th></th>
<th>L-T</th>
<th>S-T</th>
<th>Outlook</th>
</tr>
</thead>
<tbody>
<tr>
<td>Moody's</td>
<td>(P)Aa1</td>
<td>(P)P-1</td>
<td>Negative</td>
</tr>
<tr>
<td>S&amp;P</td>
<td>--</td>
<td>--</td>
<td>--</td>
</tr>
<tr>
<td>Fitch</td>
<td>AAA</td>
<td>F1+</td>
<td>Stable</td>
</tr>
</tbody>
</table>

Source: Rating agencies, UniCredit Research

- On the following slides, we summarize the rationale of the rating agencies as well as the rating triggers for the ESM.
ESM – Rating agencies' view - Moody's

- **Moody’s bases its rating on four key rating factors:**
  - the ESM’s anticipated low leverage
  - the creditworthiness of the ESM’s members, the euro-area member states
  - the sound liquidity and capital management policy with an Early Warning System (EWS) that ensures that funds will be available on time
  - the ESM’s preferred creditor status

- Moody’s describes the ESM’s purpose as being to provide an inter-governmental support mechanism that extends financial assistance to members that are either unable to access the capital markets or able to do so only at very high interest rates.

- **1. Anticipated low leverage:** The first key rating factor underlying Moody’s decision to assign a Aaa rating to the ESM relates to its anticipated low leverage. This relates to the ESM’s lending capacity (both loans extended to and purchases of securities issued by supported member states) of EUR 500bn and subscribed capital of EUR 700bn. If the ESM’s capital is reduced (e.g. due to losses resulting from a borrower default), the leverage ratio – defined as lending capacity/subscribed capital which must not exceed 71% – would automatically limit the lending capacity and thereby stabilize the structure of the ESM funding. In such a scenario, loans under existing programs would continue to be disbursed, but any new lending commitments surpassing the lending capacity would require a simultaneous increase in the ESM’s capital.

- **2. Creditworthiness of shareholders:** Moody’s second key rating factor underpinning the Aaa ratings is that the ESM’s shareholders are the euro-area member states, which provide capital to the ESM according to the same capital key that is applied to the European Central Bank (ECB). The ESM therefore benefits from the very high credit quality of its shareholders and the very high likelihood that they will be able to comply with their capital-related obligations.
3. Strong liquidity and capital-management policy: Moody’s third key rating factor is the ESM’s strong liquidity and capital-management policy. In particular, the policy aims to ensure that all payments over the next 12 months are fully covered by the ESM’s own liquidity reserves. Moody’s highlights the additional credit-enhancing feature, the ESM’s EWS. This system provides an assessment of borrowers’ repayment capacity well in advance of the repayment date, thereby ensuring that capital calls can be made and implemented well in advance of any payment shortfall. Moody’s points to the ESM treaty, which places a legal obligation on the ESM’s managing director to call capital if needed without requiring the approval of the board of governors or the board of directors. With respect to its capital-management policy, the ESM invests in liquid Aa2 or higher-rated instruments, mainly government securities or the equivalent.

4. Preferred creditor status: Moody’s fourth key rating factor is the ESM’s preferred creditor status, which is junior only to that of the IMF. This status distinguishes the ESM from its predecessor entity, the EFSF, which ranks pari passu with senior unsecured bondholders.

Following the downgrade of France to Aa1 from Aaa by Moody’s on 19 Nov 2012, the rating agency also downgraded the ESM to Aa1 from Aaa. The ratings remain on negative outlook. The short-term ratings are not affected.

Rationale: According to Moody’s, the rating action was driven by the downgrade of France and the high correlation in credit risk which is believed to be present among the ESM’s largest financial supporters. France is the second largest contributor to the two entities’ financial resources, as a provider of callable capital for the ESM. Moody's thinks that there is a high correlation in credit risk among the entities' supporters given the close institutional, economic and financial linkages among the major euro area sovereigns. As a result, the credit risks and ratings of the ESM are closely aligned to those of its strongest supporters.
ESM – Rating agencies' view - Fitch

The ESM's key strengths are:
- exceptionally strong mechanism for exercising callable capital, including an "early warning system" to ensure timely management of capital needs
- relatively high capitalization ratio and the requirement that paid-in capital/reserves will always be equal to at least 15% of outstanding debt
- high-quality and liquid assets that will always be equivalent to at least 12 months of maturing ESM liabilities
- the ESM's preferred creditor status (PCS)
- the strength of its governance in terms of management as well as the composition of its board of governors, underscoring the strong political support for the ESM
- prudent investment guidelines adopted by the ESM for the management of its reserves and capital.

High capitalization ratio: The ESM maximum lending capacity of EUR 500bn is backed by EUR 700bn of paid-in and callable capital. In addition, 92% of the EUR 500bn lending capacity (which would be financed by the ESM from public debt markets) would be covered by paid-in capital and the callable capital of the shareholders currently rated AA- and above by Fitch, which compares favorably to other AAA multilateral lending institutions. Fitch notes that the explicit and legally binding mechanism to pay in additional capital if required to maintain the creditworthiness of the ESM is crucial for offsetting the principal credit and rating weakness relative to peers, which is the potentially large and very concentrated risk exposures that it may incur.

The ESM will be better capitalized than other European multilateral lending institutions: it will be endowed with a significant amount of capital, representing 11.4% of subscribed capital, and disbursed in five equal installments (20% each) over 2012-2014. The founding treaty limits ESM lending to EUR 500bn and stipulates that paid-in capital must represent at least 15% of debt issued during the phase-in period; as lending will be funded by debt. This means that the ratio of paid-in capital to loans must be maintained above 15% of outstanding loans. Hence, when operating at full capacity, the equity-to-assets ratio will be at 13.8%, which is in line with other AAA rated European multilateral lending institutions, according to Fitch.
ESM – Rating agencies' view – Fitch (continued)

- **Capital calls:** The shareholders of the ESM are the 17 eurozone countries; their share is calculated on the basis of their contribution key and equal to their share in the European Central Bank's capital. Subscribed capital amounts to EUR 700bn, of which EUR 80bn will be paid in between 2012-2014. The remaining share, EUR 620bn, can be called on in case of need. According to the ESM's founding treaty, a capital call can be launched to revise the ESM's lending capacity or replenish capital in the event of credit losses. **Most importantly, to avoid a default from the ESM on its debt obligations, an emergency capital call procedure unique among multinational lending institutions has been established.** To ensure timely payment, it allows the ESM's managing director to call capital without the approval of the governing bodies. Capital call payments have to be received within seven days and the shareholders' commitment to provide callable capital is legally binding.

- **The shareholders' strong willingness to support the ESM is also reflected in the preferred creditor status (PCS) granted to the ESM, which materially reduces the ESM's sovereign credit risk arising from its lending facilities and enhances recovery prospects in the unlikely event of a default.** In contrast with other multilateral lending institutions, PCS is clearly stated in the ESM founding treaty. Thus, ESM instruments will be junior only to the IMF. However, the PCS will not apply to EFSF facilities existing at the time of signing of the ESM treaty in February 2012 that are transferred to or supplemented with additional financing from the ESM, including the EUR 100bn in support of Spanish bank recapitalization. Given that financial assistance will be subject to policy conditionality as set down in a memorandum of understanding, the ESM could choose to suspend loan disbursements in the event that the conditions are not met.

- **The ESM will always have sufficient liquidity to meet all its obligations over the next 12 months.** Funds from the paid-in capital will not be lent, but used as a liquidity buffer consisting of two tranches: 1. There is a short-term (ST) tranche made up of highly liquid investments with a minimum rating of AA that will have to cover at least six months of future payments due from beneficiary countries, with a minimum overall size of EUR 5bn. 2. The remainder will be managed in a medium and long-term (MLT) tranche, made up of longer-term assets (three years maturity maximum) and may include eurozone sovereign assets rated below AA (but not the assets of sovereigns in receipt of ESM financial assistance). The ESM's operational guidelines specify that the ST tranche plus 50% of the MLT tranche must cover the ESM's liquidity needs for the next 12 months. They also state that the maximum amount that the ESM is allowed to invest in eurozone sovereign bonds rated below AA is limited at EUR 5bn and this amount is not included in the calculation of the liquidity buffer needed to cover the ESM's obligations over the next 12 months.
## EFSF – Rating agencies' view

### Ratings of EFSF

<table>
<thead>
<tr>
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</tr>
<tr>
<td>S&amp;P</td>
<td>AA+</td>
<td>A-1+</td>
<td>Negative</td>
</tr>
<tr>
<td>Fitch</td>
<td>AAA (exp)</td>
<td>F1+(exp)</td>
<td>--*</td>
</tr>
</tbody>
</table>

*Note that Fitch assigns ratings to individual EFSF debt issues and thus does not assign outlooks to individual debt issues. Source: Rating agencies, UniCredit Research*
### EFSF and ESM – Rating Triggers

<table>
<thead>
<tr>
<th></th>
<th>Moody’s</th>
<th>S&amp;P</th>
<th>Fitch</th>
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</thead>
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<tr>
<td><strong>EFSF</strong></td>
<td>- Deterioration of the creditworthiness of the guarantors,</td>
<td>- Downgrade der Ratings der</td>
<td>- Deterioration of the credit quality of the largest guarantors</td>
</tr>
<tr>
<td></td>
<td>in particular DE, FR und NL</td>
<td>AAA/AA+ Garantiegeber (DE, FR, AT, NL, FI, Lux) niedriger als AA+</td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Decreasing political support</td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>ESM</strong></td>
<td>- Deterioration of the</td>
<td>--</td>
<td>- No effect of a downgrade of the AAA countries to AA</td>
</tr>
<tr>
<td></td>
<td>creditworthiness of the guarantors,</td>
<td></td>
<td>- Change of the treaty (e.g. new instruments could influence rating)</td>
</tr>
<tr>
<td></td>
<td>in particular DE, FR und NL</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>- Decreasing political support</td>
<td></td>
<td></td>
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Source: Rating agencies, UniCredit Research
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Glossary

- **EFSF** – European Financial Stability Facility

- **EFSF 1.0** – initial setup of the EFSF (including EUR 440bn of guarantees, 120% over-guarantee, and liquidity reserves; bonds issued under this structure 07/16, 12/16, and 07/21)

- **EFSF 2.0** – amended structure; ratified mid-October 2011 (including EUR 780bn in guarantees, and 165% over-guarantee)

- **EFSM** – European Financial Stabilization Mechanism (lending program of EUR 60bn of the EU as part of the European rescue package)

- **EIB** – European Investment Bank (Europe's development bank)

- **ESM** – European Stability Mechanism (permanent mechanism)

- **EU** – European Union

- **German Finanzagentur** – Debt Management Office in Germany (in charge of debt issuance, cash and risk management for EFSF)
Links to important documents related to ESM/EFSF

ESM
- ESM Treaty (Link)
- ESM By-Laws (Link)
- ESM FAQs (Link)
- ESM Investor Presentation (Link)
- ESM Guidelines on Investment Policy (Link)
- ESM Guidelines on Borrowing Operations (Link)

EFSF
- EFSF Framework Agreement (Link)
- EFSF FAQs (Link)
- EFSF Investor Presentation (Link)
- EFSF Prospectus (Link)
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EFSF, EU, KFW, EIB 2, 3 n.a.
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RECOMMENDATIONS, RATINGS AND EVALUATION METHODOLOGY

<table>
<thead>
<tr>
<th>Company</th>
<th>Date</th>
<th>Rating</th>
<th>Currency</th>
<th>Target price</th>
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<td>n.a.</td>
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Marketweight: We recommend having the same portfolio exposure in the name as the respective iBoxx index. We expect that the average total return of the instruments of the issuer is equal to the total return of the index.

Overweight: We recommend having a higher portfolio exposure in the name as the respective iBoxx index. We expect that the average total return of the instruments of the issuer is greater than the total return of the index.

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Outright recommendations:
Hold: We recommend holding the respective instrument for investors who already have exposure. We expect that the total return of the instruments of the issuer is equal to the yield.
Buy: We recommend buying the respective instrument for investors who already have exposure. We expect that the total return of the instruments of the issuer is greater than the yield.
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