

## European Financial Stability Facility (EFSF)

### 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 May 9<sup>th</sup> 2010 and incorporated in Luxembourg under Luxembourgish law on June 7<sup>th</sup> 2010<sup>1</sup>. 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 activity<sup>2</sup>

Following the conclusion of all necessary national procedures, these amendments to the EFSF Framework came into force on 18<sup>th</sup> October 2011<sup>3</sup>.

#### ➤ 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
- 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.

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<sup>1</sup> See [http://www.consilium.europa.eu/uedocs/cms\\_Data/docs/pressdata/en/misc/114977.pdf](http://www.consilium.europa.eu/uedocs/cms_Data/docs/pressdata/en/misc/114977.pdf)

<sup>2</sup> See [http://www.consilium.europa.eu/uedocs/cms\\_data/docs/pressdata/en/ecofin/123979.pdf](http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/123979.pdf)

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



➤ A3 – How are EFSF issues backed?

EFSF issues are backed by guarantees given by the 17 euro area Member States for up to €780 billion in accordance with their share in the paid-up capital of the European Central Bank (see table below)

	New EFSF Guarantee Committments (€m)	New EFSF contribution key (%)	EFSF Amended Guarantee Committments* (€m)	EFSF amended contribution key* (%)
Austria	21,639	2.78	21,639	2.99
Belgium	27,032	3.47	27,032	3.72
Cyprus	1,526	0.20	1,526	0.21
Estonia	1,995	0.26	1,995	0.27
Finland	13,974	1.79	13,974	1.92
France	158,488	20.31	158,488	21.83
Germany	211,046	27.06	211,046	29.07
Greece	21,898	2.81	-	0.00
Ireland	12,378	1.59	-	0.00
Italy	139,268	17.86	139,268	19.18
Luxembourg	1,947	0.25	1,947	0.27
Malta	704	0.09	704	0.10
Netherlands	44,446	5.70	44,446	6.12
Portugal	19,507	2.50	-	0.00
Slovakia	7,728	0.99	7,728	1.06
Slovenia	3,664	0.47	3,664	0.51
Spain	92,544	11.87	92,544	12.75
<b>Total</b>	<b>779,783</b>	<b>100</b>	<b>726,000</b>	<b>100</b>

As of 18 October 2011

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

➤ A4 - Where is the EFSF headquartered?

The EFSF is located at 43 Avenue John F. Kennedy, L-1855 Luxembourg.

➤ A5 – How big is the EFSF?

The EFSF is a very lean organisation. It has staff of around 20 people. The lean structure is possible because the German DMO (front and back office) and the European Investment Bank provide support to the EFSF. Additionally, the European Commission ensures consistency between EFSF operations and other assistance to euro area Member States.

➤ 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 stand alone solution to support euro area countries?

The European Financial Stability Facility is part of a wider safety net to preserve financial stability within Europe. The means of the EFSF are combined with loans of up to € 60 billion coming from the European Financial Stabilisation Mechanism (EFSM), i.e. funds raised by the European Commission and guaranteed by the EU budget, and up to € 250 billion from the International Monetary Fund for a financial safety net up to € 750 billion.

➤ A10 - 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.

➤ A11 - Are EFSF bonds eligible for ECB repo facilities?

EFSF debt instruments are eligible as collateral in European Central Bank refinancing operations<sup>4</sup>.

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.

➤ A12 - What rating does the EFSF have?

All three major credit rating agencies assigned the best possible credit rating – Standard & Poor’s “AAA”; Moody’s “Aaa”; Fitch Ratings “AAA” - to the EFSF<sup>5</sup>. On 5 December Standard & Poor’s placed EFSF’s ‘AAA’ long-term credit rating on CreditWatch negative.

EFSF has also been assigned the highest possible short term rating from the credit rating agencies – Standard and Poor’s “A-1+”; Moody’s (P) P-1 and Fitch Ratings “F1+”.

All of EFSF’s issues have been assigned the highest credit rating by all credit rating agencies.

➤ A13 - How would a downgrade of a member country affect EFSF?

There is a credit enhancement structure used under the Framework Agreement which constitutes the EFSF. Therefore a downgrade of a member country would not necessarily lead to a downgrade of EFSF securities.

➤ A14 - 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)

<sup>4</sup> 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](https://mfi-assets.ecb.int/query_EA.htm)

<sup>5</sup> See [http://www.efsf.europa.eu/investor\\_relations/rating/index.htm](http://www.efsf.europa.eu/investor_relations/rating/index.htm)

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

➤ [A15 - Will the EFSF bail out banks?](#)

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.

➤ [A16 – 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

➤ [A17 – Do the guarantees vary between series of bonds?](#)

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

➤ [A18 - Can countries step down from a guarantee already made?](#)

No – guarantees are “irrevocable and unconditional”

➤ [A19 - Will EFSF be a permanent institution?](#)

The EFSF has been created as a temporary institution. In accordance with its Articles of Association, the EFSF will be liquidated on the earliest date after 30 June 2013 on which there are no longer loans outstanding to a euro-area Member State and all Funding Instruments issued by EFSF and any reimbursement amounts due to Guarantors have been repaid in full.

This means that after June 2013, EFSF would not enter into any new programmes but will continue the management and repayment of any outstanding debt and will close down once all outstanding debt has been repaid.

On 24 June 2011, EU Heads of State and Government confirmed to establish a new permanent crisis mechanism, the European Stability Mechanism (ESM) (see Section G).

## Section B – Funding

### ➤ B1 - Does the EFSF do its own funding?

Issues may be made via syndications (such as the first three issues) but may also be made by auctions, private placements, new lines and tap issues.

Up until now, the German Debt Management Office (Bundesrepublik Deutschland – Finanzagentur GmbH) has acted as Issuance Agent and has been responsible for the placement. However, EFSF is the issuer. The funding strategy should be described as SSA (Sovereign, Supranational, Agency) type through benchmark issuance, with focus on a high standard of liquidity.

The issuance calendar including the most suitable funding instruments will be defined with the country on a case-by-case basis.

Due to the change of the guarantors and guarantee amounts following the amendments of the EFSF Framework Agreement, it is no longer possible to tap the three issues placed (25 January, 15 and 22 June) before the amendments entered into force

### ➤ B2 – What is the EFSF's funding strategy?

Up until now, the funding instruments have had in general the same profile as the related loans to the country in difficulty.

However as the new tasks assigned to the EFSF will lead to a broadening of its funding volumes, this will naturally have consequences on the funding strategy which will become more flexible and more diversified. This also means that EFSF will implement a short term funding strategy which could be structured around a Bill programme.

### ➤ B3 – Which banks have been appointed as lead managers?

The lead managers are mandated from the 47 international institutions that make up the EFSF Market Group<sup>6</sup>. The lead managers are chosen following a rigorous and transparent selection process.

Banks mandated as joint lead managers for each issue are as follows:

EFSF's inaugural issue on 25 January 2011 for Ireland: Citi, HSBC and Société Générale.  
EFSF's first issue for Portugal on 15 June 2011: Barclays Capital, Deutsche Bank and HSBC.  
EFSF's second issue for Portugal on 22 June 2011: BNP Paribas, Goldman Sachs International and Royal Bank of Scotland.  
EFSF's second issue for Ireland on 7 November 2011: Barclays, Crédit Agricole CIB and JP Morgan.

### ➤ B4– 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](http://www.efsf.europa.eu/investor_relations/issues/index.htm) ).

### ➤ B5 - Can EFSF and EFSM<sup>7</sup> be in the market at the same time?

<sup>6</sup> See [http://www.efsf.europa.eu/attachments/efsf\\_market\\_group\\_en.pdf](http://www.efsf.europa.eu/attachments/efsf_market_group_en.pdf)

<sup>7</sup> See [http://ec.europa.eu/economy\\_finance/eu\\_borrower/efsm/index\\_en.htm](http://ec.europa.eu/economy_finance/eu_borrower/efsm/index_en.htm)

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.

➤ B6 – Does EFSF issue in euro 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.

➤ 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

➤ B8 - Can EFSF pre-fund?

EFSF is able to pre-fund but there is a consensus by finance ministers not to access markets for a specific country programme until a euro member has submitted a request for support.

## **Section C – questions related to lending within a macro-economic adjustment programme**

➤ C1 - What triggers an EFSF lending programme?

The Facility can only act after a support request is made by a euro area Member State and a country programme has been negotiated with the European Commission and the IMF and after such a programme has been accepted by the euro area finance ministers and a Memorandum of Understanding (MoU) is signed. This would only occur when the country is unable to borrow on markets at acceptable rates.

➤ C2 - How fast can the EFSF provide financial support?

Following a request from a euro area Member State for financial assistance, it takes three to four weeks to draw up a support programme including sending experts from the Commission, the IMF and the ECB to the country in difficulty. Once euro area finance ministers have approved the country programme, the EFSF would need several working days to raise the necessary funds and disburse the loan.

➤ C3 - Is EFSF's support linked to conditions?

Yes, any financial assistance to a country in need 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. 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.

➤ C4 - 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.

➤ C5 – What is EFSF's lending capacity?

Following the increase of guarantee commitments to €780 billion, EFSF's effective lending capacity is intended to be €440 billion. This is explained by the credit enhancement structure which includes an overguarantee of up to 165% in order to ensure EFSF's triple A credit rating.

➤ C6 - 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.

➤ C7 – How will 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.

➤ C8 - What is the interest rate of EFSF loans?

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

➤ C9 - 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.

➤ C10 - 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 facility<sup>8</sup>; for countries outside the EU there is the Macro-Financial Assistance programme<sup>9</sup>. Furthermore, the EFSM could support all European Union Member States.

## Section D – New instruments for EFSF

### Bank recapitalisations<sup>10</sup>

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

The objective is to limit contagion of financial stress by ensuring capacity of a government (typically those with “small country, large financial sector problem”) to finance recapitalisation of financial institution(s) at sustainable borrowing costs.

➤ D2 - Which countries could 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 - Will EFSF make loans directly to financial institutions?

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<sup>8</sup> See [http://ec.europa.eu/economy\\_finance/financial\\_operations/balance/index\\_en.htm](http://ec.europa.eu/economy_finance/financial_operations/balance/index_en.htm).

<sup>9</sup> See [http://ec.europa.eu/economy\\_finance/financial\\_operations/market/third\\_countries/index\\_en.htm](http://ec.europa.eu/economy_finance/financial_operations/market/third_countries/index_en.htm).

<sup>10</sup> See EFSF Guideline on Recapitalisation of Financial Institutions

[http://www.efsf.europa.eu/attachments/efsf\\_guideline\\_on\\_recapitalisation\\_of\\_financial\\_institutions.pdf](http://www.efsf.europa.eu/attachments/efsf_guideline_on_recapitalisation_of_financial_institutions.pdf)

No, EFSF will only loan 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.

➤ D6 – What will be the request procedure?

The request for and control of this instrument needs to be 'lighter' than in the case of a regular macro-economic adjustment programme in order to increase the speed of funding as well as to reflect the sectorial nature of the loan. The request must be made by the government of the Member State to the chairman of the Eurogroup. This will be followed by an independent assessment provided by the Commission in liaison with the ECB, and where appropriate with the relevant European supervisory authority (EBA, ESMA, EIOPA).

### **Precautionary Programmes<sup>11</sup>**

➤ D7 –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).

➤ D8 –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 fixed amount of credit protection equal to a percentage of the principal amount of the sovereign bond. Access to the ECCL+ corresponds, as a

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<sup>11</sup> See EFSF Guideline on Precautionary programmes  
[http://www.efsf.europa.eu/attachments/efsf\\_guideline\\_on\\_precautionary\\_programmes.pdf](http://www.efsf.europa.eu/attachments/efsf_guideline_on_precautionary_programmes.pdf)

basis, to the same criteria and conditionality as that of the ECCL, while reflecting the specific circumstances requiring the issuance of a PPC.

➤ D9 –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 intervention<sup>12</sup>**

➤ D10 - 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.

➤ D11 – 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.

➤ D12 –Would conditionality be attached?

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

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

**Secondary market intervention<sup>13</sup>**

➤ 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

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<sup>12</sup> See EFSF Guideline on Primary Market Purchases  
[http://www.efsf.europa.eu/attachments/efsf\\_guideline\\_on\\_primary\\_market\\_purchases.pdf](http://www.efsf.europa.eu/attachments/efsf_guideline_on_primary_market_purchases.pdf)

<sup>13</sup> See EFSF Guideline on interventions in the secondary market  
[http://www.efsf.europa.eu/attachments/efsf\\_guideline\\_on\\_interventions\\_in\\_the\\_secondary\\_market.pdf](http://www.efsf.europa.eu/attachments/efsf_guideline_on_interventions_in_the_secondary_market.pdf)

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 a country need to submit a request?

Yes.

➤ D22 – Would a Memorandum of Understanding be required?

Yes.

➤ 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.



## Maximising the EFSF's lending capacity<sup>14</sup>

### ➤ E1 – Why is there a need to leverage?

Over recent months the sovereign debt markets of some Member States have been 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 give the holder the right to claim his entitlement against this loss in EFSF bonds and cash under the condition that the certificate holder also holds an underlying bond of the defaulted Member State.
- 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 will EFSF leverage?

- The degree of leverage will depend 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 will be developed so as to be attractive to the international investor community. They should cover different investor needs to unfold the maximum impact. We firmly believe that the two approaches chosen provide a robust strategy which will allow attracting these investors.
- The EFSF will have the flexibility to use these two options simultaneously to increase the robustness of the financing strategy.

### ➤ E4 – When will the leveraging be operational?

<sup>14</sup> Please see Terms of Reference Maximising the capacity of EFSF [http://www.efsf.europa.eu/attachments/efsf\\_terms\\_of\\_reference\\_maximising\\_the\\_capacity.pdf](http://www.efsf.europa.eu/attachments/efsf_terms_of_reference_maximising_the_capacity.pdf)

On 29 November, the euro area Finance Ministers agreed on the terms and conditions to extend EFSF's capacity through the introduction of the partial risk participation and co-investment approach.

EFSF will now implement these two approaches to be ready early in 2012 to use them effectively in the context of the guidelines for the EFSF instruments.

➤ E5 – 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 can now set up all practical arrangements. Among others it is broadening its funding strategy and is setting up the necessary infrastructure.

➤ E6 – 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.

➤ E7 – 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.

➤ E8 – Would these options have an impact on EFSF's triple A credit rating?

The current basis of EFSF's AAA rating is that no value is assigned by the agencies to the underlying assets and that the AAA rating rests on the guarantees provided by the AAA Member States.

➤ E9 - 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.

➤ E10 - Will these options be focused just on Italy and Spain?

The options are designed to give the EFSF maximum flexibility to deploy mechanisms which can be most effective in the circumstances of any particular situation or country.

### **Option 1 – Credit enhancement**

➤ E11 - 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.

➤ E12 - 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

➤ E13 - 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 his entitlement against this loss in EFSF bonds under the condition that the certificate holder also holds an underlying bond of the defaulted Member State.

➤ E14 - 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.

➤ E15 - Will the certificate cover more than one country?

No.

➤ E16 - 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 with a AAA rating.

➤ E17 - Who are the likely users of the scheme?

Institutional investors willing to detain European Sovereign with credit enhancement.

➤ E18 - 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.

➤ E19 - 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.

➤ E20 - 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.

➤ E21 – Has EFSF had direct conversations with investors and what were their reactions?

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

## Option 2 – Co-Investment Fund (CIF)

### ➤ E22 – 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.

### ➤ E23 - What will be the investment policy of a vehicle?

Each vehicle will have a clearly stated investment mandate.

### ➤ E24 - 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.

### ➤ E25 – 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.

### ➤ E26 - 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.

### ➤ E27 - 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.

### ➤ E28 - Can investors from outside the euro area participate?

Yes

➤ E29 - 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.

➤ E30 - 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

➤ E31 - 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.

➤ E32 - What is the expected size of the CIF portfolio?

This will depend on market circumstances and investor demand.

➤ E33 - 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.

➤ E34 - 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.

➤ E35 - 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.

➤ E36 - 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

### ➤ F1 – How much is the programme for Ireland?

On 28 November 2010, the ECOFIN Ministers concurred with the European Commission and the ECB that providing a loan to Ireland was warranted to safeguard the financial stability in the euro area and the EU as a whole. The total lending programme for Ireland is €85 billion.

### ➤ F2 – How will the programme be financed?

The programme for Ireland will be financed as follows:

- €17.5 billion contribution from Ireland (from the Treasury and the National Pension Fund Reserve)
- €67.5 billion in external support including
  - €22.5 billion from IMF
  - €22.5 billion from EFSM
  - €17.7 billion from EFSF + bilateral loans from the UK (€3.8 billion), Denmark (€0.4 billion) and Sweden (€0.6 billion)

### ➤ F3 – What are the conditions of the programme?

The programme rests on three pillars:

- An immediate strengthening and comprehensive overhaul of the banking system (€35 billion designated)
- An ambitious fiscal adjustment to restore fiscal sustainability, including through the correction of the excessive deficit by 2015
- Growth enhancing reforms, in particular on the labour market, to allow a return to a robust and sustainable growth, safeguarding the economic and social position of its citizens

### ➤ F4 – What is the issuance calendar for Ireland?

In 2011, subject to revision due to Ireland's requirements and to quarterly reviews by the Commission in cooperation with the IMF and in liaison with the ECB, EFSF intends to issue up to €8 billion. The first tranche was a €5 billion bond issued on 25 January 2011. Out of the €5 billion issued, €3.6 billion was disbursed to Ireland. A second issue for €3 billion was placed on 7 November 2011.<sup>15</sup>

Initial focus is on issuing benchmark size and building a liquidity curve. However, EFSF may complement its funding needs by smaller bond issues, either through taps or through targeted transactions.

In 2012/2013, and again subject to revision, EFSF intends to issue up to almost €11 billion in support of Ireland.

### ➤ F5 – What are the details of the first issue made for Ireland?

The first issue made by EFSF in support of the Irish programme was placed on 25 January 2011. Details are as follows:

Amount issued	€5 billion
Maturity	18/07/2016

<sup>15</sup>The issuance calendar has been revised from the amounts initially announced in Dec 2010  
<http://www.efsf.europa.eu/mediacentre/news/2010/2010-006-eu-and-efsf-funding-plans-to-provide-financial-assistance-for-ireland.htm>

Issuance spread	Mid swap + 6bp
Coupon	2.75%
Reoffer yield	2.89%
Reoffer price	99.302%
Settlement date	1 February 2011
Effective lending cost to Ireland	5.9%
Amount transferred to Ireland	€3.6 billion

Investor interest was exceptionally strong with an order book almost 9 times oversubscribed from more than 500 investors. Investor interest was diversified both in geographical terms and by client type. Particularly strong interest came from Asia which represented around 38% of the issue.

➤ **F6 – What are the details of the second issue made for Ireland?**

The second issue made by EFSF in support of the Irish programme was placed on 7 November 2011. Details are as follows:

➤ Amount issued	€3 billion
➤ Maturity	04/02/2022
➤ Issuance spread	Mid swap + 104bp
➤ Coupon	3.50%
➤ Reoffer yield	3.591%
➤ Reoffer price	99.216%
➤ Settlement date	14 November 2011
➤ Amount transferred to Ireland	€3 billion

## 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 has 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.

After 2011, and again subject to revision, EFSF is expected to issue up to €20 billion to complete its issuance programme for Portugal.

➤ 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

## Section H – Financial support for Greece

➤ H1 – Will there be a second programme for Greece?

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.

➤ H2 – How much is the new Greek programme?

The official sector stands ready to provide additional programme financing of up to €100 billion until 2014. The contribution from private sector involvement will be added to this amount.

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

Euro area Member States are willing to contribute to the PSI package up to €30 billion. For the private sector, the nominal discount is expected to be around 50% on notional Greek debt although discussions are ongoing. The bond exchange is voluntary and the exchange of bonds should be implemented at the beginning on 2012.

➤ **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.

**Section I – European Stability Mechanism<sup>16</sup>**

➤ **I1 – What is the European Stability Mechanism (ESM)?**

On 24 June 2011, the European Council decided to establish a permanent crisis resolution mechanism – the European Stability Mechanism (ESM).

The function of the ESM will perform the same activities as the amended EFSSF:

- 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
- 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.

The ESM will use an appropriate funding strategy so as to ensure access to broad funding sources and enable it to extend financial assistance packages to Member States under all market conditions.

➤ **I2 - What will be the legal form of the ESM**

The ESM will be established as an intergovernmental organisation under public international law.

➤ **I3 – Where will the ESM be headquartered?**

The ESM's office will be in Luxembourg

➤ **I4 – Who will govern the ESM?**

The ESM will have a Board of Governors consisting of the Ministers of Finance of the euro area Member States (as voting members) with the European Commissioner for Economic and Monetary Affairs and the ECB President as observers.

The ESM will also have a Board of Directors. Each euro area country will appoint one Director and one alternate Director.

The Board of Governors will appoint a Managing Director responsible for the day-to-day management of the ESM. The Managing Director will chair the Board of Directors.

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<sup>16</sup> For further details, please consult the European Council Conclusions of 25 March 2011

[http://www.consilium.europa.eu/uedocs/cms\\_data/docs/pressdata/en/ec/120296.pdf](http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ec/120296.pdf)

9 December 2011

➤ I5 – When will the ESM become operational?

The ESM treaty will enter into force as soon as Member States representing 90% of the capital commitments have ratified it. The common objective is for the ESM to enter into force in July 2012.

The CEO of the EFSF has been tasked with the practical preparation of setting up the ESM. He will make regular progress reports to the Euro Working Group

➤ I6 – What will happen after EFSF is due to expire in mid 2013?

EFSF will remain operational in a purely administrative function until it has received full payment of the financing granted to Member States and it has repaid its liabilities.

➤ I7 – How will the ESM's capital be structured?

The ESM will have a total subscribed capital of € 700 billion. Of this amount, € 80 billion will be in the form of paid-in capital provided by the euro area Member States being phased in from July 2013 in five equal instalments. In addition, the ESM will also dispose of a combination of committed callable capital from euro area Member States to a total amount of € 620 billion. During the transitory phase from 2013 to 2017, Member States commit to accelerate, in the unlikely event that this is needed, the provision of appropriate instruments in order to maintain a minimum 15 percent ratio between paid-in capital and the outstanding amount of ESM issuances.

➤ I8 - What will be the ESM's shareholder contribution key?

The ESM shareholder contribution key will be based on the ECB contribution key. Member States with a GDP per capita of less than 75% of the EU average will benefit from a temporary correction for a period of 12 years after their entry in the euro area.

The temporary correction will be three quarters of the difference between GNI and ECB capital shares. The downwards compensation on those countries is redistributed among all the other countries according to their ECB key shares:

Country	ESM Key (%)
Austria	2.783
Belgium	3.477
Cyprus	0.196
Estonia	0.186
Finland	1.797
France	20.386
Germany	27.146
Greece	2.817
Ireland	1.592
Italy	17.914
Luxembourg	0.250
Malta	0.073
Netherlands	5.717
Portugal	2.509
Slovakia	0.824
Slovenia	0.428
Spain	11.904
<b>Total</b>	<b>100</b>

➤ I9 - Will the ESM require specific credit enhancements?

The ESM will aim to obtain and maintain the highest credit rating from the major credit rating agencies.

The ESM will have a capital structure similar to multilateral lending institutions. It can be expected that this will be reflected in the assessment by credit rating agencies in line with their general standards for subscribed capital and operating procedures of such institutions.

Unlike the EFSF, ESM's structure will comprise paid-in capital, callable capital and guarantees. This therefore means that the ESM would not require the credit enhancements (over-guarantee, cash buffer and cash reserve) that the EFSF requires in order to secure a AAA rating.

➤ I10 - What will be the ESM's lending capacity?

The ESM's effective lending capacity will be €500 billion. However at the EU summit held on 9 December 2011, EU Heads of Government and State agreed to reassess the adequacy of the overall ceiling of the EFSF/ESM of €500 billion in March 2012

➤ I11 – Will the private sector be involved when the ESM is activated?

ESM's rules will provide for a case by case participation of private sector creditors, consistent with IMF policies. In order to facilitate this process, standardized and identical collective action clauses (CACs) will be included in the terms and conditions of all new euro area government bonds starting in June 2013.

➤ I12 – Will the IMF be involved in the ESM?

The ESM will cooperate very closely with the IMF in providing financial assistance. In all circumstances, active participation of the IMF will be sought on a technical and financial level. The debt sustainability analysis will be jointly conducted by the Commission and the IMF, in liaison with the ECB. The policy conditions attached to a joint ESM/IMF assistance will be negotiated jointly by the Commission and the IMF, in liaison with the ECB.

➤ I13 – Will ESM loans have creditor status?

ESM will claim preferred credit status (except for countries under a European financial assistance programme in June 2011).

➤ I14 – Can non euro area Member States participate in ESM programmes?

Non euro area Member States may participate on an ad hoc basis alongside the ESM in financial assistance operations for euro area Member States.

➤ I15 – What is the procedure for activating ESM assistance?

Financial assistance from the ESM will in all cases be activated on a request from a Member State to the other euro area Member States.

If ESM Stability Support (ESS) is requested, the Commission together with the IMF and in liaison with the ECB will assess the actual financing needs of the Member State and the nature of the required private sector involvement.

Based on this assessment, the Commission will negotiate, together with the IMF and in liaison with the ECB, a macro-economic adjustment programme with the Member State, detailed in a Memorandum of Understanding (MoU)

Following endorsement of the macro-economic adjustment programme by the Council, the Commission will sign the MoU on behalf of the EAMS.

ESM's Board of Directors will then approve the financial assistance agreement containing the technical aspects of the assistance.

The Commission, together with the IMF and in liaison with the ECB, will be responsible for monitoring compliance with the policy conditionality.

## 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
<b>Total</b>	<b>440,000</b>	<b>100</b>

#### ➤ 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.