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The European Financial Stability Facility (EFSF) and the European Stability Mechanism (ESM)

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No bail-out clause

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Article 125 of the Treaty on the Functioning of the European Union

1. ***The Union shall not be liable for or assume the commitments of central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of any Member State, without prejudice to mutual financial guarantees for the joint execution of a specific project. A Member State shall not be liable for or assume the commitments of central governments, regional, local or other public authorities, other bodies governed by public law, or public undertakings of another Member State, without prejudice to mutual financial guarantees for the joint execution of a specific project. /…/.***

Bilateral loans package for Greece. May 2010

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In the context of a three year joint programme with the IMF, the financial package makes available € 110 billion to help Greece meet its financing needs, with euro area Member States ready to contribute for their part € 80 billion, of which up to € 30 billion in the first year. The first disbursements will be made available before the payment obligations of the Greek government fall due on 19 May.

EFSM

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The European Financial Stabilisation Mechanism (EFSM) is a European Union instrument. It has a volume of EUR 60 billion (May 2010).

The European Commission administers it: it raises funds in the markets guaranteed by the EU budget.

The EFSM is similar to the balance of payments assistance facility set to help the non-euro area Member States (Latvia, Hungary and Romania have benefited from it).

EFSF

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The European Financial Stability Facility (EFSF) is intergovernmental. It is incorporated in Luxembourg under Luxembourg law (June 2010).

The EFSF provides loans and - with the support of the German DMO – issues bonds or other debt instruments on the markets to raise the funds needed for the loans.

Issues are backed by guarantees by euro area Member States of up to EUR 440 billion.

Thus, total current volume of the EU safety net is EUR 750 billion: EUR 60 billion (EFSM) plus EUR 440 billion (EFSF) plus up to EUR 250 billion from the IMF.

Ireland. December 2010

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The Union's assistance to Ireland would reach up to EUR 22,5 billion under the EFSM (EFSM). Further, contributions from the EFSF (EUR 17,7 billion), and bilateral lending from the United Kingdom, Sweden, and Denmark (EUR 4,8 billion in total). In addition, Ireland has requested a loan from the IMF of 19,5 billion Special Drawing Rights (equivalent to around EUR 22,5 billion).

Portugal. May 2011

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The financial package of the programme will cover financing needs up to € 78 billion, which should be shared equally (€ 26 billion each) amongst: (i) the European Financial Stabilisation Mechanism (EFSM), (ii) the European Financial Stability Facility (EFSF), and (iii) the IMF. <u>At the same time, the Portuguese authorities will undertake to encourage private investors to maintain their overall exposures on a voluntary basis.</u>

Treaty change: new Article 136(3) of the Treaty on the Functioning of the European Union

'3. The Member States whose currency is the euro may establish a stability mechanism to be activated if indispensable to safeguard the stability of the euro area as a whole. The granting of any required financial assistance under the mechanism will be made subject to strict conditionality.'.

ESM

The ESM is intergovernmental. It will be an international organisation established by means of an international Treaty.

It will replace the EFSM and the EFSF. It will have an overall effective lending capacity of 500 billion euros.

The ESM effective lending capacity will be ensured by establishing the appropriate mix between paid-in capital, callable capital and guarantees. Until the entry into force of the ESM, the agreed lending capacity of 440 billions euros of the EFSF will be made fully effective.

Any operation will be taken by unanimity on the basis of a debt sustainability analysis of the Member State concerned conducted by the Commission and the IMF, in liaison with the ECB.

Financial assistance from the ESM and EFSF will take the form of loans. However, the ESM and the EFSF may also, as an exception, intervene in the debt primary market in the context of a programme with strict conditionality.

Calendar: new EFSF agreement in June 2011; ESM operational in June 2013.

Open questions

The European Council Conclusions of March 2011 annexed the General Futures of the ESM agreed upon by the Eurogroup in November 2010 which provide, among others, for the following:

a) ***a case by case participation of private sector creditors, fully consistent with IMF policies. In all cases, in order to protect taxpayers' money, and to send a clear signal to private creditors that their claims are subordinated to those of the official sector, an ESM loan will enjoy preferred creditor status, junior only to the IMF loan;***

b) ***for countries considered solvent (debt sustainability analysis) the private sector creditors would be encouraged to maintain their exposure according to international rules and fully in line with the IMF practices. In the unexpected event that a country would appear to be insolvent , the Member State has to negotiate a comprehensive restructuring plan with its private sector creditors, in line with IMF practices with a view to restoring debt sustainability. If debt sustainability can be reached through these measures, the ESM may provide liquidity assistance;***

Open questions

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c) *collective action clauses (CACs) will be included, in such a way as to preserve market liquidity, in the terms and conditions of all new euro area government bonds starting in June 2013 (CACs would be consistent with those common under UK and US law after the G10 report on CACs, including aggregation clauses);*

d) *we restate that any private sector involvement based on these terms and conditions would not be effective before mid-2013.*