European Stability Mechanism

FAQ on ESM/EFSF financial assistance for Greece

I - Greece's financial assistance from the ESM

1. What is the total amount of loans that Greece will receive under the new ESM programme?

Greece may receive up to €86 billion in loans under the new ESM programme. This amount will be disbursed in tranches over three years. This overall amount was determined in an assessment of Greece's financing needs, conducted by the European Commission, the European Central Bank (ECB) and the International Monetary Fund (IMF), and agreed by the euro area Member States.

The IMF is also expected to contribute to this financing plan with its own programme, which should subsequently reduce the €86 billion in ESM financing.

The actual disbursed amounts will also depend on Greece's effective implementation of an extensive package of policy reforms. Successful implementation is expected to ensure that Greece returns to market financing at reasonable cost before the programme ends. This was the case with previous financial assistance programmes, including for Greece. Privatisation proceeds may also reduce the overall sum.

2. How will these funds be used?

The funds will be used mainly for debt service and banking sector recapitalisation; a small amount will be available for arrears clearance and/or budget financing. The funds will thus ensure financial stability in Greece, providing liquidity and stimulating the economy. They will give Greece time to complete its reform agenda within the euro area, modernise its administration, and deliver growth and jobs.

3. How much will the first tranche of the programme be?

The first tranche of the ESM programme will be €26 billion. This includes an up-front €10 billion buffer (cashless, to be disbursed in ESM notes) to repair the Greek banking system as requested by the July euro area summit. These notes will not be transferred to Greece, instead they will go into a segregated account managed by the ESM in Luxembourg. They can be disbursed following a request by Greece. Depending on some criteria, this request has to be confirmed either by the Single Supervisory Mechanism, the Single Resolution Board or the Bank of Greece. Approval by the ESM Board of Directors is also required, once certain requirements (e.g. performing stress tests of banks, compliance with state-aid rules) are met.

This first tranche will also include €16 billion to cover the repayment of the €7.2 billion bridge loan granted in July from the European Financial Stabilisation Mechanism (EFSM), the upcoming ECB and IMF payments, and some arrears. This part of the tranche will be released in separate payments: the

first €13 billion immediately upon programme approval, with the other €3 billion to be disbursed no later than 30 November 2015, if Greece completes additional prior actions.

4. How will the ESM fund the programme?

The ESM will fund the programme through the issuance of notes (bills and bonds) in a broad range of maturities, aiming to raise the funds smoothly in the market via the ESM's wide investor base, and taking into consideration market conditions and investor needs.

5. What does the ESM programme for Greece mean for the ESM and EFSF funding programmes?

Due to the new programme, the ESM funding programme for the remainder of the year 2015 is expected to be €18 billion.

The EFSF funding programme of €12.5 billion for 2015 has now been completed. No further funding is expected from the EFSF for the remainder of this year.

6. What will the average maturity of the ESM loan tranches be?

The maximum weighted average maturity of the loan tranches will be 32.5 years, in line with the existing European Financial Stability Facility (EFSF) loan to Greece.

7. Will there be an interest rate deferral and a grace period for principal repayment?

Greece will start paying interest from the start of the programme. The start of the principal repayment will be defined for each disbursement of an ESM loan tranche. Greece is expected to begin repaying its principal about 15 years after the programme ends.

8. What will the interest rate be?

There is no fixed interest rate. The ESM charges its own funding cost in the markets to programme countries, plus a very small margin and service fee to cover operational costs. The ESM's funding cost is very low, reflecting its high-quality ratings (Fitch: AAA, Moody's: Aa1). Currently, the ESM charges around 1% on average, but this rate can change, depending on market conditions.

9. What policy conditions did the Greek government agree to implement?

The Memorandum of Understanding (MoU) contains a reform agenda, which was designed to provide the basis for a sustainable Greek economic recovery. The reforms are built around four pillars:

- Restoring fiscal sustainability: achieve a medium-term primary surplus of 3.5% of gross domestic product (GDP) by 2017 through measures such as VAT and pension reform, strengthen tax compliance and public financial management;
- Safeguarding financial stability: reduce non-performing loans; complete bank recapitalisation by the end of 2015;
- Enhancing growth, competitiveness and investment: introduce labour and product market reforms;
- Developing a modern state and public administration: improve public sector efficiency; reform the judicial system; intensify the fight against corruption; strengthen the institutional and operational independence of key institutions, such as the revenue administration and statistics office (ELSTAT).

10. A privatisation fund is to be set up – how will it operate?

The privatisation fund will be established in Greece and be managed by the Greek authorities under the supervision of the relevant European institutions. The fund will monetise Greek assets through privatisations; a total amount of €50 billion is targeted.

The funds from the asset sales will be used to make loan repayments to the ESM (including loans for bank recapitalisation), to decrease Greece's debt-to-GDP ratio, and for investments. The fund is expected to be operational by year-end. The legislation to establish the fund shall be adopted in agreement with the European institutions.

11. Will quarterly reviews of the programme be carried out, as in the past?

Yes, representatives of the institutions (European Commission, ECB, IMF and the ESM) will conduct quarterly reviews of the progress made in implementing the agreed MoU policy measures. The disbursement of successive loan tranches will depend on the positive outcome of these reviews.

12. Is Greek debt sustainable?

Debt sustainability was assessed by the European Commission, in liaison with the ECB and with input from the ESM. While the analysis expressed serious concerns about the current situation, it concluded that debt sustainability could be achieved through a far-reaching and credible reform programme and additional debt relief, excluding nominal haircuts.

The analysis also noted that Greece already benefits from very low debt servicing in the coming years due to low interest rates, interest deferral, and a long grace period on both EFSF loans and the bilateral loans that euro area countries provided to Greece, i.e. the Greek Loan Facility (GLF) loans.

13. How will the IMF participate in the financial assistance programme?

The IMF announced in a statement[1] that it would remain closely engaged with the Greek government and the European partners. The IMF actively participated in the negotiations and made a positive assessment of the policy conditionality contained in the MoU. It will continue to be involved in the quarterly programme reviews.

The Eurogroup welcomed the IMF management's intention to recommend to the IMF Executive Board that it consider further financial support for Greece. According to its statement, the IMF will make an assessment of its participation in the additional financing to Greece "once the steps on the authorities' program and debt relief have been taken".

14. Will there be any debt relief measures for Greece?

In principle, and in line with the Euro Summit's 12 July statement, the Eurogroup stands ready to consider necessary, additional measures aimed at ensuring that Greece's gross financing needs remain sustainable. Debt relief for Greece – such as longer grace and repayment periods – will be considered after the first programme review.

15. When did Greece request this third programme?

The Greek Minister of Finance Euclid Tsakalotos presented a request for 'stability support', the term the ESM Treaty uses for financial assistance, to the Chairperson of the ESM Board of Governors[2] on

[1] http://www.imf.org/external/np/sec/pr/2015/pr15377.htm.

[2] The ESM Board of Governors is composed of the finance ministers of every ESM Member. Jeroen Dijsselbloem, President of the Eurogroup, chairs this board.

8 July 2015. In the request, Greece said it was seeking a loan facility for a three-year period, to meet Greece's debt obligations and to ensure the stability of the financial system.

16. Was Greece eligible for a third programme?

Yes, on 10 July 2015, the European Commission published an assessment, prepared in liaison with the ECB, and with input from the IMF, concerning Greece's request. It confirmed that Greece was eligible and recommended the start of negotiations. According to the assessment, the provision of stability support to Greece was critical to restore the confidence of depositors and markets in Greek banks and safeguard the country's financial stability, as well as to avoid risks for other EU Member States and the euro area as a whole.

17. Were there additional policy conditions for Greece to start negotiating a new programme?

Yes. There was a need to reinforce trust between Greece and the European partners, after doubts had mounted as to whether Greece was committed to the reforms needed to remain in the euro area.

At the Euro Summit of 13 July 2015, Greece agreed to implement additional measures to be able to start negotiations: two sets of prior actions including VAT and pension reform, transposition of the Bank Resolution and Recovery Directive, safeguarding the independence of ELSTAT, and adoption of the Code of Civil procedure. A number of additional reform measures were required to reach agreement on the MoU.

The euro area leaders also said that Greece was expected to address a request for financial assistance to the IMF as a precondition for a new ESM programme, which Greece did on 24 July 2015.[3]

Greece generally met all these conditions and later completed a new set of prior actions before the first disbursement of the programme.

18. Did Member States agree to this third programme?

Yes, there is a strong democratic process that needs to be followed for any ESM programme. Under standard procedures, granting ESM financial assistance requires its Members' unanimous agreement. Some Members also require parliamentary approval.

The Eurogroup agreed to start negotiations on 16 July 2015,[4] and the ESM Board of Governors decided to grant, in principle, stability support to Greece on 17 July 2015.[5] This decision paved the way for negotiations on the MoU and was followed by the completion of national procedures. On August 14, the Eurogroup reached a political agreement on the MoU and the proposal for a new financial assistance facility agreement (FFA) for Greece. Following the completion of national procedures, the ESM Board of Governors and the ESM Board of Directors approved the programme on 19 August 2015.

19. This is the third financial assistance programme for Greece. What were the previous two and how much money did Greece receive?

[3] The full Euro Summit statement is available here.
[4] The Eurogroup statement is available here.
[5] ESM press release available here.

The first financial assistance package for Greece was agreed in 2010. It consisted of the bilateral Greek Loan Facility (GLF). Under the GLF, €52.9 billion was disbursed. There were also loans from the IMF worth €22 billion. The EFSF provided the second programme (€141.8 billion disbursed, outstanding loan amount €130.9 billion) and there was a second IMF programme under which it disbursed €12.8 billion. From its two programmes, the IMF has a total €17 billion outstanding.

II - EFSF financial assistance programme for Greece – expired on 30 June 2015

1. How much did the EFSF disburse to Greece?

The EFSF did not exist when the first programme of bilateral loans by the euro area Member States for Greece, the GLF, was agreed in early 2010. The EFSF programme, part of the second Economic Adjustment Programme for Greece, started on 1 March 2012. The EFSF disbursed €130.9 billion, making it Greece's largest creditor by far. The GLF had a total volume of €52.9 billion. The International Monetary Fund (IMF) disbursed €34.8 billion.

2. When did the EFSF programme for Greece end?

Without an agreement to extend it, the EFSF programme expired on 30 June. Greece's euro area partners were prepared to extend the EFSF programme further, just as they had extended it twice in the past. Instead of ending on 31 December 2014, the EFSF Board of Directors' decision of 19 December 2014 extended the programme until 28 February 2015. On 27 February 2015, the EFSF Board of Directors extended the availability period of the EFSF loan contract with Greece, called the Greek Master Financial Assistance Facility Agreement (MFFA), by a further four months, until 30 June 2015.

3. What happens with EFSF loans now that Greece defaulted on the IMF?

For the EFSF, Greece officially defaulted on the IMF when the IMF Managing Director informed the IMF Board on 1 July 2015 that Greece had failed to meet a payment obligation. According to the EFSF loan contract (Master Financial Assistance Facility Agreement, MFFA) with Greece, such a default triggers the MFFA's cross-default clause.

In line with a recommendation by the EFSF CEO, Klaus Regling, the EFSF Board of Directors decided on 3 July 2015 to opt for a reservation of rights on EFSF loans to Greece. The other two possible options were to request immediate repayment of its loans or to waive the EFSF's right to action. By issuing a reservation, the EFSF keeps all its options open as a creditor as events in Greece evolve. The EFSF will continuously monitor the situation.

Greece cleared its arrears with the IMF and Bank of Greece when it received a loan from the European Financial Stabilisation Mechanism (EFSM). During the default period, Greece made all scheduled payments to the EFSF in a timely manner.

4. Wasn't it clear from the start that the EFSF strategy would not work in Greece?

The EFSF and ESM strategy of providing loans against macroeconomic reforms, called 'conditionality', worked successfully. Ireland, Spain, and Portugal reformed their economies and budgets, regained full market access at very favourable conditions, and started growing again. This shift had also begun in Greece. Current account and budget deficits declined strongly, signs of positive growth returned, and Greece became a top reformer, according to the Organisation for Economic Co-operation and Development and World Bank assessments. In response, the markets started to accept Greek debt issuance again in mid-2014. But these improvements were interrupted in late 2014, leading to a renewed recession and loss of market access. With the new ESM programme, Greece should return to the previous path of economic recovery.

5. What kind of progress did Greece make in the implementation of reforms?

After six years of recession, Greece's economy returned to growth in 2014. In recent years, Greece significantly improved its fiscal balance: the government deficit was reduced to -3.5% of gross domestic product (GDP) in 2014 from -12.3% in 2013. It recorded a positive primary balance (i.e. excluding interest payments on debt) of around 1% of GDP in 2014 which was expected to continue in coming years.

Greece made important progress on public finances and completed the recapitalisation of the four largest banks. It also made headway in correcting public expenditure, including downsizing the public administration. Labour cost competitiveness and the business environment improved. The government implemented several important structural reforms in health care, the opening of professions, and public financial management.

A major success for Greece was its return to the bond markets in 2014, when it issued 3-year and 5-year bonds. This was a sign that it had started to regain investor trust.

Background on financial assistance to Greece

6. What led to Greece's economic problems?

In the decade before the crisis, Greece failed to modernise its economy towards efficiency and productivity gains while the public sector grew at unsustainable levels. After Greece adopted the euro in 2001, it was able to borrow at much lower interest rates despite its deteriorating competitiveness and public finances.

While government spending and borrowing increased, tax revenues – the main source of government income – weakened due to poor tax administration. At the same time, rising wages undermined Greece's competitiveness compared to other euro area countries. Low productivity and structural problems also contributed to the increasing economic difficulties. As a result, Greece's economy contracted and unemployment began to climb to alarming levels.

Greece's reliance on external financing for funding budget and trade deficits left its economy very vulnerable to shifts in investor confidence. In 2009, the Greek government revealed that previous governments had been misreporting government budget data. Much higher-than-expected deficits eroded investor confidence, causing the yields on Greek sovereign bonds, which correspond to the cost of borrowing money, to rise to unsustainable levels. The situation worsened to the point where

the country was no longer able to refinance its borrowing, and it was forced to ask for help from its European partners and the IMF.

7. What did the first package of financial assistance for Greece consist of?

The first financial support programme for Greece, agreed in April 2010, consisted of bilateral GLF loans, amounting to €52.9 billion, and a €20.1 billion loan from the IMF. The EFSF, which was only established in June 2010, did not take part in this programme.

8. What kind of reforms and policy measures did Greece agree to implement?

The objective of the macroeconomic adjustment programme was to durably restore Greece's credibility with private investors by securing fiscal sustainability, safeguarding the stability of the financial system, and boosting potential growth and competitiveness.

This was to be achieved by carrying out fiscal consolidation, aimed at increasing government revenues and reducing expenses. Another major part of the programme was the implementation of structural reforms, including reforms in the: labour market to stimulate job creation and increase wage flexibility; product markets, especially in the services sector; public administration; and pension system. In addition, Greece was to privatise and restructure state-owned enterprises.

Reforms were also initiated to fight waste and corruption, along with measures to tackle tax evasion and step up collection of unpaid taxes.

9. Why was it necessary to have a second financial assistance package for Greece from the EFSF?

Greece made major efforts to implement wide-ranging measures, which were tied to the first financial assistance package. The challenges confronting Greece remained significant, however, with a wide competitiveness gap, a large fiscal deficit, a high level of public debt, and an undercapitalised banking system. The economic recession in Greece proved to be more serious and damaging than expected. The financial assistance provided under the first programme through bilateral loans from euro area countries and the IMF was not sufficient for Greece to make the necessary adjustments and to regain market access.

Furthermore, Greece's public debt-to-GDP ratio was considered unsustainable. A restructuring of debt held by private creditors became necessary to bring the total debt level back to a sustainable path. Additional time and funds were required to underpin Greece's fiscal consolidation efforts with structural reforms, to boost growth, and improve competitiveness.

10. What was the Private Sector Involvement (PSI) and what was the EFSF's role in it?

Under the PSI, Greek debt held by private investors, mainly banks, was restructured in March 2012 to lighten Greece's overall debt burden. About 97% of privately held Greek bonds (about €197 billion) took a 53.5% cut off the face value (principal) of the bond, corresponding to an approximately €107 billion reduction in Greece's debt stock.

The EFSF provided two facilities to Greece to encourage bondholders to participate in the PSI. These were the:

- PSI facility – as part of the voluntary debt exchange, Greece offered investors 1- and 2-year EFSF bonds. These EFSF bonds, provided to holders of bonds under Greek law, were subsequently rolled over into longer maturities.
- Bond interest (accrued interest) facility – to enable Greece to repay accrued interest on outstanding Greek sovereign bonds under Greek law which were included in the PSI. Greece offered investors EFSF 6-month bills. The bills were subsequently rolled over into longer maturities.

11. What decisions did the Eurogroup take in November 2012?

When the second programme was agreed, the Eurogroup noted that the outlook for the sustainability of Greek government debt had worsened compared to March 2012, mainly due to a deterioration in the macroeconomic situation and delays in programme implementation. The Eurogroup therefore approved a set of measures designed to ease Greece's debt burden and bring its public debt back to a sustainable path, so that debt-to-GDP could be reduced to 124% by 2020 and to substantially below 110% by 2022. These measures included:

- reducing the interest rate charged to Greece on the bilateral GLF loans by 100 basis points.
- cancelling the EFSF guarantee commitment fee (conditional upon the continued implementation of reforms by Greece) of 10 basis points, which Greece pays on the EFSF loans. It is estimated that this measure will save a total of €2.7 billion over the entire period of EFSF lending to Greece.
- extending the maturity of GLF and EFSF loans by 15 years (to an average loan maturity of over 30 years), significantly improving the country's debt profile.
- deferring interest rate payments on EFSF loans by 10 years, allowing Greece to reduce substantially its financing needs after a decade. This operation will not create any costs for the EFSF since Greece will pay interest charges on the deferred interest. It is estimated that this measure will lower the country's financing needs by €12.9 billion by 2022.
- passing on to Greece an amount equivalent to the income of the ECB's Securities Markets Programme portfolio accruing to their national central bank as from budget year 2013.

12. How did Greece benefit from the extension of loan maturities and deferral of interest payments decided in November 2012?

The extension of loan maturities and deferral of interest payments significantly reduced Greece's annual financing needs. This was instrumental in helping to bring Greece's public debt service back to a sustainable path, and made it easier for Greece to return to bond markets in 2014.

EFSF financial assistance in general has generated substantial savings for Greece: in 2013, these savings amounted to €8.6 billion, or 4.7% of Greece's GDP. For 2014, they were €7.9 billion, or 4.4% of Greece's GDP (based on reasonable assumptions; for details see the ESM 2013 and 2014 Annual Reports). These savings were possible because the EFSF provided loans to Greece (as well as to

Ireland and Portugal) at much lower interest rates than those that the market theoretically would have offered.

The savings increase further when we include all the other measures the euro area governments took to alleviate Greece's debt burden, such as the extension of the maturity of the EFSF and bilateral GLF loans to more than 30 years, the reduction in the GLF interest rates, the 10-year interest rate deferral or the cancellation of the interest rate margin. All combined, these improvements produced an economic reduction of the debt burden of 49% of Greece's 2013 GDP or of 50% of the European official sector loans. These savings greatly improved debt sustainability and provided Greece with fiscal space.

The EFSF and ESM – brief comparison

What is the difference between the EFSF and ESM?

The European Financial Stability Facility (EFSF) was created as a *temporary* crisis resolution mechanism by the euro area Member States in June 2010. The EFSF has provided financial assistance to Ireland, Portugal and Greece. No further funds are available from the EFSF; it will be dissolved and liquidated when all financial assistance provided to euro area Member States and all funding instruments issued by the EFSF have been repaid in full. [6]

The European Stability Mechanism (ESM) is a *permanent* rescue mechanism, which started its operations on 8 October 2012. The ESM is currently the sole mechanism for responding to new requests for financial assistance by euro area Member States. It has provided loans to Spain and Cyprus. The Greek government requested financial assistance from the ESM on 8 July 2015.[7]

[6] More information about the EFSF is available on the EFSF website.
[7] More information about the ESM is available on the ESM website.