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Commission proposes better financial terms for EU loans to Ireland and Portugal

Two proposals were adopted by the European Commission today, suggesting reduced interest rate margins and extended maturities for loans granted by the European Union (EU) to Ireland and Portugal. The loans are provided by the EU under the European Financial Stabilisation Mechanism (EFSM) as part of financial assistance packages to the two countries. The improved terms are expected to enhance liquidity and contribute to the sustainability of both countries in support of their strong economic and reform programmes.

The proposals are expected to be approved by the Council in the coming weeks. In line with the 21 July 2011 conclusions of the Heads of State and Governments, similar conditions are expected to be adopted for the lending that the European Financial Stability Facility (EFSF) is providing to Ireland and Portugal.

The Commission proposes to align the EFSM loan terms and conditions to those of the long standing the Balance of Payment Facility. Both countries should pay lending rates equal to the funding costs of the EFSM, i.e. reducing the current margins of 292.5 bps for Ireland and of 215 bps for Portugal to zero. The reduction in margin will apply to all instalments, i.e. both to future and to already disbursed tranches.

Furthermore, the maturity of individual future tranches to these countries will be extended from the current maximum of 15 years to up to 30 years. As a result the average maturity of the loans to these countries from EFSM would go up from the current 7.5 years to up to 12.5 years.

In addition to the substantial cash savings for Ireland and Portugal, the new financial terms will bring benefits such as enhanced sustainability and improved liquidity outlooks. Moreover, indirect confidence effects through the enhanced credibility of programme implementation should result in improved borrowing conditions for the sovereign as well as the private sector.

Ireland and Portugal are receiving loans as part of joint assistance packages from the EU (EFSM), EFSF and the International Monetary Fund. The EU and the EFSF, rated AAA/Aaa/AAA by the major rating agencies, fund their loans by issuing debt instruments in the capital markets.

Background

Assistance package for Ireland

Ireland receives, as part of the joint financial support package agreed in December 2010, loans from the EU under the European Financial Stabilisation Mechanism (EFSM), from the European Financial Stability Facility (EFSF), the International Monetary Fund (IMF) as well as bilateral loans. The agreed assistance amounts to € 67.5 billion over 3 years; EU (EFSM), EFSF (including bilateral loans) and the International Monetary Fund (IMF) are contributing each with € 22.5 billion.

Currently, the EFSM loan to Ireland carries a margin of 292.5 bps and allows for a maximum average maturity of the overall facility of 7.5 years with individual disbursements having maturities between 2 and 15 years.

Under the EFSM, three disbursements have been made so far to Ireland: € 5 billion on 12 January 2011, € 3.4 billion on 24 March 2011, and € 3 billion, on 31 May 2011. Further, the EFSF disbursed € 3.3 billion to Ireland on 1 February 2011.

Assistance package for Portugal

For Portugal, the financial assistance package was agreed by the Eurogroup and the EU's Council of Economics and Finance Ministers on 17 May. The financial package covers Portugal’s financing needs of up to € 78 billion. The European Union (EU), through the use of the European Financial Stabilisation Mechanism (EFSM) and the European Financial Stability Facility (EFSF) both provide loans up to € 26 billion each, to be disbursed over 3 years. Further support is been made available through the International Monetary Fund (IMF) with loans of up to € 26 billion.

Currently, the EFSM loan to Portugal carries a margin of 215 bps and allows for a maximum average maturity of the overall facility of 7.5 years with individual disbursements having maturities between 2 and 15 years.

Under the EFSM, two disbursements to Portugal have been made: € 1.75 billion on 31 May and € 4.75 billion on 1 June 2011. Two further disbursements have been made by the EFSF: € 3.6 billion on 22 June and € 2.2 billion on 29 June 2011.

The EU as a borrower

The European Commission is empowered to contract borrowings on the behalf of the EU for the purpose of funding loans made under the European Financial Stabilisation Mechanism (EFSM). The EFSM is a Treaty-based mechanism, covering all EU Member States. Under the EFSM, the EU can borrow up to € 60 billion to on-lend to any EU Member State in financial difficulties. It has currently been activated for Ireland and Portugal.

Further, under the Balance of Payments (BoP) facility, support is available to Member States which have not yet adopted the euro and face difficulties as regards their balance of payments. Also under the BoP Regulation, the European Commission is empowered to raise funds up to € 50 billion on behalf of the EU and on-lend to the beneficiary countries. Currently, Romania, Latvia and Hungary have benefitted from the BoP facility. Loan disbursements made so far amount to a total of € 13.4 billion.

Investor relations website: http://ec.europa.eu/economy_finance/eu_borrower/