European Union

Aaa / AAA / AAA

Investor Presentation

December 2010

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- EU's history, institutions and decision-making procedures

Section 1

The EU as an issuer

The EU: Who we are and why we are in the market

- The **European Commission on behalf of the EU operates 3 programmes** funded by issuing debt instruments in the capital markets:

NEW	European Financial Stabilisation Mechanism (EFSM)	Support to **Euro Area Member States** (EA MS) , up to EUR 60 billion (**activated for Ireland for up to EUR 22.5 billion**)
	Balance of Payments (BoP)	Support to **non-EA MS**, up to EUR 50 billion (EUR 12 billion outstanding)
	Macro-Financial Assistance (MFA)	Financial aid programme to assist countries that are **not EU MS** (EUR 600 million outstanding)*

- *The European Commission manages the EUR 80bn euro area package of pooled bilateral loans from EA MA to Greece (2 tranches disbursed so far, EUR 14.5 billion and EUR 6.5 billion).*

**See Annex for more details.*

The EU: Who we are and why we are in the market

- **Three top ratings and zero risk weighting**
  - EU debt service does not depend on the beneficiary country.
  - Borrowing is only possible when there is a legal basis in the Treaty.
  - The EU cannot borrow to finance its budget.
  - Top class credit: Legally binding obligation of its 27 Member States to fully cover all liabilities of the EU.
  - This underpins the EU's AAA, Aaa and AAA ratings and its zero risk weighting.

- **Borrowing**
  - Total borrowing plan for 2011: about EUR 20 billion (EUR 19 billion under EFSM for Ireland and about EUR 1.5 billion under BoP).
  - Bond issues are euro denominated only, mostly in the 5- to 10-year maturity range.
  - Total debt outstanding: EUR 12.6 billion.

Section 2

EU's response to the crisis

European Stabilisation Actions – financial support

10 May 2010: up to EUR 750 billion committed for European support package to secure stability within the Euro Area, in conjunction with the IMF.

1. **EUR 60 billion of loans funded by EU bonds (EFSM)**
   - Structure similar to existing BoP facility which exists for non-EMU Member States.
   - Based on Article 122, EFSM is available to and guaranteed by all 27 EU Member States.

2. **EUR 440 billion of guarantees by 16 EMU Member States (EFSF)**
   - Established for 3 years to provide loans and arrange funding transactions for EMU Member States.
   - Guarantees will be given according to each EMU Member States' share in the paid up capital of the ECB.
   - On 28-29 October the European Council agreed on the need to set up a permanent crisis mechanism. The European Stability Mechanism (ESM) will be based on EFSF. Any private sector involvement in a debt restructuring plan would not be effective before mid-2013.

3. **Potential IMF funding worth up to half the amount drawn from the EFSF and EFSM**

4. **ECB purchases of sovereign debt in the secondary market, along with additional liquidity provisions**
   - The Securities Markets Programme empowers the ECB to intervene in eurozone public and private debt markets, ensuring "liquidity in those market segments which are dysfunctional".
   - The ECB has re-established USD FX swap lines with the Fed, and it is temporarily offering unlimited allotment in its longer term refinancing operations (LTRO).

28 November 2010: up to EUR 85 billion for three-year joint EU/IMF financial assistance programme for Ireland.

European Stabilisation Actions – request procedure

- EMU Member State countries can request assistance.

- European Commission negotiates stabilisation programme including strong conditionality - in cooperation with the IMF and in liaison with the ECB.

- A common Memorandum of Understanding is established between the Commission, the IMF and the beneficiary country and submitted to Ecofin/Eurogroup, IMF Board and National Parliament of beneficiary country.

- Based on a proposal by the Commission, the Council Decision determines the overall amount of the country programme, and the loan terms and condition.

European Stabilisation Actions – programme for Ireland

- **Objectives of the programme:**
  - Immediate strengthening and comprehensive overhaul of the banking sector.
  - Ambitious fiscal adjustment to restore fiscal sustainability, correction of excessive deficit by 2015.
  - Growth enhancing reforms, in particular on the labour market, to allow a return to a robust and sustainable growth.

EUR 35 billion

EUR 50 billion

- **Financing:**
  - The total EUR 85 billion of the programme will be financed as follows:
    - EUR 17.5 billion contribution from Ireland (Treasury and National Pension Reserve Fund)
    - EUR 67.5 billion external support, EUR 22.5 billion for each of
      - 1/3 from the IMF
      - 1/3 from the **EFSM**
      - 1/3 from the EFSF + bilateral loans from the UK, Denmark and Sweden

- **Disbursements will be made over 3 years with an average maximum maturity of 7.5 years.**

EU funding plan 2011

- EU (**EFSM**): A total of EUR 19 billion in 4 benchmark transactions of EUR 3 to 5 billion and possibly complemented by 1 or 2 smaller bond issues.
    - Q1: 2 benchmark issues
    - Q2: 1 benchmark issue
    - Q4: 1 benchmark issue

- EU (**BoP**): 1 benchmark transaction of EUR 1.2 billion in Q1 2011 based on existing loan commitments to Romania.

EFSF – a Supranational by 16 EMU Member States

- **Form:** A “société anonyme” headquartered in Luxembourg having the 16 EMU Member States as its shareholders on the basis of their ownership stake in the ECB.
  - The Framework Agreement*, dated June 7, 2010 describes the key terms of the EFSF.

- **Mandate:** To ensure financial stability by issuing bonds in the capital markets and using the proceeds to assist euro-area Member States, if necessary.
  - EFSF is an emergency lending facility available to all EMU Member States.

- **EFSF AAA/Aaa/AAA ratings:** Derived from the ability and willingness to honour claims on a timely basis.
  - All liabilities will be covered by AAA guarantees and AAA assets.
  - Over-guarantee of 120 per cent on each bond.
  - Up-front cash reserve which equals the net present value of the margin of the EFSF loan and a service fee.
  - Loan specific cash buffer to ensure full AAA cover of liabilities.
  - The available liquidity under the cash reserve and cash buffer will be invested in highly safe and liquid AAA securities and deposits.

EFSF FRAMEWORK AGREEMENT

between

KINGDOM OF BELGIUM
FEDERAL REPUBLIC OF GERMANY
IRELAND
KINGDOM OF SPAIN
FRENCH REPUBLIC
ITALIAN REPUBLIC
REPUBLIC OF CYPRUS
GRAND DUCHY OF LUXEMBOURG
REPUBLIC OF MALTA
KINGDOM OF THE NETHERLANDS
REPUBLIC OF AUSTRIA
PORTUGUESE REPUBLIC

REPUBLIC OF SLOVENIA
SLOVAK REPUBLIC
REPUBLIC OF FINLAND
HELLENIC REPUBLIC

AND

EUROPEAN FINANCIAL STABILITY FACILITY

7 June 2010

*http://www.efsf.europa.eu/attachment/efsf_framework_agreement_en.pdf

European Stabilisation Actions – fiscal & economic measures

- The financial support is accompanied by fiscal and economic measures. There is a comprehensive strategy to ensure fiscal coordination, surveillance and consolidation, and economic reforms aimed at reducing the differences in competitiveness among EMU Member States through:

- **<u>Reversal in fiscal trends:</u>**
  - The Commission has already assessed the fiscal policies of 12 Member States and concluded that the envisaged consolidation paths are appropriate, that measures already taken have been sufficient to achieve the 2010 targets and, in most cases, invited the Member States to specify measures to substantiate the targets for the years beyond 2010.

- **<u>Improvement of economic policy coordination:</u>**
  - The heads of government of the EAMS established the Van Rompuy Task Force.
    - Strengthening the stability and growth pact.
    - Strengthening surveillance of macro-economic imbalances (competitiveness).
    - Developing a permanent crisis resolution mechanism.

- **<u>Legislation on measures to improve financial oversight:</u>**
  - A “European systemic risk board” will be set up to monitor high-level risks to the EU’s financial system.
  - Three supervisory authorities will be created to oversee banking, insurance, and securities markets.

Section 3

The EU – a AAA rated issuer: The credit story

European Union – Summary of credit strengths

- **The EU's AAA/Aaa/AAA ratings reflect:**
  - Borrowings are **direct and unconditional obligations** of the EU and **guaranteed** by the 27 Member States.
  - Should a beneficiary country default, the payment will be made from the budget of the European Union. EU Member States are legally obliged to ensure that the budget always has sufficient funds to meet the EU's obligations. For this purpose the Commission may draw on all Member States. Thus **investors are only exposed to the credit risk of the EU, not to that of the beneficiary of loans funded**.
  - A conservative approach to budget management: Budget resources are derived almost entirely from revenue paid by Member States independently of national parliaments including tariffs and duties on imports into the EU and levies on each Member State's VAT receipts and GNI. **The EU may not borrow to finance a budget deficit**.
  - "Back-to-back" lending ensures that the **EU budget does not assume any interest rate or foreign exchange risk**.

European Union – Strong credit ratings

Agency	Rating	Comments
STANDARD & POOR'S	AAA / Stable	▪Solid membership support ▪Multiple layers of debt-service protection ▪Prudent budget policies
MOODY'S	Aaa / Stable	▪Firm support of the 27 Member States ▪Several degrees of protection for loan repayments ▪Prudent budget management
FitchRatings	AAA / Stable	▪Rating driven by strong support of the EU's Member States ▪EU member states are legally obliged, jointly and severally, to make sure that the EU's budget is balanced ▪Highly conservative and prudential rules set up by the EU on lending and borrowing activities

Section 4

The EU – a benchmark issuer: The funding story

What determines EU funding?

- EU loans are financed exclusively **with funds raised on the capital markets** and not by the other Member States nor from the budget.

- The funds raised are in principle lent **back-to-back** to the beneficiary country, i.e. with the same coupon, maturity and amount. However, a loan margin of 292.5 basis points is being paid by Ireland under the EFSM.

- **This back-to-back principle imposes constraints on EU issuance (timing, amounts, maturities…)*.**

- The Council Decision determines the overall amount of the country programme, instalments and the maximum average maturity of the loan package. Subsequently, the Commission and the beneficiary country have to agree loan/funding parameters, instalments and tranches thereof. In addition, all but the first instalment of the loan depend on compliance with various policy conditions similar to those of IMF packages, which is another factor influencing timing of funding.

- This implies that timing and maturities of issuance are **dependent on the related EU lending activity**.

- **As a frequent benchmark borrower, within the above parameters the EU intends to build a liquid yield curve. The EU commits lead managers to provide an active secondary market, quoting two-way prices at all times and it monitors that such commitments are applied.**

**Note that EFSM would allow for pre-funding between tranches under the same country programme. Back-to-back would however be applied from the disbursement date of the instalment.*

Key Features of EU issuance

- The EU has so far issued benchmark-size bonds under its **Euro Medium Term Note programme** (EMTN), which has been recently upsized to EUR 80 billion to take into account issuance under the EFSM. The resumption in benchmark issuance is recent (end of 2008), driven by the crisis.
- With the activation of EFSM for Ireland, the EU will be a frequent benchmark issuer: 2011/2012 up to EUR 22.5 billion, mainly in EUR 3 to 5 billion transactions.
- Funding is **exclusively denominated in euros.**
- As EU assistance is of a medium-term nature, the maturity spectrum is normally 5 to 10 years, but can be expanded to 3 years up to 15 years.
- **"Back-to-back" on-lending** ensures that the EU budget does not assume **any interest rate or foreign exchange risk.**
- Notwithstanding the back-to-back methodology, **the debt service of the bond is the obligation of the European Union which will ensure that all bond payments are made in a timely manner.**

EU issuance December 2008 - September 2010

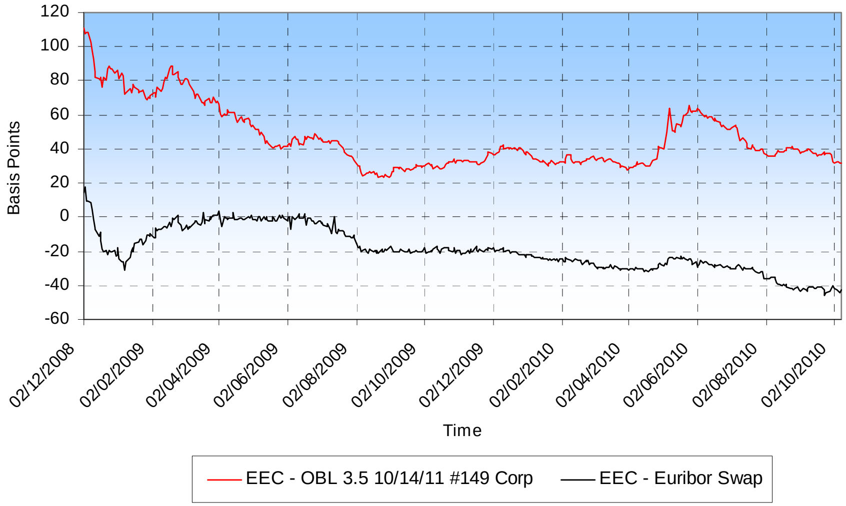
Bond issue	Issue Date	Maturity	Amount Issued (EUR)	Issued at MS	Currently trading at MS*
EEC 3,250 2011	09/12/2008	09/12/2011	2.000.000.000	+15	-30
EEC 3,125 2014	25/02/2009	03/04/2014	1.000.000.000	+30	-4
EEC 3,250 2014	26/03/2009	07/11/2014	2.000.000.000	+35	+2
EEC 3,125 2015	27/07/2009	27/01/2015	2.700.000.000	+25	+6
EEC 3,625 2016	06/07/2009	06/04/2016	1.500.000.000	+40	+7
EEC 2,375 2017	22/09/2010	22/09/2017	1.150.000.000	+8	+11
EEC 3,375 2019	10/03/2010	10/05/2019	1.500.000.000	+20	+11

Source: Bloomberg, as of 06 December 2010.

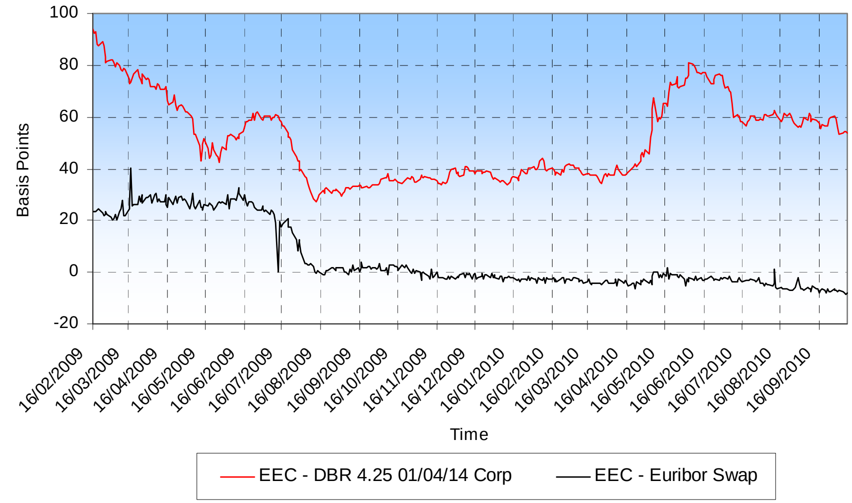
EEC is the Bloomberg Ticker referring to the original name of the current EU, see page 33

EU issuance – secondary market performance

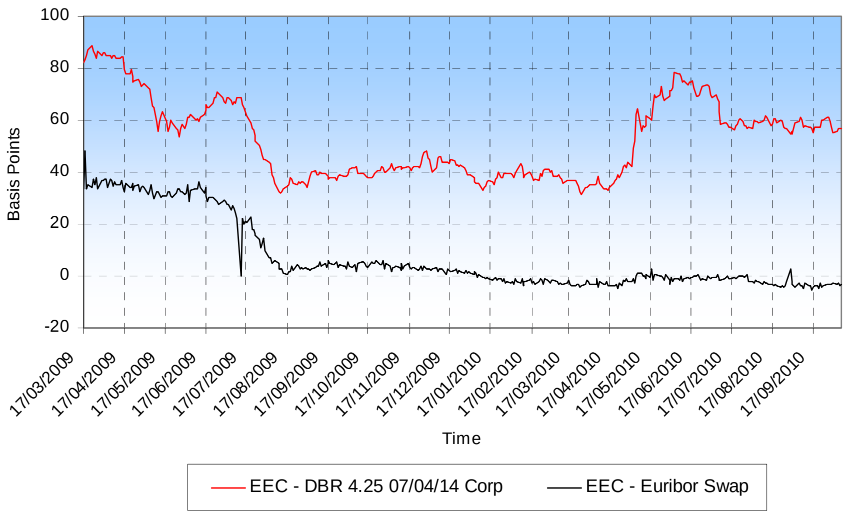
EEC 3.25 12/09/11 Corp - Secondary Market Performance



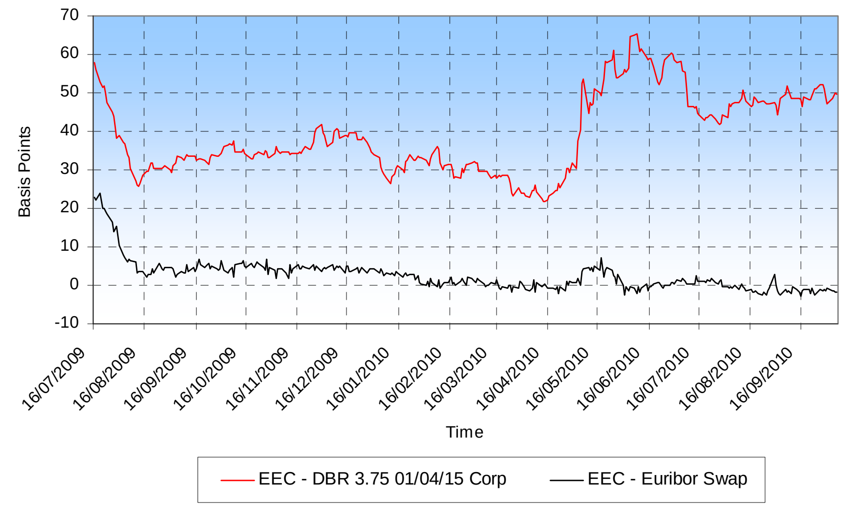
EEC 3.125 04/03/14 Corp - Secondary Market Performance



EEC 3.25 11/07/14 Corp - Secondary Market Performance

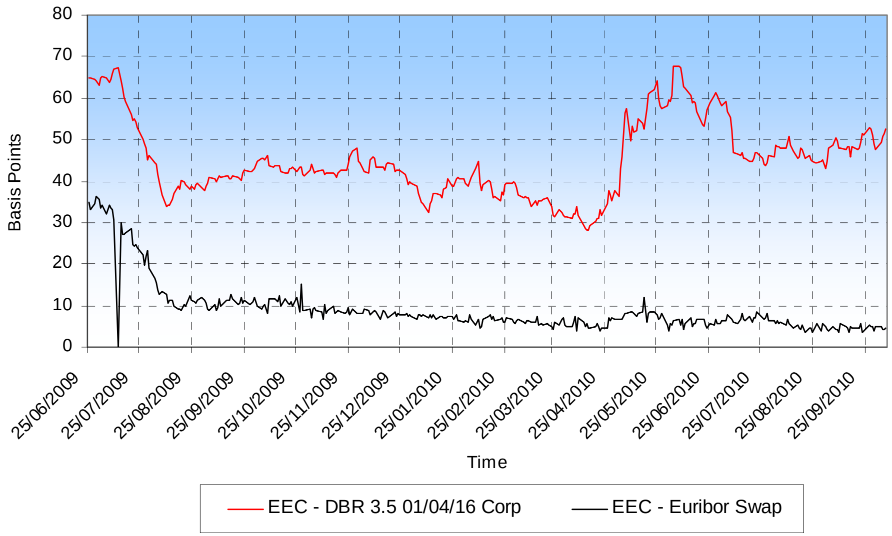


EEC 3.125 01/27/15 Corp - Secondary Market Performance

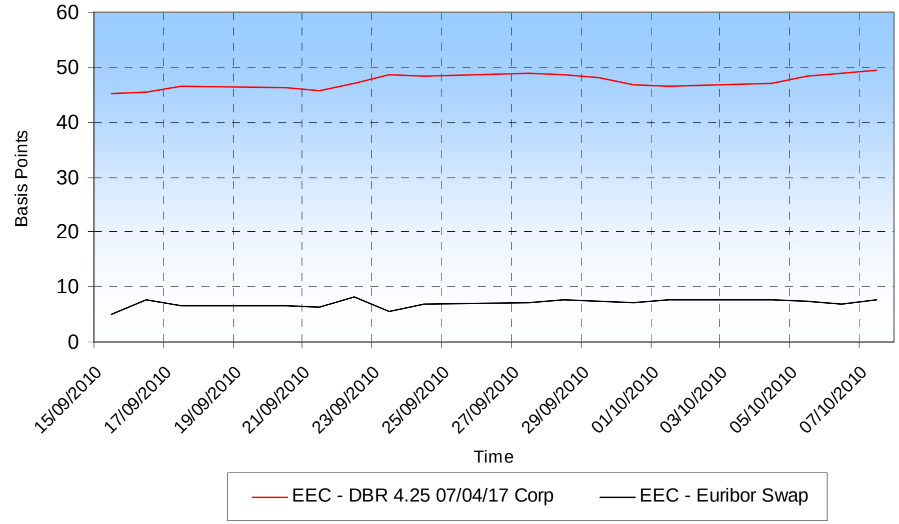


EU issuance – secondary market performance

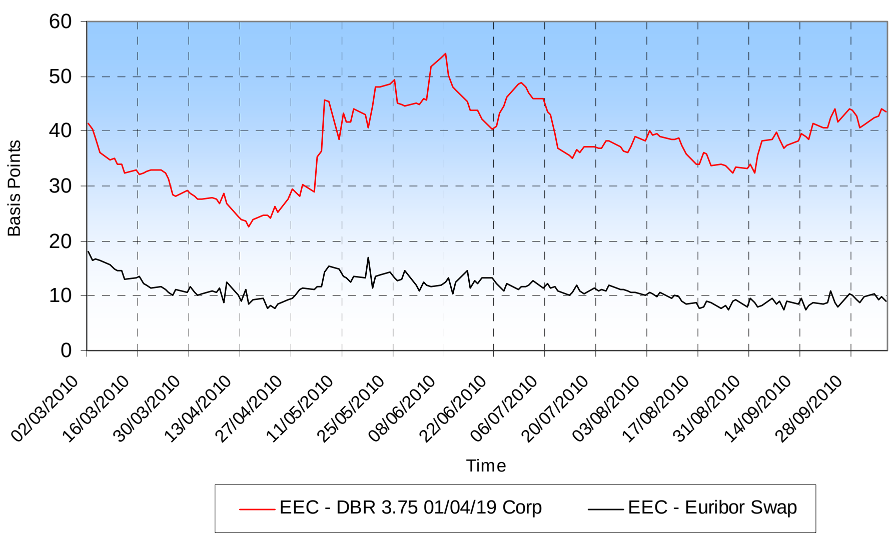
EEC 3.625 04/06/16 Corp - Secondary Market Performance



ECC 2.375 07/04/17 Corp - Secondary Market Performance



ECC 3.375 05/10/19 Corp - Secondary Market Performance



Annex

Transaction reviews

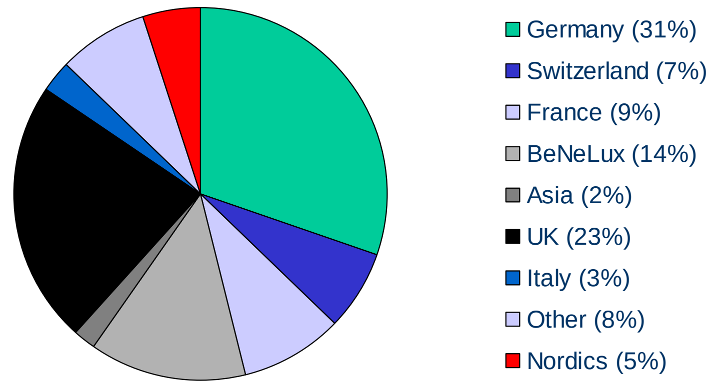
EU EUR 1.15bn benchmark due Sep-2017, issued 15-Sep-10

Key terms

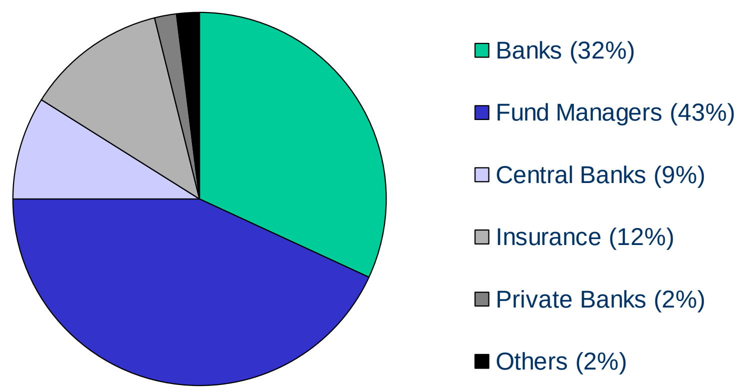
Issuer	**European Union (EU)** **Represented by the European Commission**
Rating	AAA/Aaa/AAA
Bloomberg Ticker	EEC
Guarantee	27 Member States
Tenor	22 September 2017
Size	EUR 1.15 billion
Format	2.375%, annual coupon, Act/Act
Spread	Mid-swaps +8 basis points
Risk Weighting	0% [1]
Lead Managers	Citi, Deutsche Bank, MS, Natixis
Issue Date	15 September 2010
Market	Eurobond
Listing	Luxembourg Stock exchange
Denominations	EUR 1,000 / 1,000
ECB Eligible	Yes, category 2
Law	English

1. Basel Committee on Banking Supervision, *Article 56, p20. "Claims on the Bank for International Settlements, the International Monetary Fund, the European Central Bank and the European Community may receive a 0% risk weight*

Investor distribution by region



Investor distribution by type



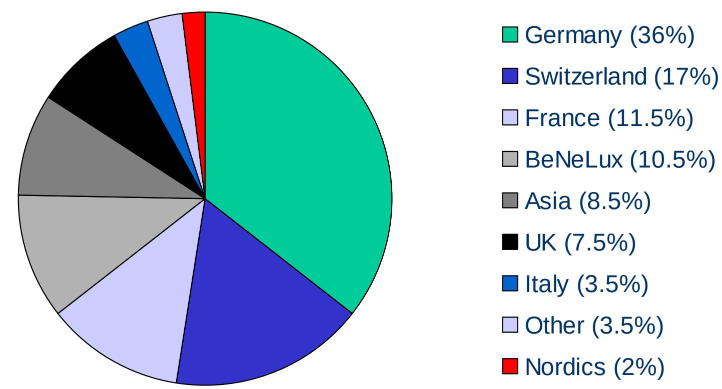
EU EUR 1.5bn benchmark due May-2019, issued 02-Mar-10

Key terms

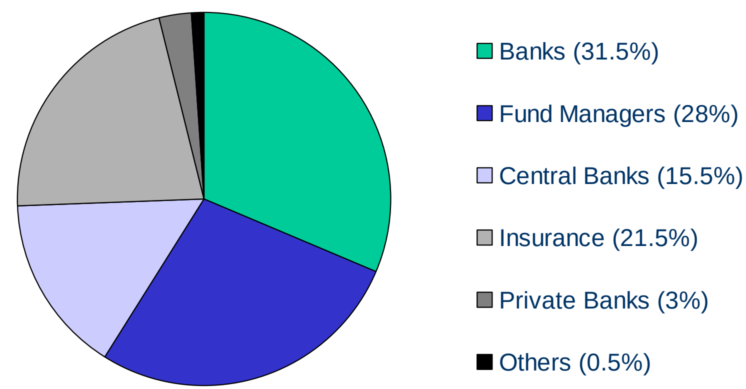
Issuer	**European Union (EU) Represented by the European Commission**
Rating	AAA/Aaa/AAA
Bloomberg Ticker	EEC
Guarantee	27 Member States
Tenor	10 May 2019
Size	EUR 1.5 billion
Format	3.375%, annual coupon, Act/Act
Spread	Mid-swaps +20 basis points
Risk Weighting	0% [1]
Lead Managers	Barclays, HSBC, SG
Issue Date	02 March 2010
Market	Eurobond
Listing	Luxembourg Stock exchange
Denominations	EUR 1,000 / 1,000
ECB Eligible	Yes, category 2
Law	English

1. Basel Committee on Banking Supervision, *Article 56, p20. "Claims on the Bank for International Settlements, the International Monetary Fund, the European Central Bank and the European Community may receive a 0% risk weight*

Investor distribution by region



Investor distribution by type



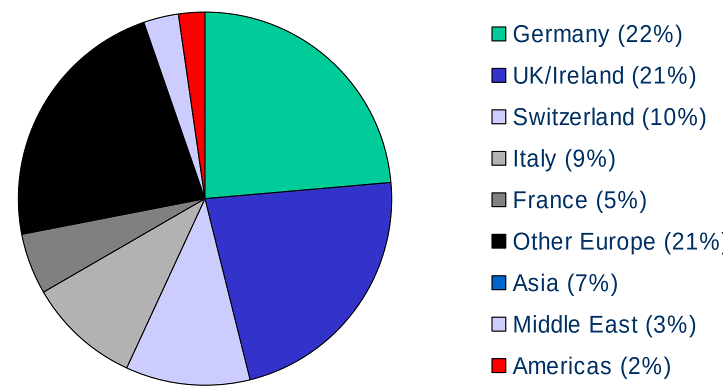
EC EUR 2.7bn benchmark due Jan-2015, issued 15-Jul-09

Key terms

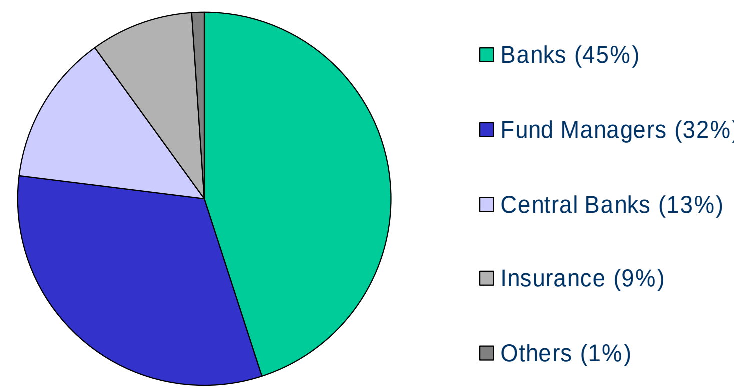
Issuer	**European Community (EC)** **Represented by the European Commission**
Rating	AAA/Aaa/AAA
Bloomberg Ticker	EEC
Guarantee	27 Member States
Tenor	27 January 2015
Size	EUR 2.7 billion
Format	3.125%, annual coupon, Act/Act
Spread	Mid-swaps +25 basis points
Risk Weighting	0% [1]
Lead Managers	BNPP, Deutsche Bank, UBS, UniCredit
Issue Date	27 July 2009
Market	Eurobond
Listing	Luxembourg Stock exchange
Denominations	EUR 1,000 / 1,000
ECB Eligible	Yes, category 2
Law	English

1. Basel Committee on Banking Supervision, *Article 56, p20. "Claims on the Bank for International Settlements, the International Monetary Fund, the European Central Bank and the European Community may receive a 0% risk weight*

Investor distribution by region



Investor distribution by type



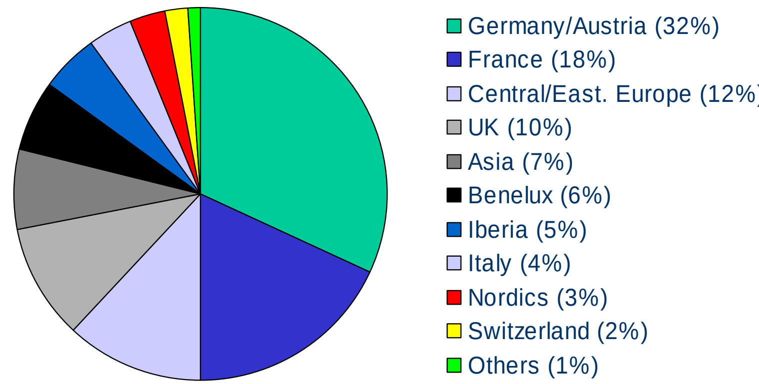
EC EUR 1.5bn benchmark due Apr-2016, issued 24-Jun-09

Key terms

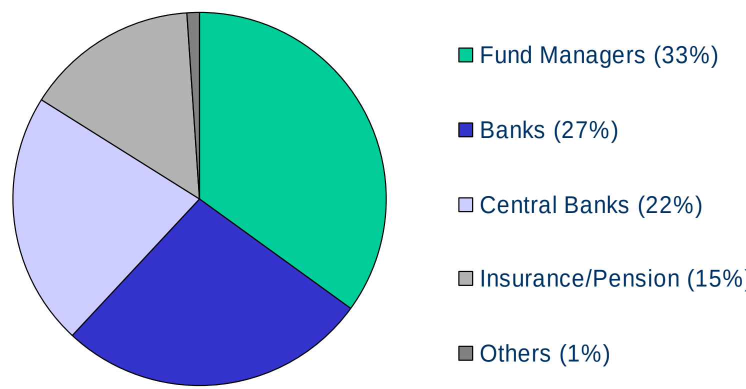
Issuer	**European Community (EC)** **Represented by the European Commission**
Rating	AAA/Aaa/AAA
Bloomberg Ticker	EEC
Guarantee	27 Member States
Tenor	06 April 2016
Size	EUR 1.5 billion
Format	3.625%, annual coupon, Act/Act
Spread	Mid-swaps +40 basis points
Risk Weighting	0% [1]
Lead Managers	Calyon, Goldman Sachs, UniCredit Group
Issue Date	06 July 2009
Market	Eurobond
Listing	Luxembourg Stock exchange
Denominations	EUR 1,000 / 1,000
ECB Eligible	Yes, category 2
Law	English

1. Basel Committee on Banking Supervision, *Article 56, p20. "Claims on the Bank for International Settlements, the International Monetary Fund, the European Central Bank and the European Community may receive a 0% risk weight*

Investor distribution by region



Investor distribution by type



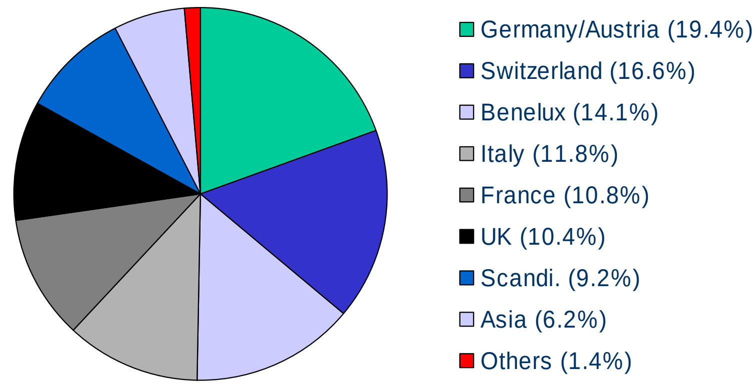
EC EUR 2bn benchmark due Nov-14, issued 26-Mar-09

Key terms

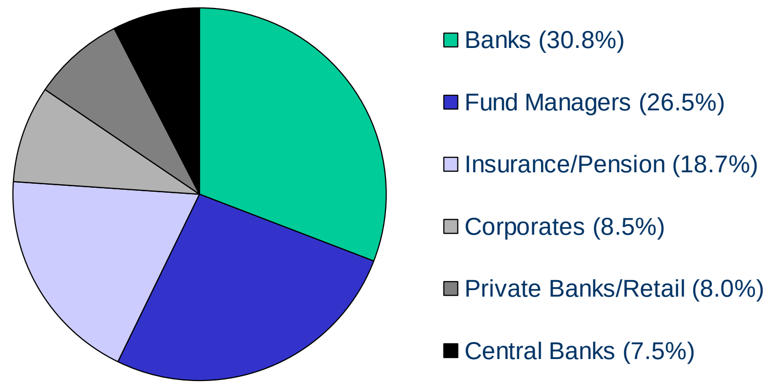
Issuer	**European Community (EC)** **Represented by the European Commission**
Rating	AAA/Aaa/AAA
Bloomberg Ticker	EEC
Guarantee	27 Member States
Tenor	7 November 2014
Size	EUR 2 billion
Format	3.25%, annual coupon, Act/Act
Spread	Mid-swaps +35 basis points
Risk Weighting	0% [1]
Lead Managers	Credit Suisse, HSBC, JP Morgan
Issue Date	26 March 2009
Market	Eurobond
Listing	Luxembourg Stock exchange
Denominations	EUR 1,000 / 1,000
ECB Eligible	Yes, category 2
Law	English

1. Basel Committee on Banking Supervision, *Article 56, p20. "Claims on the Bank for International Settlements, the International Monetary Fund, the European Central Bank and the European Community may receive a 0% risk weight*

Investor distribution by region



Investor distribution by type



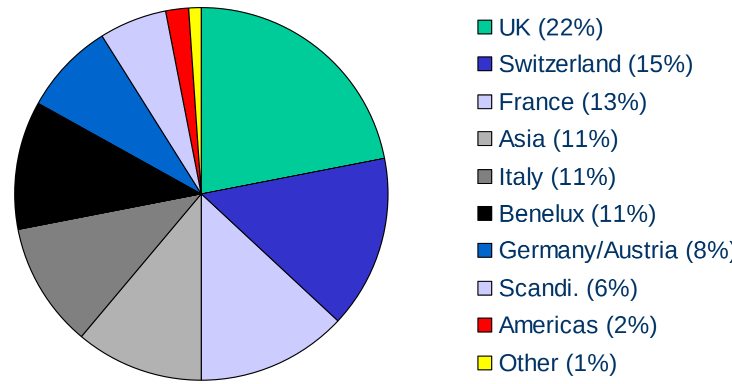
EC EUR 1bn benchmark due Apr-14, issued on 23-Feb-09

Key terms

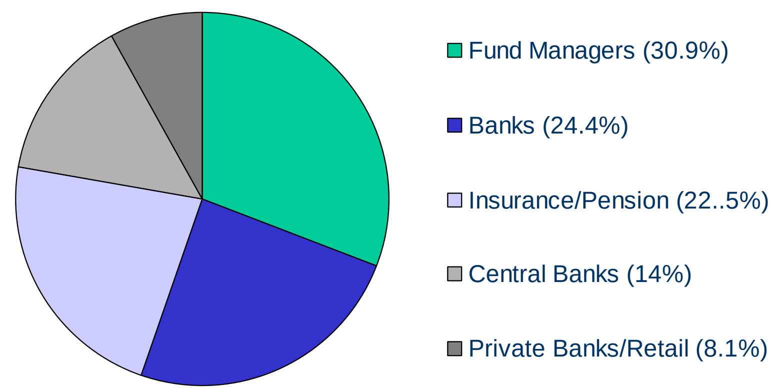
Issuer	**European Community (EC) Represented by the European Commission**
Rating	AAA/Aaa/AAA
Bloomberg Ticker	EEC
Guarantee	27 Member States
Tenor	3 April 2014
Size	EUR 1 billion
Format	3.125%, annual coupon, Act/Act
Spread	Mid-swaps +30 basis points
Risk Weighting	0% [1]
Lead Managers	Credit Suisse, HSBC, JP Morgan
Issue Date	23 February 2009
Market	Eurobond
Listing	Luxembourg Stock exchange
Denominations	EUR 1,000 / 1,000
ECB Eligible	Yes, category 2
Law	English

1. Basel Committee on Banking Supervision, Article 56, p20. "Claims on the Bank for International Settlements, the International Monetary Fund, the European Central Bank and the European Community may receive a 0% risk weight

Investor distribution by region



Investor distribution by type



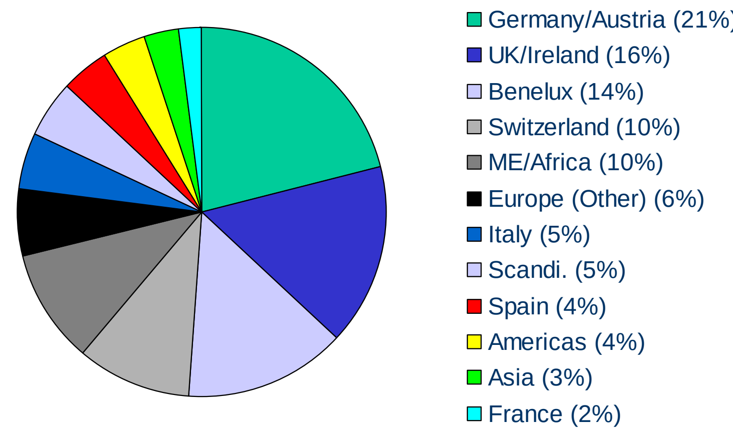
EC EUR 2bn benchmark due Dec-11, issued on 09-Dec-08

Key terms

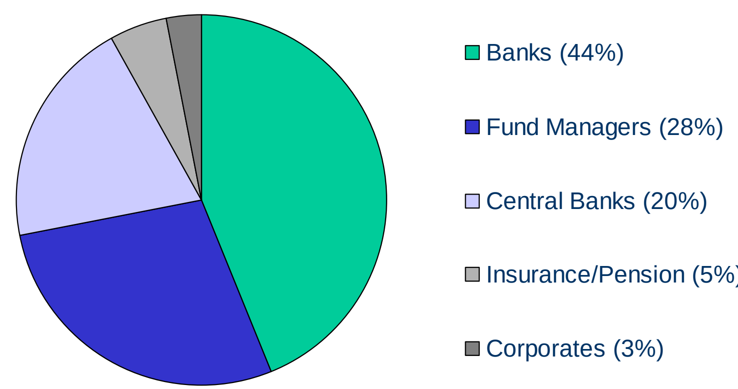
Issuer:	**European Community (EC) Represented by the European Commission**
Rating	AAA/Aaa/AAA
Bloomberg Ticker	EEC
Guarantee	27 Member States
Tenor	9 December 2011
Size	EUR 2 billion
Format	3.25%, annual coupon, Act/Act
Spread	Mid-swaps +15 basis points
Risk Weighting	0% [1]
Lead Managers	Barclays, BNPP, Deutsche Bank, GS
Issue Date	9 December 2008
Market	Eurobond
Listing	Luxembourg Stock exchange
Denominations	EUR 1,000 / 1,000
ECB Eligible	Yes, category 2
Law	English

1. Basel Committee on Banking Supervision, Article 56, p20. "Claims on the Bank for International Settlements, the International Monetary Fund, the European Central Bank and the European Community may receive a 0% risk weight

Investor distribution by region



Investor distribution by type



Annex

Macro-Financial Assistance to non-Member States

Macro-Financial Assistance (MFA)

- Financial assistance to countries which are **not members of the EU** to help them deal with serious, but generally medium-term, balance-of-payments or budget difficulties.

- Country requests support from the EU, decided by the European Parliament and the Council. European Commission negotiates economic and financial details in close coordination with the IMF.

- MFA may take the form of grants or loans. Grants are financed from the EU budget. Loans are funded in the capital markets.

- Size of the EU loans in the package is typically of the order of tens of millions, always denominated in euro.

Annex

EU's history, institutions and decision-making procedures

European Union – History

- **1957: Foundation of the European Economic Community “EEC”.**

- In 1993, the Treaty on European Union (more popularly known as the Treaty of Maastricht) renames the EEC the European Community (EC) and establishes the European Union (EU).

- Pursuant to the Lisbon Treaty, which came into effect on 1 December 2009, the European Union replaced and succeeded the European Community. The EU has since become the formal name for all the Communities and these policies, so EU = EC = EEC.

- **Currently 27 Member States:**
  - Austria, Belgium, Bulgaria, Cyprus, Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden and United Kingdom.
  - The current candidate countries are Croatia, the former Yugoslav Republic of Macedonia, and Turkey.

- **Today, the EU has a population of about 500 million inhabitants. In 2009, the GDP was EUR 12.2 trillion.**

Institutions and other bodies of the EU

- The **main institutions** are:
  - The European Commission
  - The European Parliament
  - The Council of the European Union*
  - The Court of Justice of the European Union
  - The European Court of Auditors

- Important **other bodies**:
  - The European Central Bank (ECB)
  - The European Investment Bank (EIB)

** Not to be confused with the Council of Europe, which is <u>not</u> an EU institution*

The ECB, the euro and European Monetary Union

- The European Central Bank (ECB) sets monetary policy for the euro area.
- Not all EU Member States have adopted the euro (EUR, €), the single currency of the European Monetary Union (EMU), as various criteria for exchange rate stability, inflation, interest rates, public sector deficits and debt have to be met.
- 16 EMU Member States: Austria, Belgium, Finland, France, Germany, Ireland, Italy, Luxembourg, the Netherlands, Portugal and Spain (1999), Greece (2001), Slovenia (2007), Cyprus and Malta (2008), Slovakia (2009).
- Denmark, Sweden and the United Kingdom have chosen not to adopt the euro.
- All other EU Member States will in principle adopt the euro once they fulfil the criteria*.

**On 12 May 2010, the European Commission recommended that Estonia joins the euro area in 2011 and become its 17th member.*

EU decision-making: Institutions

- The EU's decision-making process mainly involves three institutions:
  - **The European Parliament,** the members of which are elected directly every five years by voters in all 27 Member States. The number of seats per country take into account the population of that country, albeit with a weighting towards proportionately more representatives for smaller countries. The last elections took place in June 2009.
  - **The Council of the European Union,** which represents the individual Member States. Its meetings are attended by one minister from the appropriate ministry from each of the EU's national governments. Several times a year the Heads of State and Government of the Member States, together with the President of the European Commission, meet as the "**European Council**". These 'summit' meetings set overall EU policy and resolve outstanding issues, and are chaired by the President of the European Council.
  - **The European Commission** is the executive arm of the EU, i.e. it implements policy. It is led by the College of Commissioners, one from each country, one of whom is appointed President, and has a staff of 23,000 civil servants. This institution resembles national ministries.

EU decision-making: Procedures

- There are several decision-making procedures. In all cases, the European Commission has the right of initiative, i.e. it makes the proposals, but the European Parliament and the Council may request proposals.

- The most frequently used procedure is that of **ordinary legislative procedure** in areas where the European Parliament and the Council share legislative power.

- Under other procedures the Parliament is consulted on its consent if requested.

- The procedure may result in either a Regulation, a Directive or a Decision. A **Regulation** is directly applicable in the Member States. A **Directive** requires Member States to adapt national legislation.

- Once decisions are made in principle, day-to-day decision making may of course be delegated to the Commission within the appropriate legislative framework.

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