EUROPEAN COMMISSION

Brussels, 16.12.2010
C(2010) 9304 final

COMP Operations

PUBLIC VERSION

WORKING LANGUAGE

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Subject: State aid N 520/2010 - Sweden
State guarantee in favour of Volvo Personvagnar AB (Volvo Car Corporation)

Sir,

I have the honour to inform you that the Commission has decided not to raise objections to the state aid mentioned in reference.

I. PROCEDURE

(1) By decision of 5 June 2009, the Commission declared not to raise objections with regard to a State guarantee to be granted by Sweden covering a loan from the European Investment Bank ("EIB") for an amount of EUR 500 million to Volvo Personvagnar Aktiebolag (Volvo Car Corporation, hereinafter: "VCC")[1]. The guarantee thus approved has however not been implemented.

(2) Recently, VCC and its new mother company, Shanghai Geely Zhao Yuan Intnl Investment Co. Ltd ("Geely"), expressed their interest to benefit from such a loan. In

[1] Case N 80/2009 (OJ C 172, 24.07.2009).

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consequence, after a pre-notification process, Sweden notified, on 11 November 2010, a new guarantee project for an EIB loan of the same amount.

(3) In its notification Sweden claims that the rating and the overall financial situation of VCC has changed and the markets have improved substantially since the approval decision in June 2009, which may justify a lower guarantee fee.

(4) By email dated 12 November 2010, the Commission requested further information. Sweden submitted additional information on 12 November, 22 November and 2 December 2010.

II. THE AID MEASURE

II.1. The beneficiary

(5) The intended beneficiary is the car manufacturer Volvo Car Corporation (VCC). VCC is incorporated in Sweden and has its headquarters in Göteborg. Previously owned by Ford, VCC is currently owned by Geely.

(6) VCC has no separate credit rating. The Swedish National Debt Office (*Riksgäldskontoret*, hereinafter: "NDO") carried out a rating assessment according to which VCC can be rated in the […]* to […] range. NDO decided to take a conservative approach and apply the rating of […] for the purposes of the notified aid measure.

II.2. The Swedish Government's Aid Package for the Automotive Industry

(7) A dramatic reduction in demand in the second half of 2008 has led to serious problem for car makers. In to provide support for the car sector in the present financial crisis with the objective of preserving an industry with the potential to be competitive, the Swedish government has brought forward a series of measures.

(8) As part of this package, the Swedish Parliament had given the Government powers to issue State guarantees to undertakings in the automotive sector, to be used as collateral for loans from the EIB intended to finance a transition to green technologies.

II.3. The EIB Loan

(9) VCC is undertaking a project concerning research and engineering activities which is related to (i) automotive fuel efficiency aiming at less CO2 emissions and (ii) safety. The project will run until 2012.

(10) In order to fulfil this financing plan, VCC has applied for a EUR 500 million loan from the EIB[2].

(11) On 16 November 2010, the EIB Board of Directors took a preliminary decision to grant VCC a loan of EUR 500 million.

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[2] The European Clean Transport Facility (ECTF) is a major EIB financing facility to support investments targeting research, development and innovation in the areas of emission reduction and energy efficiency in the European transport industry.

* Covered by the obligation of professional secrecy.

II. 4. The State guarantees and the premium to be paid

(12) Based on the powers it has received from Parliament, on 11 November 2010 the Swedish Government instructed the NDO to start negotiations with VCC on the State guarantee to be issued for the EIB loan.

(13) The NDO is empowered to issue such guarantees. However, the Government must approve the guarantee in each particular case. After the decision of the Government, the NDO will provide the guarantee to VCC. The signing of the guarantee agreement, between the NDO and VCC, constitutes the granting of the legally binding guarantee.

(14) The NDO's guarantee will be divided into two separate guarantees.

(15) The first guarantee will cover 90% of the loan, i.e. EUR 450 million out of EUR 500 million. In return for the guarantee, VCC will pay the Swedish State a premium amounting to [between 68-170] basis points ("bps") per annum ("p.a.") for the first two years that the guarantee applies, i.e. [0,68%-1,70%] of the instalments received by VCC. After this period of two years, VCC will pay a premium amounting to [between 80-200 bps (0,8%-2,00%)] p.a. for the remainder of the validity of the guarantee. This guarantee is referred to as "guarantee A" in this decision.

(16) The second guarantee will cover the remaining 10% of the loan, i.e. EUR 50 million out of EUR 500 million. For this, VCC will pay the Swedish State a premium of […] bps p.a., i.e. [...]% of the amount covered by the guarantee. This guarantee is referred to hereinafter as "guarantee B".

(17) The two guarantees will apply *pari passu*, i.e. without any preference or seniority between the two; such that any sum paid out under the global guarantee will be covered pro rata by the two guarantees jointly (i.e. 90% will be covered by the first guarantee and 10% by the other). The two guarantees will have the same duration of the loan that they cover. In any case, they will not be in force after the end of 2020.

(18) In addition to the premium payable for the guarantee, VCC will provide the Swedish government with high-quality collateral covering the full guaranteed amount. This collateral will be callable by the Swedish State if it has to pay out any money under the guarantee.

(19) Before every instalment of the EIB loan, the NDO shall ensure that VCC has pledged adequate collateral for the guarantee and that VCC is able to provide the required co-financing of the project costs.

III. ASSESSMENT

III.1. Existence of State Aid

General remarks

(20) Article 107(1) of the Treaty on the Functioning of the European Union (hereinafter: "TFEU")[3] provides that any aid granted by a Member State or through State resources

[3] With effect from 1 December 2009, Articles 87 and 88 of the EC Treaty have become Articles 107 and 108, respectively, of the TFEU. The two sets of provisions are, in substance, identical. For the purposes of this

in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market.

(21) For the sake of clarity, it should be underlined that it is only the guarantee notified by Sweden that is covered by this decision, not the EIB loan.

(22) The Commission has published detailed guidance on the application of the State aid rules of the Treaty to guarantees[4] (hereinafter: "the Guarantee notice"), making it clear that the general criteria of Article 107(1) TFEU equally apply to guarantees. As indicated in the Guarantee notice, the benefit of a State guarantee for the beneficiary is constituted by the fact that the risk associated with the guarantee is carried by the State.

(23) As regards the application of the State aid criteria of Article 107(1) TFEU to guarantees A and B, the Commission considers the following. As the guarantees are based on powers given by Parliament and can be issued only upon express decision by the Government, the decision to grant the guarantees is clearly imputable to the State. The guarantees are granted from State resources since, in the event that the Swedish state would actually have to pay out money under the guarantees, the necessary funds would be drawn from the central State budget, which is consequently burdened by the financial risk linked to the guarantees. The guarantees are also selective since the Government has discretion to choose the undertakings that will benefit from such guarantees. Finally, as there is extensive trade in cars and car parts between several operators within the European Union, the advantage granted to VCC by means of the guarantees would be liable to affect competition and trade between the Member States.

(24) In order to establish whether the guarantees contain State aid, the Commission must also assess whether they provide an advantage to VCC. As indicated in the Guarantee notice, a State measure is not State aid unless it also provides the beneficiary with an advantage it would not otherwise have been able to obtain on market terms. In this context, in order to determine whether an advantage is being granted through a guarantee, the Commission should base its assessment on the principle of an investor operating in a market economy[5] (hereafter referred to as the "market economy investor principle"). Account should therefore be taken of the possibilities for a beneficiary to obtain equivalent financial resources by having recourse to the capital market. State aid is not involved where a new funding source is made available on conditions which would be acceptable for a private operator under the normal conditions of a market economy.

(25) Sweden takes the view that guarantee A is State aid, but compatible with the internal market in light of the Commission's communication "Temporary framework for State aid measures to support access to finance in the current economic and financial crisis"[6] (hereinafter: "the TF").

Decision, references to Articles 107 and 108 of the TFEU should be understood as references to Articles 87 and 88, respectively, of the EC Treaty where appropriate.

[4] Commission notice on the application of Article 87 and 88 of the EC Treaty to State aid in the form of guarantees (OJ C 155, 20.6.2008, p. 10).

[5] This follows from an extensive ECJ case law, se e.g. case C 278-280/92, Hytasa.

[6] OJ C 16, 2.1.2009, p. 1, as amended by Commission Communication of 25 February 2009 (a consolidated version of the TF was published on 7 April 2009, see OJ C 83, p.1.).

(26) However, concerning guarantee B, Sweden argues that it is not State aid under the market economy investor principle precisely because the terms are such as to be acceptable for a private operator under the normal conditions of a market economy.

(27) It therefore appears appropriate to first examine whether the State aid criteria are met in the case of guarantee B, and then to assess guarantee A.

Guarantee B

(28) In section 3.2 of the Guarantee notice the Commission gives detailed guidance on the conditions in which the presence of State aid in an individual guarantee can be ruled out by application of the market economy investor principle. However, when some of these conditions are not met the Member States has to duly substantiate its claim according to which a given guarantee does not contain State aid.

(29) The Commission notes the fact that the guarantee can be properly measured i.e. is linked to a specific financial transaction, for a fixed maximum amount and is limited in time. These aspects are pre-requisite to any finding of absence of State aid as otherwise it would not be possible to calculate a market premium for that guarantee (see the Guarantee notice section 3.2(b)).

(30) Furthermore, a market-oriented price should be paid for Guarantee B (section 3.2(d) of the Guarantee notice). Indeed, risk-carrying should normally be remunerated by an appropriate premium on the guaranteed amount. When the price paid for the guarantee is at least as high as the corresponding guarantee premium benchmark that can be found on the financial markets, the guarantee does not contain aid. The Guarantee notice goes on to indicate that if no corresponding guarantee premium benchmark can be found on the financial markets, the total financial cost of the guaranteed loan, including the interest rate of the loan and the guarantee premium, has to be compared to the market price of a similar non-guaranteed loan. In both cases, in order to determine the corresponding market price, the characteristics of the guarantee and of the underlying loan should be taken into consideration. This includes: the amount and duration of the transaction; the security given by the borrower and other experience affecting the recovery rate evaluation; the probability of default of the borrower due to its financial position, its sector of activity and prospects; as well as other economic conditions. This analysis should notably allow the borrower to be classified by means of a risk rating.

(31) Sweden has notified a premium of […] of the guaranteed amount per annum. Sweden’s view is that this price is market-conform.

(32) On the issue of collateralisation, Sweden has made a commitment to secure full collateral for each tranche of the guarantee. The Swedish authorities have submitted a study ordered from the independent audit firm KPMG[7], itemising and valuating the VCC assets available to be pledged to the State as collateral for the guarantees[8].

[7] "Assessment of Geely Sweden Group – Analysis in connection to Swedish National Debt Office evaluation of a guarantee for a loan from the EIB”, November 2010.

[8] Sweden has notified that the pledge of full collateral will be secured for both guarantees A and B.

(33) The estimated value is based on a prudent valuation at orderly liquidation value. According to this method, the fixed assets[9] available as collateral are estimated at EUR […] million.

Table 1: Collaterals offered by VCC in exchange for the State guarantee

Collateral	Estimated value EUR
Land and Buildings	[…] million
Machinery and Equipment	[…] million
TOTAL	**[…] million**

(34) Further to the guidance of the Guarantee notice, the Commission has sought data for the premium for comparable guarantees on commercial markets. Such data has however not been readily available, and Sweden has not provided evidence of a similar guarantee effectively granted on market terms. The Commission has then, following the methodology laid down in the Guarantee notice, sought evidence concerning the total financial cost of similar non-guaranteed debt on the commercial markets.

(35) The Commission notes that the use of RAROC (Risk adjusted return on capital) to estimate a proxy for the market guarantee premium, as it was used in the 2009 VCC decision, is not justified anymore under the current circumstances, given that the market for debt paper issued by European car manufacturers is no longer dysfunctional. Hence there is sufficient data available on the market indicating the cost of comparable non guaranteed debt. Therefore, the Commission has sought and analysed data on CDS spreads of issuances that are as similar as possible in terms of issuer business activity, issuer credit rating, and debt maturity ("peer analysis"). In a second step, recent senior debt CDS spreads of the […] European car manufacturer have been increased with rating-differential specific top-ups, […]. Based on broader Bloomberg data analysis, adequate top-ups have been determined. Third and finally, a new issuance premium has been added to the sum of the peer CDS spreads and the corresponding top-ups. The sum of the above three components results in proxies for the market-based guarantee fee that lie close to […]. Hence the proposed [...] guarantee fee seems to be roughly in line with current market conditions.

(36) As regards the applied rating, the Commission notes that the NDO, using Moody's approach[10], estimated a credit rating of […] (Moody's) or […] (S&P).

(37) As regards the overall situation on the financial markets, the Commission takes note of the fact that over the last quarters, and in particular since the second quarter of 2009, market sentiment has significantly improved. Credit markets, both in the bond market and in the loan market, have eased. As a result, new issuance volumes in the corporate bond market have increased, credit spreads have tightened significantly and the primary market for sub-investment grade issuers has gradually re-opened. As a

[9] Land and Buildings, Machinery and Equipment.

[10] The NDO selected the developed methodology for the "Global Automobile Manufacturer Industry" to assess the rating of VCC. The relevant methodology developed by Moody's is applied to 17 automobile manufacturers and covers a wide range of ratings. Moody's methodology is based on the review of 13 rating sub-factors covering 5 areas (each called a "factor"). Based on such analysis, NDO came to the conclusion that a […] to […] rating in Moody's scale (or […] to […] rating in the S&P scale) was reasonable. The Commission has not found any manifest error in the NDO application of this methodology and accepts the proposal by Sweden to opt for the lowest rating of the proposed range, i.e. […] (Moody's) or […] (S&P) for Volvo in this decision.

consequence, for a given credit risk exposure, the risk premium required by market investors has significantly decreased since the second quarter of 2009.

(38) With these elements, the Commission has established a benchmark margin for a similar transaction on the markets. On that basis, the Commission accepts that the fee paid for guarantee B is at least as high as the margin (to which a reference rate like the EURIBOR rate would be added) for a similar non-guaranteed loan, and that guarantee B therefore does not comprise State aid. Indeed, the total cost of the loan for VCC consists of the reference rate (like the EURIBOR rate) plus the aforementioned margin, as well as any operating costs the EIB may charge.

(39) In view of the elements above, the Commission considers that guarantee B doesn't entail State aid.

Guarantee A

(40) Sweden has notified Guarantee A as State aid but argues that it is compatible with the internal market on the basis of Article 107(3)(b) TFEU in view of the guidance provided in the TF.

(41) The Commission shares Sweden's views that guarantee A constitutes State aid. Indeed, in view of the above-mentioned findings of the present market benchmark premiums for guarantees in the automotive sector, it appears excluded that VCC would have been able to obtain a similar guarantee at the same price on the market. Guarantee A therefore contains State aid within the meaning of Article 107(1) TFEU.

III.2. Compatibility of Guarantee A

(42) The Commission will in the following assess the compatibility of guarantee A against the criteria in section 4.3 of the TF.

(43) For large companies such as VCC, the Member State may grant a reduction of up to 15% of the annual premium for new guarantees in accordance with the safe-harbour provisions in Annex 1 to the TF. This reduction in the premium may be applied for a maximum of two years following the granting of the guarantee. If the duration of the underlying loan exceeds 2 years, Member States may apply for an additional maximum period of 8 years the safe-harbour premiums set out in Annex 1 to the TF without reduction.

(44) For a company with a […] credit rating, the safe-harbour minimum premium indicated in Annex 1 of the TF is [between 80-200] bps, provided that the guarantee has high collateralisation, defined for these purposes as a loss given default below or equal to 30%[11].The Commission considers that Sweden has provided credible evidence that high-quality assets collateral is available (see points (32)-(33) above) that would allow Sweden to ensure a loss given default of less than 30%, i.e. a high collateralisation of the guarantees within the meaning of the TF. The Commission further notes Sweden's commitment that no instalments will be disbursed unless collateral for the full amount has been secured from the high-quality assets. On this basis, the Commission is satisfied that the guarantees will be highly collateralised within the meaning of the TF.

[11] See footnote 20 to the TF.

(45) Under section 4.3.2 (d) of the TF the maximum loan must not exceed the total annual wage bill of the beneficiary (including social charges as well as the cost of personnel working on the company site but formally in the payroll of subcontractors) for 2008. It appears from the notification that VCC's wage bill for 2008 was EUR […] million, i.e. more than the total notified loan of EUR 500 million. This condition is thus met.

(46) The Commission further notes that Sweden explicitly confirmed that the guarantee will be granted before the end of December 2010, i.e. that the signing of the guarantee agreement will take place before 31 December 2010. The condition of point 4.3.2(e) of the TF is thus fulfilled.

(47) Guarantee A does not exceed 90% of the EIB loan, which meets point 4.3.2 (f) of the TF.

(48) According to Annex 1 to the TF, the safe-harbour premium for a highly collateralised guarantee to an undertaking with VCC's rating is [between 80-200] basis points. As regards the guarantee premium, the Commission records that Sweden will apply a 15% reduction of the safe-harbour premium ([between 68-170 basis points]) for a maximum of two years following the granting of the guarantee, and after these two years apply the full safe-harbour premium without reduction for an additional maximum period of 8 years. Sweden confirmed that the loan will be totally reimbursed within ten years after the granting of the guarantee. This is in line with point 4.3.2 (h) of the TF.

(49) The beneficiary must not have been in difficulty within the meaning of the Rescue and restructuring guidelines on 1 July 2008 (point 4.3.2 (i) of the TF). In this connection, Sweden has provided data as per 30 June 2008 showing that VCC's total equity was, on conservative estimates, […] times its share capital and that consequently VCC was a well-capitalized undertaking. In addition, Sweden has confirmed that VCC was not insolvent, having a significant amount of net cash[12], and no problems paying its debts. In view of this, the Commission considers that VCC was not in difficulty on 1 July 2008[13].

(50) Finally, Sweden has expressly committed to ensure that the notified aid will not be cumulated with de minimis aid (point 4.7 of the TF) and to comply with the reporting and monitoring provisions of point 6 of the TF.

(51) The Commission consequently finds that Guarantee A complies with all the conditions in section 4.3 of the TF.

CONCLUSION

(52) For the reasons indicated above, the Commission finds that Guarantee B does not contain state aid within the meaning of Article 107(1) TFEU and that Guarantee A is compatible with the internal market on the basis of Article 107(3)(b) TFEU.

The Commission notes that Sweden accepts the decision to be adopted in the English language. If this letter contains confidential information which should not be disclosed to third parties, please inform the Commission within fifteen working days of the date of receipt.

[12] SEK […] million net cash as per 30 June 2008.

[13] This was already assessed by the Commission in its previous decision (Case N 80/2009, OJ C 172, 24.07.2009). In addition, Sweden has provided evidence that Volvo is not to be considered in difficulty today.

If the Commission does not receive a reasoned request by that deadline, you will be deemed to agree to the disclosure to third parties and to the publication of the full text of the letter in the authentic language on the Internet site:
http://ec.europa.eu/community_law/state_aids/state_aids_texts_sv.htm

Your request should be sent by registered letter or fax to:

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Yours faithfully,
For the Commission

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