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PUBLIC VERSION

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Subject: State aid SA.39958 (2014/N) – Portugal
Third prolongation of the Portuguese Guarantee Scheme on EIB lending

Sir,

1. PROCEDURE

(1) On 27 June 2013 the Commission approved the measure under the Portuguese Guarantee Scheme on EIB lending ("the scheme") by its decision in State aid case SA. 36180 ("the original decision")[1].

(2) On 7 October 2013 the Commission approved an amendment of the scheme by its decision in State aid case SA. 37417 pursuant to which State guarantees granted under the scheme would not trigger the obligation of the beneficiary bank to submit a restructuring plan[2].

(3) On the basis of subsequent notifications, the Commission approved the prolongation of the scheme in its decisions of 17 December 2013 in State aid case SA. 37688[3] and 30 July 2014 in State aid case SA. 38778[4].

[1] OJ C 220, 1.8.2013, p. 3.
[2] OJ C 251, 1.8.2014, p. 4.
[3] OJ C 117, 16.4.2014, p. 25.
[4] OJ C 393, 7.11.2014, p. 9.

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(4) On 26 November 2014 Portugal notified a prolongation of the scheme until 30 June 2015.

(5) For reasons of urgency, Portugal accepts that exceptionally the present decision is adopted in the English language.

2. FACTS

2.1. Description of the scheme

(6) The Scheme is based on Portuguese Law 112/97 of 16 September and Article 103-A of Law 64-B/2011 of 30 December as amended by Law 20/2012 of 14 May 2012. Furthermore, on 7 December 2012 the Republic of Portugal and the European Investment Bank ("EIB") reached an agreement ("Garantia de Carteira") on the terms and conditions of the scheme.

(7) The total budget of the Scheme is EUR 2.8 billion, covering up to EUR 6 billion of existing and new funding from the EIB to the real economy in Portugal.

(8) The ongoing exceptional turbulences in the global financial markets, and, in particular, the sovereign debt crisis that has stricken Portugal over recent years, gave rise to rating downgrades of large parts of the Portuguese financial sector. In response, Portugal brought forward the scheme to preserve on the one hand the stability of the financial system and, on the other hand, to maintain existing lending and to increase future lending from the EIB to the real economy in Portugal.

(9) Currently, the EIB grants loans to undertakings in Portugal ("the final borrowers") either directly, with banks guaranteeing those loans ("the guarantors"), or through intermediary banks which lend on the funds to the final borrowers.

(10) A detailed description of the scheme is provided in the original decision, in particular at recitals 15 to 22.

2.2. Utilisation of the scheme

(11) Regarding the utilisation of the scheme, Portugal submitted a quarterly report of existing guarantees. As of 30 September 2014, they included a set of operations with the maximum guaranteed amount of EUR 3.32 billion.

3. POSITION OF PORTUGAL

(12) Portugal requests a prolongation of the scheme until 30 June 2015, under the same conditions as approved through the previous Commission decisions regarding the scheme.

(13) Portugal reiterates the commitments made at the last prolongation of scheme[5].

(14) Portugal submits that the scheme constitutes State aid within the meaning of Article 107(1) of the Treaty on the Functioning of the European Union ("TFEU"), but is of the view that the proposed prolongation is compatible with the internal market on the basis of Article 107(3)(b) TFEU as it is necessary to remedy a serious disturbance in the economy of Portugal.

(15) Portugal submitted a letter by the Bank of Portugal further supporting the need for the proposed prolongation to safeguard the stability of the financial system in Portugal, because prevailing market conditions do not allow for a termination of the scheme.

(16) Portugal provided information on emissions of debt by Portuguese financial institutions on the international debt market during 2014. They consisted of eight issuances, by five institutions, with maturities of 3 and 5 years, totalling an amount of 5.35 billion EUR. Portugal submits that although those operations constitute a progress in market sentiment of investors towards the Portuguese entities, they do not represent a complete normalization of the financing conditions of the Portuguese banking system and, in particular, the full restoration of its access to capital markets.

(17) In line with the requirements of the 2011 Prolongation Communication[6], Portugal provided an indicative fee (estimation) for each financial institution eligible to benefit from those guarantees. The estimation was based on an application of the scheme's remuneration formula and recent market data.

(18) Portugal submitted its intention to continue to determine the guarantee fee for banks which still have a traded CDS on the basis of the CDS of the sample of Union banks in the "BBB- and lower" rating category, as has been approved through the previous prolongation decision regarding the scheme.

(19) Portugal confirmed that the credit institutions benefiting from the scheme have complied with their obligations in relation to the guaranteed operations, as well as with the payment of the guarantee fee to the Portuguese State.

4. ASSESSMENT

4.1. Existence of State Aid

(20) According to Article 107(1) TFEU, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods

[5] See footnote 4.

[6] Communication from the Commission on the application, from 1 January 2012, of State aid rules to support measures in favour of banks in the context of the financial crisis, OJ C 356, 6.12.2010, p. 7.

shall, in so far as it affects trade between Member States, be incompatible with the internal market.

(21) Although the terms and conditions of the scheme may not give rise to an advantage in relation to new exposures, the scheme is devised as a single mechanism which covers both existing and new exposures of a portfolio of revolving credits. For the reasons indicated in the original decision, the Commission notes that the scheme concerns the provision of State resources to a certain sector, i.e. the financial sector, which is open to intense international competition. The scheme essentially provides the guarantors with an advantage, as it allows them not to post additional collateral in relation to existing exposures but still remain eligible for the purposes of the EIB in guaranteeing new EIB loans. However, Portugal has committed that the participating banks will not retain any advantage from the scheme that could serve to develop other business activities. The banks will either pass the full advantage of the State guarantee to the final recipients of the funds provided by EIB or they will pass the advantage to the Portuguese State.

(22) The measure is selective because it is only open to the financial sector and indeed only to guarantors who have issued or will issue guarantees for funding provided by the EIB. The provision of that advantage to the guarantors is capable of affecting intra-Union trade. As the measure is a scheme covering several elements, and as at least one or some of the elements of the scheme constitutes State aid, the measure therefore involves State aid within the meaning of Article 107(1) TFEU.

4.2. Compatibility of the scheme

4.2.1 Legal basis for the compatibility assessment

(23) Under the scheme Portugal intends to provide aid in the form of guarantees, subject to certain conditions, in favour of the guarantors for the funding granted by the EIB to the final borrowers, either directly or indirectly through banks

(24) Given the exacerbation of tensions in sovereign debt markets that has taken place since 2011 and in light of the persisting circumstances and risks, the Commission considers it appropriate, as confirmed by the 2013 Banking Communication[7], to examine the measure under Article 107(3)(b) TFEU.

(25) Article 107(3)(b) TFEU empowers the Commission to find that aid is compatible with the internal market if it is intended "to remedy a serious disturbance in the economy of a Member State". The Commission has acknowledged that the global financial crisis can create a serious disturbance in the economy of a Member State and that measures supporting banks are apt to remedy that disturbance. That assessment has been confirmed in the Recapitalisation Communication[8] and the

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[7] Communication from the Commission on the application, from 1 August 2013, of State aid rules to support measures in favour of banks in the context of the financial crisis, OJ C 216, 30.7.2013, p. 1.

[8] Commission Communication - Recapitalisation of financial institutions in the current financial crisis: limitation of the aid to the minimum necessary and safeguards against undue distortions of competition, OJ C 10, 15.1.2009, p. 2.

Restructuring Communication.[9] The Commission still considers that the conditions for State aid to be approved pursuant to Article 107(3)(b) TFEU are present. The Commission confirmed that view by adopting the 2013 Banking Communication[10].

(26) The Commission does not dispute the position of the Portuguese authorities that the prolongation of the scheme is necessary for reasons of financial stability and to both maintain and increase EIB lending to critical sectors of the Portuguese economy suffering from an acute credit crunch. Hence, the Commission finds that the scheme aims at remedying a serious disturbance in the Portuguese economy.

(27) Therefore, the Commission continues to base its assessment of State aid measures in the banking sector on Article 107(3)(b) TFEU.

(28) In order for an aid to be compatible under Article 107(3)(b) TFEU, it must comply with the general principles for compatibility under Article 107(3), viewed in the light of the general objectives of the Treaty. Therefore, according to the Commission's case practice[11] any aid or scheme must comply with the following conditions: (i) appropriateness (ii) necessity and (iii) proportionality.

(29) The 2013 Banking Communication and the Restructuring Communication formulate assessment criteria which reflect those general principles and their requirements in light of the specific policy context.

4.2.2 Compatibility assessment of the scheme

Appropriateness

(30) The scheme should be appropriate to remedy a serious disturbance in the Portuguese's economy. The objective of the scheme is to temporarily offer appropriate measures for the Portuguese financial system in a timely and efficient manner, where financial institutions face difficulties in maintaining their eligibility as guarantors vis-à-vis the EIB in the context of the financial crisis and the resulting material credit rating downgrades of Portuguese financial institutions.

(31) Pursuant to point 61 of the 2013 Banking Communication, in exceptional cases the Commission may also approve guarantees covering exposures of the EIB towards banks for the purpose of restoring lending to the real economy in countries with severely distressed borrowing conditions compared to the Union average. In assessing such measures, the Commission examines in particular whether they do not confer an undue benefit that could for example serve to develop other business activities of those banks.

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9 Commission Communication on the return to viability and the assessment of the restructuring measures in the financial sector in the current crisis under the State aid rules, OJ C 195, 19.8.2009, p. 9.

10 See points 4 to 6 of that Communication.

11 See Commission decision of 6.9.2013 in State Aid Case SA.37314 "Rescue aid in favour of Probanka", OJ C314, 29.10.2013, p. 1 and Commission decision of 6.9.2013 in State Aid Case SA.37315 "Rescue aid in favour to Factor Banka", OJ C 314, 29.10.2013, p. 2.

(32) The Commission notes that Portugal has committed to ensure that the guarantors do not retain any undue benefits that could for example serve to develop other business activities of those banks. In addition, the original description of the scheme, recital 17 of the original decision, restrictively defines the elements of the aggregate fee that the guarantors can charge final borrowers.

(33) The scheme is limited to guarantors who have issued or will issue guarantees for funding provided by the EIB.

Necessity

(34) With regard to the scope of the measure, the Commission notes positively that Portugal has limited the size of the guarantee scheme by setting its maximum budget at EUR 2.8 billion and that the scheme applies until 30 June 2015.

(35) Additionally, the State guarantee is issued for a maximum period of seven years and will expire as soon as a guarantor regains credit rating eligibility status for the EIB, whichever happens earlier.

(36) Regarding the remuneration level, the Commission observes that Portugal, in line with point 59(c) of the 2013 Banking Communication, has committed to follow the pricing and other conditions for State guarantees laid down in the 2011 Prolongation Communication which requires, in particular, the application of a pricing method based largely on market data.

(37) For Member States currently or recently subject to a financial assistance programme, it is appropriate to consider the CDS spreads of individual banks located there as temporarily non-representative of the intrinsic risk of those banks, because the respective CDS rates reflect not only the banks' intrinsic risk profile, but also the sovereign risk. This appears to continue to be the case in Portugal for the time being, although recent economic developments indicate a positive outlook for Portugal's sovereign risk and CDS.

(38) On that basis, the Commission does not object to Portugal's intention to continue to determine the guarantee fee for banks which still have a traded CDS on the basis of the CDS of the sample of Union banks in the "BBB- and lower" rating category. The Commission will review its assessment of the macro-economic situation and appropriateness of that exceptional pricing mechanism whenever a further prolongation of the scheme is notified.

Proportionality

(39) The Commission notes that Portugal has committed, in line with point 59(f) of the 2013 Banking Communication, to a number of behavioural safeguards such as a ban on advertisements referring to the State support and a ban on any aggressive commercial strategies which would not take place without the State support. Such safeguards help ensure that the participating institutions do not misuse the received State support to expand their activities.

(40) Finally, the Commission welcomes that Portugal undertakes to submit individual restructuring or liquidation plans, within two months, for banks which cause the guarantee to be called upon, in line with point 59(e) of the 2013 Banking Communication.

(41) As regards the combination of the scheme with other aid measures, the Commission recalls that, as indicated in the Annex to the Restructuring Communication, the restructuring plans to be submitted should contain all State aid received as individual aid or under a scheme during the restructuring period.

(42) Furthermore, based on point 16 of the Restructuring Communication, the Commission recalls that, should further aid not initially foreseen in a notified restructuring plan be necessary for the restoration of viability, such additional aid cannot be granted under an approved scheme but needs to be subject to individual ex ante notification. All State aid measures received by a bank as individual aid or under the scheme during the restructuring period will be taken into account in the Commission's final decision on that bank.

Monitoring

(43) The Commission welcomes, in line with point 60(c) and (d) of the 2013 Banking Communication, that Portugal undertakes to present every three months a report on the operation of the scheme, on guaranteed issuances and on the actual fees charged and to supplement it with updated available data on the cost of comparable non-guaranteed debt issuances (nature, volume, rating and currency).

(44) Portugal has put in place a monitoring system that ensures that participating banks abide by the terms and conditions of the scheme. In particular, if banks retain any additional benefits they will have to pay it back to the State, with interest.

(45) Portugal commits to re-submit the scheme for State aid analysis every six months.

Conclusions on the compatibility of the aid measure

(46) The scheme remains an appropriate, necessary and proportionate measure to remedy a serious disturbance of the Portuguese economy and does not alter the Commission’s previous assessment in the original decision. The notified prolongation therefore complies with the requirements set out above and is compatible with the internal market pursuant to Article 107(3)(b) TFEU.

(47) In line with the Commission’s decisional practice, the scheme can therefore be prolonged until 30 June 2015. Any further prolongation will require the Commission’s approval and will have to be based on a review of the developments in financial markets and the scheme’s effectiveness.

5. CONCLUSION

The Commission has accordingly decided to consider the aid to be compatible with the internal market and not to raise objections to the scheme.

Portugal exceptionally accepts that the present decision be adopted in the English language, for reasons of urgency.

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

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Yours faithfully,
For the Commission

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