European Stability Mechanism

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European Stability Mechanism
Guideline on the Secondary Market Support Facility

Article 1
Objective

1. The Secondary Market Support Facility (SMSF), in accordance with Article 18 of the ESM Treaty, aims to support the good functioning of the government debt markets of ESM Members in exceptional circumstances where the lack of market liquidity threatens financial stability, with a risk of pushing sovereign interest rates towards unsustainable levels and creating refinancing problems for the banking system of the ESM Member concerned. An ESM secondary market intervention is intended to enable market making that would ensure some debt market liquidity and incentivise investors to further participate in the financing of ESM Members.
2. The collaboration between the European Commission and the MD whenever the ESM Treaty or this guideline confers tasks to both of them shall follow the modalities in the Memorandum of Cooperation.

Article 2
Eligibility

1. Access to an SMSF is open to an ESM Member that has entered into a loan facility (as loan is detailed under Article 16 of the ESM Treaty), as long as it continues to comply with the policy conditionality attached to it.
2. Access to an SMSF may be open to an ESM Member that has not entered a loan facility (as loan is detailed under Article 16 of the ESM Treaty), but subject to financial market disruptions, as long as the Member's economic and financial situation remains sound and on the basis of a global assessment, conducted by the European Commission in liaison with the ECB, of the following criteria:
   (a) Respect of the commitments under the Stability and Growth Pact. An ESM Member under excessive deficit procedure may still access a SMSF, provided it fully abides by the Council decisions and recommendations aimed at ensuring a smooth and accelerated correction of its excessive deficit.
   (b) A sustainable general government debt.
   (c) Respect of the commitments under the Excessive Imbalances Procedure (EIP). An ESM Member under EIP may still access a SMSF, provided it is established that the Member remains committed to and capable of addressing the imbalances identified by the Council.
   (d) A track record of access to international capital markets on reasonable terms.
   (e) A sustainable external position.
   (f) The absence of financial institution solvency problems that would pose systemic threats to the stability of the euro area banking system or that of its Member States.

(g) The beneficiary ESM Member shall ensure a continuous respect of the eligibility criteria and adopt where appropriate corrective measures in consultation with the European Commission in liaison with the ECB.

Article 3
Procedure of activation for ESM Members under stability support

1. An ESM Member shall address a request to access the SMSF to the Chairperson of the Board of Governors. On receipt of such a request, the Board of Governors shall entrust:
   (a) The ECB with the task of assessing whether there are exceptional market circumstances and whether there is a risk to the financial stability of the euro area as a whole or of its Member States. The analysis shall be transmitted to the Board of Directors, unless the ECB has already submitted such analysis beforehand upon its own initiative.
   (b) Both (i) the Managing Director and (ii) the European Commission in liaison with the ECB, with the task of confirming compliance with the Memorandum of Understanding ("MoU") before the ESM Member is able to access the SMSF.
2. On the basis of the request of the ESM Member and the assessments conducted under paragraphs 1(a) and 1(b), the Managing Director shall prepare a proposal for a SMSF consistent with the aforementioned assessments and taking into account the financial situation of the ESM. The Board of Governors may then decide to grant, in principle, a SMSF in accordance with Article 13(2) of the ESM Treaty.
3. The Managing Director of the ESM shall prepare a financial assistance facility agreement (FFA) in the form of an SMSF, specifying the financial terms and conditions under which the secondary market purchases are to be conducted, to be adopted by the Board of Governors in accordance with Article 13(3) of the ESM Treaty.
4. The Managing Director shall sign the FFA, subject to approval by the Board of Directors.

Article 4
Procedure of activation for ESM Members which are not under stability support

1. An ESM Member shall address a request to access an SMSF to the Chairperson of the Board of Governors. Upon receipt of such a request, the Board of Governors shall entrust:
   (a) The ECB with the task of assessing whether there are exceptional market circumstances and whether there is a risk to the financial stability of the euro area as a whole or of its Member States. The analysis shall be transmitted to the Board of Directors, unless the ECB has already submitted such analysis beforehand upon its own initiative.
   (b) Both (i) the Managing Director and (ii) the European Commission in liaison with the ECB, together with the task of conducting the assessments provided for in Article 13(1)(b) and Article 13(1)(c) of the ESM Treaty.
2. On the basis of the request of the ESM Member and the assessments conducted under paragraphs 1(a) and 1(b) and Article 2(2), the Managing Director shall prepare a proposal for an SMSF consistent with the aforementioned assessments and taking into account the financial situation of the ESM. The Board of Governors may then decide to grant, in principle, a SMSF in accordance with Article 13(2) of the ESM Treaty.
3. If a decision is adopted pursuant to paragraph 2, the Board of Governors shall, in accordance with Article 13(3) of the ESM Treaty, entrust:
   (a) (i) the Managing Director and (ii) the European Commission in liaison with the ECB, together with the task of negotiating, with the ESM Member concerned, an MoU detailing the policy

conditionality attached to the SMSF. The MoU shall be completed within 2 (two) business days and shall specify the actions needed.

(b) the Managing Director, with the task of preparing a proposal for a FFA, detailing the financial terms and conditions of the SMSF, to be adopted by the Board of Governors.

4. The MoU shall be signed on behalf of the ESM by the European Commission and the Managing Director, subject to prior compliance with the conditions set out in Article13(3) of the ESM Treaty and approval by the Board of Governors. The Managing Director shall sign the FFA, subject to approval by the Board of Directors.

Article 5
Implementation of the SMSF

1. The Board of Directors shall establish pro-tempore intervention caps for the implementation of the facility. A technical sub-committee shall be established to decide on the means of implementation of secondary market interventions under the SMSF. Its composition and operating rules shall be approved by the Board of Directors, acting on a proposal from the Managing Director. Market sensitive decisions are taken in secrecy.
2. The Managing Director shall stop implementing secondary market interventions upon a request of the beneficiary ESM Member.

Article 6
Monitoring and Reporting

1. Both (i) the Managing Director and (ii) the European Commission in liaison with the ECB, together shall be entrusted with monitoring compliance by the beneficiary ESM Member with the policy conditionality specified in the MoU and shall report to the Board of Directors.
2. The technical sub-committee referred to in Article 5(1) shall report on a monthly basis to the Board of Directors on the technical implementation of the facility. The Managing Director shall forward a monthly report to the Board of Governors on the implementation of the SMSF. The report shall be followed with reassessment of the programme, including a decision of the Board of Governors on its continuation.
3. Where necessary, the reports described in paragraph 2 will be made available for the restricted committees in National Parliaments retaining the secrecy of market sensitive information.
4. The Managing Director shall establish an appropriate warning system, in accordance with Article 13(6) of the ESM Treaty, to ensure that the ESM receives any repayments due by the ESM Member under the stability support in a timely manner.
5. In case (a) the assessment in paragraph 1 concludes that the beneficiary ESM Member deviates from its policy conditions or (b) the assessment in paragraph 2 concludes that the SMSF has become inadequate to contain the financial disturbance, the Board of Directors, acting on a proposal from the Managing Director, shall reconsider the adequacy of the SMSF.

Article 7
Management of the portfolio of bonds

1. The bonds purchased under a SMSF can be managed in the following manner:

(a) Can be sold (i) if the bond market of the beneficiary ESM Member has returned to normal functioning and if it is unlikely to reduce the capacity of the ESM Member to lodge its issuances on the primary market, or (ii) to mitigate the risk of realising a loss in relation to its holdings of securities of the ESM Member concerned, irrespective of a possible decision to sell them;

(b) Can be held to maturity;

(c) Can be sold back to the beneficiary ESM Member;

(d) Can be used for repos with commercial banks to support the liquidity management of the ESM.

2. The Managing Director shall propose portfolio investment options to the Board of Directors together with the proposal to disburse provided for in Articles 3(2) and 4(2).
3. The Managing Director shall implement the agreed portfolio management strategy.
4. The beneficiary ESM Member shall be informed about the implementation of the strategy. It shall approve the conduct of operations under paragraph 1(a) in case they would create any liability for the concerned ESM Member, unless the ESM were to face a significant risk of realising a loss in relation to its holding of securities of the ESM Member concerned, irrespective of a possible decision to sell them.