AXIS BANK

# EURO SUMMIT STATEMENT: KEY TAKEAWAYS

The EFSF would support Sovereign debt and Bank recapitalization in any of the following ways:
(a) Provision of Risk insurance of the bonds issued by member states in the primary market . The exact %'age of first loss to be borne by EFSF to be specified in the November Summit
(b) Funding for the EFSF would be a mix of Private and Public sources arranged through SPV's. The nature of leverage and uses of the fund would be decided on a need based approach / response to specific market situations.

- The Eurogroup "invites" bond holders to take a 50% haircut on Greek debt voluntarily.
July saw all bondholders take a voluntary haircut of 21% on Greek bonds and the IIF and the Determination Committee of ISDA agreed that since 90% of all Greek bondholders acquiesced, this should not be construed to be a credit event and forestalled triggering of CDS contracts written on the Hellenic state. This "invitation" in October now will have been issued after taking the IIF and DC, ISDA on board. Bondholders have really no choice as most Greek bonds are trading at 30-40 cents on the dollar. The haircut is actually an accounting treatment which will make it mandatory for all bondholders to disclose their losses officially on their Balance sheets at 50% haircut, which is better for market transparency as these were being marked down only by 21% hitherto.

- The IMF has been sounded out to try and arrange for some resources that could possibly be used to augment resources for the EFSF.
It is very ironic that the IMF that is headed by the ex-FM of France cannot till date "find" adequate resources to augment the EFSF. This shows to what extent the IMF is controlled by the US which has refused to "throw more good money to recover bad money". G20 which includes the BRICS has also steadfastly refused to have anything to do with what is being viewed as an extraordinary demand on the scarce resources of careful and thrifty peoples for the benefit of maintaining expensive lifestyles of highly leveraged people.
The EFSF capital after providing for Greece and Banking recap is Euro 200 Bio. The document specifically mentions a leverage of 4-5 for the EFSF. That translates into a funding of close to Euro 1 Trillion.

- Banks have been told to achieve a Tier 1 Capital of 9% of Risk weighted assets by 30 June 2012 after accounting for sovereign debt write-downs as on 30 Sep 2011. Banks should first use private sources of capital, the absence of which should direct them to their respective national governments. If EU Nations are unable to help their banks, an application should be made to the EFSF which would arrange for the loanable funds available on conditions. The EBA should ensure that excessive deleveraging in Banks due to the above target does not cause a severe restriction of credit in EU states. Banks have been told to constrain bonus payments and dividends until this target is reached.

Note the jarring dichotomy between the two dates in the first sentence above. This, the statement reveals, is justified due to the "exceptional circumstances".

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The IMF could help the EFSF by either contributing capital or by investing in the bonds issued by the EFSF. Participation in capital would be most beneficial because every dollar of increase in capital increases the size of the total fund by 4-5 dollars. However if that is not possible, the IMF could help by buying EFSF bonds along with private investors- that would keep yields lower than if the IMF were to be absent totally.

The 9% Tier 1 capital by 30 June 12 based on sovereign debt write-downs as on 30 Sep 11 is another example of how EU zone policy makers are going down the same road taken by Japan and the US of saving their banks at the cost of severely constraining credit to the deserving sectors of the economy in order to justify throwing good money after bad credit decisions of the past. We have been calling for the clear demarcation of bad assets into one single "Bad Bank" which will have separate recovery targets and capitalization. The rest of the "good banks" should function better with wiser credit targeting and allocation without the haunting fear of the ghosts of the past which irrationally constrains credit even to deserving candidates. We say this out of the experience of Sweden, China and Ireland. Notifying EBA to ensure that a credit-choke does not occur with Banks trying to achieve their June 30 2012 targets will not help because managers and shareholders in their mistaken zeal to reopen variable pay/dividend spigots will try and beat the June 30 2012 deadline to an earlier date.

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