~FACTSHEET~
European Stability Mechanism

The Treaty establishing the European Stability Mechanism (ESM) has been ratified by all 17 euro area member states. It entered into force on 27 September 2012, nine months earlier than initially foreseen[1]. The treaty was signed by euro area member states on 2 February 2012. The ESM board of governors held its inaugural meeting on 8 October 2012.

The ESM is an intergovernmental institution based in Luxembourg, set up to provide financial assistance to eurozone member states experiencing, or being threatened by, severe financing problems, if this is indispensable for safeguarding financial stability in the euro area as a whole. The initial maximum lending capacity of the ESM is set at €500 billion. This is achieved with subscribed capital of €700 billion (€ 80 billion paid-in capital, the rest callable).

A first version of the treaty was signed on 11 July 2011, but it was subsequently modified to incorporate decisions taken by the heads of state and government of the euro area on 21 July and 9 December 2011 to improve the effectiveness of the mechanism.

As a permanent mechanism, the ESM will take over the tasks currently fulfilled by the European Financial Stability Facility (EFSF) and the European Financial Stabilisation Mechanism (EFSM). With the accelerated entry into force, the ESM will now operate alongside the EFSF for nine months.

In March 2012, the Eurogroup agreed to raise the overall ceiling for ESM/EFSF lending to €700 billion[2]. Already during the transitional period, until mid-2013, the ESM will be the main instrument for the financing of new programmes. While the EFSF will, as a rule, only remain active in financing programmes that were started before the ESM entered into force, it may engage in new programmes in order to ensure a full fresh lending capacity of €500 billion.

The effective lending capacity of the ESM will be built up gradually, as the required paid-in capital is transferred to the ESM by its members. The heads of state and government of the euro area agreed in March 2012 that the first two tranches of capital (€16 billion each) should be paid in 2012, followed by two tranches in 2013 and a final tranche in the first half of 2014. The schedule for capital payments can be accelerated if required to maintain a 15% ratio between the paid-in capital and the outstanding amount of ESM issuances.

The ESM offers the same financing instruments as the EFSF. These include loans (article 16), precautionary financial assistance (article 14), loans to member states for recapitalisations of financial institutions (article 15), as well as primary and secondary bond market purchases (articles 17 and 18). Maturities can extend up to 30 years.

ESM assistance will be provided under strict economic policy conditionality. Moreover, as of 1 March 2013, member states must have ratified the so-called "fiscal compact", i.e. the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union, in order to qualify for ESM assistance (recital 5). One year after the latter enters into force (the target date is 1 January 2013), they must comply with an additional condition, namely the timely transposition of the balanced budget rule in their national legislation.

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[1] the treaty had initially been set to enter into force in July 2013.
[2] http://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/ecofin/129381.pdf

The ESM will have a board of governors and a board of directors, as well as a managing director. Klaus Regling, the chief executive officer of the EFSF, was appointed by the Eurogroup in July 2012 as managing director of the ESM.

The most important decisions under the ESM will be taken by its board of governors (finance ministers) by mutual agreement. The ESM treaty provides for an emergency procedure whereby a decision to grant financial assistance can be taken by a qualified majority of 85% of votes cast. This procedure can be used if both the Commission and the European Central Bank conclude that a failure to urgently adopt such a decision would threaten the economic and financial sustainability of the euro area. When this procedure is used, "a transfer from the reserve fund and/or the paid-in capital to an emergency reserve fund is made in order to constitute a dedicated buffer to cover the risks arising from the financial support granted under this procedure" (article 4(4)).

The ESM will cooperate closely with the International Monetary Fund (IMF) in providing stability support. The active participation of the IMF will be sought, in both technical and financial terms. The treaty also requires collective action clauses to be included, as of 1 January 2013, in all new euro area government securities with maturities above one year (recital 11 and article 12(3)).

For ESM Treaty:
http://www.eurozone.europa.eu/media/582311/05-tesm2.en12.pdf