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Poland: Guarantee Scheme

Manuel Leon Hoyos

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Poland: Guarantee Scheme

Manuel León Hoyos[1]

January 16, 2019

Abstract

Faced with the Global Financial Crisis (2007-2009), Poland implemented a scheme of State support to financial institutions. In view of a potential global credit crunch, it aimed at improving short- and medium-term liquidity of domestic financial institutions. The scheme came into force on March 13, 2009 and was approved by the European Commission under EU State aid rules on September 25, 2009. It enabled the Ministry of Finance, on behalf of the State Treasury, to provide support in the form of Treasury guarantees on newly issued bank debt and the exchange of Treasury bonds for less liquid assets. This case examines exclusively Treasury guarantees. Initially, only domestic banks, including subsidiaries of foreign financial institutions, could apply for guarantees. In 2011, eligibility was expanded to include cooperative savings and credit institutions and the National Cooperative Savings and Credit Institution (NCSCI). An initial overall cap of PLN 40 billion ($13.7 billion) was set before being raised to PLN 160 billion ($54.8 billion) in 2012. The European Commission has approved eighteen prolongations of the scheme—the last in July 2018. As of April of 2018, no institutions had applied for coverage and the issuance window was set to expire on November 30, 2018.

Keywords: Poland, financial crisis, financial institutions, State aid, guarantee, liquidity

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[1] Research Associate, Yale Program on Financial Stability. manuel.leonhoyos@yale.edu.

Poland: Guarantee Scheme

At a Glance

Faced with the Global Financial Crisis (2007-2009), Poland implemented a scheme of State support to financial institutions. In view of a potential global credit crunch, it aimed at improving short- and medium-term liquidity in the interbank market. The scheme came into force on March 13, 2009 and was approved by the European Commission, consistent with EU State aid rules, on September 25, 2009.

The scheme enabled the Ministry of Finance, on behalf of the State Treasury, to provide support to solvent financial institutions in the form of Treasury guarantees on newly issued bank debt and the exchange of Treasury bonds for less liquid assets. This case examines exclusively the Treasury guarantees component of the scheme.

Initially, eligibility for Treasury guarantees was restricted to domestic banks, including subsidiaries of foreign financial institutions. In 2011, guarantees were expanded to include cooperative savings and credit institutions and the National Cooperative Savings and Credit Institution (NCSCI).

Summary of Key Terms	
Purpose: To facilitate short- and medium-term liquidity in the interbank market to solvent financial institutions in Poland.	
Announcement Date	November 30, 2008
Operational Date	March 13, 2009
Date of First Guaranteed Loan Issuance	N/A
Issuance Window Expiration Date	Initially December 31, 2009; after 18 extensions November 30, 2018
Program Size	Initially PLN 40 billion ($13.7 billion); increased in 2012 to PLN 160 billion ($54.8 billion).
Usage	None
Outcomes	N/A
Notable Features	

An initial overall cap of PLN 40 billion [$13.7 billion] was set before being increased to PLN 160 billion ($54.8 billion) in 2012. There were no individual caps on a given bank's participation and the scheme had no currency restrictions. Treasury guarantees were limited to newly issued commercial bank senior debt and explicitly excluded subordinated debt. Eligible maturities ranged from three months to three years (in special cases five years). The fees varied based on the maturity of the debt and soundness of the issuing bank or institution. Initially, the fees were based on the 2008 European Central Bank Recommendations, but in 2010 the European Commission increased the fees to reflect downgrades in the creditworthiness of financial institutions.

The European Commission has approved eighteen prolongations of the scheme of six months each (the last one in July 2018). As of April of 2018, no institutions had applied for coverage and the issuance window was set to expire on November 30, 2018.

Summary Evaluation

No institutions have applied for coverage under the scheme. Polish authorities stated that "[the scheme] should remain in place as it has a positive effect on credit institutions and their clients. More specifically, it ensures stability of the Polish financial sector, which still faces the increased volatility of global financial markets and the uncertainty related to the extent and pace of the economic recovery. Therefore, in order to avoid any negative spill-over effects to the financial sector, the scheme should remain available."

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7. Only solvent institutions were allowed to benefit from the scheme. 5
8. Treasury guarantees were limited to commercial bank senior debt and explicitly excluded subordinated debt. 5
9. Debt with maturities ranging from three months to three years (in special cases five years) could be issued with Treasury guarantees. 5
10. The scheme had no currency restrictions. 5
11. There were no individual caps on a given bank's participation. 5
12. The fees for guarantees varied based on the maturity of the debt and the soundness of the issuing bank or institution. 5
13. Polish authorities agreed to ban advertisements referring to the support provided by the State Treasury. 6
14. The issuance window for the scheme was initially December 31, 2009. After 18 prolongations of six months each, the current expiration date is November 30, 2018. 6

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I. Overview

Background

The Global Financial Crisis (2007-2009) restricted liquidity to financial institutions around the world as confidence in counterparties weakened. Poland was the only EU member state not to face recession in 2009. (IMF 2010). However, given Poland's links within the EU, and the fact that the majority of the banks in Poland are subsidiaries of EU entities, the Polish financial sector remained exposed to financial risks.

In order to strengthen Poland's economy in view of a potential global credit crunch, on November 30, 2008, the government of Poland announced the "Stability and Development Plan" (*Plan Stabilności i Rozwoju*) consisting of a series of anti-crisis initiatives totaling PLN 91.3 billion ($32.2 billion)[2]. (NBP 2009). Some of the initiatives included:

- Stimulating both consumption and investment by providing tax cuts and speeding up investments co-financed with EU funds.
- Maintaining liquidity of financial institutions by facilitating Treasury guarantees on newly issued bank debt and the exchange of Treasury bonds for less liquid assets.
- Ensuring sustainability in public finances by limiting the level of the budget deficit.
- Strengthening small- and medium-sized enterprises by facilitating loans.
- Alleviating distress of the unemployed by providing assistance on mortgage payments.

In addition to the Plan, the Polish government:

- Established the Financial Stability Committee, composed of the Ministry of Finance, the National Bank of Poland and the Polish Financial Supervision Authority.
- Increased deposit insurance from € 22,500 to € 50,000.
- Adopted an "Anti-crisis Package" negotiated with labor unions and employers aimed at preserving employment. It contained measures such as wage subsidies, flexible working hours, elimination of certain taxes, and increases in the minimum wage.

As envisioned in the Plan, on February 12, 2009, the Parliament of Poland passed the Act on State Treasury support to financial institutions which aimed at reinforcing the stability of Polish financial markets[3]. The Polish President signed the bill on February 25, 2009 and the scheme ("support scheme" or "Law on support") came into force on March 13, 2009.

[2] The November 2008 monthly average NPB exchange rate was 1 Dollar = 2.92 PLN.
[3] Journal of Laws No. 39, item 308.

The European Commission approved it on September 25, 2009, as consistent with EU State aid rules[4] [5].

The scheme enabled the Ministry of Finance, on behalf of the State Treasury, to facilitate short- and medium-term financing needs of solvent institutions by providing support in the form of Treasury guarantees and Treasury bonds. This case focuses exclusively on the Treasury guarantee component of the scheme.

Program Description

The issuance window to benefit from the scheme was restricted by the European Commission to a period of six months. Any further prolongations would have to be notified to the Commission in due time. (EC 2009).

The Ministry of Finance, on behalf of the State Treasury, would guarantee the institutions' new issuance of debt in exchange for a fee and collateral[6]. The guarantees included only commercial bank senior debt and explicitly excluded subordinated debt. There were no currency restrictions. (EC 2009).

Treasury guarantees would cover debt with maturities ranging from three months to three years. Only in justified cases could maturities up to five years be guaranteed. Debt guaranteed by the State Treasury with maturities exceeding three years would be restricted to a maximum of ⅓ of the value of all guaranteed debt of the particular beneficiary. (EC 2009).

The overall cap for the scheme in State Treasury guarantees was initially set to PLN 40 billion[7] and increased to PLN 160 billion in 2012[8]. (EC 2012b). There were no individual caps on a given bank's participation.

Participation in the scheme was voluntary and guarantees were available only to solvent institutions that met Polish capital and solvency requirements. Initially, only domestic banks could apply for guarantees. In 2011, eligibility was extended to include cooperative

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[4] The scheme contained EU State aid elements compatible with the EU common market as "necessary to remedy a serious disturbance in the Polish economy" within the meaning of Articles 107(1) and 107(3)(b) of the Treaty of Functioning of the European Union (TFEU) .

[5] The European Commission received notification of the scheme on April 7, 2009. On May 15, the Commission requested additional information from Poland. On June 8, Polish authorities requested a deadline extension which was approved on June 12. Poland provided additional information on June 26. On August 19, the Commission requested further information which Poland provided on September 11.

[6] Collateral would cover the full amount of the support including interest. Additional collateral would be needed if the collateral provided decreased in value or did not cover the entire amount of the liability and incidental receivables.

[7] According to the State budget adopted for 2009, the limit of all State Treasury guarantees (including outside of the scheme) was PLN 40 billion.

[8] The Polish budgetary law for 2012 increased the total limit for State Treasury guarantees to PLN 200 billion. This have justification for an increase in the budget available under the scheme.

savings and credit institutions and the National Cooperative Savings and Credit Institution (NCSCI). (EC 2011).

The terms of the guarantee fees were not addressed in the Polish Law on State Treasury support to financial institutions. The initial fees were based on the 2008 European Central Bank Recommendations (ECB 2008).

For short-term debt with maturities of less than or equal to one year, the fee would be an overall flat fee of 50 basis points, paid ex ante.
For medium-term debt with maturities exceeding one year, the fee would equal an add-on fee of 50 basis points, plus the following:

1) A fee based on the bank's credit default swap (CDS) spreads.
2) For banks without CDS data but with a credit rating, an equivalent CDS spread would be derived from the rating category of the bank, based on a representative sample of Euro-area banks.
3) For banks without CDS data and without a credit rating, an equivalent CDS spread would be derived from relevant data from the lowest rating category (but now lower than A), based on a representative sample of Euro-area banks. (EC 2009).

In 2010, the fees were increased. The European Commission stated that downgrades in banks' credit status since 2008 were not taken into account in existing fees. Therefore, the fees should be brought closer to market conditions reflecting individual banks' creditworthiness. This required the fees to be increased by at least 20 basis points for banks with the rating of A+ or A; 30 basis points for banks rated A-; and 40 basis points for banks rated below A-. Banks without rating would be considered to belong to the category of banks with a BBB rating. (EC 2010a, EC 2010b).

From 2012, the government of Poland provided a table with indicative fees (estimates) for eligible financial institutions based on the formula provided in the 2011 Prolongation Communication and using recent market data. (EC 2012, Appendix B).

For institutions that default on their liabilities or have their guarantees called, Polish authorities committed to file individual restructuring or liquidation plans within a period of six months. (EC 2009).

Poland committed to behavioral safeguards such as a ban on advertisements or any aggressive commercial strategies referring to the State support. Polish authorities indicated that they would consider further restrictions during the guarantee period such as on dividend payments, bank executives´ severance packages, bonus payments, wage increases and board remuneration. (EC 2009).

Outcomes

Originally, the issuance window of the scheme was set to expire on December 31, 2009. The European Commission has approved eighteen prolongations of the scheme for six months each, with the last one in July 2018. As of April 2018, no institution had applied for coverage under the scheme and the current issuance window was set to expire on November 30, 2018. (EC 2018a, EC 2018b).

II. Key Design Decisions

1. The Treasury guarantees for newly issued debt was one component of the scheme of State support introduced in March 2009.

In response to the Global Financial Crisis, on November 30, 2008, the government of Poland announced the "Stability and Development Plan" (*Plan Stabilności i Rozwoju*) which consisted of a series of anti-crisis initiatives totaling PLN 91.3 billion. Some of the initiatives included:

- Stimulating both consumption and investment by providing tax cuts and speeding up investments co-financed with EU funds.
- Maintaining liquidity of financial institutions by facilitating Treasury guarantees on newly issued bank debt and Treasury bonds in exchange for less liquid assets
- Ensuring sustainability in public finances by limiting the level of the budget deficit.
- Strengthening small- and medium-sized enterprises by facilitating loans.
- Alleviating distress of the unemployed by providing assistance on mortgage payments.

In addition to the Plan, Poland raised deposit insurance from € 22,500 to € 50,000. The Polish government adopted an "Anti-crisis Package" negotiated with labor unions and employers aimed at preserving employment. It contained measures such as wage subsidies, flexible working hours, elimination of certain taxes, and increases in the minimum wage.

As envisioned in the Plan, the scheme of government support to financial institutions came into force on March 13, 2009. The scheme enabled the Ministry of Finance, on behalf of the State Treasury, to provide support in the form of Treasury guarantees on newly issued debt and the exchange of Treasury bonds for less liquid assets.

2. The Act on State Treasury of February 12, 2009, passed by the Polish Parliament, established the scheme.

The Parliament of Poland passed the Act on State Treasury support to financial institutions on February 12, 2009 (Journal of Laws No. 39, item 308, as amended). The Polish President signed the bill on February 25, 2009 and the scheme ("support scheme" or "Law on support") came into force on March 13, 2009.

3. In accordance with EU State aid rules, the scheme required European Commission approval to be implemented.

Poland notified the European Commission of the scheme on April 7, 2009. The Commission approved the scheme on September 25, 2009 and has since approved eighteen prolongations—the last one in July 2018. The current expiration date is November 30, 2018.

4. The scheme was administered by the Ministry of Finance, on behalf of the State Treasury.

5. An initial overall cap of PLN 40 billion was set for guarantees before being raised to PLN 160 billion in 2012.

6. Initially, eligibility to apply for Treasury guarantees was restricted to domestic banks, including subsidiaries of foreign financial institutions.

Polish authorities indicated that this eligibility standard was established "in order to give special treatment to banks since they conduct operations consisting mainly of acceptance of deposits and granting loans, which are considered to be activities with pivotal importance for the correct functioning of the economy." (EC 2009).

In 2011, Treasury guarantees became accessible to cooperative savings and credit institutions and the National Cooperative Savings and Credit Institution (NCSCI). Under EU law, cooperative savings and credit institutions constitute credit institutions. Polish authorities stated that these institutions provide services similar to banks and recent changes in domestic legislation had increased their significance. The greater supervision allowed them to issue bonds.

7. Only solvent institutions were allowed to benefit from the scheme.

Polish authorities would make sure that eligible financial institutions fulfilled adequate legal provisions such as concentration limits, value of net assets, solvency margin, and maintenance of a liquid reserve.

8. Treasury guarantees were limited to commercial bank senior debt and explicitly excluded subordinated debt.

9. Debt with maturities ranging from three months to three years (in special cases five years) could be issued with Treasury guarantees.

10. The scheme had no currency restrictions.

11. There were no individual caps on a given bank's participation.

12. The fees for guarantees varied based on the maturity of the debt and the soundness of the issuing bank or institution.

The terms of the fees were not addressed in the Polish Law on support and were based on the 2008 European Central Bank Recommendations (ECB 2008).

For short-term debt with maturities of less or equal than one year, the fee would be an overall flat fee of 50 basis points, paid ex ante.

For medium-term debt with maturities exceeding one year, the fee would equal an add-on fee of 50 basis points, plus the following:

1) A fee based on the bank's credit default swap (CDS) spreads.
2) For banks without CDS data but with a credit rating, an equivalent CDS spread would be derived from the rating category of the bank, based on a representative sample of Euro-area banks.
3) For banks without CDS data and without a credit rating, an equivalent CDS spread would be derived from relevant data from the lowest rating category (but now lower than A), based on a representative sample of Euro-area banks.

In 2010, the European Commission increased the fees in view of downgrades in credit worthiness of banks. These were increased by at least 20 basis points for banks with the rating of A+ or A; 30 basis points for banks rated A-; and 40 basis points for banks rated below A-. Banks without rating would be considered to belong to the category of banks with a BBB rating.

From 2012, Poland provided a table with indicative fees (estimates) for eligible financial institutions based on the formula provided in the 2011 Prolongation Communication and using recent market data (See Appendix B).

13. Polish authorities agreed to ban advertisements referring to the support provided by the State Treasury.

Poland committed to behavioral safeguards such as a ban on advertisements or any aggressive commercial strategies referring to the State support. Polish authorities indicated that they would consider further restrictions during the guarantee period such as on dividend payments, wage increases, bonus payments, board remuneration and bank executives´ severance packages. These safeguards would help ensure that participating institutions did not misuse the received State support to expand their activities.

14. The issuance window for the scheme was initially December 31, 2009. After 18 prolongations of six months each, the current expiration date is November 30, 2018.

III. Evaluation

There have been no formal evaluations of the scheme. Even if no institution applied for coverage under the scheme, Polish authorities have stated that "[the scheme] should remain in place as it has a positive effect on credit institutions and their clients. More specifically, it ensures stability of the Polish financial sector, which still faces the increased volatility of global financial markets and the uncertainty related to the extent and pace of the economic recovery. Therefore, in order to avoid any negative spill-over effects to the financial sector, the scheme should remain available." (EC 2010c).

The European Commission has indicated that "even if the scheme has not been put into effect so far, the Commission would accept that the existence of the schemes without banks actually making use of it contributes to the stability of the financial markets because it provides a safety net for the financial sector by ensuring the access to liquidity in case of urgency." (EC 2009).

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VI. Appendices

Appendix A: Prolongations of the Scheme

Status	Date of Approval	State Aid Case
Scheme	September 25, 2009	N208/2009
1st Prolongation	February 9, 2010	N 658/2009
2nd Prolongation	June 29, 2010	N 236/2010
3rd Prolongation	December 16, 2010	(SA.31923) N 533/2010
4th Prolongation	June 28, 2011	(SA.33008) (SA.32946)
5th Prolongation	February 8, 2012	(SA.34081)
6th Prolongation	July 9, 2012	(SA.34811)
7th Prolongation	January 29, 2013	(SA.35944)
8th Prolongation	July 23, 2013	(SA.36965)
9th Prolongation	February 3, 2014	(SA.38023)
10th Prolongation	July 29, 2014	(SA.39015)
11th Prolongation	January 27, 2015	(SA.40096)
12th Prolongation	August 24, 2015	(SA.42560)
13th Prolongation	February 1, 2016	(SA.43924)
14th Prolongation	July 1, 2016	(SA.45575)
15th Prolongation	December 19, 2016	(SA.46871)
16th Prolongation	July 5, 2017	(SA.48227)
17th Prolongation	December 7, 2017	(SA.49404)
18th Prolongation	July 11, 2018	(SA.51235)

The European Commission declared them compatible with the TFEU.

Appendix B: Fees[9]

Indicative Fees - Fifth Prolongation

- **An indicative fee (estimate) for guarantees covering debt with a maturity of one year or more for financial institutions envisaged, given certain conditions, to be eligible for the scheme, based on an application of the formula indicated in point 11 using recent market data.[13]**

A. For the banks with an external rating

Bank name	Guarantee fee (in bp)
Powszechna Kasa Oszczędności Bank Polski SA – PKO BP S.A.	[70-90]*
Pekao Bank Hipoteczny S.A.	[70-90]
ING Bank S.A.	[70-90]
Getin Noble Bank S.A.	[90-110]
Credit Agricole Bank Polska S.A.	[90-110]
BRE Bank Hipoteczny S.A	[90-110]
Bank Zachodni WBK S.A.	[70-90]
Bank Ochrony Środowiska S.A.	[90-110]
Bank Gospodarstwa Krajowego	[70-90]
Bank Gospodarki Żywnosciowej S.A.	[90-110]
Bank BPH S.A.	[90-110]
Bank Millennium	[90-110]
Kredyt Bank S.A.	[70-90]
BRE Bank S.A.	[70-90]
Bank Handlowy w Warszawie S.A.	[70-90]
Bank Polska Kasa Opieki SA-Bank Pekao S.A.	[70-90]

B. For the banks without any external rating or CDS data

An indicative fee (estimate) for financial institutions, which are not listed in the table above and which do not have any CDS data or an external credit rating, calculated in line with the 2011 Prolongation Communication was determined to be [90-110] **bp.**

[13] For the purpose of the estimation of the fees applicable under the scheme, 30 December 2011 was set as the cut-off date. Therefore, the reference period is 30/11/2008-30/11/2011. For that period following parameters of the formula were derived:

- (parameter A) The median value of five-year CDS spreads for the rating category of the bank concerned, based on a representative sample of large banks in the Member States in the relevant rating bucket, e.g. sample of A-rated ("A-rating bucket") or BBB-rated or below banks ("BBB-rating or below"). The derived value for the banks of the A-rating bucket is [125-150] bp, for the banks of the BBB-rating and below bucket: [325-350] bp;
- The median iTraxx Europe Senior Financials five-year index (parameter B): 134.7 bp;
- The median five-year senior CDS spread of all Member States (parameter C): 121.7 bp;
- The median five-year senior CDS spread of Poland (parameter D): 145.4 bp.

Based on the above data, the fee applicable for the banks with the reference rating A is [70-90] bp, for the banks rated BBB or below or without any external rating, the fee applicable under the scheme is estimated at [90-110] bp.

* Confidential information

[9] Subsequent prolongations of the scheme contain a similar chart with updated indicative fees reflecting recent market data.