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**Christine LAGARDE,**
Minister for the Economy, Industry and Employment

# France's plan for ensuring the financing of the economy and restoring confidence

Monday, October 13, 2008

*Press kit*

The Prime Minister has submitted an amended budget bill designed to restore confidence in the banking and financial system, and to ensure adequate financing for the French economy.

The measures included in the bill will have no direct impact on the budget. However, the Constitutional Bylaw on Budget Acts *(Loi Organique Relative aux Lois de Finances)* makes a budget act mandatory for State guarantees to be established.

These measures are part of the concerted plan of action agreed to by eurozone Member States and announced by President Sarkozy on October 12th.

They will enable the State to ensure the continuity and efficiency of the arrangements through which private individuals, businesses and local governments obtain funding by providing banks with both the medium-term resources they need and the capital required to restore confidence in the industry.

The State may henceforth offer a guarantee at commercial rates of up to 360 billion euros (320 billion euros + 40 billion euros) on new loans granted by a fund for refinancing credit institutions and by a State company for investment in financial institutions, as well as on loans by companies in the Dexia Group, pursuant to the agreement signed with the governments of Belgium and Luxembourg.

Financial institutions that wish to benefit from these arrangements must undertake to finance the real economy and pledge that they and their executive officers will comply with a code of ethics that serves the general interest, whether on the basis of a formal agreement with the State or of conditions attached to recapitalization.

Because the aim of this State intervention is to restore confidence, it will be temporary in nature.

The Minister for the Economy, Industry and Employment has set forth the specifics of the new arrangements and the conditions under which the guarantee will be granted.

### *Inject liquidity into the banking system to finance the economy*

To ensure that the financing needs of households and businesses are met, the amended bill provides for the establishment of a new system to guarantee the refinancing of medium-term debt (maturities of up to five years) for French banks. This measure supplements the short-term bank refinancing support provided by the central bank.

A refinancing fund closely supervised by the State and the Banque de France shall be authorized to seek financing in the capital market, backed by an explicit State guarantee. Any financial institution operating in France may borrow money through the fund, provided it furnishes collateral in the form of loans to the economy.

Under the amended bill, the financial institutions that wish to benefit from these arrangements guaranteed by the State must sign an agreement with the State that sets the conditions they are to fulfill.

The State guarantee shall be provided at commercial rates, so that the beneficiaries shall obtain such financing on an arm's length basis. It shall remain in force until December 31, 2009.

### *Provide financial institutions with sufficient capital*

Recapitalizing the banks was identified at the latest international meetings as a prerequisite for restoring confidence.

And although France's banks amply comply with European solvency requirements, the amended bill will empower a State-owned company to subscribe for subordinated debt issues and preference shares. This will give the banks the greater resources they need to restore confidence and provide the economy with a normal level of financing.

As with the liquidity injection provision, the State will set the eligibility conditions in such a way as to ensure that the resulting increase in bank capital is effectively used to finance the economy and that the beneficiaries comply with a code of ethics serving the general interest.

This measure comes in addition to the Government's commitment to subscribe as needed for new share issues in order to stabilize financial institutions faced with difficulties. Such equity investments will be carried out by the same State company, and under conditions that allow it to influence the beneficiary's turnaround strategy and to replace the existing management if it sees fit.

### *Validation of the guarantees provided by the State to secure the financial system*

En lien avec the measures described above, the amended budget bill provides for the validation of the three guarantees provided by the State:

- The guarantee covering the new arrangements created by the bill for refinancing financial institutions.
- The guarantee provided to enable the State investment company to increase or stabilize the capital of financial institutions.
- The guarantee covering Dexia's interbank transactions, in accordance with the terms set forth in the intergovernmental agreement signed on October 8, 2008 with Belgium and Luxembourg.

### *Budget outturn in 2008*

The Minister for the Budget, Public Accounts and the Civil Service has summarized the budget outturn in the amended budget bill, which is in line with the forecast for 2008 released when the budget bill for 2009 was submitted. The deficit for 2008 should reach an estimated €49.4 billion, a figure €7.7 billion euros higher than planned in the initial 2008 budget bill. Three main factors should be mentioned in this connection:

- An estimated €5 billion decrease in tax revenue.
- A €4 billion increase in debt service, due in particular to a higher-than-anticipated inflation rate.
- A €1.3 billion improvement in other budget items (most notably non-tax revenue and special accounts).

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# Call to a financial center meeting on accounting standards

Christine Lagarde has asked the *Conseil National de la Comptabilité* (National Accounting Board) and the three financial supervisory authorities in France—the *Autorité des Marchés Financiers*, the *Commission bancaire* and the *Autorité de Contrôle des Assurances et des Mutuelles*—to call a financial center meeting with the *Compagnie Nationale des Commissaires aux Comptes* (National Organization of Statutory Auditors). The meeting will be held at the offices of the *Autorité des Marchés Financiers* on Tuesday, October 14, 2008.

In light of recent statements by the International Accounting Standards Board (IASB), the Securities and Exchange Commission (SEC) and the Financial Accounting Standards Board (FASB) in the U.S., this meeting will focus on the accounting treatment for certain financial instruments that the current market turmoil has made it impossible to value reliably.

The aim is to provide the necessary clarification on how to close the books (including for the September 30, 2008 balance sheet date) based on currently applied accounting standards. This must be seen as part of an overall drive toward European convergence and transparency, particularly since similar efforts are under way elsewhere in Europe, most notably in Germany.

This pragmatic, cooperative approach by the four financial industry supervisory authorities is closely related to the measures decided on by France to enhance confidence in the banking and financial system, and to ensure that the French economy operates smoothly and consistently with the latest initiatives taken by the EU and the G7.

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# Measures for recapitalizing French financial institutions

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| *Objective* | Recapitalize France's financial institutions to restore confidence in the financial system.<br>If need be, acquire a stake in a troubled bank whose failure would create a systemic risk. |
| *Legislation* | - Provide a State guarantee on issues by the State investment company. |
| *Timetable for voting on the bill* | - The bill will be submitted to the Council of Ministers on Monday, October 13.<br>- It will then be submitted to Parliament using the fast-track procedure. |
| *Regulations* | - Implementation does not require any additional regulations. |
| *Term of the company* | - Of unlimited duration, although its activities are meant to be temporary. |
| *Control of the investment company* | - The State shall be the sole shareholder in the company.<br>- Its executive officers shall be appointed by decree.<br>- For each guaranteed financing transaction, a decision by the Minister for the Economy shall specify the guarantee term and ceiling. |
| *Conditionality* | - The State may require commitments from the financial institutions that take advantage of the new arrangements, such as commitments to a specified volume of lending to the economy, and compliance by such institutions and their officers with a code of ethics that serves the general interest. |
| *Use of the company's resources* | - The company shall subscribe for securities representing Tier 1 capital of financial institutions. |

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| *Types of securities that the company may subscribe for* | - When increasing the capital of banks to raise confidence, the company may subscribe for hybrid securities, preference shares accepted as Tier 1 capital for financial institutions.<br>- When supporting a troubled bank, the company may subscribe for ordinary shares and securities conferring entitlement to equity. In any event, ownership of said securities shall give the State special rights in relation to the issuer and its officers. |
| *Eligible institutions* | - Financial institutions established in France that are covered in Article L 562-1 of the Monetary and Financial Code. |
| *Management of debt issuance* | - The Agence France Trésor shall be responsible for administering and planning the issuance of debt by the company. |

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# Measures for enhancing the refinancing of French financial institutions

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| *Objective* | Enable credit institutions to refinance their medium-term activities on more favorable terms by obtaining loans backed by collateral furnished by a company covered by the State guarantee. |
| *Legislation* | The law provides for the following:<br>- Creation of a company whose purpose is to refinance credit institutions.<br>- The company's basic operating principles.<br>- The basis on which the State guarantee is granted to the company so that it can raise capital in the market. |
| *Timetable for voting on the bill* | - The bill will be submitted to the Council of Ministers on Monday, October 13.<br>- It will then be submitted to Parliament using the fast-track procedure. |
| *Regulations* | - Implementation does not require any additional regulations. |
| *Control of the company* | The Banking Commission shall exercise control over the company on behalf of the State. |
| *Conditionality* | The State may require commitments from the institutions that take advantage of the new arrangements, such as commitments to a specified volume of lending to the economy, and compliance by such institutions and their officers with a code of ethics that serves the general interest. Said commitments shall be set by formal agreement with the State. |
| *Term of the company* | Refinancing activities covered by the State guarantee shall expire on December 31, 2009. |
| *Resources of the company* | - The company shall obtain debt financing in the capital markets. Its debt shall be covered by the State guarantee. |
| *Use of the company's resources* | - The company shall grant loans to credit institutions.<br>- Loans from the "refinancing fund" shall be backed by collateral (loans to economic agents). |

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| *Eligible institutions* | - Credit institutions established in France, including subsidiaries of foreign companies. Said institutions must meet capital adequacy requirements as provided for by law. |
| *Characteristics of the loans to the banks* | - Maturities of up to five years.<br>- An interest rate with two components: (i) a rate corresponding to the financing cost to the company, plus (ii) an additional return corresponding to the cost of the State guarantee (cf. below). |
| *Collateral accepted by the company* | Only high-quality assets:<br>- First-mortgage real-estate loans (or offering equivalent security).<br>- Real-estate loans for the acquisition of property in France, backed by guarantees from a financial institution.<br>- Loans to government authorities.<br>- Loans to businesses with credit ratings in at least the top four ranks.<br>- Consumer credit to private individuals residing in France.<br>The procedures for monitoring the quality of assets accepted as collateral shall be set through cooperation with the Ministry of the Economy and the Banque de France. |
| *State guarantee charge* | - The principle of charging for the guarantee shall be legally sanctioned.<br>- The charge for the guarantee shall comprise a commission in addition to the interest charged, with the amount to be determined at the time of issue. This charge shall be set in such a way as to ensure that the refinancing cost to each credit institution shall be equivalent to the cost it would be bear if it sought the same refinancing in normally operating capital markets. |
| *Management of debt issuance* | - The Agence France Trésor (AFT) shall be responsible for administering and planning the issuance of debt by the company.<br>- Issuance policy shall be coordinated with the issuance policy for government securities. |