

# Fund for Orderly Bank Restructuring (FROB)

**October 2011**

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# 1. The Fund for Orderly Bank Restructuring (FROB): characteristics, objectives and functions.

## 1. The FROB: Main characteristics

The Fund for Orderly Bank Restructuring (FROB) is a public entity created by Royal Decree-law 9/2009, of 26 June, concerning bank restructuring and reinforcing the equity of credit entities.

### Characteristics of the FROB:

**Strongly  
capitalized\*:  
€9,000Mn**

**Public control by:**

- Parliament
- The Ministry of Economy
- National Court of Auditors

**Guarantee by the  
Kingdom of Spain,  
up to €27.0bn**

**Strict and  
independent  
governance:**

- chaired by the Banco de España and
- with the participation of the Ministry of Economy and the Deposit Guarantee Funds (FGD)

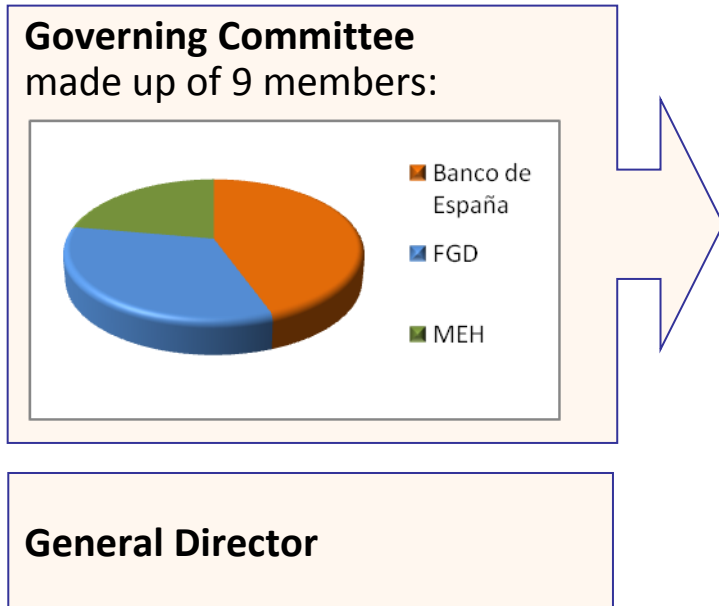
\* In addition, a new law , that is expected to be passed in the coming days, will assure FROB´s capital integrity. The Deposit Guarantee Fund , that is furnished with contributions made by credit entities, will compensate the FROB for the losses that it could suffer in the restructuring of the banking system .

# 1. The FROB: Main characteristics

**Initial allocation of €9,000Mn\***, €6,750Mn has been contributed by the State Budget and €2,250Mn by the Deposit Guarantee Funds

**Public control:** report submitted to the Ministry of Economy every four months, quarterly parliamentary control and every time there is a FROB action; audited by National Court of Auditors

## FROB Governance



- **4 members from the Banco de España (BdE)**
  - Deputy Governor (Chairman of the Governing Committee).
  - General Director of Supervision (Deputy Chairman of the Governing Committee)
  - General Director of Regulation
  - General Secretary (Secretary of the Governing Committee)
- **2 members from the Ministry of Economy and Finance**
  - General Director of the Treasury and Financial Policy
  - General Director of Budgets
- **3 members on behalf of the Deposit Guarantee Funds**
- **A representative (without voting right) of the General Comptroller Department of the State Administration (*Intervención General de la Administración del Estado*) will also sit in on the meetings of the Governing Committee**

\* In addition, a new law , that is expected to be passed in the coming days, will assure FROB´s capital integrity. The Deposit Guarantee Fund , that is furnished with contributions made by credit entities, will compensate the FROB for the losses that it could suffer in the restructuring of the banking system .

## 1. The FROB: Objectives and Functions.

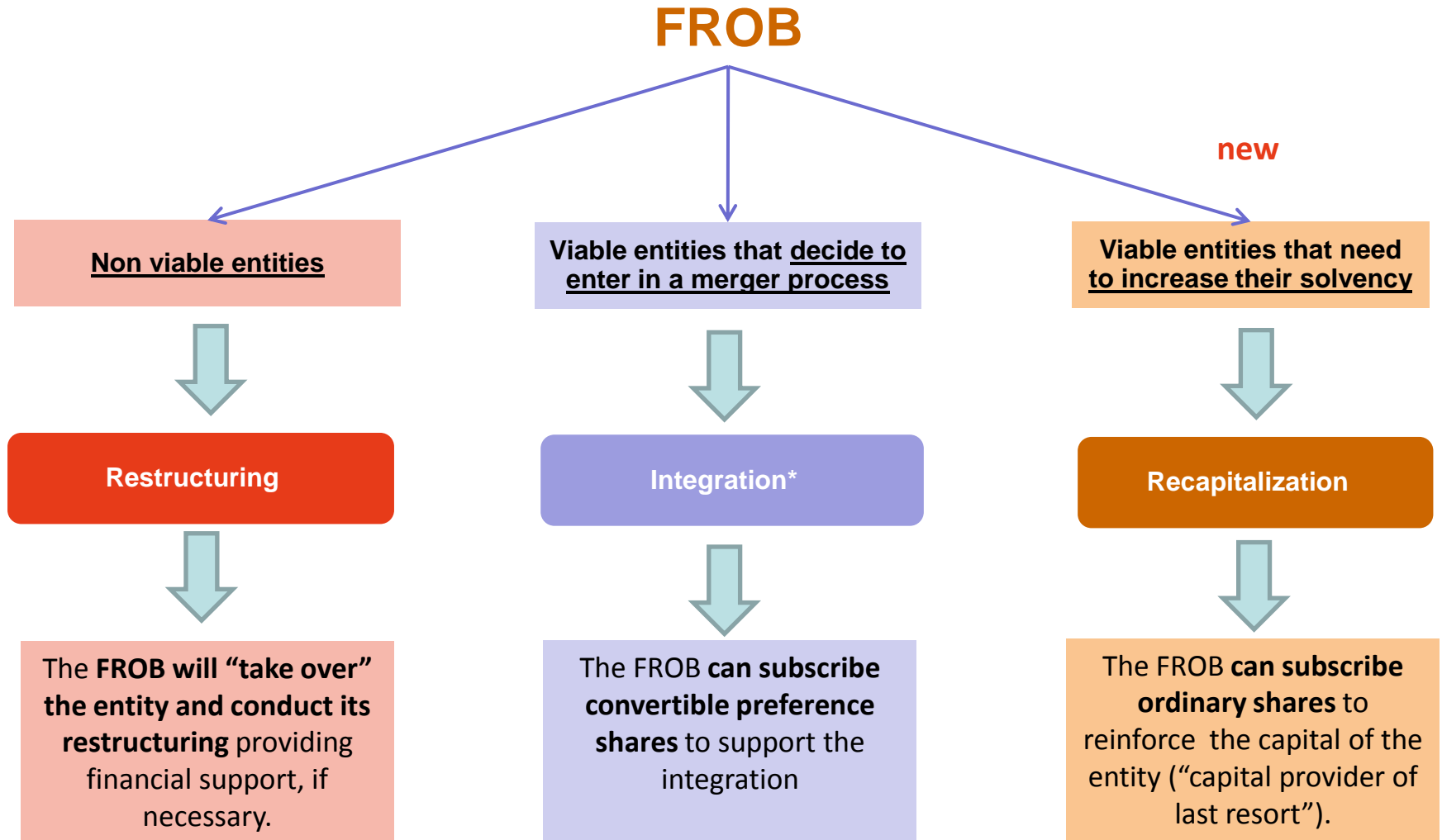
**Final purpose of the FROB:** credit institution equity reinforcement and orderly restructuring of credit entities.

**Helping entities which could have difficulties to adapt to the new setting**

- Adjusting productive capacity and costs
- Increasing efficiency and productivity
- Improving management capacity
- Reinforcing their resiliency and solvency

With the aim of resuming the normal furnishing of credit to companies and households

# 1. The FROB: Objectives and Functions: the three ways



\*After the amendments introduced by RD-law 2/2011, from 2011 Feb. 20<sup>th</sup> and onward s, this option is only available for credit cooperatives.

# 1. The FROB: Objectives and Functions: the three ways

	Restructuring	Integration*	Recapitalization
Eligible entities	Non viable entities	Viable entities that <u>decide to enter in a merger process</u>	Viable entities that need to increase their solvency
Objectives	To avoid a disorderly resolution process entailing losses for creditors and depositors that could raise concerns on the overall stability of the banking sector	To foster financial stability and adapt the capacity of the sector to the level of demand and the current economic environment	To allow entities to comply with the new capital requirements with the aim of regaining market confidence.
FROB's role / Form of support	Loans; guarantees; assets protection schemes; purchase of assets and/or capital provision	Subscription of convertible preference shares. Entities must repurchase the preference shares within a period of 5 years (can be extended for 2 further years)	Subscribing ordinary shares issued by banks or credit cooperatives . The support will be on a temporary basis (the FROB must divest within 5 years)
Way to proceed	<p>The FROB will be appointed to interim administrator of the entity and will draw up a <b>restructuring plan</b> to be approved by BdE which may include financial support and meanwhile could provide rescue aid for keeping the institution afloat</p> <p>The plan will result in a merger or in the transfer of the assets and liabilities of the ailing bank to a financial institution to be chosen through a competitive process</p>	<p>The entities involved are required to tackle an integration process aimed at diminishing the global capacity of the sector .</p> <p>The integration plan has to be approved by BdE and must include goals in terms of reorganization, efficiency gains and productivity improvement.</p>	<p>A <b>recapitalization plan</b> must be submitted to the BdE. The subscription of these instruments will cause the immediate inclusion of the FROB in the entity's board of directors.</p> <p>In the event that the requesting entity is a savings bank or an Institutional Protection Scheme (IPS), the entity or entities must transfer the financial activity to a commercial bank.</p>

\*After the amendments introduced by RD-law 2/2011, from 2011 Feb. 20<sup>th</sup> onward this option is only available for credit cooperatives.

# 1. The FROB: Objectives and Functions: the three ways

	Restructuring	Integration*	Recapitalization
State aid treatment	EU approval required on a case by case basis	The EC approved a scheme that has been in force till 2010 Dec. 31st . New processes will need specific approval.	EU approval required on a case by case basis
Cases	CajaSur	7 integration processes involving 26 savings banks: -Catalunya Caixa -UNNIM -Caja España-Duero - NovaCaixaGalicia - SIP MareNostrum - SIP Banca Cívica - SIP Bankia	-
Funds committed	<b>€ 392 million</b> (asset protection scheme granted to facilitate the transfer of the assets an liabilities to BBK)	<b>€ 9,674 million</b>	According to the data released by the BdE, the maximum needs will amount to € 15.9 bn

Thus, the FROB contributes to the resizing and restructuring of the Spanish banking system as a whole, against the backdrop of the international financial crisis, and complements the role of the deposit guarantee funds in crisis resolution at individual entities.

\*After the amendments introduced by RD-law 2/2011, from 2011 Feb. 20<sup>th</sup> and onwards, this option is only available for credit cooperatives.

## 2. The restructuring of the Spanish banking system (I).

Phase one: the consolidation in the savings bank sector

## 2. The restructuring of the Spanish banking system. The consolidation in the savings bank sector

**The Spanish banking system has proved a strong relative resistance** by virtue of:

- Lack of toxic assets
- Retail business model with high level of efficiency
- Stringent regulation and supervision: high anti-cyclical provisions, control of off balance sheet operations

Systemic entities **have not needed government bail-outs** and emerge from the crisis in a **stronger position**

**Certain small and medium-sized entities**, especially in the savings bank sector, **were facing problems** due to:

- The length and depth of the financial crisis and its impact on the real economy. As business adjusted to the new demand conditions, it became clear there was excess capacity, implying the need to adjust the size of the banking sector.
- The economic environment had made it more difficult for entities to conduct their business efficiently with various factors putting pressure simultaneously on their income statements: rising defaults, especially in the real estate sector, tightening financing conditions on the wholesale markets with the consequent effect on financing costs and the adjustment in business volume mentioned above.

## 2. The restructuring of the Spanish banking system. The consolidation in the savings bank sector

Looking to the future and under this adverse scenario for the savings banks in particular, **a large-scale transformation of their structure**, increasing the average size of the entities or groups and harnessing synergies, **was necessary to gain solidity and raise efficiency**, as an essential condition in order to enhance not only the savings banks' competitive position but also their market credibility.

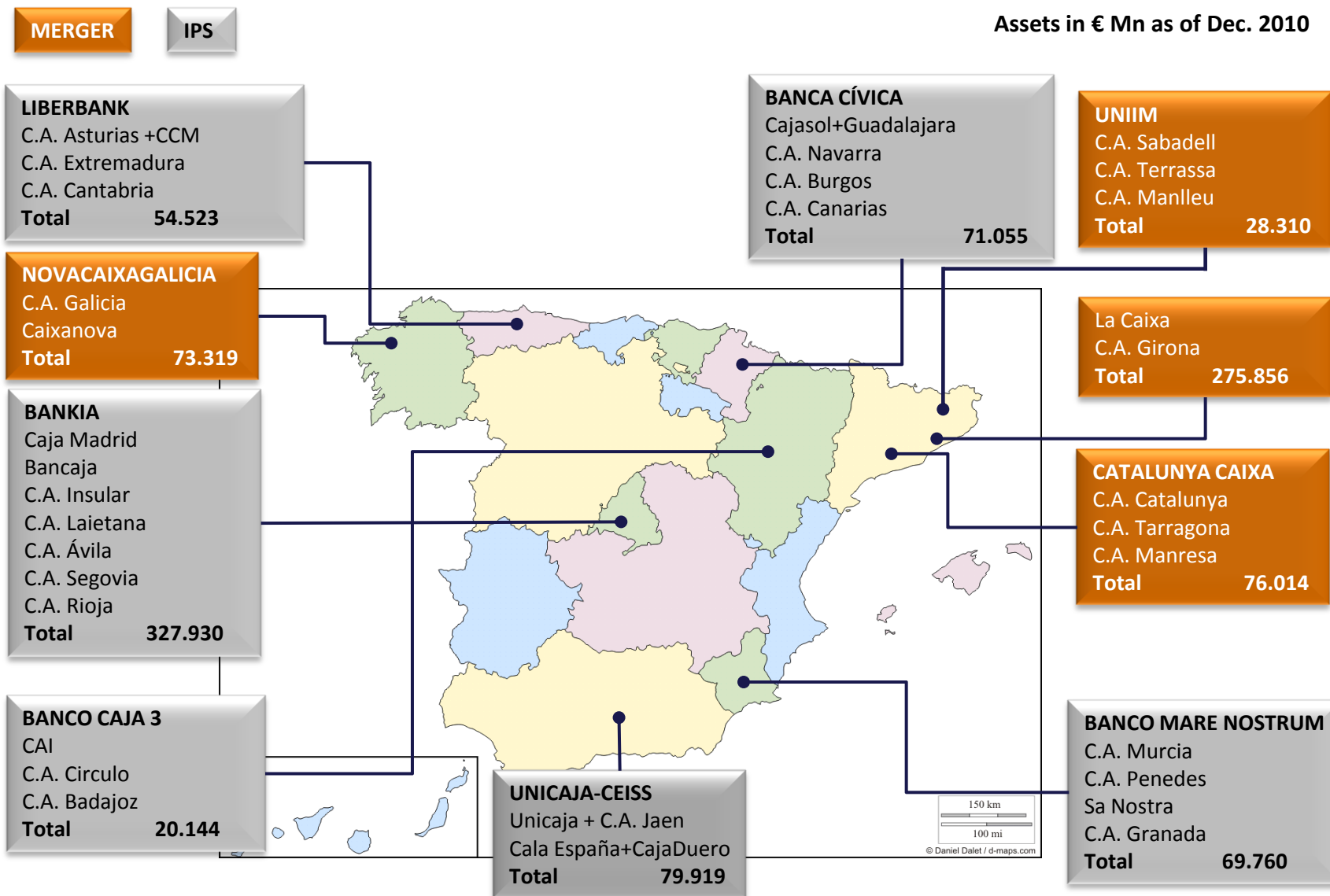
**The savings bank sector has been restructured through several integration processes**, through mergers or Institutional Protection Schemes (IPS), **involving so far 40 out of the 45 Spanish savings banks**. The restructuring of another institution, **Cajasur, taken over by the FROB in May 2010, culminated on December 31<sup>st</sup> with the transfer of its whole assets and liabilities to BBK Bank and CAM is also under FROB's control and its restructuring process is in progress.**

**In total, 42 savings banks are participating in the restructuring of the sector** and only 3 savings banks have not been involved in this process, so far.

The FROB participates in these merger processes when requested to do so by the entities concerned. Not all of the mergers agreed have requested aid from the FROB.

The main figures of this concentration process are summarized in the next slides.

## 2. Integration processes roadmap



## 2. The restructuring of the Spanish banking system

**Seven<sup>1</sup> integration processes have requested aid from the FROB totaling €9.7 billion.**

**Additional FROB funds for €392 million were granted for the restructuring of CajaSur.**

The total funds committed during this first stage amount **€10.1 bn.**

	Entities involved	Type	FROB aid (million)	FROB's approval	Stage
<b><u>Approved by Bank of Spain, with FROB aid</u></b>					
1	Catalunya-Tarragona-Manresa	Merger	1,250	25/03/2010	Completed
2	Manlleu-Sabadell-Terrassa	Merger	380	25/03/2010	Completed
3	España-Duero	Merger	525	25/03/2010	Completed
4	Galicia-CaixaNova	Merger	1,162	29/06/2010	Completed
	<b>BANCO FINANCIERO</b>				
5	Madrid-Bancaja-Laietana-Insular Canarias-Ávila-Segovia-La Rioja	IPS	4,465	29/06/2010	Completed
	<b>BANCO MARE NOSTRUM</b>				
6	Murcia-Penedés-Sa Nostra-Granada	IPS	915	29/06/2010	Completed
	<b>BANCA CÍVICA</b>				
7	Navarra-Cajasol+Guadalajara-General Canarias-Municipal de Burgos	IPS	977	22/12/2010	Completed
	<b>Total committed<sup>1</sup></b>		<b>9,674</b>		

1. Another IPS involving 4 cajas, Banco BASE, that initially had requested FROB support amounting €1,5 bn has been cancelled.

## 2. Consequences and impacts of the restructuring

The first steps in the restructuring of the saving banks sector can be considered almost completed:

€10.1 bn

- Strengthening solvency: **€10.1 bn of FROB's funds has been injected** into the new entities and groups.

€22 bn

- Increasing write-downs and provisions that will cover expected losses: **additional provisions amounting around €22 bn have been constituted** against equity at the time of integration, by the entities that have requested FROB's support.

17  
savings  
banks\*

- Strong concentration increasing the average size of the entities: **from 45 savings banks in 2009 to 17 as of May 31<sup>st</sup> 2011**. This will entail economic benefits for the resulting entities through lower operating costs, access to the wholesale markets, better managerial practices,...

-20%  
capacity

- Tackling the problem of the excess of capacity in the sector boosting the entities efficiency: **closure of 20 to 25% of branches and reducing staff by 15%**, in average (in progress).

\* Excluding CECA

### 3. The restructuring of the Spanish banking system (II).

Phase two: improving solvency

### 3. Improving solvency: RD-law 2/2011

Despite the initial main goals of the restructuring process have been achieved and the positive results of the measures adopted so far, the Spanish Government has adopted new measures to complete the transformation of sector and contribute to regain markets' confidence.

For this purpose, new legal reforms are being carried out to reinforce sector's solvency and transparency. Main ways of action are the following:

- **To encourage entities transparency**, through new information requirements regarding credit risk exposures to each sector
- **To strengthen solvency and capital quality requirements**, preparing the entities in advance to meet not only the international capital standards but also the most stringent stress tests that could be carried out in the future in the EU.

Contributing, by this way, to take advantage of market discipline benefits and, in particular, of those regarding governance.

### 3. Improving solvency: RD-law 2/2011

#### The new capital requirements laid down in RD-law 2/2011

- The **solvency requirements** of commercial banks, savings banks and credit cooperatives **have been made more stringent.**
- On a general basis the Royal Decree-law requires a **so-called *capital principal*<sup>1</sup> equal to or above 8%** of their risk-weighted assets (RWAs).
- For credit **entities which are highly dependant on wholesale markets (in other words, a wholesale funding ratio above 20%), the *capital principal* ratio is increased to 10%.** As an exception, **the 8% ratio is maintained when the relevant entity has 20% or more of its capital or voting rights placed among third parties,** either in the stock market or among private investors.
- The **ratio may also be increased for entities that do not pass the stress tests carried out by the EU.**
- These legal measures **will allow the FROB, if necessary, to subscribe the bank shares in market conditions** and on a temporary basis (up to 5 years) in order to allow it to comply with the new capital requirements.

<sup>1</sup> *Capital principal* = core capital + convertible preference shares subscribed by FROB + debt instruments mandatory convertible into common shares before 31 Dec. 2014.

### 3. Improving solvency: RD-law 2/2011

The Banco de España has released, on a case by case basis, the capital shortfalls that have arisen because of the new solvency requirements:

Entitiy	Starting core capital (Mn)	Level to meet	p.p. to reach the level required	Additional capital to reach the level required (€Mn)	Situation as of 30 <sup>th</sup> September	
					FROB's final support	Comments
Bankinter	2,144	8%	1,10%	333	0	Issue of bonds mandatory convertible completed
Bankpyme	24	8%	2,00%	8	0	Taken over by Caixabank
Barclays	1,005	8%	2,80%	552	0	Capital increase completed
Deutsche	729	8%	1,60%	182	0	Capital increase completed
<b>Bancos</b>	<b>3,902</b>			<b>1,075</b>	<b>0</b>	
Bankia	14,125	10%	2,90%	5,775	0	IPO process completed
CAM	2,364	10%	5,10%	2,800	2,800	Restructuring process in progress
Cívica	3,687	10%	1,90%	847	0	IPO process completed
Mare Nostrum	3,343	10%	1,60%	637		Deadline extended. RWAs reduction. - Expected support, if necessary, will be lower than estimated
Catalunya Caixa	3,148	10%	3,50%	1,718	1,718	
NovacaixaGalicia	2,851	10%	4,80%	2,622	2,465	RWAs reduction
Caja España-Duero	2,062	10%	1,80%	463	0	Merge with Unicaja
Liberbank	2,703	10%	1,60%	519		Deadline extended. Divestments in progress. Expected support, if necessary, will be lower than estimated
Unnim	1,150	10%	3,30%	568	568	
<b>Cajas</b>	<b>35,433</b>			<b>15,949</b>	<b>7.551</b>	
<b>Total</b>	<b>39,335</b>			<b>17,024</b>	<b>7.551</b>	

### 3. Improving solvency: RD-law 2/2011

#### Calendar to meet the new requirements

- Entities must comply with the applicable core capital ratio before 10 March 2011, on the basis of the risk-weighted assets as at 31 December 2010.
- However, there is an adjustment period for entities that do not meet this deadline, which ends on 30 September 2011. These entities must submit a recapitalization plan with their strategy and timeframe to the Bank of Spain.
- Exceptionally, the Bank of Spain may extend the compliance term up to 31 December and, for entities involved in listing procedures, until the first quarter of 2012.
- **If the entities are not able to raise the capital they need, the FROB will subscribe the shares, in market conditions, and will take a stake on the entity.**

## 4. Financial structure of the FROB.

## 4. Financial structure of the FROB

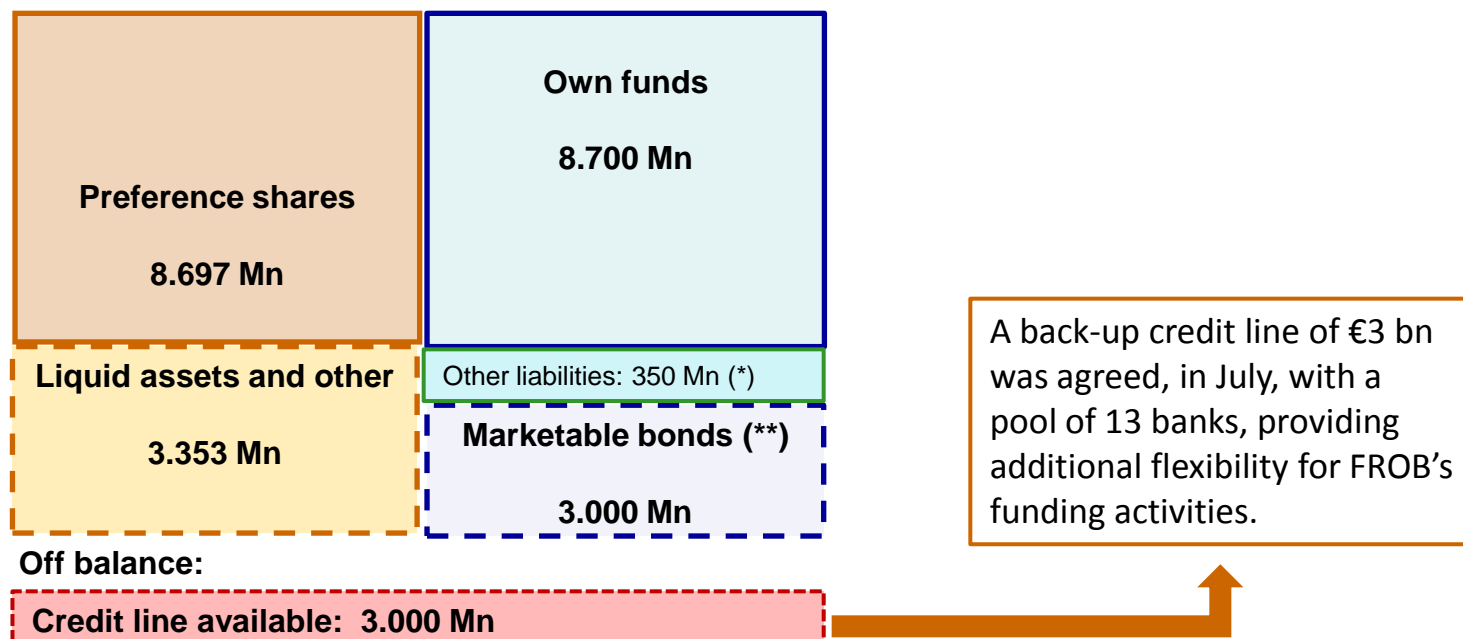
**Initial allocation of €9,000Mn**, 75% of which is furnished by State Budget and 25% by the FGD.

**Debt capacity of €27 bn** (3 times its allocation)...**and can be increased up to 10 times, €90 bn**, with the approval of the Ministry of Economy.

**... with the explicit, unconditional and irrevocable guarantee of the Kingdom of Spain** (guarantee of €27 bn, already granted)

**Strong position in liquid assets** (current account or Public Debt)

**FROB's balance sheet. 31 Dec. 2010**

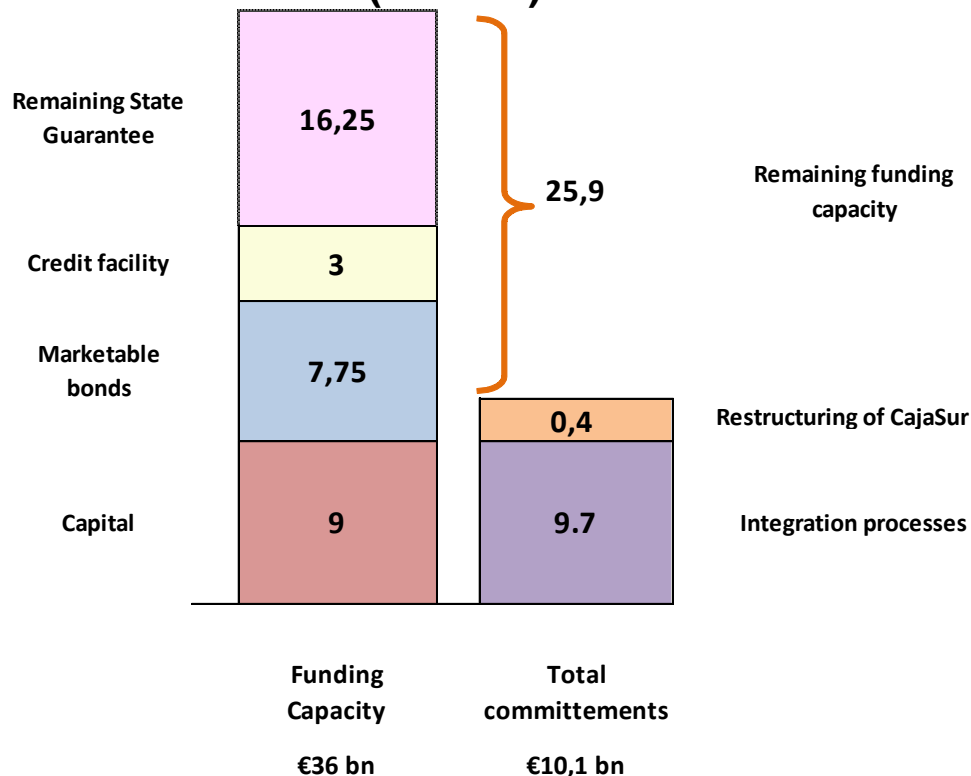


\*NPV of the aid for CajaSur restructuring

\*\* A second €3 bn issue was placed in January 2011. Subject to possible new issuances

## 4. Financial structure of the FROB

### Commitments vs. funds available (current)



#### Main conclusions:

- Funds available are sufficient to support the restructuring and recapitalization processes
- Only 10.1 bn have been committed vs. a total funding capacity of 36 bn
- Strong liquidity position: 6.8 bn in cash + 3bn immediately available.
- Financial incomes expected in 2011 amount to € 700 Mn

## 5. Securities issued by the FROB: the guarantee of the Kingdom of Spain

## 5. Securities issued by the FROB

### Simple bonds...

**...with the explicit, unconditional and irrevocable guarantee of the Kingdom of Spain...** (Current rating: Aa2 (Moody's); AA (S&P); AA+ (Fitch))

- **Equity Requirements for credit risk: 0% RWA**  
(confirmed by the Banco de España)
  
- **Eligible as guarantee assets in ECB monetary policy operations**  
(confirmed by the Banco de España)
  - **Up to 5 years: Haircut: 4.5%**
  - **Between 5 and 7 years: Haircut: 5.5%**

### Trading on the Public Debt Entry Book Market

**The Banco de España will act as a payment agent in FROB issues.**

**Equivalent treatment for tax purposes to that of the Government bonds**

## 5. Guarantee of the Kingdom of Spain

**Limit of guarantee granted<sup>1</sup>:** €27 bn of principal plus the pertinent ordinary interests (€ 16,25 bn still available).

**Characteristics:** Explicit, unconditional, irrevocable and waiving the right of excussion

**Guaranteed operations:** Marketable securities, loans or credits in euros or other currency with a term no longer than 7 years, formalised prior to 15.12.2016. Payments agent: Banco de España

**Clearing in the event of execution:** At the EONIA rate for the days elapsed between the maturity date of the guaranteed obligation and the date of payment by the guarantor, provided the execution of the guarantee is requested within the 5 days following the maturity date

**Execution procedure:** The Banco de España, as the payment agent, and on behalf of the legitimate creditors, will claim, at the General Directorate of the Treasury and Financial Policy, the payment through it of the amount not paid to the holders of the affected securities or loans

**Payment by the Government:** The General Directorate of the Treasury and Financial Policy is authorised by Royal Decree 9/2009 to carry out the payments arising from the execution of the guarantee, immediately and with no need for further budget-related steps.

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<sup>1</sup> From 01.01.2010 onwards can be increased up to 10 times, €90,000 Mn, with the approval of the Ministry of Economy.

# Annex I. Issuances post-mortem

## Annex I. FROB inaugural issue: post-mortem

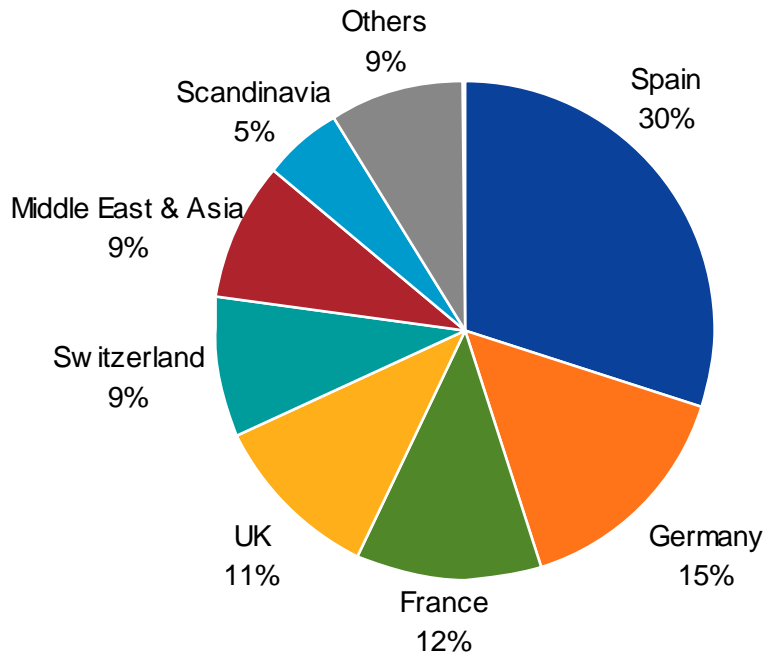
<b>Issuer:</b>	<b>Fondo de Reestructuración Ordenada Bancaria (FROB)</b>
<b>Amount:</b>	<b>€3,000,000,000</b>
<b>Face value</b>	50.000 €
<b>Issue rating:</b>	<b>Aaa (Moody's) / AA+ (S&amp;P) / AAA (Fitch) *</b>
<b>Type:</b>	Simple bonds. Single repayment on maturity (bullet). Fixed interest rate.
<b>Range:</b>	Senior, guaranteed
<b>Guarantor:</b>	<b>Kingdom of Spain</b>
<b>Term:</b>	5 years
<b>Settlement date:</b>	19 <sup>th</sup> November 2009
<b>Maturity date</b>	19 <sup>th</sup> November 2014
<b>Coupon:</b>	3,00% annual (Act/act)
<b>Re-offer price:</b>	99,881%
<b>Re-offer spread:</b>	MS+25 bps
<b>Listing:</b>	Madrid. Mercado de Deuda Pública en Anotaciones( Entry Book Public Debt Market) (governing body: Bank of Spain)
<b>Representation of bonds:</b>	By book entry
<b>Registration:</b>	Iberclear
<b>Payments Agent:</b>	BANK OF SPAIN
<b>Lead managers:</b>	<b>Barclays Capital, BBVA, Calyon, Deutsche Bank, HSBC</b>

\* At the time of issuance. Current ratings are: Aa2; AA; AA+

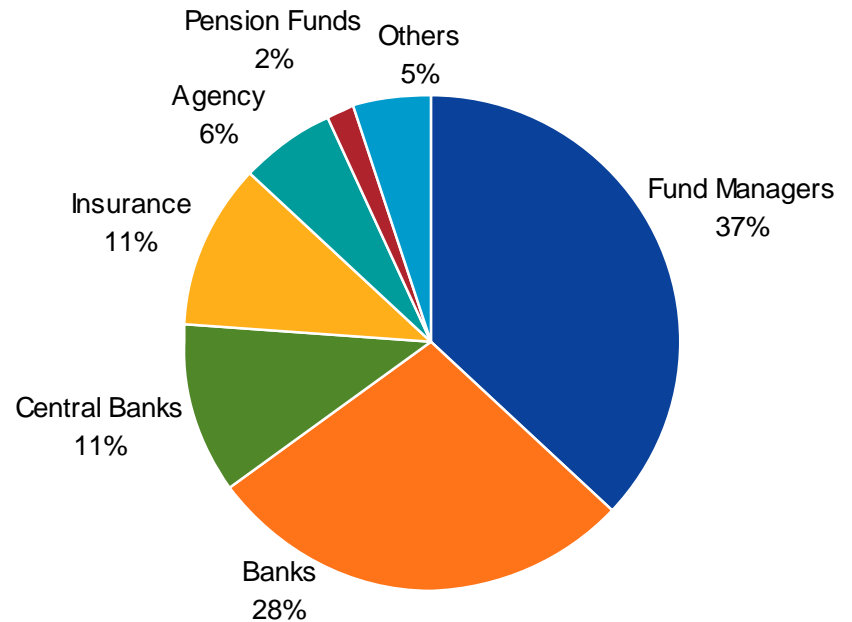
# Annex I. FROB inaugural issue: post-mortem

## Summary of Placement

*By region*



*By investor type*



## Annex I. FROB second issue: post-mortem

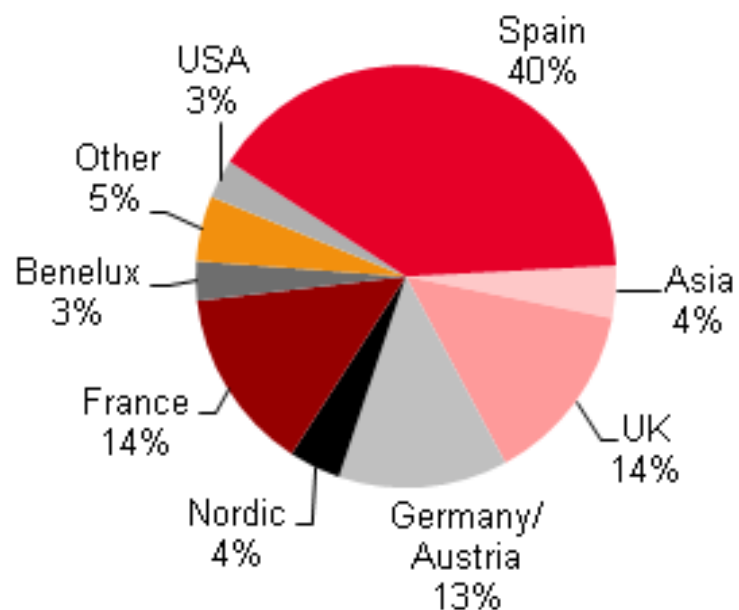
<b>Issuer:</b>	<b>Fondo de Reestructuración Ordenada Bancaria (FROB)</b>
<b>Amount:</b>	<b>€3,000,000,000</b>
<b>Face value</b>	100.000 €
<b>Issue rating:</b>	<b>Aa1 (Moody's) / AA (S&amp;P) / AA+ (Fitch) *</b>
<b>Type:</b>	Simple bonds. Single repayment on maturity (bullet). Fixed interest rate.
<b>Range:</b>	Senior, guaranteed
<b>Guarantor:</b>	<b>Kingdom of Spain</b>
<b>Term:</b>	3 years
<b>Settlement date:</b>	3 <sup>th</sup> February 2011
<b>Maturity date</b>	3 <sup>th</sup> February 2014
<b>Coupon:</b>	4,50% annual (Act/act)
<b>Re-offer price:</b>	99,92%
<b>Re-offer spread:</b>	MS+220 bps
<b>Listing:</b>	Madrid. Mercado de Deuda Pública en Anotaciones( Entry Book Public Debt Market) (governing body: Bank of Spain)
<b>Representation of bonds:</b>	By book entry
<b>Registration:</b>	Iberclear
<b>Payments Agent:</b>	BANK OF SPAIN
<b>Lead managers:</b>	<b>Citi, HSBC, RBS, Santander, Soc Gen</b>

\* At the time of issuance. Current ratings are: Aa2; AA; AA+

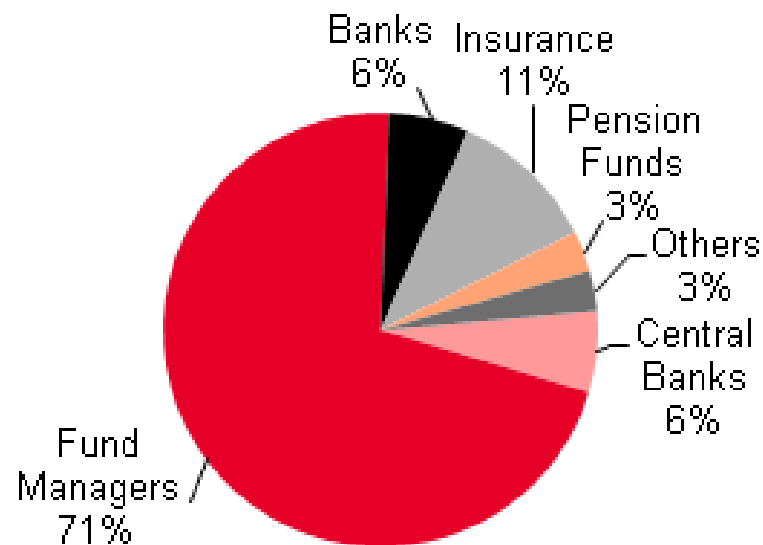
## Annex I. FROB second issue: post-mortem

### Summary of Placement

*By region*



*By investor type*



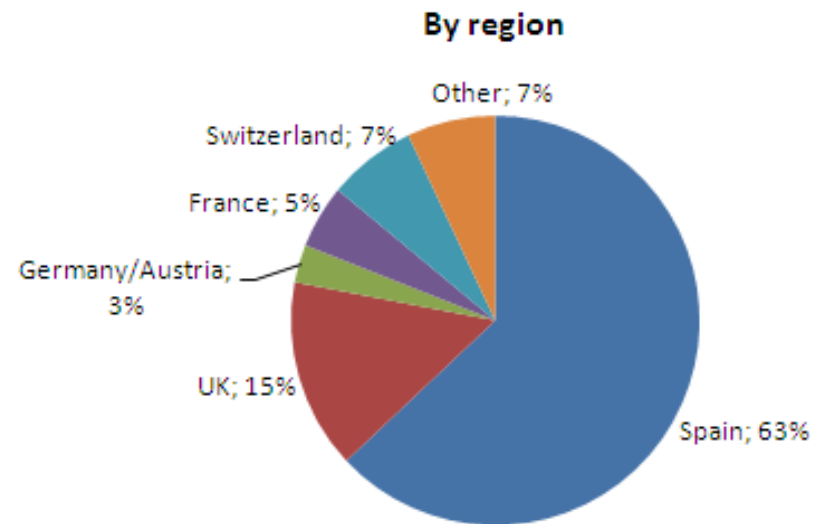
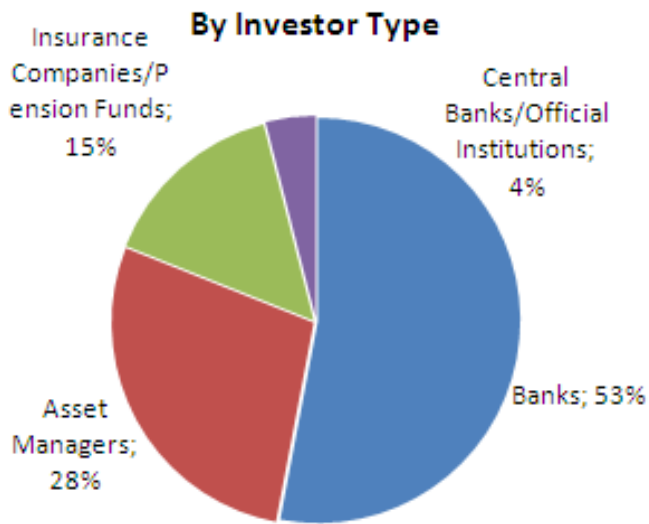
## Annex I. FROB third issue: post-mortem

<b>Issuer:</b>	Fondo de Reestructuración Ordenada Bancaria (FROB)
<b>Amount:</b>	€1,750,000,000
<b>Face value</b>	100.000 €
<b>Issue rating:</b>	Aa2 (Moody's) / AA (S&P) / AA+ (Fitch) *
<b>Type:</b>	Simple bonds. Single repayment on maturity (bullet). Fixed interest rate.
<b>Range:</b>	Senior, guaranteed
<b>Guarantor:</b>	<b>Kingdom of Spain</b>
<b>Term:</b>	5 years
<b>Settlement date:</b>	12 <sup>th</sup> July 2011
<b>Maturity date</b>	12 <sup>th</sup> July 2016
<b>Coupon:</b>	5,50% annual (Act/act)
<b>Re-offer price:</b>	99,889%
<b>Re-offer spread:</b>	MS+270 bps
<b>Listing:</b>	Madrid. Mercado de Deuda Pública en Anotaciones( Entry Book Public Debt Market) (governing body: Bank of Spain)
<b>Representation of bonds:</b>	By book entry
<b>Registration:</b>	Iberclear
<b>Payments Agent:</b>	BANK OF SPAIN
<b>Lead managers:</b>	Barclays, BBVA, BNP Paribas, Deutsche Bank y Natixis

\* At the time of issuance. Current ratings are: Aa2; AA; AA+

# Annex I. FROB third issue: post-mortem

## Summary of Placement



Further and detailed information can be consulted on the website of  
the Fund for Orderly Bank Restructuring (FROB):

[www.frob.es](http://www.frob.es)

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