

Economics

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Ireland

ECB Continues to Oppose Promissory Note Restructuring

- In an important speech in Dublin, Jörg Asmussen of the ECB Executive Board laid out the ECB's case against promissory note restructuring. **First**, the ECB insists that any restructuring must not delay the decline in financing from the Eurosystem by Irish banks: *"Any proposal to reorganize and strengthen the Irish banking sector, and in this context to replace promissory notes with support from the EFSF must meet important criteria, including that it should improve the chances of both the State and the banks returning to market-based funding, and of the banks reducing their extraordinary reliance on the Eurosystem."* In measuring the reliance of Ireland's banks on the Eurosystem, Asmussen combines ELA and normal liquidity assistance. *"Before the EU/IMF programme was agreed, the total Eurosystem loan support for Ireland (combining monetary policy operations to all eligible banks and emergency liquidity assistance from the Central Bank of Ireland) amounted to about 100% of Irish GDP. Our total loan provision now stands at above EUR 125 billion"* This implies that the ECB is unlikely to be happy with the recent transaction, whereby this year's promissory note payment (which allows the IBRC to repay ELA) is funded by the issue of new Irish government debt that is immediately financed via repo through the Eurosystem. Such transactions effectively replace ELA funding of the IBRC with Eurosystem funding of BOI, and would not achieve the ECB's aim of cutting Ireland's aggregate *"extraordinary reliance on the Eurosystem"*. The ECB is likely to argue against further such moves.
- **Second**, the ECB argues that the financing saving for 2012 from the promissory note restructuring is a bit irrelevant, because the Troika programme covers promissory note payments *"When the programme for Ireland was designed, the costs of the banking sector measures already in place, including the promissory notes, were fully factored in. The annual cash repayments of promissory notes is thus financed by programme resources."* This implies that the Troika programme would have been smaller if the Troika had allowed for promissory note restructuring. **Third**, the ECB believes that market credibility is best achieved by sticking exactly to the Troika programme, which includes the promissory note payments, and that any slippage puts at risk the ultimate aim of regaining normal market access *"Any deviation from that programme should be considered very carefully indeed. The perceptions that have built-up around Ireland's successes in the programme should not be jeopardised. It has been hard-won and it is worth fighting for. Therefore, the ECB remains of the opinion that Ireland should honour its commitments stemming from the promissory notes, as foreseen. This in our view is the best way to regain sustainable market access."* **Fourth**, the ECB believes that promissory note restructuring would contaminate Ireland's sovereign debt, by undermining the government's reputation for meeting its payments. *"With the guarantee of 2008, large parts of the debt of Irish banks became a debt of the State, and any desire to offload this debt could have dire consequences."* **In our view, the ECB's attitude is likely to run up against the painful reality that continued economic weakness will prevent Ireland returning to a sustainable fiscal path.**

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