

# Potential for a Portuguese 'development bank' to stimulate economy

THURSDAY, 24 JANUARY 2013 14:26



## Government's intent to create financial institution based on German KfW model is met with questions

While the idea of a local 'development bank' for Portugal is nothing new, the concept was recently reignited following a visit from German Chancellor Angela Merkel. The suggestion now is that Portugal establishes a financial institution akin to Germany's model KfW to participate in projects and investments to bring support and exports to the Portuguese economy.

When faced with a choice of how best to stimulate a flagging economy, the Portuguese Government had two blueprints for inspiration. It could follow the recent Spanish example, where the Government created a 'bad bank' to collate bad debts. Alternatively, it could follow the long-established KfW. KfW was created in 1948 to effectively serve as a state bank post-World War II. It is jointly owned by Federal Republic and the regional states and provides loans to German citizens and companies with a remit of promoting economic growth.

A new bank would therefore provide stimulus to the economy, but lawyers point out that this 'development' tag is misleading. The institution would not operate like the European Investment Bank, the European Bank for Reconstruction and Development or the World Bank. Portugal, like many troubled countries, is suffering from a lack of banking liquidity, meaning obtaining financing for business expansion is very hard. Such investments would likely be the priority.

"I do not think this will be a 'development bank' in that it will not be providing long-term debt to infrastructure and energy projects," explained Pedro Siza Vieira, national Managing Partner and Head of Finance at Linklaters in Portugal. "The suggestion is that the bank would instead channel lines of credit to SMEs or leverage off EU funds that are made available."

The concept has met with some cynicism. First, there is the speculative nature of the idea in terms of going ahead, but also the logic of establishing a new bank.

"There have been political announcements but not much more," says Pedro Cassiano Santos, Head of Banking and Finance at Vieira de Almeida. "One obvious criticism is why would the Portuguese Government go about setting up a new bank? It already holds a stake in a reputable bank, notably Caixa Geral de Depósitos (CGD) and its investment division, so why not use that?"

Other lawyers have also expressed bewilderment at the decision not to use CGD. The bank already has an established business (last month it placed a three-year €500m bond for instance) and a loan book, so it perhaps it would not provide so much 'new capital' as a stand-alone entity. Even so, there are political overtones, say lawyers; a new bank would be a decent response to criticism that the government is not doing as much as it can to support the economy.

Lawyers agree that the plan to establish a bank is feasible but the big questions are what form would a new bank take and where would the capital come from? "There has been no specific design for the project," says Siza Vieira. "It is all very unclear and so hard to predict what will come from it, if anything."

Lawyers also question whether the Portuguese Government has enough resources to inject into a new bank. One suggestion is that the Government or CDG would hold the share capital equity with funding also sought from alternative sources. More adventurous ideas include formally linking up with other similar banks, such as KfW, to help lead the push.

"The Government could put in its own capital, via the bailout fund, or launch an IPO for a part of the capital to bring in private investors," says Cassiano Santos. "There is also the option of a joint

venture." The Government will soon undertake another review with the Troika, he adds, and so we may have a clearer idea in February 2013.

A major IPO, joint venture or capital injection would, of course, demand the services of corporate, capital markets and finance lawyers. Even so, few top legal experts are predicting a trophy instruction within the near future. Portugal remains in a volatile position and is subject to further financial scrutiny that could reshape ambitions.

