



MINISTÉRIO DAS FINANÇAS E DA ADMINISTRAÇÃO PÚBLICA

GABINETE DO MINISTRO DE ESTADO E DAS FINANÇAS

Press Release

Statement of the Ministry of Finance and Public Administration about the Government's decision regarding Banco Privado Português

On 27 April 2009, Banco Privado Português submitted a Recovery Plan to the Bank of Portugal. This plan essentially suggested the following:

- Addressing the problems with Absolute Return by constituting a special investment fund that takes up the portfolios of the vehicles used by this product. This fund would be managed by an entity external to the bank.
- Negotiation with the Absolute Return clients to replace the capital guarantee provided by the bank with a 'return to better fortune' clause.
- A capitalisation operation of the bank for the sum of EUR 300 m to EUR 350 m: the State with EUR 150 m to EUR 200 m, other banks with EUR 125 m and private shareholders (current BPP shareholders) with EUR 25 m. Of the State's contribution, EUR 50 m would correspond to ordinary three-year reimbursable shares without guaranteed redemption and EUR 100 m would take the form of preferential shares without voting rights, amortizable over 25 years and offering 3% remuneration. The Plan further involves an additional contribution from the State of EUR 50 m in the form of supplementary capital, with no remuneration.

The Bank of Portugal produced a Report on this plan which it submitted to the Government last 13 May, to which the Government replied on 19 May, requesting further information and clarifications, since the solution as presented was unworkable, and the continuation of work towards a final solution proposal through collaboration with the Bank of Portugal and CMVM (the Portuguese Securities and Exchange Regulator).



MINISTÉRIO DAS FINANÇAS E DA ADMINISTRAÇÃO PÚBLICA

GABINETE DO MINISTRO DE ESTADO E DAS FINANÇAS

Due to its size, market share and business model, which is based essentially on wealth management, BPP does not amount to relevant systemic risk that constitutes a public interest and justifies the use of public money, as requested in the plan, especially considering the national and international financial system's current constraints. Also, the Recovery Plan proposed by BPP does not comply with recapitalisation regulations defined in Law no. 63-A/2008, nor the guidance on this topic from the European Union regarding EU competition regulation compliance, now that the situation has required intervention from the State.

As mentioned above, BPP based its business model essentially on wealth management. In particular, 'Absolute Return' clients placed their savings under the management of the bank, which used them to acquire financial instruments spread over a wide number of vehicle companies based in offshore jurisdictions.

The financial instruments acquired by these vehicles were not only financed by the sums invested by the Absolute Return clients, but also by debt, which allowed these companies to leverage their activity, and resulted in liabilities for the clients' portfolio.

The Absolute Return clients thus own assets in those vehicle companies, consisting of loan notes issued by the vehicles. The value of these loan notes and their remuneration is thus subject to the fluctuations in the financial markets that increase, or otherwise decrease, the value of the underlying assets (market risk, exchange rate risk, interest rate risk, etc.).

However, despite the risk inherent in these products, BPP stated a remuneration rate and guaranteed all the capital invested by these clients upon maturity. This guarantee's existence was never communicated to the supervisory authorities nor was it included and recorded on the bank's Balance Sheet. If it had been, BPP would have needed higher equity levels to cover for the liabilities taken on upon conceding such a guarantee to clients. By concealing this liability, the bank's shareholders were spared from having to inject more capital to meet the legal and regulatory requirements in force.

BPP's current inability to honour its commitments to guaranteed Absolute Return clients arises not only from the vehicles' debt and the unfavourable performance of the financial markets during the crisis affecting us, but also from the fact that by



MINISTÉRIO DAS FINANÇAS E DA ADMINISTRAÇÃO PÚBLICA

GABINETE DO MINISTRO DE ESTADO E DAS FINANÇAS

concealing the existence of those guarantees, they failed to equip the bank with the capital needed to address the current situation.

Aside from this, the investigation by CMVM and the Bank of Portugal found serious irregularities that amount to criminal practice on the part of BPP, regarding fictitious operations which harmed the clients and accounting falsification, which led to inquiries and several timely interventions from the Public Prosecutor.

Despite the irregularities found in the way these financial instruments were sold, a commitment from BPP remains in effect arising from the guarantee provided. However, the Government's view, which is shared by the regulatory and supervisory authorities, is that the guarantee does not mean the Absolute Return investments are a bank deposit, and therefore, that the liability for the guarantee issued is the bank's and should continue to be the bank's. Thus, BPP's previous administration and shareholders should be answerable for this guarantee, and not the State, or (effectively) taxpayers.

Nevertheless, the Government is not insensitive to the concerns of clients whose investments are jeopardised by those financial instruments. Thus, the Government has worked with the supervisory authorities to identify a solution that minimises eventual losses and may address as far as possible the interests of those clients. The solution envisaged by the Government has the following features:

- The creation of a new financial instrument, representative of the current indirect Absolute Return portfolio, that replaces the current investors' positions;
- Each Absolute Return client participating in this solution will have a right to their allocation of securities at the portfolio's market value, in proportion to their position in the portfolio;
- The clients retain their rights regarding BPP over the guarantees offered by the latter;
- The financial instrument will be issued and managed by an entity that is independent of BPP and owned and managed by national banking institutions;



MINISTÉRIO DAS FINANÇAS E DA ADMINISTRAÇÃO PÚBLICA

GABINETE DO MINISTRO DE ESTADO E DAS FINANÇAS

- The financial instrument will be remunerated, redeemable annually under a timeframe and conditions to be defined and may be divested under market conditions to offer liquidity;
- The SII (Investor Indemnification System) will be activated immediately under the terms of the Law.

Lisbon, 12th June 2009

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