

>> **ESPIRITO SANTO BANK:  
Nothing is indestructible**

Lisbon >> 08 >> 2014

Peace never stays in Portugal for long. Two months after the Troika left the country and Portugal recovered its economic sovereignty, one of the biggest national banks, needed to be rescued. The economic recovery has been affected by this situation and Portuguese are flabbergasted witnessing how one of the greatest economic institutions of the country, owned by the richest family in Portugal, is being rescued. Nothing is indestructible.

After several weeks of daily scandals in the media, and its respective depreciation of assets, a temporary solution for the BES (*Espirito Santo Bank*) crisis was taken during the late hours in the first weekend of August. Different members of the Government, *Banco de Portugal*, the European Commission and the ECB locked themselves in a room and did not leave until they had a viability plan for the BES. No doubts they were in a hurry: the Friday before, the bank's share was €0.10 at the closure of the Stock Exchange of Lisbon. Five days before the share was around €0.5 (just a month before it was ten times higher).

The reasons for this depreciation were found in the publication of their half-year results which showed losses of about 3,755 million euros. This extremely high loss made it impossible for the bank to propose a capital increase and therefore without any financing capacity. It was an unsustainable situation; a total blockade. The fear to the collapse of the bank in the Stock Exchange the following day speeded up a solution on Sunday.

Through electronic signatures the Government approved the plan without convening the Council of Ministers (something permitted by law in special occasions) and gave full power to the Governor of the *Banco de Portugal* to negotiate the best solution. Early morning the President announced the legislative modification approved in the Emergency

Ordinance. The BES was divided last Sunday into two different parts: on one side there is the "bad bank" which compiles the toxic assets such as family business and other companies of the group with troubled assets. The final objective of the bad bank is to disappear. This is one of the key-points of the plan: BES current shareholders lose, apparently, all their investment. We will see if they get something back.

On the other side, last Sunday a license for a new financial institution, *Novo Banco*, was opened. It will keep the profitable assets, all the clients and old deposits from the BES. Once peace is back and after a few months, *Novo Banco* will be sold. In order to have financing capacity, the bank has received 4,400 euros capital from the Bank Resolution Fund (created by the banking system which already had €500 million). The Bank Resolution Fund has received money directly from Europe, through the *Banco de Portugal*. This capital is part of the line of credit opened for Portugal in 2011 by the Troika and which was not fully used.

This is the first time Europe implements such a solution and it is completely supported by the Commission, which quickly backed the operation. The main actor interested on the success of this measure is the Commission, since this solution goes in line with the new meaning of politics demanded by European citizens: those responsible have to pay, not even a cent must be spent to save banks (that we shall see), and middle class deposits must be protected.

**HOW HAVE WE GOT HERE?**

At the beginning of June this year, the BES made a capital increase of more than one billion euros, which was approved by the Portuguese regulator! When issued, they recognized their credit exposure was far above the sector's average. Investors were aware BES was not exactly the most solvent bank, but the seriousness of the situation was unknown for the public.

The Media attention was focused then on the BES and their movements and figures. Those bad numbers which were not a big worry just a few weeks and months before appeared all of a sudden in covers of the main newspapers, the news, and became a daily a scandal, a constant and endless polemic.



During those first weeks, thanks to journalistic investigations, KPMG covert audits which were uncovered and BES declarations to their subsidiaries and appearances, crucial data became available. If we could identify the very first sin that would be in 2008 when the holding decided to cover losses of €180 million on their Espirito Santo International subsidiary. This “small” loss reached in 2013 €1,300 million. During those five years, the group tried several movements in order to cover real results (movements which in the next few months someone will have to decide which ones were legal and which ones were immoral).

“This was the shocking and live fall of the most powerful family of the country and its vehicle to success: the bank”

This complicated the global accounts of the bank and the whole group and the situation was worsening by risky operations. By the end of 2013 only the 20 biggest clients of the bank represented almost 13% of the entity’s overall exposure.

All front pages during the last weeks have put in the eye of the storm the BES, its companies, participations and specially its directors. Pressured by the public opinion and wandering about the steps to be taken, the help of *Banco de Portugal* and the Ministry of Economy and Finances not been very useful. It has been a “striptease” of suspicious accounts and financial movements; then, the management of the family Espirito Santo was completely naked to the public. And finally, the cherry on the cake: the untouchable former president, Ricardo Salgado, forced to resign two days before, was arrested at his home due to fraud in a parallel process held by the Judicial Police.

This was the shocking and live fall of the most powerful family of the country and its vehicle to success: the bank.

## KEYS

What conclusions can be made? What is next? How does this situation affect the Portuguese Economy? What should be taken into account?

- **The BES crisis has had a measurable but moderated impact in the Portuguese Economy.** Since the beginning of the scandal, the Portuguese risk premium has grown in 30 points regarding the German one (from 220 to 250). The PSI-20 (Portuguese Stock Index) has fallen from 7,400 at the beginning of June to 5,700 during the first week of August. There can be other reasons for this behavior, but there is no doubt the BES is the main responsible. September should be a month to improve if there are not more scandals regarding the BES or similar cases.
- **Impact on the country’s situation and reputation: a reality and also an opportunity.** Economy is all about trust, and the BES crisis has created a feeling of uncertainty in external markets regarding investments in the country (something which will be clearly seen in numbers in the near future). There is also a lack of

movement between businessmen and managers which are still wondering how it can affect the economy recuperation’s rhythm.

» An essential key is how the Government and the *Banco de Portugal* will manage the crisis during the next weeks and months. The crisis should be framed in a past scenario which has no vacancy now in order to isolate the problem and protect and save the economic data. The system has known how to face a financial group which has covered losses and which was not transparent,

and has saved the citizen’s money and arrested those considered untouchable and those to blame, no matter who they are and where do they come from. If they do a good management, the situation could turn into a great communication chance for the Government in the medium term.

» The governor of *Banco de Portugal* has firmly said that all responsibilities will be cleared. There is no doubt justice will act quickly in this crisis.

- **Stability is guaranteed...so far.** Although the solution was taken too fast it has all the support needed: *Banco de Portugal*, the Government, the European Commission and even the political opposition in Portugal who did not want to argue the plan’s conditions. Another positive point is the political stability which has finally arrived to the coalition government PSD-CDS.
- **The future of Novo Banco.** During the first days no great capital flights have been registered. There is an expectation feeling rather than nervousness among consumers and communication media.
  - » There is already interest on buying the bank once it will be on sale in a few months (the exact data is not being set and it will not be until the operation is viable). It is already an attracting identity due to its implementation, number of clients and quality of its assets. What it is of great importance is that the operation will have to be treated with great sensitivity facing the public opinion, once the situation has been studied and there is an alley structure (good defense to face possible attacks).
- **Autumn of recuperation with possible surprises.** The only aspect that should worry Portugal is the legal one. The Constitutional Court will still declare about the constitutionality of some cut measures by September/October. If it is an adverse resolution, the Government will have to reduce even more the expenditure approved for 2014 and the state’s budget for next year. There are constant rumors about an increase on tobacco and alcohol (wine included) taxes as well as the creation of new taxes on products with excessive amounts of sugar and fat.



>> **Carlos Ruiz Mateos** is Director of operations by LLORENTE & CUENCA in Lisbon (Imago-LLORENTE & CUENCA) and a member of the company's Steering Committee for the Iberian Peninsula since July 2013. Carlos Ruiz Mateos coordinates the activity in Portugal of our online communications, public affairs and corporate communications teams, where he advises clients such as Endesa, Banco Best, Sonae Sierra and BPI. Specialized in public affairs and institutional communication, Mr. Ruiz Mateos joined the firm in 2007 and has since developed various political, cultural and crisis communications projects (Ministry of Environmental Affairs, Iberdrola, SGAE, Grupo Siro, L'Oréal) and public affairs projects (Altadis, Peugeot, Ecoembes). Between 2011 and 2013, he was part of our team in Panama and advised clients such as the Ministry of Foreign Relations of Panama, Telefónica and Gas Natural. A Bachelor of Humanities and Journalism from Universidad Carlos III de Madrid, he holds a post-graduate degree in Election Campaign Management from ICADE and is a specialist in Peaceful International Conflict Resolution from the Spanish National Distance Education University (UNED).

AMO is the leading global network of strategic and financial communications consultancies, with over 940 professional consultants and offices in more than 20 countries.

The network brings together local market leaders with unrivalled knowledge of financial markets and cross-border transactions in the key financial centers of Europe, Asia and the Americas.

Providing sophisticated communications counsel for M&A and capital market transactions, media relations, investor relations and corporate crises, our member firms have established relationships with many S&P 500, FTSE 100, DAX 30, SMI, CAC 40 and IBEX 35 companies.

[www.amo-global.com](http://www.amo-global.com)



d+i es el Centro de Ideas, Análisis y Tendencias de LLORENTE & CUENCA.

Porque asistimos a un nuevo guión macroeconómico y social. Y la comunicación no queda atrás. Avanza.

d+i es una combinación global de relación e intercambio de conocimiento que identifica, enfoca y transmite los nuevos paradigmas de la comunicación desde un posicionamiento independiente.

d+i es una corriente constante de ideas que adelanta nuevos tiempos de información y gestión empresarial.

Porque la realidad no es blanca o negra existe d+i LLORENTE & CUENCA.

[www.dmasillorenteycuenca.com](http://www.dmasillorenteycuenca.com)

