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Eurozone agrees second Greek bail-out

By Peter Spiegel and Alex Barker in Brussels

Evangelos Venizelos, Greek finance minister, and Lucas Papademos, Greek prime minister, give a joint press conference after the Eurogroup meeting

Eurozone finance ministers reached a long-delayed €130bn second bail-out for Greece early on Tuesday after strong-arming private holders of Greek bonds to take even deeper losses than they had accepted last month.

Although Greek bondholders agreed in October to accept a 50 per cent cut in the face value of their bonds in face-to-face negotiations with Nicolas Sarkozy, France's president, and German chancellor Angela Merkel, they will now be offered a "voluntary" deal with a haircut of 53.5 per cent, eurozone officials announced.

"The new programme provides a comprehensive blueprint for putting the public finances and the economy of Greece back on a sustainable footing," said Jean-Claude Juncker, chairman of the eurogroup of finance ministers.

Both Mr Juncker and Christine Lagarde, managing director of the International Monetary Fund, emphasised at a post-meeting press conference that Greece still had to live up to a series of "prior actions" by the end of the month before eurozone governments or the IMF can sign off on the new programme.

In addition, the bail-out comes with tough new terms, including a permanent team of monitors in Greece to ensure Athens lives up to the terms of the bail-out deal and an escrow account which Greece will ensure always holds three months worth of debt payments. The escrow account will be temporary, however, and Athens has agreed to change its constitution to make debt repayment the top priority in government spending.

The euro jumped on news a deal had been agreed to as high as $1.3293 against the dollar, before later falling back to $1.3262. European shares are expected to open higher at the open of trading at 0800 GMT.

According to European diplomats, the German and Dutch finance ministers pushed for further "haircuts" in Greek bonds after a confidential debt analysis showed the previously-negotiated deal would cost international lenders €136bn and would only lower Greek debt to 129 per cent of economic output by 2020.

The diplomats said Jan Kees de Jager, the Dutch finance minister, and Wolfgang Schäuble, his German counterpart, sent Greek leaders back to bondholder representatives, who were nearby in Brussels for the all-night meeting, to agree further cuts at least four times over the course of nearly 14 hours of negotiations.

Official lenders also agreed to increase their burden to get Greek debt levels to 120.5 per cent of economic output by 2020, officials said. They agreed to cut the interest rates on bail-out loans to Greece by 0.5 percentage points over the next five years and 1.5 percentage points thereafter. Officials estimated this would cut €1.4bn from the bail-out package and lower debt levels by 2.2 percentage points in 2020.

Those lower rates mean eurozone member states may actually be lending to Greece below levels that they can borrow, meaning they will be losing money on the loans. In order to compensate for those losses, the European Central Bank agreed to distribute profits on its €40bn in Greek debt holdings to member states, which will bank the returns.

In addition, eurozone countries agreed that their national central banks, which hold €12bn in Greek bonds, will contribute all income generated from those bonds to Greece through the end of the decade. Officials said that would cut an additional €1.8bn from the bail-out package and lower Greece's debt by 1.8 percentage points in 2020.

The most unexpected development, however, came with the private bondholders. Negotiators had believed they had a deal with government officials last month which would have reduced the long-term value of their bonds by about 72 per cent.

But in the bond swap that will be used to execute the debt restructuring, private bondholders will not only receive new bonds with a lower face value, but their interest rates will be significantly lower than the deal struck last month. In a statement issued by representatives of private bondholders, the new interest rates – 2 per cent for the first three years, 3 per cent for the next five, and 4.2 per cent thereafter – were described as "well below market rates".

The statement from Charles Dallara, managing director of the Institute of International Finance, and Jean Lemierre of French bank BNP Paribas, falls short of an outright endorsement of the new deal. Instead, the two lead negotiators said they recommend "all investors carefully consider the proposed offer" saying that it is "broadly consistent" with the deal they struck with Mr Sarkozy and Ms Merkel in October.

Left unannounced was how the new bail-out programme would be divided between the EU and the IMF. Ms Lagarde would say only that "the eurogroup expects the IMF to make a significant contribution". Initial figures distributed last week suggested the IMF would only contribute €13bn to the €130bn in new Greek funding.

Ms Lagarde reiterated her desire to see the eurozone increase the size of its rescue funds and said that the IMF board would consider progress on the proposal "to set up a decent firewall" in weighing its contribution. Mr Juncker said he was optimistic such a deal could be reached at an EU summit in March, though Germany has been reluctant.

Klaus Regling, head of the eurozone's rescue fund, said his agency would quickly issue €70.5bn in bonds for the bond swap, which is likely to be launched in a matter of days. That includes €35bn needed to ensure Greek banks maintain access to ECB funds for day-to-day operations during the bond swap, when Greece is likely to be declared in "selective default".

Mr Regling said he also stood ready to issue additional bonds if needed to recapitalise Greek banks quickly.