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Germany's and France's potential losses if Greece declares insolvency

As speculation grows over Greece's possible exit from the Eurozone, or its insolvency within the Eurosystem, what are the financial implications of both scenarios for the German and the French states? This question is best answered by taking a look at the figures involved.

Should Greece become insolvent and exit the Eurosystem, Germany and France would face losses of up to 82 billion euros or 62 billion euros, respectively. If, however, Greece were to become insolvent but remain in the Eurozone, Germany and France must reckon with losses of up to 89 billion euros and 67 billion euros, respectively.

These figures take into account the amounts already paid out from both bail-out packages for Greece, purchases of Greek sovereign bonds by the central banks of the Eurozone countries, the Target liabilities of the Greek central bank (status: end of April 2012), Greek liabilities arising from its disproportionate issuance of bank notes and the Greek central bank's claims against the Greek banking system. They do not take into account the write-off losses of German and French private creditors, notably banks and insurance companies.

International funds for Greece – Germany's and France's exposure

Funds paid out (data as of 24 July 2012) in billions of euros

		Total	German share	French share
(1)	First Euro countries' bail-out package	52.9	15.2	11.4
(2)	First IMF bail-out package	20.1	1.2	0.9
(3)	Second Bail-out package (EFSF)	73.9	21.5	16.1
(4)	Second IMF bail-out package	1.6	0.1	0.1
(5)	Greek sovereign bond purchases	45	12.4	9.3
(6)	Greek Target liabilities (April 2012)	96.9	27.0	20.3
(7)	Greek liabilities arising from the dis-proportionate issuance of bank notes (April 2012)	17.4	4.8	3.6
	Total in the case of insolvency and exit (sum of entries 1 to 7)	**307.8**	**82.2**	**61.7**
(8)	Greek central bank claims against the	137.5	38.3	28.8

	banking system (June 2012)			
	Total in the case of insolvency within the Eurozone (sum of entries 1 to 5 and 8)	**331.0**	**88.7**	**66.6**

Notes:
(1) and (2): The original amounts were 80 billion euros and 30 billion euros, respectively; the sums not paid out were transferred to the second bail-out package.
(5): estimate, excluding purchases of Greek sovereign bonds by the Greek central bank.

Germany's and France's shares
Of (1): contractually fixed
Of (2) and (4): based on the country's respective IMF quota (6.1% and 4.5%)
Of (3): share in the EFSF contribution key; adjusted for "Stepping out Guarantors" Greece, Ireland and Portugal (29.1% and 21.8% for Germany and France, respectively)
Of (5), (6), (7) and (8): share in ECB's capital excluding Greece (27.8% and 20.9% for Germany and France, respectively).

In the first sum the two countries' losses are calculated for the case that Greece becomes insolvent and exits the Eurozone. In this scenario the legal relationship between the ECB and Greece's commercial banking system is dissolved, but the ECB's target claims against Greece, as well as its claims arising from the Greek central bank's disproportionate issuance of bank notes, have to be written off. Germany and France would only stand to lose their respective shares in these ECB claims. For Germany this would be a loss of up to 82.2 billion euros, and for France one of 61.7 billion euros.

The second sum relates to the scenario in which Greece becomes insolvent, but remains in the Eurozone. In this case, the calculation is somewhat different because the ECB system as a whole would still hold claims against the Greek banks, as well as Emergency Liquidity Assistance (ELA) claims against the Greek state, which overlap with Target claims, and these claims would have to be written off. Based on the assumption that if a state declares insolvency its banks will also be bankrupt, and given that the collateral given by these banks to their central bank in any case mainly consists of sovereign bonds or state-guaranteed securities, the losses are even higher than if Greece exits. If no refinancing loans can be repaid, losses also arise from the share of the normal refinancing loans given in Greece itself that enabled the Greek central bank to provide the Greek economy with liquidity. In this scenario, instead of shouldering their share of the losses arising from Target credit, Germany’s and France’s exposure would equal the sum of the Greek central bank’s claims against the Greek banking system. Since the latter total 137.5 billion euros and Germany’s share equals 27.8%, the 27 billion euros in Target losses and 4.8 billion euros in losses arising from the issuance of bank notes cited in the calculation above would now be 38.3 billion euros, adding up to a total loss of 88.7 billion euros, as indicated in the last line of the table. A similar calculation for France results in a loss of 66.6 billion euros.

Sources: German Federal Ministry of Finance, IMF, EU Commission, EFSF, ECB, Bank of Greece, calculations by the Ifo Institute.