

Guidelines of the Swiss National Bank (SNB) on Monetary Policy Instruments

of 25 March 2004 (as at 1 January 2010)

1. Purpose and applicability

These guidelines outline the instruments and procedures used by the Swiss National Bank (SNB) to implement its monetary policy. They set out the details of operations summarised in art. 9 para.1 of the Swiss National Bank Act (NBA) of 3 October 2003, which the SNB may use in fulfilling its monetary policy mandate. The guidelines do not directly create any rights and obligations of the SNB with regard to its counterparties or any rights and obligations of counterparties with regard to the SNB. The SNB may deviate from the procedures and terms set out in these guidelines at any time without prior notification.

The guidelines are based on the SNB's current monetary policy strategy which specifies that monetary policy is implemented by influencing interest rates on the money market. For this purpose, the SNB sets a target range for the three-month Swiss franc Libor. As a rule, this target range extends over one percentage point, and the SNB generally aims to keep the Libor in the middle of the range. It steers the three-month Libor indirectly, influencing the situation in the short-term money market by means of open market operations. If the SNB wishes to prevent money market rates from rising, it will provide the market with a greater amount of liquidity at lower rates. Conversely, it can bring about a rise in money market rates by ensuring a tighter and more expensive supply of liquidity.

The present guidelines are supplemented by instruction sheets published by the SNB, which set out the terms and procedures for monetary policy operations. They are principally aimed at the SNB's counterparties. In addition, counterparties are bound by the General Terms and Conditions of the SNB and by any specific contractual agreements they have entered into. Internal regulations and the powers of signature determine the authorisations and powers of SNB executive bodies and employees in monetary policy operations.

2. Monetary policy instruments

For monetary policy instruments, a distinction is made between open market operations and standing facilities. In the case of open market operations, the SNB takes the initiative in the transaction, while for the standing facilities it

merely specifies the conditions at which counterparties can obtain liquidity. In open market operations, the focus is on repo transactions. An additional instrument is the issue of the SNB's own debt certificates. Standing facilities include the liquidity-shortage financing facility and the intraday facility. If necessary, the SNB may also use additional monetary policy instruments such as foreign exchange swaps.

Repo transactions are the SNB's major monetary policy instrument. The SNB may conduct repo transactions in the form of auctions, on the interbank market or with individual counterparties. For repo transactions within the context of open market operations, collateral eligible for SNB repos must cover 100% of the funds obtained at all times. In the case of repo transactions within the context of standing facilities, the cover must amount to at least 110% of funds obtained.

2.1 Open market operations

The purpose of SNB open market operations is to provide liquidity for the money market. The SNB is able to create liquidity and absorb it again.

Repo auctions are conducted either by volume tender or by rate tender. The SNB generally sets the maturity of repo transactions in such a way that the banking sector has to request liquidity from the SNB on a daily basis to fulfil its payment obligations and meet minimum reserve requirements. The constant demand for liquidity from the banking sector enables the SNB to influence money market rates on a daily basis.

Repo auctions are normally held daily via the Eurex Zurich Ltd electronic trading platform. The SNB sets the terms on which it will conclude repo transactions, generally at 9 a.m. via the electronic market information services and the trading system. The maturity of repo transactions may vary from one day (overnight) to several months.

The SNB may also influence price-setting in the money market at any time, by placing or accepting offers for repo transactions in the electronic market. In this way, it can help to stabilise short-term money market rates.

In addition, the SNB can issue its own interest-bearing debt certificates (SNB Bills) in order to absorb liquidity. This increases its flexibility in steering liquidity. SNB Bills are issued publicly by auction or through private placing. Auctions are conducted either by volume tender or by rate tender. The National Bank may repurchase SNB Bills during their term and sell them again. Interest on SNB Bills is payable on a discount basis. Further details on SNB Bills may be found in the document, "SNB Bills – issue conditions", as well as in the conditions for individual issues.

2.2 Standing facilities

The SNB provides a liquidity-shortage financing facility to bridge unexpected, short-term liquidity bottlenecks. These mainly occur if expected payments are not received and the required funding cannot be obtained quickly enough on

the interbank market. This facility may also be necessary to ensure that minimum reserve requirements are met at the end of a reporting period.

The liquidity-shortage financing facility is made available through overnight repo transactions at a special rate. The prerequisites for concluding special-rate repo transactions are the granting of a limit by the SNB and the provision of collateral eligible for SNB repos. Such cover must amount to 110 percent of the limit at all times. The maximum amount of liquidity that a counterparty can obtain is determined by the limit, which is normally set for a year, but may be withdrawn by the SNB, subject to a ten day period of notice.

The counterparty opens a separate safekeeping account in its own name with SIX SIS Ltd (SIS). This is known as a Custody Cover Account “SNB”. The counterparty deposits collateral eligible for SNB repos, which must be pledged in favour of the SNB. Provided the cover regulations are observed, these securities can be managed by the counterparty. In addition, they may be used during the day for obtaining intraday liquidity. SIS is responsible for monitoring compliance with the cover regulations. The SNB has the right to inspect its counterparties’ custody cover accounts at SIS at all times.

The special rate is based on the SARON (Swiss Average Rate Overnight) plus an interest premium. The special rate is announced daily through the electronic market information services. The interest premium is intended to prevent counterparties from using the facility as a permanent source of refinancing.

The SNB also provides its counterparties with interest-free liquidity during the day through repo transactions carried out within the context of its intraday facility. In this way it facilitates the settlement of payment transactions via the Swiss Interbank Clearing system (SIC) and foreign exchange transactions in the Continuous Linked Settlement system (CLS). The liquidity must be repaid by the end of the same bank working day at the latest. Consequently, these funds are not included when calculating liquidity requirements under banking law and compliance with SNB minimum reserve requirements.

2.3 Further monetary policy instruments

In addition to the monetary policy instruments mentioned above, the SNB may also use additional monetary policy instruments such as those listed here:

- The SNB may purchase or sell foreign currencies spot or forward (see art. 9 para. 1 (c) NBA). Foreign exchange transactions may be used in market interventions on the exchange markets to influence the rate of the Swiss franc against foreign currencies.
- The SNB may enter into foreign exchange swaps (cf. art. 9 para. 1 (c) NBA). These may be used to steer liquidity.
- The SNB may create, purchase or sell derivatives on receivables, securities, precious metals or pairs of currencies (cf. art. 9 para. 1 (c), (d) NBA). Derivatives on foreign currencies may also be used to step up intervention in foreign exchange markets.

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- The SNB is authorised to accept interest-bearing cash deposits (cf. art. 9 para. 1 (a) NBA), enabling it to absorb excess liquidity by implementing a deposit facility.
 - The SNB may purchase or sell Swiss franc-denominated securities for monetary policy purposes (cf. art. 9 para. 1 (c) NBA) in order to influence long-term interest rates in exceptional situations.

3. Collateral eligible for SNB repos

In accordance with art. 9 para. 1 (e) NBA, the SNB may enter into credit transactions with banks and other financial market participants, on condition that sufficient collateral is provided for the loans. As a rule, open market transactions are conducted through repo transactions, and repos are also the main instrument in the utilisation of standing facilities.

The SNB may accept securities (debt certificates) denominated in Swiss francs and foreign currency as collateral provided the following criteria are met:

- The securities are issued by central banks, public sector entities, international or supranational institutions and private sector entities. Securities issued by domestic banks and their subsidiaries abroad are not generally eligible as SNB collateral.
- The issuer is domiciled in Switzerland, in a member state of the European Union (EU) or the European Economic Area (EEA). Securities denominated in Swiss francs and securities of international or supranational institutions may be eligible as SNB collateral, irrespective of the issuer's country of domicile.
- The securities are denominated in Swiss francs, euros, US dollars, pounds sterling, Danish kroner, Swedish krona and Norwegian krone.
- Both the issuer's country of domicile and the securities have at least the equivalent of an A rating. Country and securities ratings are based on credit ratings of at least one of the rating agencies recognised by the Swiss financial market supervisory authority, FINMA. Securities issued by sovereign countries and securities issued in Swiss francs by domestic borrowers may be exempt from the rating requirements.
- The minimum volume of the securities at the time of inclusion in the list of collateral eligible for SNB repos is CHF 100 million for securities denominated in Swiss francs or the countervalue of CHF 1 billion for securities denominated in foreign currencies. The issued volume determines the minimum volume.
- As a rule, the securities are traded in Switzerland or an EU or EEA member state on a recognised stock exchange or a representative market where price data are published on a regular basis.
- The securities can be delivered through SIS. The intermediate and ultimate depository of securities is in Switzerland or an EU or EEA member state.

These conditions are set out in detail in the SNB instruction sheet on collateral eligible for SNB repos. Only securities included in the list of collateral eligible for SNB repos may be pledged as collateral for repo transactions. The SNB determines which securities are eligible for SNB repos. It may reject the inclusion of securities or withdraw securities that were previously included in the list, without providing any justification.

The SNB does not accept counterparties' own securities or those issued by persons or companies that form an economic unit with the counterparty. An enterprise is deemed to belong to the same economic unit as the counterparty if 20 percent or more of the capital or voting rights are held. This 20 percent rule does not apply to participations in mortgage bond banks or similar institutions. Failure to comply with this rule may cause the SNB to temporarily exclude the counterparty from its monetary policy operations.

Irrespective of the criteria set out in these guidelines, SNB debt certificates will be included in the list of securities eligible for SNB repos. In repo transactions, they may be delivered either by counterparties or by the SNB.

4. Eligible counterparties

All domestic banks with sight deposits at the SNB are in principle admitted as counterparties for SNB monetary policy operations.

Other domestic participants in the financial market as well as banks and other financial market participants that are domiciled abroad may be admitted as counterparties for monetary policy operations provided this serves monetary policy interests, the participants or banks contribute to the liquidity of the secured Swiss franc money market, and the requirements for opening a sight deposit account are met.

The SNB's transactions are normally concluded on the Eurex Zurich Ltd electronic trading platform and settled through SIS and SIC. In addition to holding a sight deposit with the SNB, the counterparty must therefore meet the cumulative requirements of all three partners of the SNB in order to be able to undertake monetary policy-related transactions with the SNB. SNB counterparties must have a direct connection to the SIC system.

5. Contractual basis and settlement of repo transactions

The General Terms and Conditions of the SNB and the Swiss Framework Agreement on Repo Transactions (or the PSA/ISMA Global Master Repurchase Agreement, 1995 Version with Swiss Annex) form the contractual basis for monetary policy-related repo transactions with the SNB.

In a repo transaction, the cash taker sells certificated or uncertificated securities to the cash provider. At the same time, the cash taker enters into an

agreement to repurchase securities of the same type and amount from the cash provider at a subsequent point in time. The cash taker pays interest (repo rate) for the duration of the transaction. The cash provider passes on any interest payments relating to the securities received during the period of the repo transaction to the cash taker.

SIS settles repo transactions on the basis of 'delivery versus payment'. The securities are transferred to the SIS account of the cash provider. At the same time, the funds are credited to the cash taker's SIC account. To limit counterparty risk, SIS revalues the securities daily at market prices and compares the valuation with the funding side. If there is a discrepancy between the funding and securities sides between two counterparties, this must be covered by securities or cash (margin call). The SNB may set a unilateral tolerance limit (maintenance margin) for each counterparty. When a repo transaction matures, reverse settlement is triggered by SIS. The settlement procedure factors in the repo rate.

6. Emergency liquidity assistance

In accordance with art. 9 para. 1 (e) NBA, the SNB also acts as lender of last resort. In this function, it can provide extraordinary liquidity assistance for one or more domestic banks if they are no longer able to refinance their operations on the market. This extraordinary liquidity facility depends on the following conditions:

- The bank or group of banks requiring credit must be of systemic importance for the stability of the financial system
- The bank requiring credit must be solvent
- Sufficient collateral must be provided at all times to cover the liquidity assistance

A bank or group of banks is of systemic importance if its inability to pay would seriously impair the functioning of the Swiss financial system or major parts thereof, and have a negative impact on the real economy. To assess the solvency of a bank or group of banks, the National Bank obtains an opinion from the Swiss financial market supervisory authority, FINMA. The SNB determines what collateral is sufficient.

7. Publication of data relevant to monetary policy

Under art. 7 para. 4 NBA, the SNB is required to publish data relevant to monetary policy on a weekly basis. As a guide for members of the financial community, the SNB makes the following information available:

- a) SNB benchmark interest rates
 - Target range for three-month Libor

- Three-month Libor
 - Special rate for liquidity-shortage financing facility
- b) Information on CHF repo benchmark rates
- c) Average weekly balances on sight deposits held by domestic banks
- d) Minimum reserves
- Average balances on sight deposits held by domestic banks in the previous period and in the reporting period
 - Aggregate fulfilment of the minimum reserve requirements in the past 12 reporting periods, broken down by minimum reserve requirements, eligible assets and fulfilment in percent

These data are published on the first bank working day in a calendar week on the standard market information platforms, on the SNB website and by fax to the media.

8. Amendments to these guidelines

Any amendments to these guidelines will be determined by the Governing Board.

Issued by the Governing Board on 25 March 2004.

Amended on 29 June 2006, 28 June 2007, 20 November 2008, 25 August 2009 and 17 December 2009 (entry into force on 1 January 2010).