

Other central bank functions

1 Investment of assets

1.1 Fundamentals

The National Bank's assets essentially consist of gold and foreign currency reserves as well as domestic financial assets (domestic securities and money market assets). They represent a part of Switzerland's national wealth and perform important monetary policy functions. Their composition is determined by the established monetary order and the requirements of monetary policy.

Part of the National Bank's assets serve directly for implementing monetary policy. We acquire assets in order to supply the economy with base money. These assets represent the countervalue to the monetary base, thus promoting confidence in the value of our currency. For controlling the monetary base, we employ mainly foreign-exchange swaps and domestic assets. Foreign-exchange swaps constitute dollar reserves which are hedged in the forward market.

Unhedged foreign exchange reserves are held mainly in key currencies. They represent an instrument for intervening in the market in the event of a Swiss franc weakness. We can sell unhedged foreign exchange reserves at any time against Swiss francs if we need to support the external value of our currency. Unlike foreign exchange reserves, our gold holdings cannot be used for interventions. For the time being, the Swiss franc is still linked to gold by law. This means that we can only buy and sell gold at the official price, which lies distinctly below the market price. Nevertheless, both gold holdings and foreign exchange reserves play a decisive role as a national emergency provision. They help to ensure that Switzerland remains solvent vis-à-vis foreign countries even in emergencies.

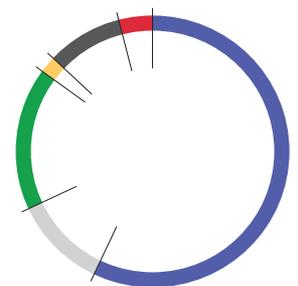
The National Bank Law specifies both the type of assets we may acquire as well as the instruments we may employ for their management. Within the limits set by legal provisions and our monetary policy mandate, it is our endeavour to manage our assets as profitably as possible. The revision of the National Bank Law which became effective on 1 November 1997 has increased our leeway for managing our gold and foreign exchange reserves. We may now invest our foreign exchange reserves in more markets and currencies, and therefore more profitably in the long term, without overall having to sustain greater fluctuations in earnings. Moreover, the revised law enables us to employ a part of our gold reserves for gold lending.

Nature and purpose of the National Bank's assets

The role of domestic assets and hedged foreign exchange reserves

The role of unhedged foreign exchange reserves and gold holdings

Increased leeway for investing our international reserves



Structure of National Bank assets in percent

Unhedged foreign exch. reserves	57
Foreign exchange swaps	11
Gold	17
Other domestic assets	2
Domestic financial assets	9
Other foreign currency assets	4

Total: Sfr 69.9 billion.
Balance sheet values, ann. average

1.2 Foreign exchange investments

Investment policy

We invest our foreign exchange reserves in safe and liquid securities, and a small proportion in time deposits at prime foreign banks. This enables us, in case of need, to sell the investments at short notice and without incurring undue losses. We are permitted by the National Bank Law to acquire easily marketable debt certificates of foreign governments, international organisations and foreign banks. When the revised National Bank Law entered into force, we began restructuring our foreign exchange investments in line with the new target portfolio. Previously, the residual maturity of any investment was not permitted to exceed twelve months.

Decision-making process concerning investments

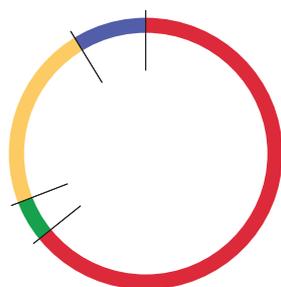
We adapted the decision-making process for investments to the new legal framework. The Governing Board issues investment policy guidelines in conformity with which the investment committee determines currency allocation and the interest rate risk. Our portfolio managers are guided by the reference portfolios for each individual currency. The yardstick for the success of our asset management are the yields achieved on the reference portfolios and the investment yield attained by an external portfolio manager with a part of our dollar investments.

Risk control

Concurrently with the expansion of the leeway for investment we also improved our risk control. The market and credit risks incurred on foreign exchange investments are constantly monitored. Internal credit limits take due account of the assessments of creditworthiness by reputed rating organisations.

Investment activity and results

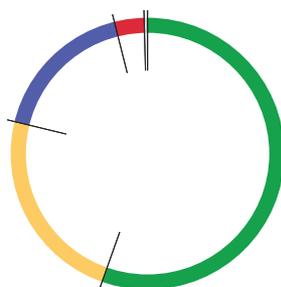
Our foreign exchange reserves have in the past been held in the currencies dollars, D-marks and yen. Since the revised National Bank Law became effective, we have also made investments in Dutch guilders. Compared to the previous year, the D-mark share was increased markedly to the detriment of the predominant dollar investments. Approximately 69% of all investments are accounted for by government securities or by securities with indirect government guarantee. The average duration of the dollar and D-mark portfolios before the revision of the National Bank Law was 4.5 months, and 3 months in the case of yen portfolios. Until the end of 1997, the duration of the entire foreign exchange reserves was extended to approximately one year. The yields achieved amounted to 5.8% for dollar investments, 3.2% for D-mark investments and 0.2% for investments in the yen. Due to the restriction on residual maturities until 1 November 1997 we



Foreign exchange reserves by debtor category in percent

Government securities 64
 Securities with indirect government guarantee 5
 Monetary institutions 22
 Remaining money market 9

Total: Sfr 49.6 billion.
 Annual average



Foreign exchange reserves by currency in percent

Dollar unhedged 55
 Dollar hedged 23
 D-mark 17
 Yen 4
 Dutch guilder 1

Total: Sfr 49.6 billion.
 Annual average

only benefited partially from the decline in interest rates in the first half-year. Leaving the exchange rate changes out of account, the overall yield on foreign exchange reserves stood at 5.2%, equivalent to gross earnings of approximately Sfr 2.5 billion.

1.3 Investment of domestic securities

Since the early nineteen-eighties we have been expanding our portfolio of domestic bonds by Sfr 100 million annually. We manage our bond holdings subject to the restriction that asset management may neither disrupt monetary policy nor profit from it. We therefore pursue an investment policy bound by rules and check its quality based on comparative indices. Purchases are spread evenly over the year. We are only authorised to buy public sector bonds, mortgage bonds and marketable bonds of domestic banks. Legally admitted debtor categories are considered more or less in relation to their market capitalisation. We avoid a concentration of investments on individual debtors by means of limits.

At the end of 1997 the market value of the portfolio amounted to Sfr 4,941 million, compared to Sfr 4,822 million in the previous year. The duration decreased from 4.3 to 3.8 years. Interest earnings on the portfolio totalled Sfr 254 million. Due to declining interest rates we achieved a price gain of Sfr 9 million. The yield on the portfolio amounts to 5.9%, which is equivalent to earnings of Sfr 263 million.

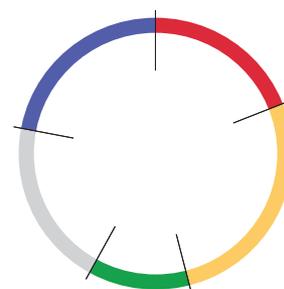
1.4 Gold lending

Since the revised National Bank Law entered into force we have engaged in gold lending business. In order not to disrupt the price structure in a relatively tight market, we exercise great restraint in building up our positions and only use a modest proportion of our gold holdings for lending. Our partners are first-class domestic and foreign banks and securities houses. They pay us interest for the temporary loan of gold. We control the risk by means of credit limits and by restricting the transaction periods.

Investment policy

Investment activity and results

Investment policy



Domestic securities by debtor category in percent

Confederation	19
Cantons	27
Communes	12
Mortgage bonds	20
Banks	22

Total: Sfr 4.8 billion.
Annual average

At the end of 1997 lending transactions covered 99 tonnes of gold. The average residual maturity of all gold lending transactions concluded amounted to approximately eight months. Between the start of this line of business and year-end we achieved earnings totalling Sfr 2.6 million, i. e. a yield per annum of 2.2%.

2 Payment transactions

2.1 Basis

Overview

In Switzerland, payment transactions are handled primarily by the National Bank, the commercial banks and the postal system. The banks' payment services are performed by the companies of the Telekurs Group. The National Bank supplies the economy (by way of the banks and the postal system) with banknotes and coins. It also acts as a settlements centre for cashless payments between the banks and between the postal service and the banks.

Developments relating to payment flows

Over the last few years, many of the organisations involved in cash transactions with the National Bank (such as the commercial banks, the postal service and security transport companies) have been rationalising their cash handling processes. Commercial banks with networks of branches are increasingly settling cash positions within their own organisations. Moreover, the banks and the postal service are tending to outsource an ever larger number of cash handling tasks to security transport firms. At the same time, flows of cash within the National Bank's network of branches are becoming more centralised. Furthermore, the fees charged by banks for cash deposits and withdrawals are causing cash transactions to shift away from the banks.

Developments relating to cashless payments

Since 1987, the Swiss National Bank – together with the Telekurs Group – has been operating the electronic SIC (Swiss Interbank Clearing) system. SIC is a Real-Time Gross Settlement (RTGS) system in which each payment transaction is performed individually via the participants' sight deposit accounts at the National Bank. These RTGS systems are already in use in some countries, while other countries are in the course of implementing them. The banks use SIC for handling their large-value payment transactions as well as part of their bulk payments. SIC is linked to the SECOM settlements system of SEGA (the Swiss Securities Clearing Corporation). This ensures that payment and delivery occur simultaneously ("delivery against payment"), thereby avoiding settlement risks. Since August 1997, the same principle has been applied to the settlement of SOFFEX transactions. The Swiss banks have recently announced the founding of a special clearing bank in Frankfurt: the Swiss Euro Clearing Bank (SECB). This will facilitate the processing of euro transactions similar to those performed in Swiss francs by SIC.

The other services provided as part of the banks' payment transactions – data carrier exchange (DTA), direct debiting (LSV) and cheque clearing – are net settlement systems. Interbank payments originating from cash withdrawals at Bancomat ATMs, ec-Direct EFT/POS transactions and (since July 1997) purchases with "CASH" prepaid cards are also settled on a net basis. The interbank claims which arise through the performance of these payments are settled at regular intervals – generally once a day – via the participants' sight deposit accounts at the National Bank. The payments system of the Swiss postal service is used mainly for bulk payments. The National Bank's postal service accounts provide a link between the payment systems of the banks and that of the postal service.

2.2 Provision of currency

Currency in circulation

In 1997, the average banknote circulation was Sfr 29 billion, i. e. 2.8% more than in 1996. At Sfr 2.1 billion, coins in circulation equalled the previous year's figure.

Manufacture and disposal of banknotes

The National Bank obtained 140 million freshly printed banknotes with a total face value of Sfr 47.8 billion from Orell Füssli Graphic Arts Ltd and added them to its stock. 142.5 million damaged or recalled notes with a face value of Sfr 19.2 billion were destroyed.

Currency turnover

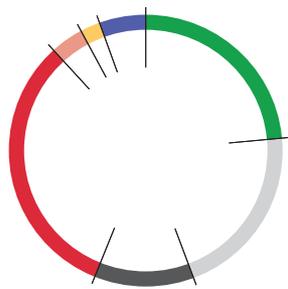
In 1997 the National Bank's branches registered a 6.1% increase in currency turnover in value terms, bringing the total to Sfr 153 billion. The branches received approximately 450 million notes (7.2% more than in 1996) and checked them for authenticity, quality and quantity.

New 10- and 200-franc notes

On 8 April 1997 the National Bank issued the new 10-franc note, the third in its new series of banknotes. This was followed on 1 October 1997 by the 200-franc note. The 10-franc note is dedicated to the architect and painter Charles Edouard Jeanneret, better known as Le Corbusier. The 200-franc note, which takes the place of the 500-franc note, depicts the writer Charles Ferdinand Ramuz. As a new security feature, a "perforated" image of the denomination "200" appears when the note is held against the light.

Completion of the new bank-note series by autumn 1998

The new 1000-franc note is appearing in the spring and the new 100-franc note in autumn 1998. The banknotes from the old series – issued between 1976 and 1979 – will remain legal tender until further notice. The notes from previous series, which were recalled in 1980, are redeemable by the National Bank up to 30 April 2000.



Bank notes in circulation

Denom. units (number in millions)



Annual average

*Issue in October 1997;
Average Oct. – Dec.

2.3 SIC payment transactions

At the end of 1997 there were 222 participants in SIC (end-1996: 218). During the year under review, an average of about 480,000 payments per day totalling approximately Sfr 182 billion were processed. About every two days, therefore, a volume roughly equivalent to Switzerland's annual gross national product is handled by the system.

Strong growth in SIC payments

Development of payment flows¹

	1993	1994	1995	1996	1997
Transactions per day (thousands)					
Average SIC	263	349	382	427	480
Average SECOM	–	–	13	20	39
Maximum SIC	580	925	1 154	1 156	1 303
Maximum SECOM	–	–	24	40	89
Volume per day (Sfr billions)					
Average SIC	133	131	128	150	182
Average SECOM	–	–	3	5	7
Maximum SIC	217	270	257	290	305
Maximum SECOM	–	–	7	10	14
Frequency of turnover²					
Average	63	61	57	58	58
Maximum	113	121	112	90	97

1 As from 27 March 1995, SECOM payments are contained in the SIC payments flow.

2 Average daily turnover per franc

SIC does not impose any restrictions regarding the size of the amounts handled. Alongside the large-scale payments, even very small sums are processed. The structure of the payments flow varies greatly in terms of volumes and amounts: whereas small sums (of up to Sfr 5,000) account for more than 80% of payments, they account for only 0.2% of the total volume. Conversely, large payments (Sfr 1 million and over) account for over 96% of the total volume but for less than 3% of the number of payments.

Structure of payments

Daily payments flow percent of total for each category

	1993	1994	1995	1996	1997
Number of payments					
Sfr 1–4 999	81.2	84.9	83.0	82.7	80.6
Sfr 5 000–999 999	15.1	12.3	14.5	14.8	17.0
Sfr 1 000 000 and over	3.7	2.8	2.5	2.5	2.4
Amount					
Sfr 1–4 999	0.2	0.2	0.2	0.2	0.2
Sfr 5 000–999 999	2.2	2.2	3.3	3.3	3.6
Sfr 1 000 000 and over	97.6	97.6	96.5	96.5	96.2

3 Statistical tasks

Basis

The National Bank collects from banks and other enterprises the statistical data necessary for performing its tasks. This data is used for analyses concerning monetary policy and economic activity and for drawing up the balance of payments. The information on the banks' balance sheets serves mainly for calculating the monetary aggregates. The data supplied by business enterprises on their foreign activities, notably direct investment, is reflected in the balance of payments. We are also responsible for compiling investment fund statistics and collect information on the money and capital markets. These statistics are drawn up by agreement with the data-reporting institutions and conform closely to international standards.

New data

In close cooperation with the banks, we developed a data base concerning the securities transactions of their customers. This should help us to gain an overview of the extent and composition of the securities portfolios managed by the banks. In 1997, the computation of interest risks was added to the statement on capital and reserves, which had been revised and considerably expanded in 1995. Within the context of the balance of payments statistics, we planned a new survey on the range of services offered by the banks.

4 Services on behalf of the Confederation

Basis

The National Bank acts as the bank of the Confederation. The National Bank Law lays down the services to be performed, prohibits deficit financing by means of central bank credits and stipulates that the services must be rendered free of charge. On this basis, we perform tasks on behalf of the Confederation in the payments field and in coinage, in borrowing on the money and capital markets and in the investment of funds.

Agent in the money market

The Confederation holds its liquid funds in the form of sight deposits and short-term time deposits at the National Bank. We pay interest on the Confederation's sight deposits up to an amount of Sfr 500 million at the call money rate, on time deposits at market rates. In the event of liquidity bottlenecks, we assist the Confederation in taking up money market credits from banks; if necessary, the Confederation must avail itself of a Lombard credit from the National Bank on the same terms as the banks.

Federal bonds and money market debt register claims

In 1997 we arranged 53 issues of money market debt register claims (MMDRC) and 7 bond issues on behalf of the Confederation. MMDRCs to the total amount of Sfr 89 billion were subscribed, and Sfr 49.8 billion were allocated. Bonds were subscribed for a total amount of Sfr 7 billion, of which Sfr 3.7 billion were allocated.

Federal bonds and money market debt register claims

	1993	1994	1995	1996	1997
Number of issues¹					
Federal bonds	16	16	7	10	7
MMDRC	24	52	52	52	53
Total subscribed in billions of francs					
Federal bonds ²	14.2	9.9	8.2	10.6	7.0
MMDRC	59.0	71.8	94.7	103.1	89.0
Total allocated in billions of francs					
Federal bonds ²	8.6	6.8	3.5	4.5	3.7
MMDRC	34.5	46.7	47.1	49.9	49.8
Outstanding at year-end in billions of francs					
Federal bonds	24.1	28.6	29.8	33.8	37.5
MMDRC	11.3	12.7	14.1	14.7	14.1

1 Based on date of payment

2 Excluding the National Bank's own tranche

Administration and processing services

The National Bank accepts payments on behalf of the Confederation and carries out remittances to third parties both in Switzerland and abroad up to the amount of the Confederation's sight balances. Federal agencies cover their cash requirements through withdrawals from the National Bank. The surplus liquid funds of the Confederation – notably those of the postal service and the Swiss federal railways – flow back to us via the banks. We also keep the federal debt register and administer security holdings and objects of value on behalf of the Confederation and associated institutions.

5 Cooperation with federal agencies

5.1 Cooperation with the Federal Banking Commission

Capital adequacy rules for market risks: revision of the Banking Ordinance and issue of guidelines by the Banking Commission

After the Basle Committee on Banking Supervision had passed the amendment to the capital adequacy agreement to include market risks in December 1995, a mixed working group under the chairmanship of the Federal Banking Commission, in which the Swiss National Bank was also represented, began translating these international minimum standards into Swiss law. The amended capital adequacy agreement for the first time provides the banks with the option of choosing between a standard procedure and models of their own for measuring a capital adequacy requirement. The draft submitted consisting of the revised capital adequacy rules of the Banking Ordinance and the relevant guidelines of the Banking Commission was submitted to the interested parties for comment in July 1997. The amended capital adequacy rules became effective on 31 December.

Comments of the National Bank

In its comments of September 1997, the National Bank welcomed the endeavours to avert potential losses of banks and securities dealers due to changes in market prices by means of adequate risk-weighted capital ratios. It regretted, however, that the implementation of the amended Basle capital adequacy agreement will, on the whole, probably lead to a lower level of capital and reserves. At the same time, it took account of the fact that due to international competition national law could hardly go beyond the minimum standards of the Basle Committee. The National Bank specifically suggested various changes to the draft of the Ordinance submitted, a number of which have been included in the final version.

Banking Law: status of the "cantonal banks"

The report – completed in December 1996 – on the status of the cantonal banks in the Banking Law, drawn up by a commission of experts in which the National Bank was also represented, was submitted to a consultation procedure by the Federal Department of Finance in February 1997. The draft of the message based on this report was submitted to the responsible federal agencies for comment on 5 November 1997 (consultation of government agencies). The major change is the abolition of the state guarantee as a constitutive element of a cantonal bank; instead, the essential characteristics of a cantonal bank will in future be a basis in a cantonal law and a participation of at least 30% by the respective canton. Moreover, all cantonal banks are to be subject to supervision by the Banking Commission. In its comments, the National Bank supported the proposed amendment to the Law. At the same time, it opposed the continued capital adequacy discount for cantonal banks as this threatens to distort competition and easily leads to the costs of the state guarantee being underestimated in actual practice.

Exchange of data between the Banking Commission and the National Bank

A joint working group of the Secretariat of the Banking Commission and the National Bank drew up a report in March 1997 on the question of whether, and if so, how the exchange of data between the National Bank and the supervisory authority could be intensified. It was established that a series of data is collected by both the Banking Commission and the National Bank. The working group recommended that the National Bank should compile these statistics and

put the required data at the disposal of the Banking Commission. To this end, the National Bank would have to introduce a number of new statistics and expand existing ones. On the other hand, the National Bank depends on the Banking Commission to supply it with the information required for resolving financial crises. The working group therefore suggested that the necessary legal basis for a mutual exchange of data should be laid down in the Banking Ordinance. In a consultation procedure involving the Swiss Bankers' Association, the Swiss Institute of Certified Accountants and Tax Consultants and the Federal Commissioner of Data Protection this proposal gained a positive reception. The text of an Ordinance is to be submitted to the Federal Council at the beginning of 1998.

5.2 Cooperation with the Federal Department of Finance

The National Bank participated in a working group under the chairmanship of the Federal Department of Finance which dealt with the implications of the introduction of the euro on the federal administration and the National Bank. In a preliminary report of October 1997, the working group identified possible problem areas and concluded that there was little need for action by the federal administration. Nevertheless, the necessary adjustments should be planned in good time in order to avoid capacity bottlenecks during the transition period. The National Bank will be affected by the introduction of the euro chiefly in the implementation of its monetary policy. On this question, the report refers to the study of the Commission for Economic Issues on the economic implications of the European Economic and Monetary Union of August 1996.

Working group on the euro

5.3 Switzerland's financial relations in the Second World War

The discussion on Switzerland's financial relations during the Second World War continued in Switzerland and abroad in 1997. It triggered activities on a broad front. The Swiss banks intensified their search for assets which had been deposited with them prior to 1945 and which have remained dormant ever since. The committee of historians appointed by the Federal Council on 19 December 1996 and chaired by Professor Jean-François Bergier began its task of investigating the fate of the assets deposited in Switzerland during the years of the National Socialist regime in Germany. In a concerted action the three big banks made Sfr 100 million available for victims of the Holocaust and their needy descendants; on 26 February 1997, the Federal Council created a special fund for this purpose. Other sectors of the business community contributed payments amounting to approximately Sfr 75 million to this fund.

Still a highly topical issue

Gold transactions of the National Bank in the Second World War

The gold transactions of the National Bank in the Second World War were also the subject of criticism. Between 1939 and 1945, within the framework of international payment transactions, the National Bank purchased gold worth Sfr 1.8 billion from the Allies and worth Sfr 1.5 billion from the Axis countries, of which Sfr 1.2 billion from Germany. The bulk of the gold acquired from the Axis countries was sold to other central banks. In a working paper of December 1997, which for the first time presented a flow chart of the Reichsbank's gold transactions, the Bergier committee of experts confirmed the National Bank's figures on their gold transactions in the Second World War. A large part of the Reichsbank's gold deliveries to Switzerland did not come from Germany's pre-war stocks, but stemmed from central banks and private persons in occupied countries. In the Washington Agreement of 1946 Switzerland undertook to pay Sfr 250 million towards the reconstruction of Europe, with the National Bank contributing Sfr 100 million to this amount. At the same time, the Allies waived all further claims to the gold acquired by Switzerland during the War. At the London gold conference in early December 1997 it was confirmed that the Allies, at the end of the War, had already possessed most of the important information on the Reichsbank's gold transactions and that therefore the Washington Agreement had been concluded in full knowledge of the facts.

The National Bank's contribution to the Holocaust Fund

The fact that from today's viewpoint the then management of the National Bank did not have a sufficiently critical attitude towards the Reichsbank, as well as the hardship experienced by the survivors of the Holocaust, however, led the Governing Board to consider a contribution to the fund in favour of needy Holocaust victims at the beginning of March 1997. On 25 June 1997, the Federal Council submitted a message to the federal parliament concerning the participation of the Swiss National Bank in the Holocaust Fund. With a generally binding federal decree, the National Bank was to be empowered to pay Sfr 100 million into the fund set up by the Federal Council. This contribution was intended as a gesture of humanity towards those still suffering from the consequences of persecution by the National Socialist regime.

Contribution to the fund on the SNB's own responsibility

In the September session, the National Council and the Council of States decided not to adopt the motion submitted by the Federal Council. In the parliamentary debates widespread approval of a contribution to the Fund by the National Bank was expressed. However, a majority in the two chambers were of the opinion that the National Bank's contribution did not require a special legal basis in the form of a federal decree, which would be subject to a referendum, but that the Bank could act on its own responsibility. Subsequently, in the second half of October, the Bank Committee and the Bank Council gave their approval to the contribution of Sfr 100 million to the Holocaust Fund. With the remittance of 3 November 1997 by the National Bank, the contributions by the Swiss business community to the Holocaust Fund totalled approximately Sfr 275 million.

Dormant accounts at the National Bank

The National Bank's first legal basis, the National Bank Law of 1905, authorised the National Bank to transact certain types of business with private persons in Switzerland and abroad. Research in our archives led to the discovery of a number of accounts and safekeeping accounts which could, in the broadest sense, be related to the issue of dormant assets. There were eight such cases to the total amount of approximately Sfr 15,000, some Sfr 11,000 of which were

attributable to foreign customers. The National Bank reported the names to the office designated by the Swiss Bankers' Association; they were included in the lists of holders of dormant accounts dating from the time prior to 1945 published on 23 July 1997 and 29 October 1997.

6 International cooperation

On an international level, the National Bank cooperates with the International Monetary Fund (IMF), the Group of Ten (G-10) – which represents the ten leading industrial countries and Switzerland – and the Bank for International Settlements (BIS). The National Bank also participates in international cooperation by providing technical assistance and specialist training.

6.1 Cooperation in the International Monetary Fund

In 1997, the responsible bodies of the IMF decided on a number of important measures, notably an increase in the capital of the IMF and a one-off selective allocation of Special Drawing Rights (SDRs).

The capital of the IMF, i. e. the quotas of the member countries, is to be increased by 45% to 212 billion SDRs. Switzerland's quota, however, is only to be raised by approximately 40% to 3.458 billion SDRs since the weight carried by Switzerland in the overall world economy, which is one of the factors taken into account for calculating the increase in the quota, declined during the reference period. Switzerland's quota will be reduced accordingly, from 1.69% to 1.63%, while the quota of the Swiss constituency will decrease from 2.70% to 2.60%.

At the IMF Annual Meeting in September 1997, it was decided to allocate 21.4 billion SDRs to the member countries on a selective basis. The holdings of SDRs were thus doubled, with allocated SDRs since then constituting a share of 29.3% of the quota for all members. For the first time, Switzerland received an amount of approximately 0.7 billion SDRs. In order to create the legal basis for a selective allocation, the IMF Articles of Agreement need to be amended.

Switzerland's IMF membership is exercised by the Federal Department of Finance and the National Bank. The National Bank finances Switzerland's contribution in the form of a reserve position in the IMF, which consists of an interest-bearing claim. The Fund pays for its activities with the member countries' reserve positions. At the end of 1997, Switzerland's reserve position amounted to 1,407.5 million SDRs, compared to 1,064.9 million SDRs at the end of 1996. (At the end of 1997, 1 SDR was equivalent to Sfr 1.96). The rise in the reserve position reflects Switzerland's contribution to the financing provided by the IMF to help resolve the financial crises in various Asian countries.

Increase in the quota

First allocation of SDRs to Switzerland

Switzerland's reserve position

Drawing on loans under the Enhanced Structural Adjustment Facility II

Based on the Federal Decree on Switzerland's participation in the prolonged Enhanced Structural Adjustment Facility (ESAF II) at the IMF of 3 February 1995, the National Bank finances the Swiss contribution to the loan account of ESAF II. This facility serves to finance long-term loans at reduced interest rates to poor developing countries. In 1997, the IMF utilised a total of 69.9 million SDRs in three drawings from Switzerland's loan commitment of 152.9 million SDRs. The individual drawings have a maturity of ten years, with repayments in instalments beginning five-and-a-half years after payment. The Confederation guarantees the National Bank the timely repayment of the ESAF credits including interest payments. It also finances the interest-rate subsidies.

Amendment to the loan agreement between the National Bank and the Monetary Fund

In September 1997, an amendment was made to the loan agreement between the National Bank and the IMF on participation in ESAF II, permitting the IMF to make drawings until 31 December 2001. The amendment to the agreement became necessary after the IMF had, in autumn 1996, prolonged the period during which loan commitments may be made to developing countries under this facility.

Election of a new Swiss Executive Director

The IMF Governors of the Swiss constituency elected Roberto Cippà of the Swiss National Bank as Executive Director of the IMF as per 1 November 1997. He succeeds Daniel Kaeser, formerly of the Federal Department of Finance.

6.2 Cooperation in the Group of Ten

The National Bank participates in the meetings of the finance ministers and central bank governors of the G-10 as well as in various of its working groups.

Prolongation of participation in the General Arrangements to Borrow

With its message of 12 November 1997, the Federal Council submitted the Federal Decree on the Prolongation of Switzerland's Participation in the General Arrangements to Borrow (GAB) of the IMF to the federal parliament. Switzerland has been associated with the GAB since 1964 and has been a participant since 1984; the Swiss National Bank is the participating institution. In the event that the IMF finds itself short of funds, the GAB permit it to borrow additional funds to the amount of 17 billion SDRs for the purpose of warding off or resolving an extraordinary crisis threatening the international monetary system. The loan commitment of the National Bank amounts to 1,020 million SDRs. The GAB are valid for five-year periods; in keeping with this, any prolongation of Switzerland's participation has so far been decided by the federal parliament every five years. In future, this will be the responsibility of the Federal Council, with the prior agreement of the National Bank. The GAB currently in force are due to expire at the end of 1998.

New Arrangements to Borrow

At the beginning of 1997, the Executive Board of the IMF approved the New Arrangements to Borrow (NAB), which constitute parallel agreements to the GAB (cf. 89th Annual Report, p. 52). The two chambers of the federal parliament decided on Switzerland's accession to the NAB in October and in December 1997 respectively. The NAB have the objective of doubling the amount available to the IMF under the GAB to respond to financial emergencies from 17 billion SDRs to 34 billion SDRs. In addition to the participants in the GAB, fourteen new participants (industrial countries and NICs) adhere to the NAB though not all of

them have joined yet. The loan commitment of the National Bank, which is also the participating institution in the NAB, will amount to 1,557 million SDRs. At the same time, this amount is the upper limit of commitments under the GAB and the NAB since these two facilities cannot be drawn on with cumulative effect. Like the GAB, the NAB are concluded for five-year periods and can be renewed. On a national level, the same regulations apply to renewal as are also envisaged for the GAB in future.

On the initiative of the G-7, a working party of the G-10 was set up to study the implications of electronic money. In April 1997, a report assessing the new electronic payment instruments with particular relevance to consumer protection, legal enforcement and supervision was published. The working party came to the conclusion that at present there is no immediate need for new institutional coordination mechanisms for electronic money on an international level.

**Working party on
electronic money**

6.3 Cooperation with the Bank for International Settlements

The central bank governors of the G-10 countries meet once a month at the BIS. Moreover, the National Bank is represented in various committees of the BIS including the Basle Committee on Banking Supervision and the Committee on Payment and Settlement Systems.

Together with the Federal Banking Commission, the National Bank participated in the tasks of the Basle Committee. The Committee cooperated with supervisors from non-G-10 countries, notably with those from emerging market nations, in working out the core principles of effective banking supervision. These are intended to make it easier for the supervisory and legislative authorities in individual countries to assess their supervisory systems and make the necessary improvements. For the first time, the Committee issued recommendations not addressed exclusively to G-10 countries and not limited to internationally active banks. The Committee also passed recommendations concerning the banks' attitude to the risks posed by interest-rate changes. The banks are strongly encouraged to oblige their top management to share in the responsibility for risks, to employ appropriate systems for measuring and regulating interest-rate risks and to hold adequate capital and reserves.

**Basle Committee on Banking
Supervision**

The Committee on Payment and Settlement Systems published two reports. The first report dealt with the settlement procedures for exchange-traded derivatives. It identified a number of risks that can arise in the processing of such transactions. The conclusions of the report did not require Switzerland to make any additional adjustments to SOFFEX and SIC. The second report provided an overview of the real time gross settlement systems of the G-10 countries. These systems, which are considered to be extremely low-risk, have in the meantime become the standard for large-value payments between the banks. Various working groups were active within the framework of the Committee on Payment and Settlement Systems. One of the working groups continued to study

**Committee on Payment and
Settlement Systems**

measures for handling the performance risk in foreign exchange trading transactions. Other working groups devoted themselves to questions relating to public payment transactions, securities lending and the processing of OTC derivatives.

6.4 Balance of payments aid

Balance of payments aid to South Korea

During the turbulences that shook Asia, South Korea slid into a monetary and financial crisis. After the country had applied to the IMF at the beginning of December 1997, an international financing package was put together. The IMF extended a three-year stand-by credit to the amount of \$ 21 billion, the World Bank and the Asian Development Bank gave credit undertakings for \$ 10 billion and \$ 4 billion respectively. Another \$ 22 billion were pledged by the Group of Ten in conjunction with Australia and New Zealand. These loans form a second line of defence which will only be drawn on in case of need. Switzerland's credit has been fixed at \$ 312.5 million. It will be granted by the National Bank in the context of the Federal Decree on Switzerland's cooperation in international monetary measures. The Confederation guarantees the National Bank the timely fulfilment of the loan agreement.

6.5 Technical assistance and specialist training

Counselling in various central bank activities

The National Bank provides technical assistance to central banks that have either been newly established or are in a state of reorganisation. Our activities ensue partly in response to requests from the IMF or the respective central banks and partly within the context of the Confederation's development programme. In 1997, considerable support was given to the Bank of Tanzania in the form of continued counselling in the management of its foreign exchange reserves.

Courses on monetary policy

The Gerzensee Study Centre again invited qualified central bank employees from various developing and transition countries to courses notably on monetary policy. In 1997, the Study Centre organised five courses with over 120 participants.

6.6 Relations with the Principality of Liechtenstein

The Principality of Liechtenstein is linked to Switzerland by the Currency Agreement of 19 June 1980. The Swiss regulations concerning monetary and credit policy, and also the protection of Swiss coins and banknotes, are directly applicable in the Principality of Liechtenstein. On 20 August 1997, the Federal Council approved the annexe to the Currency Agreement incorporating these applicable regulations in an updated version per 31 December 1996.

In 1997, the National Bank analysed the regulatory developments recorded in the financial services sector of the Principality of Liechtenstein since 1990. With the introduction of a modern banking law, a new law on investment companies, a mutual judicial assistance law and a due diligence regulation, as well as the punishment of money laundering and insider trading under criminal law, the legislative authorities of Liechtenstein took important steps to ensure the stability and integrity of the financial sector. The regulatory efforts entailed the recruitment of additional staff by the Liechtenstein banking supervisory authority. Further revisions of laws designed to complete the implementation of Liechtenstein's EEA commitments in the financial sector are under way. Overall, the regulatory gap between Liechtenstein and Switzerland pinpointed in a report on the financial relations between the two countries of 24 April 1990, drawn up under the auspices of the Federal Banking Commission, may today be considered as largely eliminated. In a meeting in November 1997, the National Bank advised a government delegation of the Principality of Liechtenstein of its findings.

Updated annexe to the
Currency Agreement of 1980

Regulatory developments
in the financial sector
of Liechtenstein