Financial information on the stabilisation fund

The SNB StabFund Limited Partnership for Collective Investment (stabilisation fund), with its sub-companies, forms a closed-end capital investment scheme within the meaning of art. 98 of the Swiss Federal Act on Collective Investment Schemes (CISA).

The subsidiaries are consolidated according to recognised accounting principles, in order to permit an economic assessment of the stabilisation fund.

The stabilisation fund's first financial year extended over 15 months. Figures for the first three months (October to December 2008) were published in the *101st Annual Report* of the Swiss National Bank. To facilitate comparability with the other disclosures in the financial report, the following information relates to the 2009 calendar year, and not the extended first financial year of the stabilisation fund.

The reporting currency of the stabilisation fund is the US dollar. The information below is therefore reported in US dollars.

1 Introduction

Structure

The fund announced in October 2008 to take over illiquid and problem assets from UBS was established as the StabFund Limited Partnership for Collective Investment (stabilisation fund). Participation units in the stabilisation fund are held by the limited partner, LiPro (LP) AG, and the general partner, StabFund (GP) AG. The shares of both the latter companies are owned by the Swiss National Bank (SNB).

In 2009, in order to take local legal specificities into consideration, sub-companies were incorporated to hold different types of assets.

The financial information on the stabilisation fund refers to data which have been consolidated at limited partnership level. All values are in US dollars.

Organisation

The SNB steers the activities of the stabilisation fund through its control of the general partner, StabFund (GP) AG, for which it provides three of the five members of the Board. The general partner is responsible for the management of the stabilisation fund. The fund has no staff of its own. Operational management tasks are performed by the SNB's StabFund unit. Although UBS acts as investment manager, the investment strategy is defined by the general partner. The assets are held in custody at an independent custodian bank.

Portfolio transfer and development

The transaction between UBS and the SNB announced in October 2008 originally involved the transfer of financial instruments totalling a maximum of USD 60 billion. In February 2009, UBS and the SNB decided to reduce the volume of the transfer, so that ultimately assets and liabilities amounting to USD 38.7 billion were transferred. The last tranche of assets was transferred from UBS to the stabilisation fund in April 2009. The amount refers to the value of the portfolio as at 30 September 2008, the date from which the SNB had committed to take over the risky assets from UBS.

The portfolio transfer took place in three tranches. In December 2008, the assets transferred were largely made up of securities; in March 2009, mainly credit derivatives and some more securities; and in April 2009 all other assets, including non-securitised loans.

From the second quarter of 2009, the market situation improved for the investment categories in which the stabilisation fund had invested. This meant that, following the substantial revaluations at the end of 2008 and in the first quarter of 2009, only certain sub-portfolios needed further value adjustments.

Some of the assets transferred have already been sold. This, together with income from repayments and interest, made it possible to repay part of the SNB loan, reducing it to USD 20.3 billion at the end of the year. In some instances, defaults on positions resulted in the SNB taking ownership of the associated collateral or, in the case of derivatives, the underlying assets. These took the form of securities, loans or real estate.

Additional information

Further information on the stabilisation fund can be found in chapter 6.5 of the accountability report.

2 Stabilisation fund balance sheet and income statement

Balance sheet as at 31 December 2009
In USD millions

	Item no. in Notes	31.12.2009	31.12.2008	Change
Assets				
Bank deposits		**660.6**	**584.7**	**+75.9**
Securities (securitised loans)	01	15 769.7	14 640.3	+1 129.4
Non-securitised loans	01	3 322.5	–	+3 322.5
Real estate	02	15.5	–	+15.5
Subtotal investments		**19 107.7**	**14 640.3**	**+4 467.4**
Interest rate derivatives	03	26.2	–	+26.2
Credit derivatives	04	105.2	–	+105.2
Subtotal derivatives		**131.4**	**–**	**+131.4**
Prepayments and accrued income		49.3	0.1	+49.2
Other assets	04	31.8	–	+31.8
Total assets		**19 980.9**	**15 225.2**	**+4 755.7**

Liabilities and equity

	Item no. in Notes	31.12.2009	31.12.2008	Change
Interest rate derivatives	03	43.5	–	+43.5
Contractual agreements		–	889.6	–889.6
Accrued expenses and deferred income		43.0	129.9	–86.9
Other liabilities		11.2	–	+11.2
SNB loan	05	20 281.9	14 255.1	+6 026.8
Deferred management fee	06	19.3	0.8	+18.5
Subtotal liabilities		**20 398.9**	**15 275.4**	**+5 123.5**
Equity capital				
Paid-in equity	07	3 896.3	1 640.5	+2 255.8
Result, carried forward		–1 690.6	–	–1 690.6
Result, current period		–2 623.8	–1 690.6	–933.2
Subtotal equity		**–418.0**	**–50.1**	**–367.8**
Total liabilities and equity		**19 980.9**	**15 225.2**	**+4 775.7**

Income statement for 2009
In USD millions

	Item no. in Notes	2009	2008 As of 1 October	Change
Net result from securities and non-securitised loans	08	3 052.6	316.8	+2 735.8
Net result from derivatives transactions	03, 04	110.6	–	+110.6
Net result from assets not yet transferred		–	–889.6	+889.6
Financing costs		–586.4	–141.6	–444.8
Gross income		2 576.8	–714.4	+3 291.2
Foreign tax expenses (–) and tax credits (+)		–0.3	–	–0.3
Operating expenses		–80.2	–10.4	–69.8
Operating income		2 496.3	–724.8	+3 221.1
Valuation gains/losses	09	–5 641.3	–965.8	–4 675.5
Realised gains/losses		521.2	–	+521.2
Net income		**–2 623.8**	**–1 690.6**	**–933.2**

3 Notes to the financial information on the stabilisation fund as at 31 December 2009

General

Stabilisation fund accounting principles

The SNB StabFund group's accounting principles conform to the requirements of the Swiss Federal Act on Collective Investment Schemes (CISA). The accounting and valuation principles for financial instruments (securities, loans and derivatives) comply with the International Financial Reporting Standards (IFRS). The figures reported here are an extract of the stabilisation fund's annual report as submitted to the Board of Directors of StabFund (GP) AG.

Reporting and comparison period

As the stabilisation fund started operations on 1 October 2008, it was decided that its first financial year would extend over 15 months. To ensure comparability with the other financial statements presented in the financial report, the figures reported here cover the 2009 calendar year, with comparison data for 2008, when the fund was incorporated. The latter data are more detailed than those disclosed in the 2008 SNB *Annual Report*; they have not, however, materially changed.

Audit

PricewaterhouseCoopers Ltd (PwC) was selected as auditor for the stabilisation fund. The disclosures of the stabilisation fund were audited for the consolidated financial statements.

Recording of transactions

The reporting of the stabilisation fund's transactions follows the principle of trade date accounting.

Transfer price of assets versus …

The assets were transferred in three tranches (December 2008, March 2009 and April 2009). However, the risks were already fully borne by the stabilisation fund as at 1 October 2008. The transfer prices (fair values) at the valuation date of 30 September 2008 were calculated on the basis of values disclosed in UBS's balance sheet and valuations provided by specialist companies.

… book values

The transferred assets were recorded at fair value at the date of the actual transfer. Differences between the fair value at the date of transfer and the transfer price determined for 30 September 2008 were recorded as valuation gains/losses.

Subsequent valuations …

A long investment horizon was applied to the acquisition of the UBS portfolio. The market values of the transferred securities and non-securitised loans are of limited use, as these instruments are thinly traded in the market. For this reason, these assets were valued at amortised cost, as prescribed by the IFRS provisions on loans and receivables.

… using the effective interest method …

The difference between the purchase value of a financial instrument and its expected repayment value is amortised by applying the effective interest rate method, which is used to calculate amortised cost. The effective interest rate discounts all future expected cash flows for a financial instrument over its lifetime to equal the instrument's purchase value.

… based on economic models

Since the stabilisation fund's portfolio consists of complex securitisation structures and claims, assumptions must be made as to the expected cash flows. These projections are based on macroeconomic scenarios and the specific features of the assets concerned.

Assets recorded at fair value

Assets which, under the IFRS provisions, cannot be assigned to loans and receivables are recorded at fair value. These assets mainly comprise derivatives and securities (securitised loans) containing embedded derivatives.

Value adjustments

Assets carried at amortised cost are subject to periodic impairment tests. The value of these financial instruments is reviewed using cash flow forecasts. If the evaluation reveals a material difference compared to current book values, values are adjusted accordingly.

Reporting currency

The reporting currency of the stabilisation fund is the US dollar. All values presented here are in that currency.

Valuation prices

Foreign currency valuation prices

	31.12.2009 In USD	31.12.2008 In USD	Change In percent
1 euro (EUR)	1.4370	1.3975	+2.8
1 pound sterling (GBP)	1.6179	1.4378	+12.5
100 Japanese yen (JPY)	1.0780	1.1010	–2.1

Notes to the balance sheet and income statement

Item no. 01

The table below compares book values (carrying values) and fair values for the securities and loans recorded in the balance sheet. These assets are generally carried at amortised cost in accordance with the IFRS. However, if the financial instrument contains embedded derivatives, it is valued and disclosed at fair value.

	31.12.2009		31.12.2008	
In USD millions	Balance sheet (carrying) value	Fair value	Balance sheet (carrying) value	Fair value
Securities (securitised loans)	15 769.7	15 647.4	14 640.3	11 828.8
at amortised cost	15 279.7	15 157.3	14 640.3	11 828.8
at fair value	490.1	490.1	–	–
Non-securitised loans	3 322.5	3 615.0	–	–
at amortised cost	3 322.5	3 615.0	–	–
at fair value	–	–	–	–

Item no. 02

The stabilisation fund owns real estate taken over in the course of foreclosure processes. Such properties are recorded at market value. For subsequent valuations, either the current book value or the current market value is used, whichever is lower.

The current market value at the balance sheet date is USD 5.1 million higher than the book value.

Item no. 03

Swaps are used to hedge interest rate risk. Depending on the term and currency (US dollar and pound sterling), the value of these instruments can vary. The positive replacement value is USD 26.2 million, and the negative replacement value is USD 43.5 million. These positions are not offset against each other. The contract volume is USD 2.8 billion.

Item no. 04

The stabilisation fund has acquired credit derivatives both as protection buyer and as protection seller. They mainly comprise credit default swaps (CDS). Holders of CDS use them to protect themselves against default by a borrower. The stabilisation fund took over the risks of the protection seller from UBS. The income from credit derivatives includes the premium for providing this protection.

The amount to be paid in the event of default (using cash held ready in bank deposits) is regularly recalculated, based on the continuous valuation of outstanding CDS contracts. If the value deteriorates, the stabilisation fund pays into this collateral pool, whereas it receives a repayment in the event of a value gain. A credit event triggers an outpayment to the holder (from the pool), as well as a reduction in the liability. Should the stabilisation fund not have sufficient liquid funds to service the outstanding payments, it could apply for an additional loan drawdown from the SNB.

At the balance sheet date, potential liabilities from credit derivatives amounted to USD 7,034.5 million, and the deposited collateral to USD 7,041.2 million. As the collateral is held by the counterparty entitled to exercise claims based on the respective derivatives transaction, these amounts were offset against each other. Collateral not used to cover the liabilities as protection seller (USD 6.8 million) is stated under *other assets*, and claims as protection buyer (positive replacement values) are stated as credit derivatives in the assets.

In USD millions	**31.12.2009**	**31.12.2008**	**Change**
Positive replacement value	105.2	–	+105.2
Negative replacement value	7 034.5	–	+7 034.5
Net contract volume	10 655.2	–	+10 655.2
Cash collateral posted	7 041.2	–	+7 041.2

Item no. 05

SNB loan to stabilisation fund

In USD millions	**31.12.2009**	**31.12.2008**	**Change**
USD	15 951.5	12 020.0	+3 931.5
EUR	1 345.3	854.9	+490.4
GBP	2 662.1	1 380.2	+1 281.9
JPY	322.9	–	+322.9
Total	20 281.9	14 255.1	+6 026.8

Item no. 06

The agreement on the UBS transaction stipulates that the remuneration payable to UBS for asset management activities is subordinate to the servicing of the SNB loan. UBS will be recompensed for such activities once the loan from the SNB has been repaid in full, and once all other obligations of the stabilisation fund have been met.

Paid-in equity corresponds to UBS's contribution of 10% of the transfer price of the assets. This contribution was also paid in respect of derivatives positions, based on the associated potential losses (exposure).

Item no. 07

Income from securities and non-securitised loans

Item no. 08

in USD millions	2009	2008 As of 1 October	Change
Interest payments	1 431.5	286.6	+1 144.9
Effective interest	1 621.1	30.2	+1 590.9
Total	3 052.6	316.8	+2 735.8

The effective interest is the amount allocated periodically to the book value of a position acquired at discount in such a way that the book amount of the financial asset corresponds to the repayment value at maturity.

Stabilisation fund income that is not required to cover operating costs is used to repay the SNB loan. In connection with the loan, a subordination agreement has been concluded by the SNB with the stabilisation fund and StabFund (GB) AG in the amount of USD 1.9 billion.

The *net valuation result* represents the result of the revaluations for assets stated at fair value, and the impairments for assets stated at amortised cost.

Item no. 09

The majority of the valuation loss is attributable to the change in the fair value of the assets between 30 September 2008 – when the risk was transferred from UBS to the stabilisation fund – and the actual asset transfer date (cf. p. 164).

Risk management

The stabilisation fund's liquidation strategy sets out the principles for liquidating the portfolio. It was agreed by the Board of Directors of StabFund (GP) AG on 23 July 2009. As a rule, an asset should be sold if its sale price exceeds the discounted expected cash flow, or if such a sale will mitigate reputational, legal or other risks.

Strategy

The strategy and the requirements for the investment manager are set out in detail in the investment guidelines. The Board of Directors reviews the asset management strategy on a quarterly basis. It also defines limits for the activities of the various decision-makers reporting to it, i.e. the investment manager and the general manager. The limits define the sales volume, but also the potential losses from sales. In addition, the investment guidelines contain requirements on the disclosure of conflicts of interest for UBS in its roles as bank and investment manager, as well as reporting requirements.

Compliance with the strategy and the investment guidelines is monitored on a continuous basis by the Risk Control section of the SNB's StabFund unit.

The system of internal controls of the stabilisation fund covers all the main responsibilities, working procedures and competences relating to the fund's management and reporting.

Types of risk

The stabilisation fund's assets mainly comprise securitised assets in the form of mortgage-backed and other asset-backed securities (MBS and ABS). These are backed with various kinds of claims (mortgages and other loans). Risks therefore derive primarily from changes in the value of this collateral. The main risk factors are the future development of the economy and movements in real estate prices in the US and some EU countries.

Interest rate risk plays a minor role. Around 65% of the stabilisation fund's securities are variable rate instruments. Most of these assets are congruently financed through the Libor-based loan from the SNB. The remaining interest rate risk is managed by the stabilisation fund using various hedging operations.

Contingent liabilities

Contingent liabilities are liabilities which may be incurred as a result of past events, and whose existence has yet to be confirmed by the occurrence of one or more uncertain future events. Such liabilities mainly stem from CDS credit events (cf. item no. 04) and outstanding irrevocable loan commitments.

In USD millions	31.12.2009
Exposure from credit derivatives	3 732.4
Irrevocable loan commitments	74.3
Total	3 806.7