

Financial information on the stabilisation fund

The SNB StabFund Limited Partnership for Collective Investment (stabilisation fund), with its subsidiaries forms a closed-end capital investment scheme within the meaning of art. 98 of the 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 reporting currency of the stabilisation fund is the US dollar. The figures reported here are therefore stated in this currency.

1 Introduction

Structure

The SNB StabFund Limited Partnership for Collective Investment (stabilisation fund) manages the illiquid assets taken over from UBS as at 1 October 2008.

The 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 companies are owned by the Swiss National Bank (SNB). To hold different types of assets, the stabilisation fund also has subsidiaries which address local legal requirements.

The financial information on the stabilisation fund is consolidated at the limited partnership level. All financial values are stated in US dollars.

Organisation

The SNB manages the activities of the stabilisation fund by controlling the general partner, StabFund (GP) AG, for which it provides three of the five members of the Board of Directors. 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 financial instruments are held in custody at an independent custodian bank.

Activities

The financial instruments taken over mainly include loans and securities (securitised loans) in the area of real estate as well as corresponding derivative positions. 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 are in the form of additional securities, loans or real estate.

The National Bank financed the purchase of investments with a loan to the stabilisation fund. Sales as well as proceeds from principal repayments and interest income make it possible to repay this loan. As at 31 December 2011, the debt to the SNB amounted to USD 8.1 billion.

In the current year, a positive result of USD 1.1 billion was recorded, taking the stabilisation fund's equity to USD 3.2 billion.

Additional information

Further information on the stabilisation fund can be found in chapter 6.7 of the accountability report.

2 Stabilisation fund balance sheet and income statement

Balance sheet as at 31 December 2011

In USD millions

	Item no. in Notes	31.12.2011	31.12.2010	Change
Assets				
Bank deposits		396.6	514.1	-117.5
Securities (securitised loans)	01	8 824.7	11 661.6	-2 836.9
Non-securitised loans	01	2 055.1	2 479.2	-424.1
Real estate	02	69.7	39.7	+30.0
Subtotal investments		10 949.5	14 180.5	-3 231.0
Interest rate derivatives	03	138.3	45.0	+93.3
Credit derivatives	04	25.5	45.4	-19.9
Subtotal derivatives		163.8	90.4	+73.4
Accrued income		41.3	54.3	-13.0
Other assets	04	232.8	129.4	+103.4
Total assets		11 784.0	14 968.7	-3 184.7
Liabilities and equity				
Interest rate derivatives	03	403.6	176.0	+227.6
Accrued interest and expenses		16.4	22.3	-5.9
Other liabilities		1.4	0.7	+0.7
SNB loan	05	8 140.4	12 618.9	-4 478.5
Deferred management fee	06	56.6	40.5	+16.1
Subtotal liabilities		8 618.4	12 858.5	-4 240.1
Paid-in equity	07	3 896.7	3 896.7	-
Foreign currency translation differences		-2.4	-0.4	-2.0
Result, carried forward		-1 786.0	-4 314.5	+2 528.5
Result, current period		1 057.3	2 528.5	-1 471.2
Subtotal equity		3 165.6	2 110.3	+1 055.3
Total liabilities and equity		11 784.0	14 968.7	-3 184.7

Income statement for 2011
In USD millions

	Item no. in Notes	2011	2010	Change
Net interest income from securities and non-securitised loans		623.2	866.6	-243.4
Effective interest (less impairments)	08	644.0	1 080.5	-436.5
Net result from derivatives	03, 04	-47.6	-141.3	+93.7
Unrealised valuation gains/losses	09	15.8	1 123.8	-1 108.0
Realised valuation gains/losses		150.1	110.3	+39.8
Financing costs		-286.9	-457.6	+170.7
Gross income		1 098.5	2 582.3	-1 483.8
Foreign tax expenses (-) and tax credits (+)		0.0	-0.1	+0.1
Operating expenses		-41.1	-53.8	+12.7
Net income		1 057.3	2 528.5	-1 471.2

3 Notes to the financial information on the stabilisation fund as at 31 December 2011

General

The SNB StabFund group's accounting principles conform to the requirements of the 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 from the stabilisation fund's annual report as submitted to the Board of Directors of StabFund (GP) AG.

PricewaterhouseCoopers Ltd (PwC) have been elected as auditors for the stabilisation fund. These disclosures on the stabilisation fund were audited as part of the overall audit of the SNB group.

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

The transferred assets were recorded at fair value at the date of the actual transfer. For assets classified as loans and receivables, this was the starting value for amortised cost accounting in conformity with IFRS provisions.

At inception of the fund, management performed an assessment and determined that there was no indication of an active market for the transferred securities and non-securitised loans. For this reason these assets were allocated to the IFRS loans and receivables category and are valued at amortised cost.

The difference between the purchase price (acquisition cost) of a financial instrument and its expected redemption value is amortised by applying the effective interest 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.

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

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

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

**Stabilisation fund
accounting principles**

Audit

Recording of transactions

Initial valuation

Subsequent valuations ...

**... using the effective
interest method**

**... based on
economic models**

**Assets recorded
at fair value**

Value adjustments

Reporting currency

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

Foreign exchange rates**Foreign exchange rates**

	31.12.2011	31.12.2010	Change
	In USD	In USD	In percent
1 euro (EUR)	1.2979	1.3396	-3.1
1 pound sterling (GBP)	1.5548	1.5577	-0.2
100 Japanese yen (JPY)	1.2955	1.2307	+5.3

Notes to the balance sheet and income statement**Item no. 01**

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

In USD millions	31.12.2011		31.12.2010	
	Balance sheet (carrying) value	Fair value	Balance sheet (carrying) value	Fair value
Securities (securitised loans)	8 824.7	9 348.0	11 661.6	12 974.2
At amortised cost	8 377.3	8 900.5	11 143.5	12 456.0
At fair value	447.4	447.4	518.1	518.1
Non-securitised loans	2 055.1	2 027.3	2 479.2	2 649.9
At amortised cost	2 055.1	2 027.3	2 479.2	2 649.9
At fair value	-	-	-	-

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

Item no. 02

Swaps are used to hedge interest rate risk. On the balance sheet date, there were outstanding interest rate swaps in US dollars and pounds sterling.

Item no. 03

At the end of 2011, the positive replacement value was USD 138.3 million, and the negative replacement value was USD 403.6 million. These positions are not offset against each other. The contract volume was USD 5.1 billion.

The stabilisation fund entered into credit derivative contracts both as protection buyer and protection seller. The credit derivatives 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 net result from derivatives includes the income from premiums (or expenses) for providing (or receiving) this protection.

Item no. 04

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. The difference between the payment and any underlying asset received in return is stated under realised valuation gains/losses. Should the stabilisation fund not have sufficient liquid funds to service the outstanding payments, it could apply for an additional loan draw-down from the SNB.

At the balance sheet date, potential liabilities from credit derivatives amounted to USD 2.0 billion, and the deposited collateral to USD 2.2 billion. As the collateral is held by the counterparty entitled to exercise claims based on the respective derivatives transaction (and amounts will be settled on a net basis), these amounts were offset against each other. Collateral in excess of the liabilities as protection seller (USD 188.6 million) is stated under other assets.

Claims as protection buyer (positive replacement values) are stated under credit derivatives on the asset side of the balance sheet.

	31.12.2011	31.12.2010	Change
In USD millions			
Net contract volume	2 823.9	5 308.6	-2 484.7
Positive replacement value	25.5	45.4	-19.9
Negative replacement value	2 021.3	3 299.3	-1 278.0
Cash collateral posted	2 209.9	3 381.0	-1 171.1

Loan commitment to stabilisation fund¹

Item no. 05

	31.12.2011	31.12.2010	Change
In USD millions			
USD	6 129.1	9 618.8	-3 489.7
EUR	360.9	756.3	-395.4
GBP	1 418.8	2 023.7	-604.9
JPY	231.6	220.1	+11.5
Total	8 140.4	12 618.9	-4 478.5

¹ Without accrued interest.

In connection with the loan, a subordination agreement has been entered into by the SNB with the stabilisation fund and StabFund (GP) AG in the amount of USD 1.9 billion. Further information on the stabilisation fund can be found in chapter 6.7 of the accountability report.

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 only be compensated 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.

Item no. 07

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

Financial instruments which are measured at amortised cost recognise income from effective interest. The latter results in an increase in book value of positions classified as loans and receivables that were initially recognised at a discount. The impairment tests conducted regularly for such positions can lead to an increase or decrease of the book values. A decrease is recorded as an impairment and an increase as accretion income. These are reported on a net basis within effective interest (less impairments) in the income statement.

Item no. 08

Unrealised valuations gains/losses consist of book profits or book losses from the revaluation of assets carried at fair value, including unrealised exchange rate gains from balance sheet date valuation of financial instruments in currencies other than the reporting currency.

Item no. 09

Risk management

The stabilisation fund's liquidation strategy sets out the principles for reducing the portfolio. 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 responsibilities relating to the fund's management and reporting.

Risks

The stabilisation fund's assets mainly include securitised assets in the form of mortgage-backed and other asset-backed securities (MBS and ABS). These are backed by various types of claims (mortgages and other loans). Risks therefore arise 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 the UK.

Interest rate risk plays a minor role. Around two-thirds 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 strategies.

The SNB's loan was mainly granted in the stabilisation fund's main investment currencies. Since the stabilisation fund is congruently financed, currency risk is modest.

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	31.12.2011	31.12.2010	Change
Exposure from credit derivatives	843.0	2 073.8	-1 230.8
Irrevocable loan commitments	21.3	36.9	-15.6
Total	864.4	2 110.7	-1 246.3