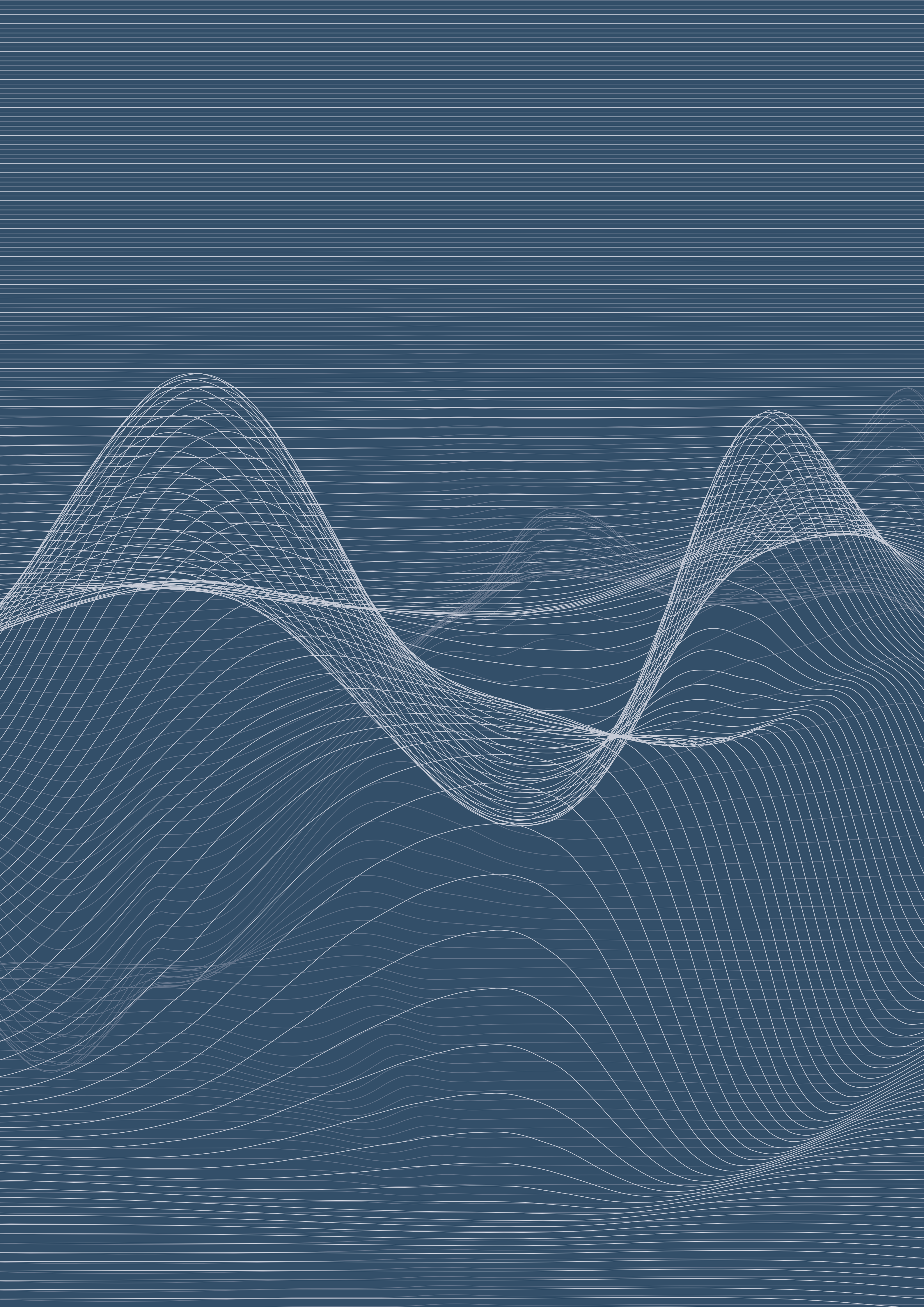


Accountability report

On 7 March 2013, the Governing Board of the Swiss National Bank (SNB) submitted its accountability report for 2012 to the Federal Assembly in accordance with art. 7 para. 2 of the National Bank Act (NBA). The report, which is reproduced below, provides information about how the SNB has fulfilled its mandate pursuant to art. 5 NBA – in particular as regards its conduct of monetary policy and its contribution to the stability of the financial system. It is submitted to the Federal Council and the General Meeting of Shareholders for information purposes.

SUMMARY

Monetary policy

The SNB pursues a monetary policy serving the interests of the country as a whole. It must ensure price stability, while taking due account of economic developments. The SNB's monetary policy strategy consists of three elements: a definition of price stability, a medium-term conditional inflation forecast, and a target range for a reference interest rate, which is the three-month Libor (London Interbank Offered Rate). Since 6 September 2011, a minimum exchange rate for the euro against the Swiss franc has also applied. In an environment in which short-term interest rates are close to zero, this allows the SNB to ensure monetary conditions that are appropriate for the Swiss economy.

In 2012, global economic growth weakened substantially, having already lost momentum in 2011. This was mainly attributable to the disappointing performance in the euro area and in Asia's emerging economies, particularly in China. The European financial and sovereign debt crisis escalated in spring and summer 2012. Despite drastic austerity measures, government debt in the euro area rose further, and financing conditions for the strongly affected countries deteriorated. Some euro area member countries were forced to apply for financial assistance to the Eurogroup and the International Monetary Fund (IMF) in order to avert the threat of state insolvency. Against the background of the financial and sovereign debt crisis, various measures were taken at European level to reinforce state budget discipline and the resilience of the financial industry. Although these helped to ease the situation, the crisis was not yet resolved. At the end of the year, the rate of unemployment in the euro area was the highest since the introduction of the single currency.

The weakening in the global economy and the continuing high level of the Swiss franc presented the Swiss economy with major challenges in 2012. Momentum slowed and profit margins remained under pressure in several industries. This was also felt in the labour market. Employment declined considerably in some industries, and unemployment rose over the course of the year. Average annual GDP was up by 1.0%, after an increase of 1.9% in the previous year. While momentum in investment and foreign trade declined significantly, consumer demand continued to buoy up economic activity.

Due to the introduction of the minimum exchange rate, pressure on producer and import prices as well as on consumer prices eased markedly in 2012. Nevertheless, consumer prices decreased by 0.7% on average over the year, after having increased slightly in 2011.

In an environment of slightly negative inflation rates and weakening growth in the global economy, the SNB's task in 2012 was to keep monetary policy sufficiently expansionary. In this situation, with short-term interest rates at zero, the minimum exchange rate was an important instrument for fulfilling the National Bank's mandate, since it substantially reduced the threat of deflation and recession. However, the long period of low interest rates contributed to a further strong increase in prices and mortgage lending volumes for residential property. The SNB thus issued repeated warnings about the build-up of risks for financial stability.

Implementation of monetary policy

The SNB fully aligned its monetary policy instruments to securing the minimum exchange rate of CHF 1.20 per euro. It consistently enforced this minimum rate throughout the entire year. For this purpose, it carried out comprehensive foreign currency purchases in the second and third quarters. Overall, the SNB purchased foreign currency for CHF 188 billion in 2012, which resulted in a substantial increase in sight deposits held at the National Bank. The target range for the three-month Libor remained unchanged at 0.0–0.25%. Throughout 2012, interest rates on the Swiss franc money market were close to zero and indeed, at times, below zero. The level of trading activity on the repo market, which had been very low for some time, dropped further.

Cash supply and distribution

The SNB supplies the economy with banknotes via its two cash distribution services at the Berne and Zurich head offices, and with coins on behalf of the Confederation. Some local cash redistribution is carried out through the cantonal banks, acting as agencies on behalf of the SNB. The National Bank closed its Geneva branch office and cash distribution service at the end of January 2012. It was the last of the eight original regional branches. In order to continue ensuring the best possible supply and distribution of cash in the Geneva area, the SNB opened an agency at the Banque Cantonale de Genève on 1 February 2012.

In 2012, the SNB conducted an extensive reassessment of its new banknote series project. In doing so, it was reacting to the technical difficulties that had emerged in autumn 2011, in an early phase of serial production. Due to the high standards with regard to security and quality as well as the production implementation aspects which apply to the new banknote series, further comprehensive tests will be needed. In conjunction with the subsequent production of the entire issue of the first banknote denomination and the logistical preparations for the issue, this means that the first banknote denomination, the CHF 50 note, cannot be issued before 2015.

Cashless payment transactions

The SNB facilitates and secures the operation of cashless payment systems. It maintains sight deposit accounts for the banks, steers the SIC interbank payment system and participates in the relevant payment system bodies. The financial market infrastructure providers have been subject to increased international competition and regulatory transformation for some time now. In view of these challenges and the importance of the financial market infrastructures, the SNB held comprehensive dialogues with SIX and the Swiss banks during 2012, covering the scope, organisation and operation of the Swiss financial market infrastructures.

Asset management

The SNB's assets fulfil important monetary policy functions. They consist mainly of gold and foreign currency investments (currency reserves) and, to a lesser extent, of assets in Swiss francs. Their size and composition are determined by the established monetary order and the requirements of monetary policy. In 2012, the currency reserves rose by CHF 171 billion to CHF 485 billion. The major part of this increase was attributable to the SNB's foreign currency purchases, with which it ensured the enforcement of the minimum exchange rate of the euro against the Swiss franc. The growth in volume was accompanied by greater demands on currency reserve management and heightened financial risk. The SNB decided to add the South Korean won as an investment currency. In addition, the share of equities in the foreign exchange reserves also grew. The SNB took care to avoid its investments having any impact on the markets and currency developments of other countries.

Financial system stability

The National Bank Act confers on the SNB the mandate of contributing to the stability of the financial system. In doing so, it works in close cooperation with the Swiss Financial Market Supervisory Authority (FINMA), the Federal Department of Finance (FDF) as well as foreign authorities and international organisations. In 2012, the SNB was involved in various activities relating to the implementation of the 'too big to fail' legislation. The main focus was on work surrounding the determination of systemically important banks and their systemically important functions. The SNB designated Credit Suisse Group and UBS as systemically important banks under the terms of the Banking Act, and in its annual *Financial Stability Report*, recommended that the big banks further strengthen their resilience. As part of a package of measures aimed at reducing risk on the mortgage market, the Federal Council created the legal basis for a countercyclical capital buffer to enter into effect on 1 July 2012. The SNB played an active role in the design of this instrument. Activation of the capital buffer is decided upon by the Federal Council following a proposal by the SNB.

International monetary cooperation

The SNB participates in international monetary cooperation activities. Important bodies are the IMF, the Bank for International Settlements (BIS), the Financial Stability Board (FSB) and the Organisation for Economic Co-operation and Development (OECD). With the continuing financial and sovereign debt crisis, IMF lending to member states in economic difficulty remained at a high level, and the IMF's fund requirements continued to be high. In summer, parliament approved the IMF's quota and governance reform, which includes a doubling of the quotas. At the 2012 Spring Meeting, Switzerland pledged a USD 10 billion participation towards the exceptional increase of the IMF's resources, subject to approval by the two chambers of Swiss parliament.

Banking services for the Confederation

The SNB provides the Swiss Confederation with banking services in the areas of payment transactions, liquidity management and the custody of securities. It also issues money market debt register claims and bonds for the Confederation.

Statistics

The SNB compiles statistical data on banks and financial markets, the balance of payments, direct investment, the international investment position and the Swiss financial accounts. In doing so, it works with the appropriate offices of the Confederation, FINMA, authorities from other countries and international organisations. In 2012, a revised version of the survey on cross-border trade in services was introduced.

1 Monetary policy

1.1 MANDATE AND MONETARY POLICY STRATEGY

Constitutional and legal mandate

Article 99 of the Federal Constitution entrusts the Swiss National Bank (SNB), as an independent central bank, with the conduct of monetary policy in the interests of the country as a whole. The mandate is explained in detail in the National Bank Act (art. 5 para. 1 NBA), which requires the SNB to ensure price stability and, in so doing, to take due account of economic developments.

Significance of price stability

Price stability is an important condition for growth and prosperity. Inflation (a sustained increase in the price level) and deflation (a sustained decrease in the price level) both hamper economic development. They complicate decision-making by consumers and producers, lead to misallocations of labour and capital, result in income and asset redistributions, and put the economically weak at a disadvantage.

By seeking to keep prices stable, the SNB creates an environment in which the economy can exploit its production potential. The aim of the National Bank's monetary policy is to ensure price stability in the medium and long term. Short-term price fluctuations, however, cannot be counteracted by monetary policy.

Appropriate monetary conditions

The SNB maintains price stability by ensuring appropriate monetary conditions. This means keeping interest rates aligned to the prevailing economic situation. Low interest rates promote the supply of money and credit to the economy, thereby increasing the demand for goods and services. The resulting shortage of production capacity leads to an increase in the price level. Conversely, increasing interest rates lead to a shortage in the supply of money and credit, thereby holding back aggregate demand. The utilisation of production capacity falls, and the upward pressure on prices weakens.

Monetary conditions are shaped not just by interest rates, but also by the exchange rate. Given Switzerland's strong integration in the global economy, the exchange rate has a substantial influence on the utilisation of production capacity and the price level. A tightening of monetary conditions as a result of a strong currency appreciation cannot be countered by lowering nominal interest rates when these are already close to zero.

Conventional monetary policy, which is based on adjustments to a reference interest rate, is thus limited when short-term interest rates are close to zero. Under such exceptional circumstances, various instruments – described as unconventional monetary policy measures – can still be used. These enable central banks to continue maintaining or to further ease their expansionary monetary policies, even when interest rates are virtually zero.

Unconventional monetary policy at near-zero interest rates

The unconventional measures primarily take three forms, with each having similar effects on interest rates and the exchange rate. First, a central bank can provide forward guidance on the expected path of short-term interest rates, with the main goal being the reduction of long-term rates. Second, a central bank can purchase domestic securities to exert downward pressure on interest rates and yields. Third, it can acquire foreign currency, and thereby directly influence the exchange rate.

Monetary policy strategy

The SNB's monetary policy strategy sets out the manner in which it intends to fulfil its statutory mandate. It consists of the following three elements: a definition of price stability, a conditional inflation forecast over the subsequent twelve quarters, and a target range for a reference interest rate – the three-month Libor (London Interbank Offered Rate). Since mid-2010, this rate has been effectively zero. Since 6 September 2011, a minimum exchange rate for the euro against the Swiss franc has also applied, which allows the SNB to maintain the desired expansionary monetary policy stance, even when interest rates are at zero, and thereby ensure price stability. Sufficiently easing monetary policy through the purchase of domestic securities is not feasible, since the long-term interest rates are already very low, and the supply of such securities in Switzerland is limited. By contrast, if the SNB sets a minimum exchange rate for the Swiss franc, this has a strong impact, given Switzerland's strong integration in the global economy.

Definition of price stability

The SNB equates price stability with a rise in the national consumer price index of less than 2% per annum. Deflation – in other words, a protracted decline in the price level – is also regarded as a breach of the objective of price stability. With its definition of price stability, the SNB especially takes into account the fact that the consumer price index tends to slightly overstate inflation and that actual inflation cannot be measured precisely.

Conditional inflation forecast

The inflation forecast published quarterly by the SNB serves as the main indicator for the monetary policy decision. It is also a key element in communication. By focusing its monetary policy on an inflation forecast, the National Bank adopts a forward-looking stance. When preparing the forecasts, the SNB takes international risks into account by simulating various scenarios.

The SNB's inflation forecast is based on the assumption that the reference interest rate communicated at the time of publishing will remain unchanged over the next three years. It is therefore a conditional forecast and shows how the SNB expects consumer prices to move in the event that the interest rate does not change. It cannot be compared with forecasts by commercial banks or research institutions, as these generally factor anticipated interest rate movements into their forecasts.

The inflation forecast takes into account the predictions of various empirical models, and is based on assumptions about the future path of the global economy. With regard to short-term changes in price levels, it is mainly indicators related to the economy, as well as exchange rates and commodity prices (crude oil), that are of relevance. Changes in the monetary aggregates and in lending are also included in the inflation forecast, since medium and long-term price movements also depend on money supply.

Target range for three-month Libor

The SNB implements its monetary policy by fixing a target range for the three-month Libor. The target range usually extends over one percentage point. As a rule, the SNB holds the Libor in the middle of the range. With interest rates reduced to almost zero in the wake of the financial crisis, the Libor target range was also gradually narrowed. Since August 2011, a target range of 0.0–0.25% has applied. The British Bankers' Association Libors are published daily in London. The Swiss franc Libors correspond to the trimmed mean of the current interest rates conditions for – at present – 11 banks.

Libor manipulation

In summer 2012, it emerged that some Libors were not being truthfully reported by certain banks. The Financial Services Authority in the UK subsequently implemented various measures to prevent future attempts at manipulation, and to restore trust in the Libors.

As regards the disclosed attempts to manipulate Swiss franc Libors, there is no indication of any fundamental tampering or significant monetary policy-relevant distortions of the interest rate. The Libors continue to be a key reference rate for numerous credit relationships in the economy, internationally and especially in Switzerland. An SNB survey carried out in 2012 showed that 80% of banks questioned use the Swiss franc Libors as a benchmark for pricing loans. They therefore play an important role in the monetary transmission mechanism.

Minimum exchange rate for euro

The minimum exchange rate for the euro against the Swiss franc, which has applied since 6 September 2011, was introduced under exceptional conditions. Switzerland's economy was seriously threatened by an extreme appreciation of the Swiss franc, which carried with it the risk of a deflationary development, at a time when short-term interest rates could not be lowered any further. The SNB did not implement the minimum exchange rate to fine-tune the economy. On the contrary: The market was to be provided with a floor during a phase of great uncertainty. The minimum exchange rate was set at a level where the value of the Swiss franc remains high.

1.2 INTERNATIONAL ECONOMIC DEVELOPMENTS

Weak growth in global economy

In 2012, growth in the global economy was weaker than expected. This was reflected in the fact that world trade recorded its lowest rate of expansion in a decade – apart from 2009, during the crisis. The sluggish economic growth was mainly due to the disappointing performance in the euro area and the Asian emerging economies, notably China. The European financial and sovereign debt crisis worsened, and activity in the euro area declined. The emerging economies felt not only the impact of waning export demand from Europe, but also the consequences of their restrictive economic policies of preceding years.

Euro area in grip of crisis

The European financial and sovereign debt crisis was especially reflected in the risk premia on government bonds of heavily indebted countries compared to those of Germany, with some premia reaching all-time highs. The euro lost value against most currencies up to the middle of the year. Thanks to measures taken to counter the crisis, the situation then gradually eased. Risk premia dropped until the end of the year, in some cases sharply, and the euro gained in value again. The euro's performance was inversely mirrored by that of the US dollar; on a trade-weighted basis, the dollar benefited when the euro was weak, and declined as soon as the euro recovered.

Volatile commodity prices

Commodity prices fluctuated sharply in 2012, which was reflected in global inflation rates. Following a marked rise at the beginning of the year, the price of crude oil declined considerably until mid-June, although it rose again slightly in the second half of the year. At year-end, Brent crude was priced at USD 110 per barrel, marginally higher than a year earlier. Prices for agricultural commodities such as cereals and soybeans soared at times, as a result of a serious drought in the US.

Slowdown in inflation

The decline in annual inflation (as measured by consumer prices), which began at the end of 2011, continued worldwide into the first half of 2012. This was followed by an increase in food and energy prices, due to weather-related crop failures and to price movements in crude oil, which resulted in a slight rise in inflation rates. Core inflation – which excludes food and energy prices – declined in 2012 on the back of the weak economic conditions in most countries. It remained stable in the euro area, despite an increase in indirect taxes and administered prices.

Moderate economic growth in US

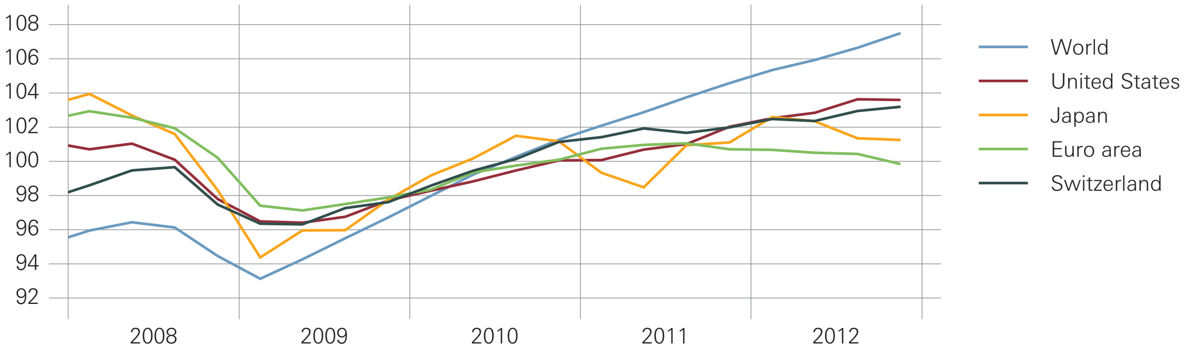
In the US, GDP increased by 2.2% in 2012, which was slightly higher than in the previous year. The gradual recovery in the labour market and, from mid-year onwards, the slow rebound in house prices bolstered private consumption, which had suffered badly in recent years from the effects of lower real estate prices. For the first time since 2005, construction activity picked up. By contrast, corporate investment slackened, and government demand decreased. In the second half of the year, fiscal policy became the focus of public attention, since at the beginning of 2013, tax relief measures were due to expire and automatic expenditure cuts go into effect. In January 2013, the US Congress agreed to extend most of the tax relief measures, and to postpone the expenditure cuts.

Continuing expansionary US monetary policy

The US Federal Reserve continued with its expansionary monetary policy, and held the target range for its reference interest rate at 0.0–0.25%. In December, it announced that it would proceed with its expansionary monetary policy for at least as long as the unemployment rate exceeded 6.5% and the mid-term inflation forecast did not rise above 2.5%. The Federal Reserve also increased the volume of its long-term securities purchases to USD 85 billion per month.

LEVEL OF GROSS DOMESTIC PRODUCT

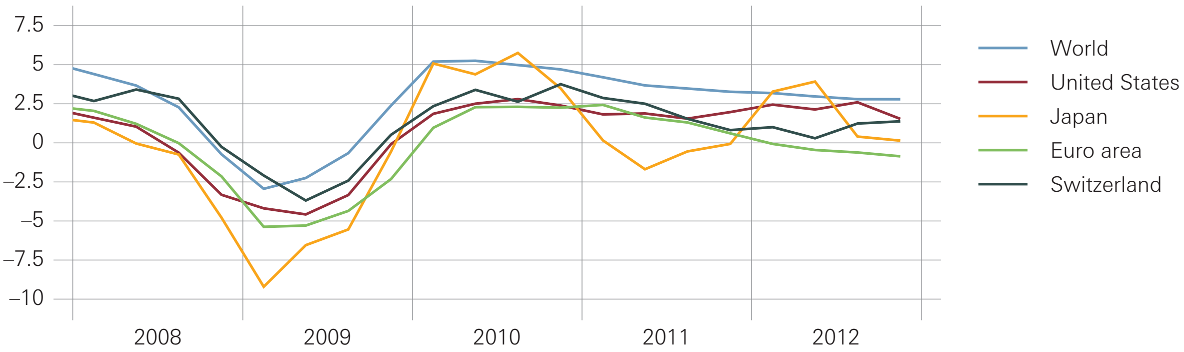
In real terms; index: 100 = period average (Q1/2008–Q4/2012)



Sources: SECO, SNB, Thomson Financial Datastream

GROWTH OF GROSS DOMESTIC PRODUCT

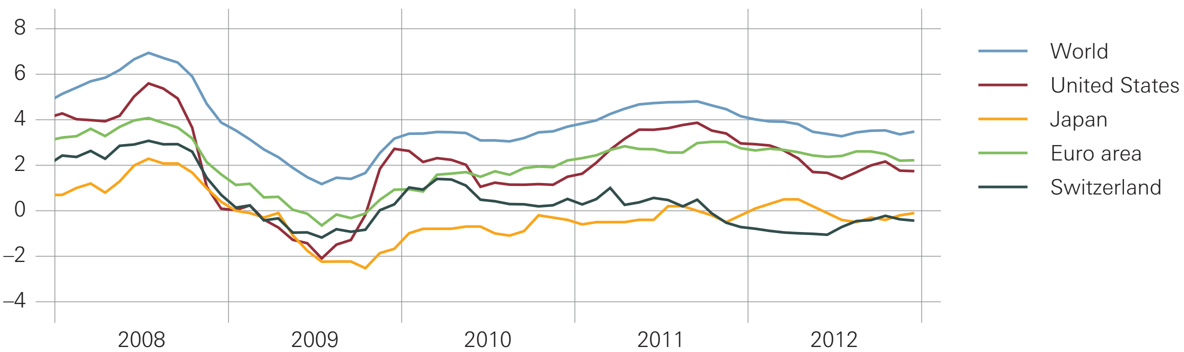
Year-on-year change in percent, in real terms



Sources: SECO, SNB, Thomson Financial Datastream

INFLATION

Consumer prices, year-on-year change in percent



Sources: IMF, SFSO, SNB, Thomson Financial Datastream

Recession in euro area

Economic developments in the euro area were strongly impacted by the financial and sovereign debt crisis. The euro area slipped into recession at the end of 2011, and this continued in 2012, which resulted in a 0.5% contraction in average annual GDP. Many countries experienced lower domestic demand. The southern euro area members remained mired in deep recession, due, among other reasons, to fiscal consolidation. The widespread loss of confidence among companies and declining demand from southern countries held back investment activity in Germany and France. The rate of unemployment in the euro area rose to 11.7% by year-end, the highest level since the inception of the currency union. Consumer price inflation remained steady at just above the European Central Bank's (ECB) price stability objective of "below, but close to, 2%".

ECB eases monetary policy

The sluggish economic performance prompted the ECB in July to lower the main refinancing rate by 0.25 percentage points to 0.75%. In addition, at the beginning of September, it launched a new purchase programme for government bonds. Under the terms of the Outright Monetary Transactions (OMT) programme, the ECB pledged to acquire short-term government bonds from member countries which applied for financial assistance to the European Financial Stability Facility (EFSF) or the European Stability Mechanism (ESM) and which were prepared to carry out a reform programme agreed with the European Commission, the ECB and the International Monetary Fund (IMF). Bond purchases may also be considered for member countries which are already pursuing reform programmes, once they have regained access to the bond market. The aim of this measure is to improve the transmission of monetary policy to the real economy, which has been obstructed by high risk premia on bond markets. No upper limit has been set on the size of the purchases, which will be conducted only on secondary markets. By year-end, the ECB had not acquired any bonds under the OMT programme.

European financial and sovereign debt crisis

The European financial and sovereign debt crisis escalated in 2012. Despite drastic austerity measures, government debt in the euro area rose to over 90% of GDP, and the financing costs of some heavily indebted countries increased. To deflect the threat of Greek insolvency, the Eurogroup and the IMF provided Greece with a second assistance programme in February. Under the terms of the programme, Greece received further financial support and its private sector creditors agreed to forego a substantial portion of their claims. Following renewed concerns about its debt sustainability, in November, it was given more time to reduce its level of indebtedness. At the same time, it repurchased some of its outstanding debt. Spain received funds from euro area countries in order to recapitalise its banking system, which was plunged into crisis after the real estate bubble burst. Cyprus also applied for assistance, mainly to provide its banking sector with new financial resources. In Portugal and Ireland, measures implemented in previous years to restructure and reform their economies were continued.

At European level, various measures were taken to bolster fiscal discipline and financial sector resilience. To this end, the euro area countries signed a fiscal agreement at the EU summit at the beginning of March on stricter budgetary rules and national debt brakes. At the EU summit at the end of June, the decision was taken to create a banking union foreseeing, inter alia, a single supervisory mechanism under the auspices of the ECB. In September, the ECB announced a programme to acquire short-term government bonds of member countries which applied for financial assistance to the EFSF or the ESM, and which were prepared to carry out a reform programme. The ESM came into effect in October, and is to gradually replace the EFSF as the permanent financing mechanism for member countries in difficulty. Overall, these measures contributed towards easing the situation.

Japanese economy weakens

At first, the economic upswing in Japan following the earthquake catastrophe of March 2011 continued into 2012, on the back of extensive government funding to support reconstruction. As the year wore on, however, the economy weakened due to subdued export demand and the expiry of a subsidy for energy-efficient cars. Taken over the whole of 2012, GDP growth averaged 1.9%. The slight decline in consumer prices continued. The Bank of Japan therefore adhered to its zero interest rate policy. It also increased the volume of its securities purchase programme introduced in October 2010, and launched a new credit facility. The Bank of Japan and the government also confirmed their determination to combat the persistent deflation.

Slowdown in emerging economies

Subdued demand from advanced economies and uncertainty surrounding the outcome of the European financial and sovereign debt crisis also adversely affected the emerging economies. In some countries, tighter fiscal policy measures implemented previously also continued to have an effect. This was particularly true for China, which saw growth slow significantly in the first half of the year. Private consumer demand, in most cases, continued to underpin growth, but 2012 saw GDP expand at significantly less than its potential in most of the countries. The relaxation of monetary policy in a number of countries and a more accommodative policy stance by some governments contributed to a modest economic revival towards the end of the year.

1.3 ECONOMIC DEVELOPMENTS IN SWITZERLAND

Moderate economic growth

The weakening of the global economy and the continuing high level of the Swiss franc presented the Swiss economy with major challenges in 2012. The economic momentum slowed, and profit margins in many industries remained under pressure. The impact of the slowdown was also felt in the labour market. However, the Swiss economy held up well compared with the situation in Europe.

Over the course of the year, the path of GDP showed some variation, with a robust first quarter followed by a slight decline in the second. Thereafter, GDP rose again. According to the first estimate by the State Secretariat for Economic Affairs (SECO), GDP increased by 1.0% in 2012, after a 1.9% advance in 2011. Consumer demand was strong, providing major support to the economy, while investment and foreign trade lost considerable momentum.

REAL GROSS DOMESTIC PRODUCT

Year-on-year change in percent

	2008	2009	2010	2011	2012
Private consumption	1.2	1.8	1.6	1.2	2.5
Government consumption	–2.5	3.3	0.7	2.0	0.7
Investment	0.7	–8.0	4.8	4.0	0.1
Construction	0.0	3.0	3.5	2.4	–3.2
Equipment	1.1	–15.5	5.8	5.2	2.8
Domestic demand	**0.5**	**0.0**	**2.3**	**1.9**	**1.5**
Exports of goods and services	2.9	–7.7	7.8	3.8	1.1
Aggregate demand	**1.4**	**–2.9**	**4.3**	**2.6**	**1.3**
Imports of goods and services	–0.3	–5.2	7.4	4.2	2.3
Gross domestic product	**2.2**	**–1.9**	**3.0**	**1.9**	**1.0**

Sources: SECO, SFSO, SNB

Foreign trade subdued

Due to the weak global economy and strong Swiss franc, growth in exports of goods and services slowed substantially. Exports of machinery and metal products continued to trend downwards, while exports of chemicals and pharmaceutical products as well as watches increased further. In the area of services, tourism receipts from foreign guests contracted further.

Imports of capital goods were subdued, despite the more favourable prices for import products as a result of the strong Swiss franc. By contrast, imports of consumer goods continued increasing due to robust consumer demand.

Lacklustre equipment investment

Following strong growth in the first quarter, the momentum in equipment investment dropped off considerably. This reflected sluggish business activity in the export industry and the high level of uncertainty about the path of the global economy. While investment in machinery increased only modestly, it expanded robustly in the area of electronic data processing.

Recovery in construction investment over course of year

In the first few months of 2012, construction investment was severely affected by the low temperatures. However, as the year progressed, it gradually recovered. Residential construction continued to benefit from the favourable financing conditions and ongoing immigration. In addition, business construction advanced slightly. By contrast, civil engineering, where public sector infrastructure projects had previously given stimulus, lost traction.

Strong growth in consumption

Private consumption rose particularly strongly, at 2.5%. Contributory factors were lower prices for consumer goods and the robust income growth, partly linked to immigration. The minimum exchange rate for the euro against the Swiss franc is also likely to have boosted domestic retail sales. Public sector consumption rose by 0.7%, thus also contributing to the growth of GDP.

Subdued growth in many industries

Many industries were significantly affected by the weaker global economy and the strong Swiss franc. The effect on the hospitality industry and some areas of manufacturing was particularly pronounced, but the momentum of industries with a domestic focus also slackened. For instance, trade recorded no more than modest growth in value added, and a decline was registered in transport. The banking industry, which has been operating in an environment that continues to undergo structural change, recorded an increase in value added, although the level is still some 15% lower than before the financial crisis. The construction, insurance and health industries also registered positive developments in value added.

Underutilised capacity

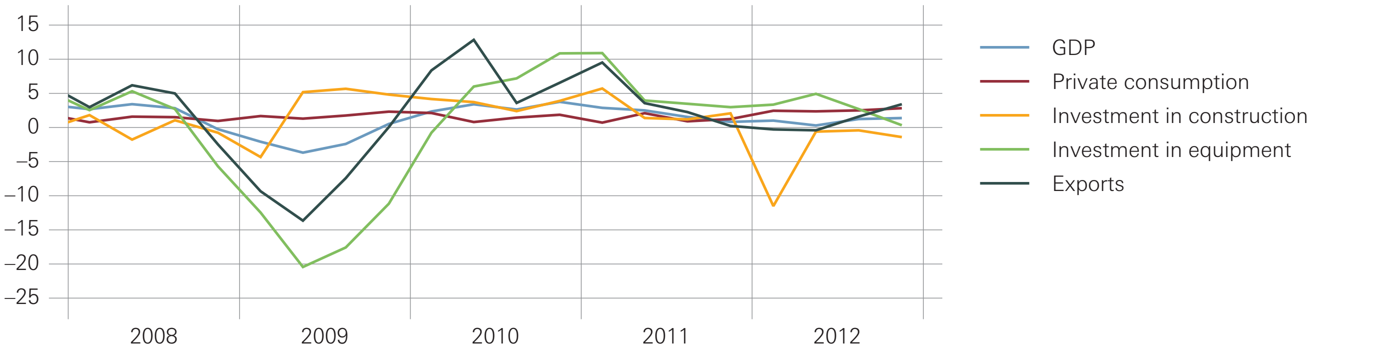
The output gap, which is defined as the percentage deviation of observed GDP from estimated aggregate potential output, shows how well the production factors in an economy are being utilised. The gap was already significantly negative at the beginning of 2012 and widened further due to the low level of growth. This reflected the decreasing utilisation of technical capacity in manufacturing and the increase in unemployment.

Labour market cools

Employment again increased in 2012. However, the situation varied very substantially from one industry to another. A significant decrease in employment was recorded, for example, in hospitality and in financial services. The rate of unemployment, which had amounted to 2.7% at the beginning of the year, rose slowly but continually thereafter. At the end of the year, it amounted to 3.1%.

GROSS DOMESTIC PRODUCT AND COMPONENTS

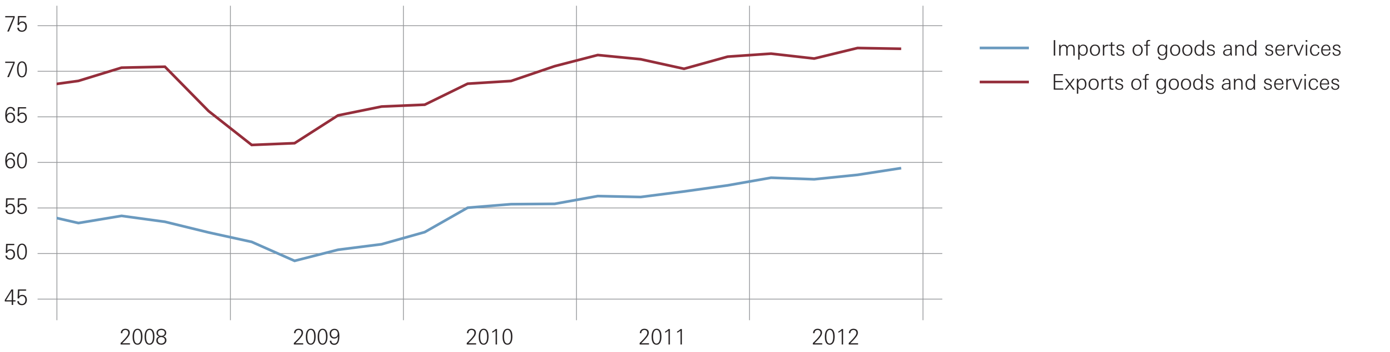
Year-on-year change in percent, in real terms



Sources: SECO, SNB

FOREIGN TRADE

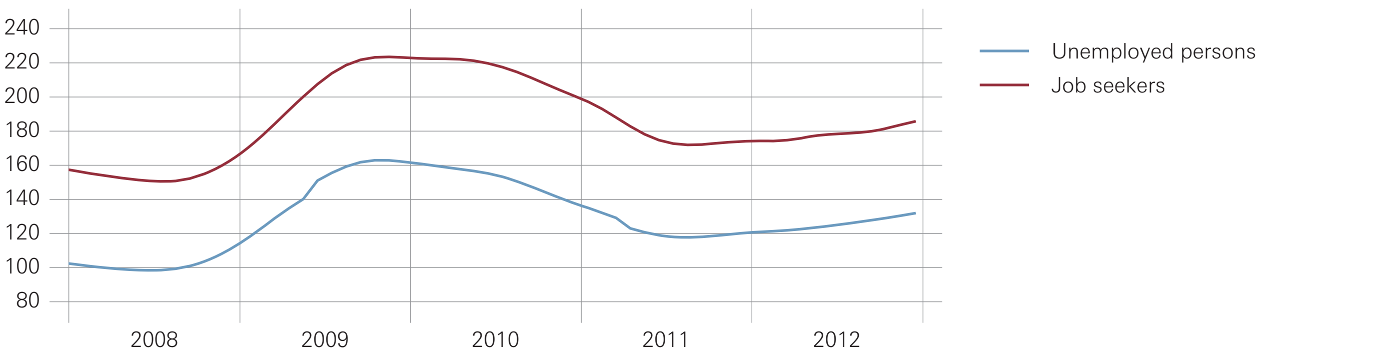
In CHF billions, in real terms, seasonally adjusted



Source: SNB

LABOUR MARKET

In thousands, seasonally adjusted and smoothed



Source: SNB

LABOUR MARKET

	2008	2009	2010	2011	2012
Employment in terms of full-time equivalents [1,2]	2.7	–0.3	0.6	1.1	1.6
Unemployment rate in percent	2.6	3.7	3.5	2.8	2.9
Number of job seekers in percent	3.9	5.2	5.0	4.2	4.1
Swiss nominal wage index [1,2]	2.0	2.1	0.8	1.0	1.1
Compensation of employees, nominal [1,2]	5.1	2.5	–0.1	3.8	3.5

1 Year-on-year change in percent.
2 2012: SNB forecast.
Sources: SECO, SFSO

Substantial increase in real wages

In 2012, real wages increased noticeably. Although, according to SNB estimates, the nominal wage increase as measured by the Swiss wage index was moderate, at 1.1%, real wages rose significantly, due to the fact that consumer prices decreased. Real wages grew by 1.8% according to the wage index and by 2.2% according to the national accounts. Together with the increase in employment, this resulted in significant growth in the compensation of employees (total labour income).

Producer and import prices stabilise

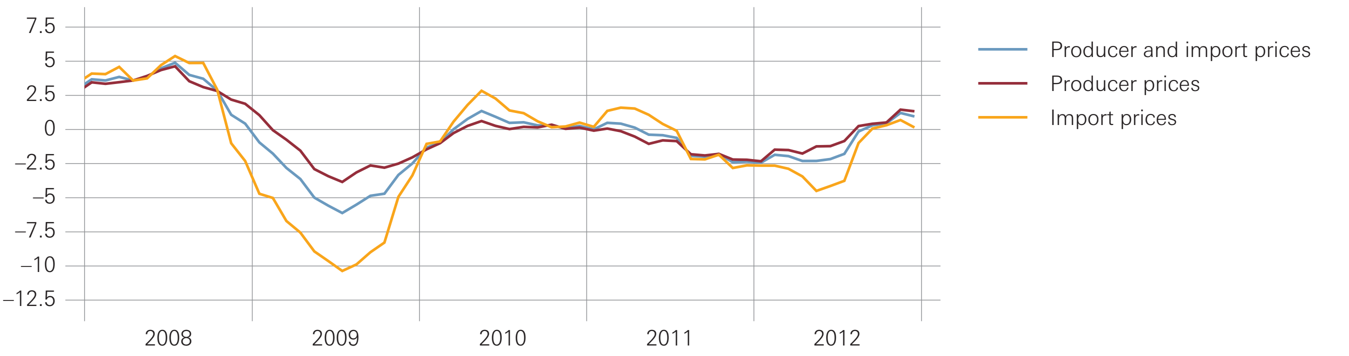
Due to the introduction of the minimum exchange rate, the substantial decline in producer and import prices came to a halt, albeit with a certain delay. Since early 2012, producer and import prices have increased slightly, and from September they were again above the corresponding level for the previous year. This increase was due mainly to higher prices for energy and export products.

Decline in consumer prices

In 2012, prices as measured by the national consumer price index (CPI) declined by an average of –0.7%, after having risen slightly in 2011 (by 0.2%). However, consumer prices also stabilised as a result of the minimum exchange rate, with year-on-year inflation increasing to –0.3% in the fourth quarter, following negative inflation rates of around –1.0% at the beginning of the year.

PRODUCER AND IMPORT PRICES

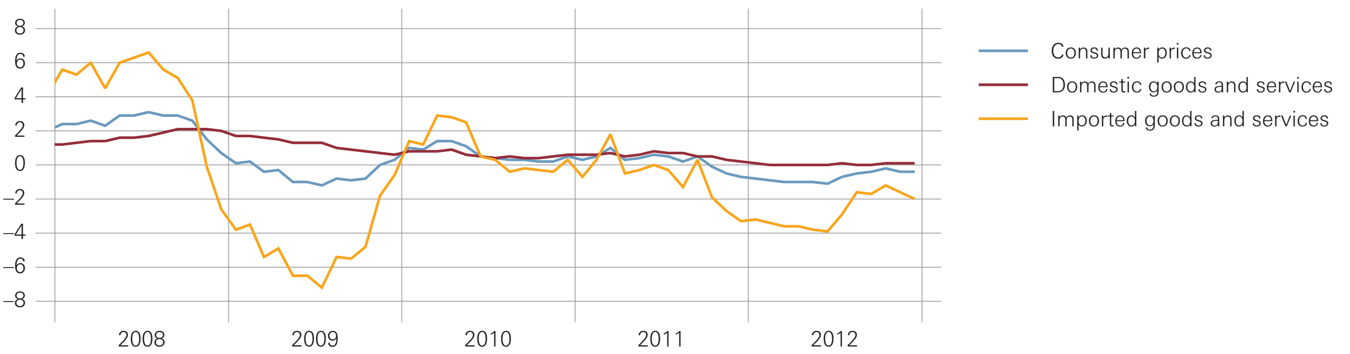
Year-on-year change in percent



Sources: SFSO, SNB

CONSUMER PRICES

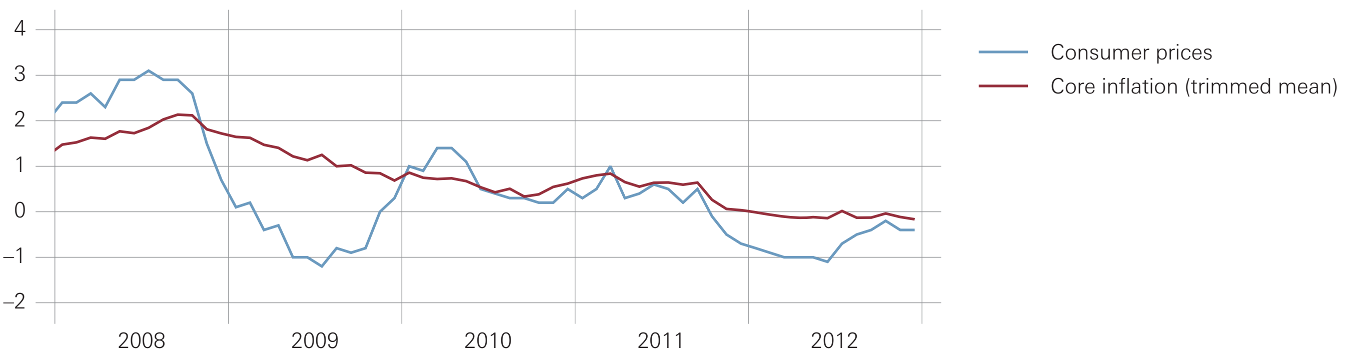
Year-on-year change in percent



Sources: SFSO, SNB

CORE INFLATION

Year-on-year change in percent



Sources: SFSO, SNB

The impact of the minimum exchange rate was most clearly manifested in the fact that the fall in prices for foreign goods was less pronounced than in 2011. Domestic services became slightly more expensive. During the year, however, the increase in rental prices slowed down considerably. This was mainly attributable to the decrease in the mortgage reference rate calculated by the Federal Office for Housing.

NATIONAL CONSUMER PRICE INDEX AND COMPONENTS

Year-on-year change in percent

	2011	2012	2012 Q 1	Q 2	Q 3	Q 4
Consumer price index, overall	**0.2**	**–0.7**	**–0.9**	**–1.0**	**–0.5**	**–0.3**
Domestic goods and services	0.6	0.0	0.0	0.0	0.0	0.1
Goods	–1.3	–1.8	–2.3	–2.1	–1.8	–1.0
Services	1.1	0.6	0.7	0.6	0.6	0.4
Private services (excluding rents)	0.8	0.6	0.7	0.6	0.6	0.5
Rents	1.3	0.6	0.8	0.7	0.6	0.2
Public services	1.8	0.4	0.6	0.3	0.3	0.6
Imported goods and services	–0.7	–2.7	–3.4	–3.8	–2.1	–1.6
Excluding oil products	–2.5	–4.2	–5.2	–4.9	–4.1	–2.5
Oil products	9.3	5.0	6.2	2.2	8.7	3.0
Core inflation						
Trimmed mean	0.5	–0.1	–0.1	–0.1	–0.1	0.0

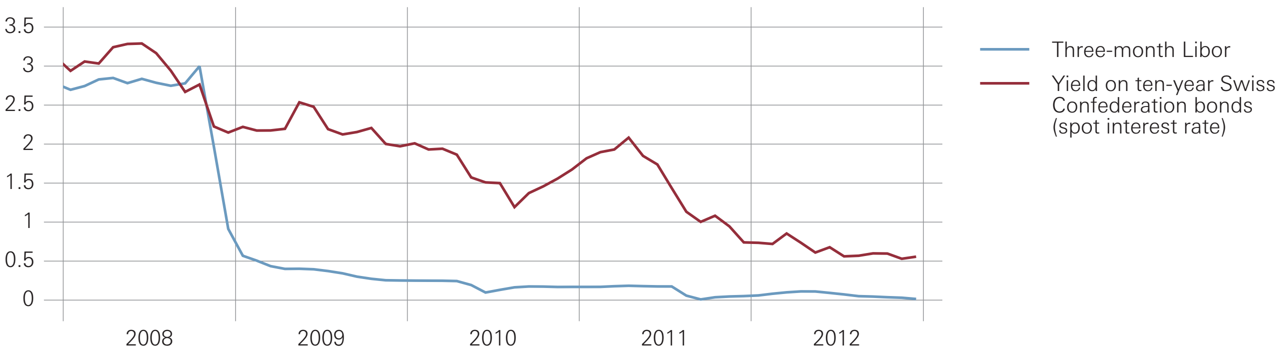
Sources: SFSO, SNB

Low and stable core inflation

Inflation, as measured by the CPI may be subject to various short-term fluctuations. In order to analyse the inflation trend, core inflation rates, such as the trimmed mean calculated by the SNB, can be used. With the trimmed mean estimator, those goods prices recording the greatest month-on-month change are excluded from the CPI basket each month (15% at either end of the distribution). On average for the year, core inflation calculated on the basis of the trimmed means method amounted to –0.1%, following 0.5% in 2011.

MONEY AND CAPITAL MARKET RATES

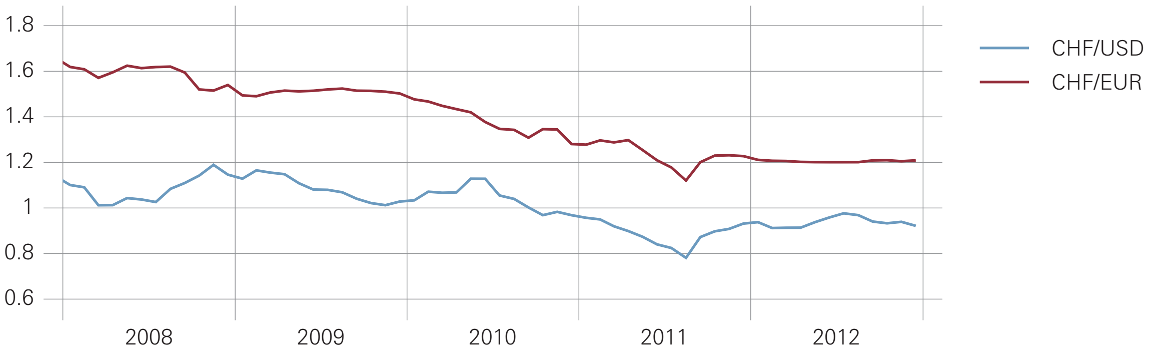
In percent



Source: SNB

EXCHANGE RATES

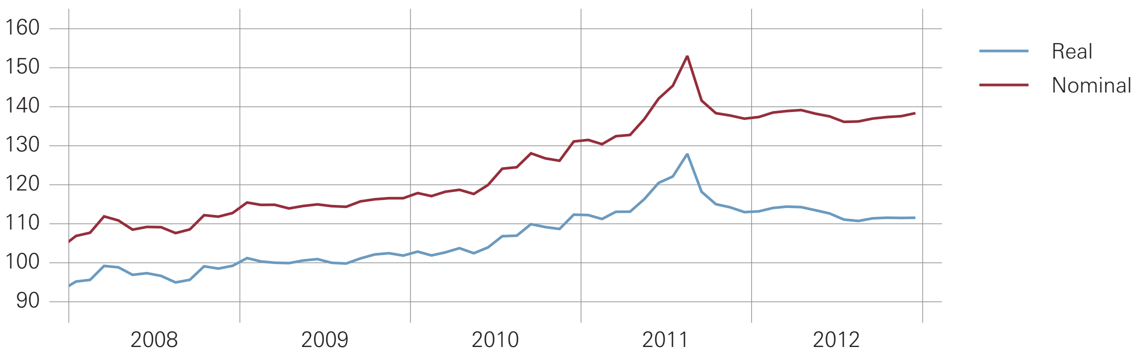
Nominal



Source: SNB

EXPORT-WEIGHTED SWISS FRANC EXCHANGE RATES

40 trading partners; index: January 1999 = 100



Source: SNB

1.4 MONETARY POLICY IN 2012

Ensuring appropriate monetary conditions

In an environment of slightly negative inflation rates and weakening growth in the global economy, the SNB's challenge in 2012 was to keep monetary policy sufficiently expansionary to counter deflationary and recessionary threats. Monetary conditions in Switzerland were dominated by a three-month Libor close to zero and the minimum exchange rate for the euro against the Swiss franc. The minimum exchange rate was an important instrument for the SNB in fulfilling its mandate, since it prevented an economic and price development that could have been destabilising.

No alternative to minimum exchange rate

In summer 2011, the extent and pace of the Swiss franc's appreciation had reached a level where the SNB saw no alternative to intervening in the foreign exchange market and, on 6 September 2011, setting a minimum exchange rate of CHF 1.20 per euro. With this measure, the SNB countered an undue tightening of monetary conditions as a result of the strength of the Swiss franc – a strength whose origin was to be found in international developments. The Swiss franc was very substantially overvalued, according to any measure, and the volatility of the exchange rate had reached an alarming level. At the same time, the international economic environment had deteriorated significantly. This situation presented an acute risk to the Swiss economy, as well as carrying the threat of a deflationary development.

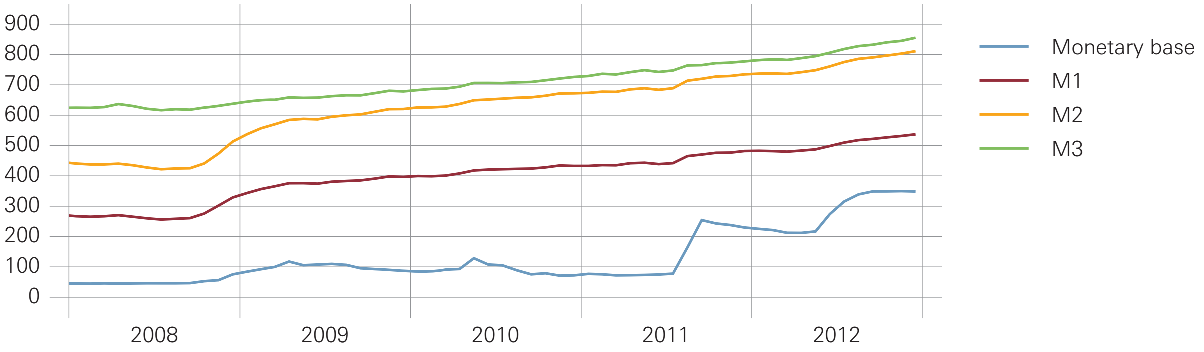
Through the minimum exchange rate, companies obtained certainty for their planning activities and the export industry was able to gain a foothold again. The deflationary risks that were threatening to become more widespread were curbed. However, the value of the Swiss franc remained high throughout the year. Consequently, an appreciation would have continued to have serious consequences for Switzerland. In view of the flagging global economy and the ongoing uncertainty as to whether turmoil would return to the international financial markets, a continuation of the minimum exchange rate policy was indispensable.

Enforcement of minimum exchange rate

The SNB consistently enforced the minimum exchange rate in 2012. At each of the quarterly monetary policy assessments, it confirmed its determination to purchase foreign currency in unlimited quantities for this purpose. The SNB would stand ready to take further measures at any time, should deflationary and economic risks make this necessary.

LEVEL OF MONETARY AGGREGATES

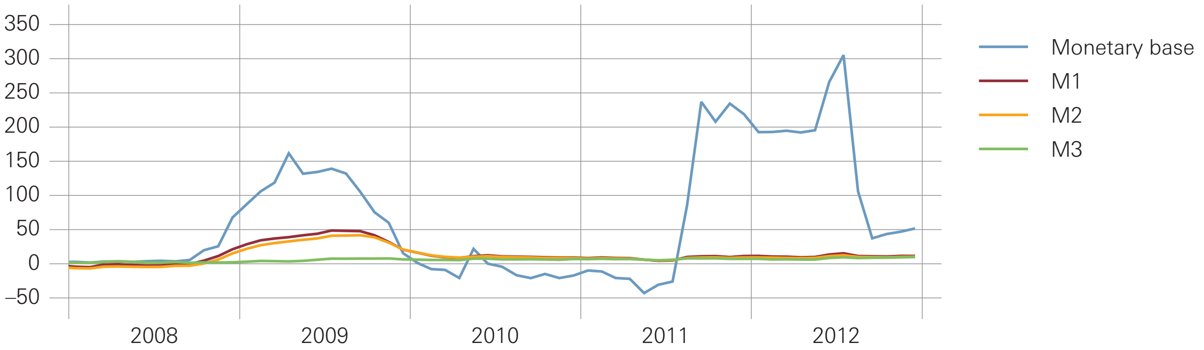
In CHF billions



Source: SNB

GROWTH OF MONETARY AGGREGATES

Year-on-year change in percent



Source: SNB

Euro above minimum exchange rate

In 2012, the euro persisted at a level just above the minimum exchange rate of CHF 1.20. Movements in the exchange rate against the Swiss franc mainly reflected changes in market participants' risk assessments. The EUR/CHF exchange rate had been fluctuating around CHF 1.23 in the fourth quarter of 2011; in spring 2012, with an escalation in the crisis and given the doubts about the survival of the monetary union, it moved closer to the minimum exchange rate. From May to August, the SNB had to purchase large amounts of foreign currency in order to enforce the minimum exchange rate. Consequently, foreign currency investments increased substantially. The upward pressure on the Swiss franc eased following the ECB's announcement in early September that it would purchase unlimited quantities of bonds of crisis-hit euro area countries under certain conditions. The euro rose to CHF 1.21, and fluctuated between CHF 1.20 and CHF 1.22 until the end of the year.

Swiss franc still high

Against the US dollar, the Swiss franc weakened somewhat during the course of the summer. In September, it gained value again, so that by the end of 2012 it was slightly stronger than at the beginning of the year. This meant that the CHF/USD rate largely followed the path of the EUR/USD rate. The real export-weighted external value of the Swiss franc, which also takes price movements in relation to those of Switzerland's trading partners into account, decreased slightly over the course of the year. However, the Swiss franc remained high in historical terms.

Target range for three-month Libor unchanged

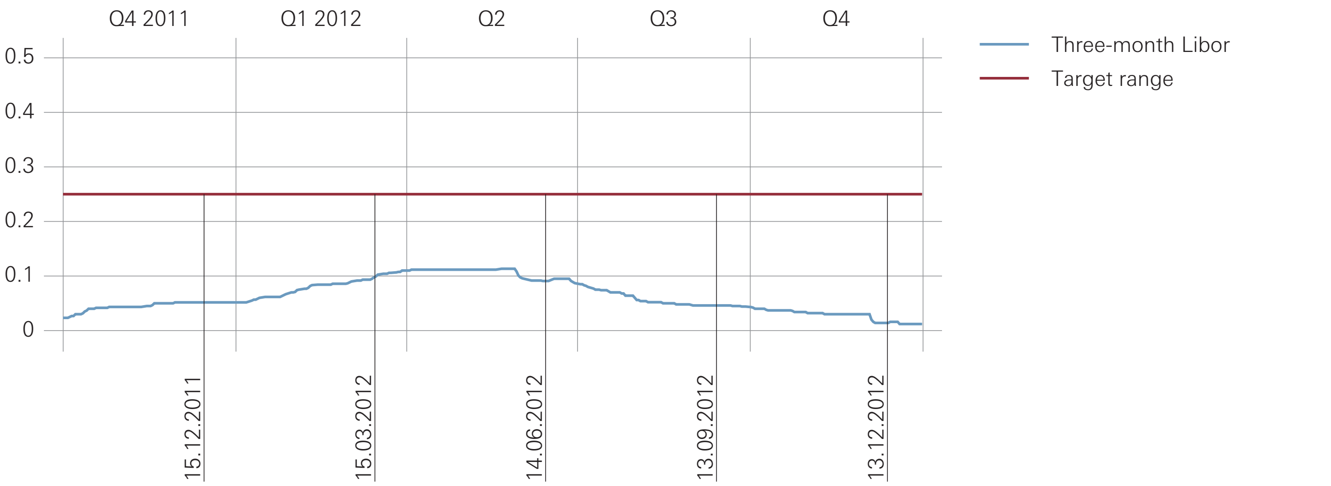
Throughout the year, the target range for the three-month Libor remained at 0.0–0.25%. Although liquidity continued to be high in the money market, the three-month Libor increased slightly to March, from 5 to 11 basis points, and persisted at this level until May. In March, the SNB confirmed its intention to continue holding the Libor as close to zero as possible. In view of the narrow target range, the SNB did not specify any target level for the three-month Libor after June. As a result of the foreign exchange market interventions, liquidity rose further, and the three-month Libor subsequently fell below 5 basis points in the summer. At the end of the year, it stood at 1 basis point.

High level of liquidity

By expanding liquidity in August 2011, the SNB was aiming to create expansionary monetary conditions in the money market, thereby exerting downward pressure on interest rates and the Swiss franc. The SNB stressed that it intended to maintain liquidity in the money market at an exceptionally high level. For this purpose, it concluded repo transactions and foreign exchange swaps between January and May. Since the SNB purchased foreign currency during the summer half of the year in order to enforce the minimum exchange rate, liquidity again increased significantly. In December, bank sight deposits were CHF 113 billion higher than a year previously.

THREE-MONTH LIBOR

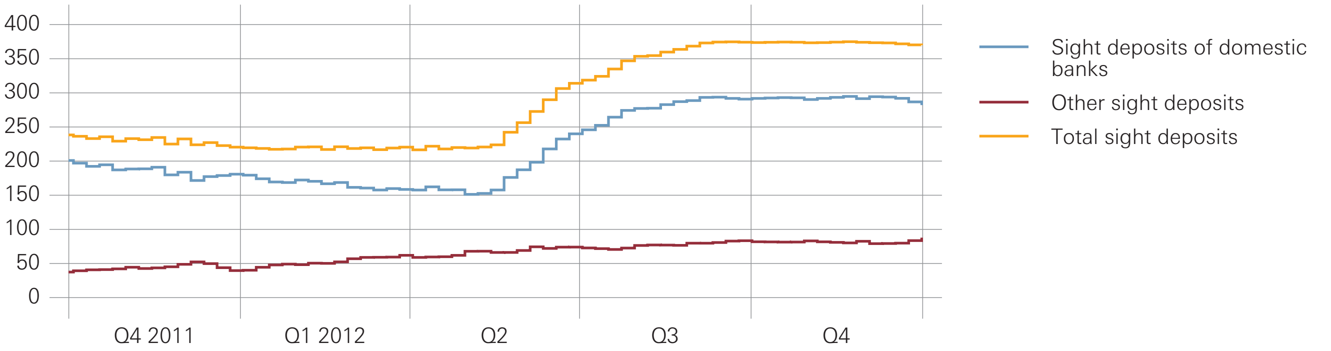
Daily values in percent



Source: SNB

SIGHT DEPOSITS AT THE SNB

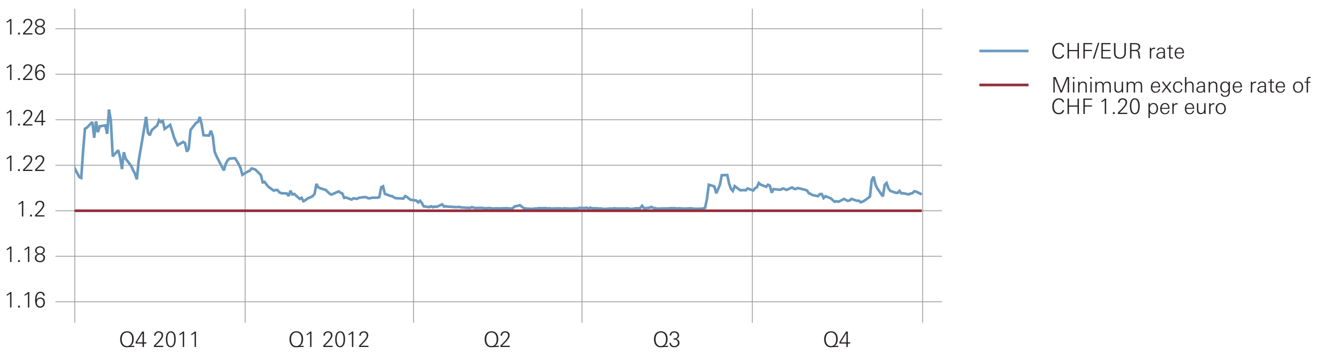
Weekly averages, in CHF billions



Source: SNB

EXCHANGE RATE

Daily rates



Source: SNB

Benefiting from the low rates of interest, the broad monetary aggregates, M2 and M3, recorded significant advances, as in previous years. On average for the year, M2 rose by 9.8% and M3 by 8.0%. Bank lending increased by 4.0% overall, thereby supporting the economy.

Outlook for global economy adjusted downwards

The scenario for the path of the global economy affects both the inflation forecast and the assessment of the domestic economy. As a result of the weak global economic growth, the SNB adjusted its international scenarios downwards during the course of the year, and this had a dampening effect on the inflation and growth forecasts for Switzerland.

Economy also weakening in Switzerland

The weakness of the global economy also affected Switzerland. Nonetheless, following a significant slowdown in GDP growth during the course of 2011, it became evident at the beginning of 2012 that the minimum exchange rate was making a significant contribution to stabilising the economic situation. Consequently, in June, the SNB increased its growth forecast for 2012 to 1.5%, compared to 1.0% in March and 0.5% in December 2011. However, a revision in the national accounts in July showed that economic growth was lower and the SNB reduced its growth forecast for 2012 to 1.0%. In December, it confirmed this figure, and forecast growth of 1.0–1.5% for 2013. Overall, the economy weakened as expected in 2012 and GDP growth was substantially lower than in 2011 (1.9%).

Low inflation expectations and long-term interest rates

Inflation expectations remained low. Results of surveys conducted among households and companies showed that medium-term inflation expectations were within a band consistent with the SNB's definition of price stability. Long-term interest rates also remained low. Following a temporary increase by some 20 basis points in March, to 0.9%, yields on 10-year Confederation bonds declined to just under 0.5% by June. Until November, they moved within a range of 0.5–0.7%; by mid-December, they had decreased to a new historical low of just under 0.4%. At the end of the year they stood at 0.6%.

Conditional inflation forecasts in 2012

Throughout the year, no risk of inflation could be identified on the basis of the SNB's conditional inflation forecasts. The low point for inflation was forecast for the second quarter of 2012, and for the year as a whole, inflation forecasts indicated negative inflation rates. The slowdown in the domestic economy and the subdued outlook for the global economy also gave rise to low medium-term inflation forecasts. The forecasts assumed a three-month Libor of zero and a weakening Swiss franc. Nevertheless, forecast inflation at the end of the 12-quarter forecast horizon did not exceed 1.0%.

Inflation forecast in March

Over the course of the year, the inflation forecasts presented at the quarterly monetary policy assessments were adjusted slightly downwards. The main reasons for this were the continuing strength of the Swiss franc and the deteriorating outlook for the global economy. At the March assessment, the inflation outlook was below that presented in December 2011. The appreciation of the Swiss franc in summer 2011 had subdued price movements more significantly than expected. In the longer term, inflation would be brought down by the worsening growth outlook for the euro area and the continuing high valuation of the Swiss franc.

Inflation forecast in June

At the monetary policy assessment in June, the inflation forecast remained largely unchanged. From 2013, the path of the inflation forecast was again more moderate than in March, since the Swiss franc had not weakened as forecast by the SNB.

Inflation forecast in September

At the September monetary policy assessment, the inflation forecast was lowered again. The further decline in the inflation outlook stemmed partly from the less favourable prospects for the global economy and a more pronounced underutilisation of production capacity in Switzerland, and partly from the fact that the forecast weakening in the Swiss franc had still failed to materialise.

Inflation forecast in December

At the December monetary policy assessment, the inflation forecast for the medium term was largely unchanged from September. The short-term inflation forecast was again lower due to a somewhat weaker economic outlook in the euro area. In addition, the impact of the appreciation in the Swiss franc was again a little stronger than had been expected.

High level of uncertainty

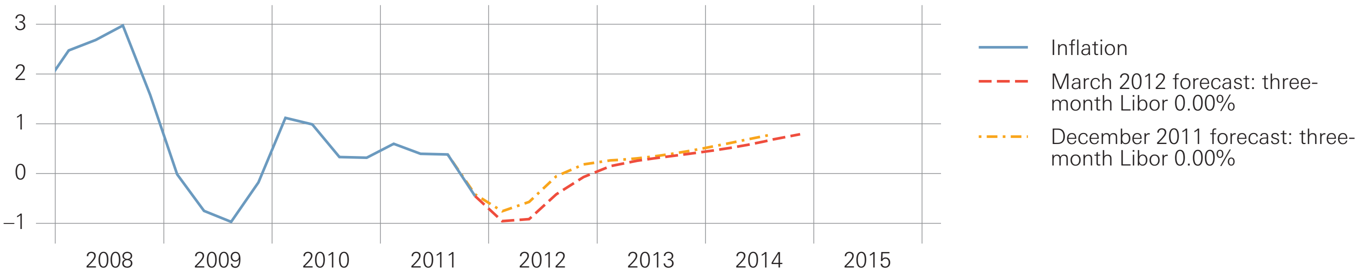
Throughout the year, the level of uncertainty about developments in the global economy and the financial markets remained high. After new governments had taken office in Greece and Italy and the European Fiscal Compact entered into force in the first quarter, the turmoil in the financial markets abated briefly. The second package of measures for Greece and the debt haircut that took place also contributed to an easing of tension. In the second quarter, the political developments in Greece, the problems in the Spanish banking industry and the weak economic data resulted in a resurgence of market turmoil. Until the ECB announced its OMT programme in September, the fragility of the situation on the financial markets was reflected in strong upward pressure on the Swiss franc. Although the situation on the financial markets calmed in the months that followed, the sovereign debt problem remained unresolved and, accordingly, the level of uncertainty was high.

Increasing imbalances in mortgage and real estate markets

As a result of low interest rates, prices on the Swiss real estate market continued to rise. The ratio of bank loans to GDP attained a new peak, thereby increasing the imbalances in the residential mortgage and real estate market (cf. chapters 6.3 and 6.4 on risks for financial stability and measures for reducing the risks in the mortgage market).

CONDITIONAL INFLATION FORECAST OF 15 MARCH 2012

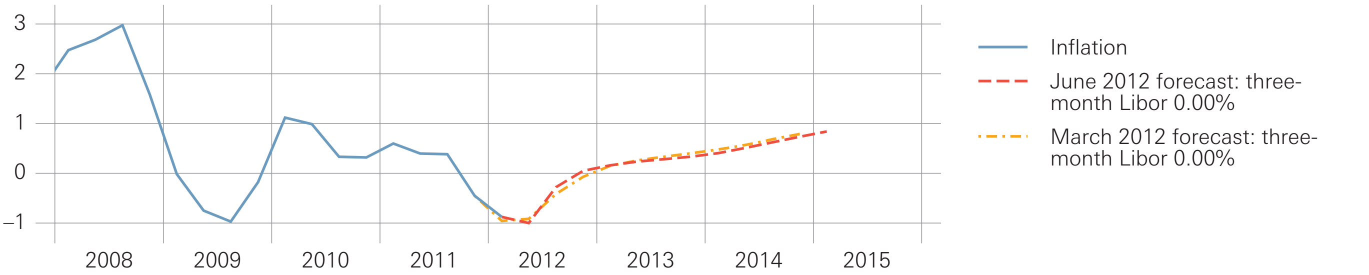
Year-on-year change in national consumer price index in percent



Source: SNB

CONDITIONAL INFLATION FORECAST OF 14 JUNE 2012

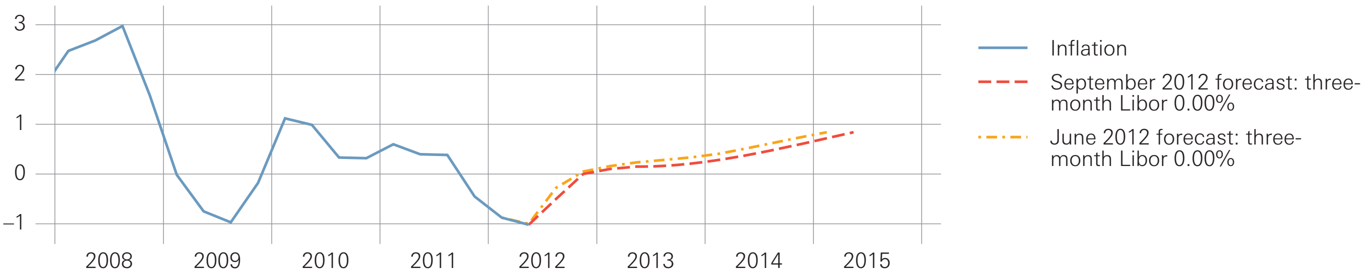
Year-on-year change in national consumer price index in percent



Source: SNB

CONDITIONAL INFLATION FORECAST OF 13 SEPTEMBER 2012

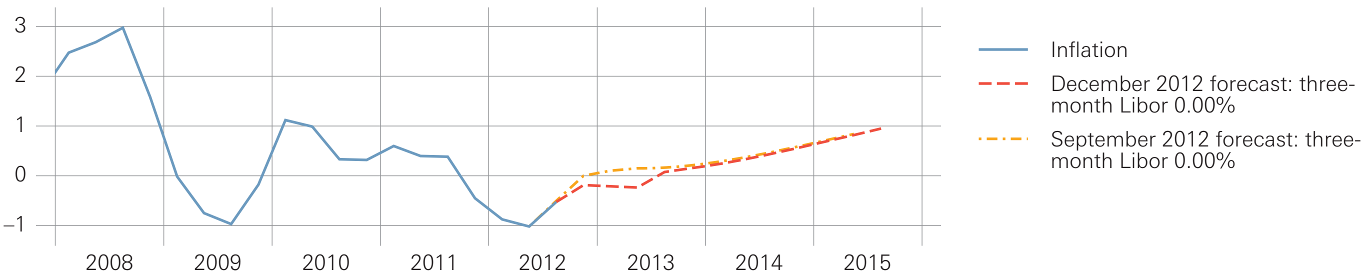
Year-on-year change in national consumer price index in percent



Source: SNB

CONDITIONAL INFLATION FORECAST OF 13 DECEMBER 2012

Year-on-year change in national consumer price index in percent



Source: SNB

2
Implementation of monetary policy

2.1 BACKGROUND AND OVERVIEW

Mandate

It is the task of the Swiss National Bank (SNB) to provide the Swiss franc money market with liquidity (art. 5 para. 2 (a) National Bank Act (NBA)). The SNB implements its monetary policy by managing liquidity on the money market and thereby influencing the interest rate level. The three-month Swiss franc Libor serves as its reference interest rate.

Scope of business and set of instruments

The framework within which the SNB may conduct transactions in the financial market is defined in art. 9 NBA. As lender of last resort, the SNB also provides emergency liquidity assistance.

The 'Guidelines of the Swiss National Bank (SNB) on monetary policy instruments' set out in detail the SNB's scope of business and describe the instruments and procedures used by the SNB for the implementation of its monetary policy. They also define the conditions under which these transactions are concluded, and which securities can be used as collateral for monetary policy repo operations.

Minimum exchange rate

The National Bank continues to enforce the minimum exchange rate, set on 6 September 2011, with the utmost determination and is prepared to buy foreign currency in unlimited quantities for this purpose. Since September 2011, all monetary policy instruments have thus been geared towards the enforcement of the minimum exchange rate. In 2012, the SNB conducted extensive foreign currency purchases, which resulted in a substantial increase in sight deposits held at the National Bank. The target range for the three-month Libor remained unchanged at 0.0–0.25%.

Sight deposits

A bank's most liquid assets are sight deposits held at the SNB, since they can be used immediately to effect payments and are deemed to be legal tender. Domestic banks hold sight deposits to satisfy minimum reserve requirements. Banks also need them for payment transactions and as liquidity reserves. The SNB influences sight deposits by utilising its monetary policy instruments. Sight deposits at the National Bank bear no interest. In addition to sight deposits held by domestic banks, total sight deposits include sight liabilities towards the Confederation, sight deposits of foreign banks and institutions, as well as other sight liabilities.

The level of sight deposits determines the extent of activity on the money market. If the supply of liquidity to the banking system is kept low, the individual financial market participants adjust their liquidity positions on the money market. Banks seeking to place funds on a short-term basis provide liquidity in the form of a loan to other banks that require short-term refinancing. These loans can be granted on a secured or unsecured basis. If there is ample liquidity in the banking system, the need for banks to adjust their liquidity positions declines and so too does trading activity on the money market.

2.2 IMPACT OF MINIMUM EXCHANGE RATE ON MONEY MARKET

Considerable increase in sight deposits

In order to keep Swiss franc liquidity at a high level, the SNB conducted liquidity-providing foreign exchange swaps and repo transactions between January and May 2012. During this time, total sight deposits at the SNB averaged CHF 219 billion per week. In spring, demand for Swiss francs on the foreign exchange market increased once again, forcing the SNB to step up its purchases of foreign currency against Swiss francs. Consequently, the liquidity-providing operations offered up to that point were discontinued as of the end of May 2012. Following the extensive purchases of foreign currency, total sight deposits at the SNB rose by September to over CHF 370 billion, and remained at this level until the end of the year.

Exceptionally low money market rates

In 2012, interest rates on the Swiss franc money market were close to zero. By May, the three-month Libor had risen to 0.11%. It declined significantly in the following months as a result of the strong increase in liquidity. At the end of the year, it stood at 0.01%. Interest rate expectations – derived from three-month Libor futures contracts – remained exceptionally low and were, at times, substantially below zero.

Low activity on repo market

As a result of the foreign currency purchases made to enforce the minimum exchange rate, Swiss franc liquidity expanded very significantly. This meant that the level of trading activity on the repo market, which had already been very low for some time, dropped further.

High level of compliance with minimum reserve requirements

Following the strong expansion of sight deposits at the SNB, the eligible assets which banks hold to satisfy statutory minimum reserve requirements increased to an average of CHF 232 billion. The average level of compliance for the year amounted to 1929%, as compared with 867% a year earlier (cf. also chapter 2.4).

2.3 USE OF MONETARY POLICY INSTRUMENTS

Foreign exchange transactions

In order to fulfil its monetary policy mandate, the SNB may purchase and sell foreign currency against Swiss francs on the financial markets.

In 2012, in order to enforce the minimum exchange rate, the SNB conducted extensive foreign exchange transactions and purchased foreign currency to a value of CHF 188 billion. Foreign exchange transactions are conducted with a wide range of domestic and foreign counterparties. The SNB accepts well over 100 banks from around the world as counterparties. With this network of contacts, it covers the relevant interbank foreign exchange market. Via electronic trading systems, banks have access at all times to the SNB's offers.

Since the introduction of the minimum exchange rate, the National Bank has continuously monitored the foreign exchange market from market opening on Sunday evening to market closing on Friday evening. The opening of the SNB's branch in Singapore in mid-2013 will facilitate round-the-clock monitoring of foreign exchange markets.

Foreign exchange swaps

In a foreign exchange swap, the purchase (sale) of foreign currency at the current spot rate and the sale (purchase) of the foreign currency at a later date are simultaneously agreed. Foreign exchange swap transactions can be conducted by way of auction or on a bilateral basis.

Until 8 May 2012, the SNB concluded foreign exchange swaps in order to provide temporary liquidity in Swiss francs. The swaps were concluded with domestic and foreign banks on a bilateral basis via electronic trading platforms or by telephone. Turnover amounted to CHF 91 billion, with terms ranging between 7 and 62 days. Swiss francs were provided against US dollars, euros, pounds sterling and Canadian dollars.

Repo transactions

In the case of liquidity-providing repo transactions, the SNB purchases securities from a bank (or other market participant admitted as a counterparty) and credits the associated sum in Swiss francs to the counterparty's sight deposit account with the SNB. At the same time, it is agreed that the National Bank will resell securities of the same type and quantity at a later date. The bank generally pays interest (repo interest rate) to the SNB for the term of the repo agreement. Repo transactions can also be used to absorb liquidity. In this instance, the bank purchases securities from the SNB, and the SNB debits the associated sum in Swiss francs to the counterparty's sight deposit account. From an economic perspective, a repo transaction is a secured loan. Like foreign exchange swap transactions, repo transactions can be conducted by way of auction or on a bilateral basis with a wide range of counterparties.

Until 24 May 2012, the SNB conducted liquidity-providing repo transactions in order to keep liquidity in Swiss francs at a high level. These transactions generally had a term of one week and were concluded on a bilateral basis. By the end of May, their average volume amounted to CHF 20 billion, while the annual average volume came to CHF 9.4 billion. The repo rate for these transactions was –0.15%. The negative rate reflected the cost of high-quality collateral eligible for SNB repos, which is required to cover repo transactions with the SNB.

Collateral eligible for SNB repos

The NBA (art. 9) requires that credit transactions with banks and other financial market participants be covered by sufficient collateral. The 'Guidelines of the Swiss National Bank (SNB) on monetary policy instruments' outline the types of securities eligible as collateral for SNB transactions. Only securities which meet the criteria listed in the 'Instruction sheet on collateral eligible for SNB repos', and which appear in the list of collateral eligible for SNB repos, are admitted for repo transactions.

The SNB has high requirements regarding the quality of the securities eligible as collateral. It accepts securities denominated in both Swiss francs and foreign currencies. The SNB's minimum requirements with regard to the market liquidity and credit rating of collateral – which have always been high by international standards – oblige banks to hold liquid assets of value on their balance sheets. This is essential if banks are to be able to refinance their operations on the money market even under difficult conditions.

The National Bank did not make any changes in 2012 to its collateral policy. Translated into Swiss francs, the volume of collateral eligible for SNB repos at the end of 2012 amounted to CHF 9,400 billion.

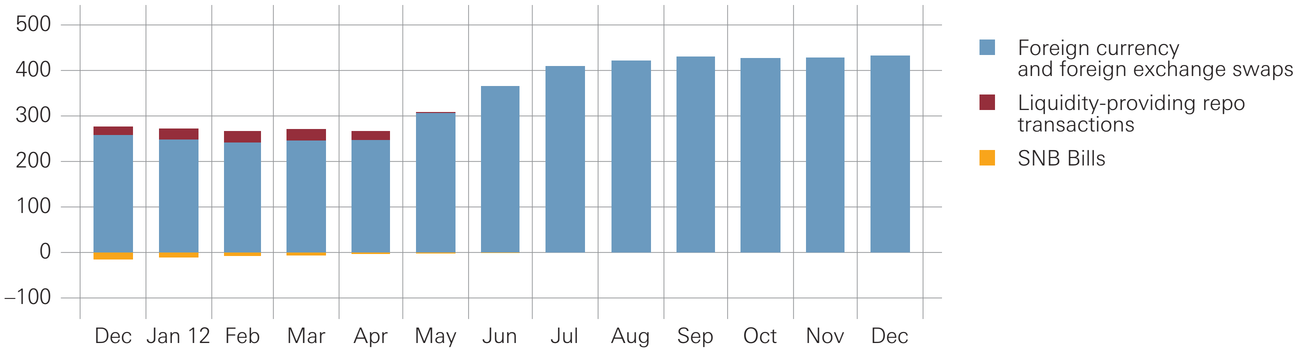
Own debt certificates

The issuance of its own debt certificates in Swiss francs (SNB Bills) allows the National Bank to absorb liquidity. The SNB can also repurchase SNB Bills via the secondary market, in order to increase the supply of liquidity to the financial system where necessary.

In 2012, no SNB Bills were issued or repurchased. The last SNB Bills fell due in July, and at the end of the year, there were no longer any outstanding.

SNB MONETARY POLICY OPERATIONS

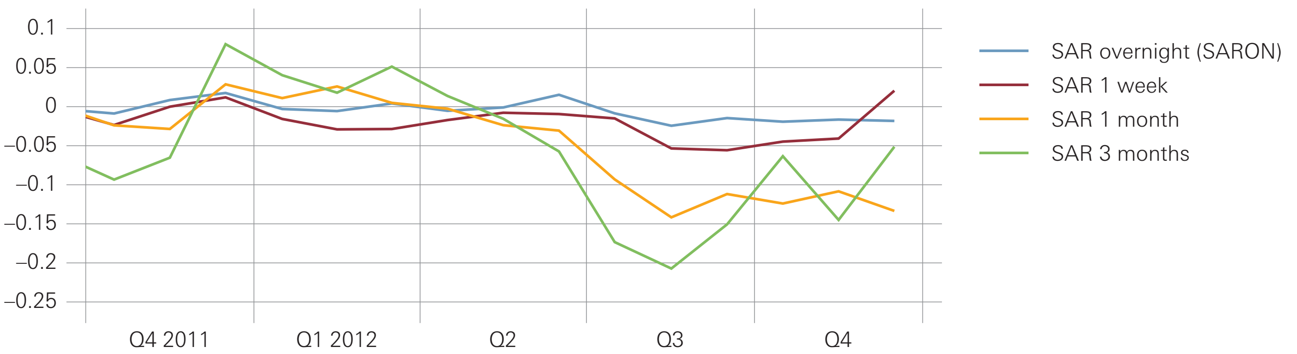
Balance sheet items relevant to monetary policy; stocks at month-end in CHF billions



Source: SNB

SWISS FRANC REFERENCE RATES (SWISS AVERAGE RATES, SAR)

Monthly averages of daily figures, in percent



Source: SNB

Intraday facility

During the day, the SNB provides its counterparties with interest-free liquidity (intraday liquidity) through repo transactions, so as to facilitate the settlement of payment transactions via the Swiss Interbank Clearing (SIC) system and the settlement of foreign exchange transactions via Continuous Linked Settlement, the multilateral payment system. The cash amounts drawn must be repaid by the end of the same bank working day at the latest.

Owing to the exceptionally high level of liquidity on the Swiss franc money market, average utilisation of the intraday facility declined to CHF 2.3 billion, compared with CHF 5.4 billion a year earlier.

Liquidity-shortage financing facility

To bridge unexpected liquidity bottlenecks, the SNB offers a liquidity-shortage financing facility. For this purpose, the National Bank grants its counterparties a limit which must be covered at all times by at least 110% collateral eligible for SNB repos. Counterparties have the right to obtain liquidity up to the limit granted until the following bank working day. The liquidity-shortage financing facility is granted in the form of a special-rate repo transaction. The special rate lies 0.5 percentage points above the call money rate and is no less than 0.5 percentage points. The basis for the rate is the SARON (Swiss Average Rate Overnight) of the current bank working day. The special rate is valid until 12.00 noon of the following bank working day.

In 2012, the liquidity-shortage financing facility was used only in individual cases and for modest amounts. Averaged over the year, the associated amount outstanding came to only a few thousand francs. At the request of financial market participants, the limits were increased by a total of CHF 0.8 billion to CHF 33.7 billion. As in 2011, a total of 91 financial market participants had been granted a limit by the end of the year.

SUPPLYING THE MONEY MARKET WITH LIQUIDITY

Monetary policy operations in CHF millions

Terms	2012 Outstanding Average[1]	2012 Turnover	2011 Outstanding Average[1]	2011 Turnover
Liquidity-providing operations	**13,666**	**721,835**	**26,437**	**709,669**
Repo transactions	9,423	443,060	8,007	397,535
Up to 3 days	–	–	0	1
4 to 11 days	8,175	426,000	7,291	381,485
12 to 35 days	1,248	17,060	716	16,049
36 days to 1 year	–	–	–	–
Foreign exchange swaps	4,244	91,190	18,430	253,950
Up to 7 days	1,064	52,040	1,853	102,543
8 to 28 days	1,024	17,016	1,933	51,762
29 to 94 days	2,155	22,133	14,643	99,645
Foreign currency purchases	–	187,585	–	17,815
SNB Bills repurchases[2]	–	–	–	40,369
Up to 28 days	–	–	–	12,975
29 to 84 days	–	–	–	14,056
85 to 168 days	–	–	–	7,403
169 to 336 days	–	–	–	5,935
Liquidity-absorbing operations	**3,011**	**–**	**95,029**	**1,140,030**
Repo transactions	–	–	15,287	761,947
4 to 11 days	–	–	14,213	733,947
12 to 35 days	–	–	1,074	28,000
SNB Bills	3,011	–	79,741	378,083
7 days	–	–	–	–
28 days	–	–	20,133	244,427
84 days	–	–	19,964	79,772
168 days	55	–	18,246	31,679
336 days	2,956	–	21,399	22,205
Standing facilities				
Intraday facility	2,251	567,177	5,361	1,361,659
Liquidity-shortage financing facility	0	5	1	234

1 Average level of monetary policy operations outstanding at the end of the day (with the exception of the intraday facility).
2 Repurchases of SNB Bills by residual term of debt certificates.

Monetary policy instruments

The SNB influences the interest rate level on the money market by means of secured liquidity-providing and liquidity-absorbing money market operations and through the applicable conditions, with the three-month Swiss franc Libor serving as its reference rate. The choice of liquidity management regime depends on monetary policy requirements and the liquidity structure in the banking system. If the banking system shows signs of being undersupplied with liquidity, the SNB provides liquidity through short-term money market operations. If, however, the banking system is oversupplied with liquidity, the SNB absorbs liquidity via short-term money market operations.

Within its set of monetary policy instruments, the SNB distinguishes between open market operations and standing facilities. In the case of open market operations, the SNB takes the initiative in the transaction. Where standing facilities are concerned – these include the liquidity-shortage financing facility and the intraday facility – it merely sets the conditions under which counterparties can obtain liquidity.

Regular open market operations include repo transactions and the issuance of SNB Bills. Further open market operation instruments, such as foreign exchange swaps and foreign exchange transactions, are available if necessary. The SNB conducts its open market operations in the form of auctions or bilateral transactions. Transactions on the money market are usually concluded via an electronic trading platform.

In principle, all banks domiciled in Switzerland and the Principality of Liechtenstein are admitted as counterparties in monetary policy operations. Other domestic financial market participants such as insurance companies, as well as banks domiciled abroad, may be admitted to monetary policy operations provided this is in the SNB’s monetary policy interest and the said institutions contribute to liquidity on the secured Swiss franc money market.

2.4 MINIMUM RESERVES

Main features of regulation

The duty to hold minimum reserves (arts. 17, 18, 22 NBA) ensures that banks have a minimum demand for base money; it thus fulfils a monetary policy objective. Eligible assets in Swiss francs comprise coins in circulation, banknotes and sight deposits held at the SNB. The minimum reserve requirement currently amounts to 2.5% of the relevant short-term liabilities, which are the sum of short-term liabilities (up to 90 days) in Swiss francs plus 20% of the liabilities towards customers in the form of savings and investments.

If a bank fails to fulfil the minimum reserve requirement, it is obliged to pay the SNB interest on the shortfall for the number of days of the reporting period during which the minimum reserve requirement was not observed. The interest rate is 4 percentage points higher than the average call money rate (SARON) over the reporting period in question.

MINIMUM RESERVES

In CHF millions

	2012 Outstanding Average	2011 Outstanding Average
Sight deposits at the SNB	225,847	83,166
Banknotes	5,680	5,651
Coins in circulation	95	97
Eligible assets	231,623	88,915
Requirement	12,008	10,254
Compliance in excess of requirement	219,615	78,661
Compliance in percent	1,929	867

Owing to the expansion of the relevant liabilities in the banking system, the statutory requirement increased in 2012 (between 20 December 2011 and 19 December 2012) to an average of CHF 12 billion. This is a 17% increase year-on-year. Eligible assets rose to CHF 231.6 billion on average, compared with CHF 88.9 billion a year previously. Banks exceeded the requirement by an annual average of CHF 219.6 billion; the average degree of compliance amounted to 1929% (2011: 867%).

The statutory minimum reserve requirement was met by almost all of the 285 banks. As regards the shortfalls, the sums involved were negligible. The total interest resulting from non-compliance with the minimum reserve requirement amounted to just CHF 1,442.

2.5 LIQUIDITY IN FOREIGN CURRENCIES

Swap agreement with Federal Reserve

In December 2012, the SNB – in coordination with the Bank of Canada, the Bank of England, the Bank of Japan and the European Central Bank (ECB) – extended the US dollar liquidity swap arrangement with the US Federal Reserve until February 2014. On the basis of this swap arrangement, the Federal Reserve will provide participating central banks with US dollars against their currencies when required, with the aim of countering undesirable tensions on the financial markets.

The swap agreements with the Federal Reserve, which were concluded for the first time in December 2007 in connection with the financial crisis, allow the SNB to conduct repo auctions in US dollars. The repo transactions are covered by collateral eligible for SNB repos. While these measures have no effect on the supply of money in Swiss francs, they enable the SNB's counterparties to gain easier access to US dollar liquidity. In 2012, the SNB offered weekly repo transactions in US dollars with a term of one week, and monthly repo transactions with a term of three months. Demand for both of these terms was limited, and the sums involved very modest.

Network of swap arrangements

In November 2011, as part of a coordinated action with the Bank of Canada, the Bank of England, the Bank of Japan, the ECB and the Federal Reserve, the SNB participated in the establishment of a network of bilateral liquidity swap arrangements. This measure allows the National Bank to provide Swiss francs to the participating central banks when required, as well as enabling the SNB to provide liquidity to its counterparties in any of the relevant currencies, should it be needed. In December 2012, in cooperation with the other central banks, the SNB extended the reciprocal swap lines until February 2014. By the end of 2012, it had not been necessary to provide liquidity in the relevant foreign currencies or in Swiss francs within the context of this agreement.

Swap agreement with NBP

In June 2012, the SNB and the National Bank of Poland (NBP) concluded a swap agreement. In the event of tensions on the Swiss franc interbank market, the facility enables the NBP to provide Swiss franc liquidity to banks in Poland. By the end of 2012, this facility had not been called upon.

2.6 EMERGENCY LIQUIDITY ASSISTANCE

SNB as lender of last resort

The National Bank can act as a lender of last resort. Within the context of this emergency liquidity assistance, the SNB can provide liquidity to one or more domestic banks if they are no longer able to obtain sufficient liquidity on the market.

Conditions

Certain conditions apply in order for emergency liquidity assistance to be granted. The bank or group of banks requesting credit must, for instance, be important for the stability of the financial system and be solvent. In addition, the liquidity assistance must be fully covered by sufficient collateral at all times. The SNB determines what securities it will accept as collateral for liquidity assistance. To assess the solvency of a bank or group of banks, the SNB obtains an opinion from the Swiss Financial Market Supervisory Authority (FINMA).

In 2012, the SNB did not provide any emergency liquidity assistance.

3
Ensuring the supply and distribution of cash

3.1 BACKGROUND

Mandate

The Swiss National Bank (SNB) is entrusted with the note-issuing privilege. Pursuant to art. 5 para. 2 (b) of the National Bank Act, it is responsible for ensuring the supply and distribution of cash (coins and notes) in Switzerland. It works to ensure an efficient and secure payment system. The SNB is also charged by the Confederation with the task of putting coins into circulation.

Role of the SNB

Banknotes and coins are supplied to the economy via the cash distribution services at the Berne and Zurich head offices, as well as 14 agencies operated by cantonal banks on behalf of the National Bank. The SNB issues banknotes and coins commensurate with demand for payment purposes, offsets seasonal fluctuations and withdraws banknotes and coins no longer fit for circulation. The role of retailer, which includes the distribution and redemption of banknotes and coins, is assumed by commercial banks, Swiss Post and cash processing operators.

3.2 OFFICES, AGENCIES AND CASH DEPOSIT FACILITIES

Turnover at offices

In 2012, the turnover (incoming and outgoing) of the offices in Berne and Zurich amounted to CHF 113.8 billion (2011: CHF 123.6 billion). They received a total of 419.3 million banknotes (2011: 451.8 million) and 1,510 tonnes of coins (2011: 1,693 tonnes). The SNB examined the quantity, quality and authenticity of the notes and coins. The incoming banknotes and coins were offset by an outflow of 446.8 million banknotes (2011: 469.9 million) and 2,180 tonnes of coins (2011: 2,364 tonnes).

Geneva office closed

As announced in March 2011, the SNB closed the Geneva branch office and its cash distribution service at the end of January 2012. The Geneva office was the last of the eight original regional branches. In order to continue ensuring the supply and distribution of cash in the Geneva area as well as possible, the SNB opened an agency at the Banque Cantonale de Genève on 1 February 2012. Since then, the main focus of the SNB's cash distribution services have been at the head offices in Berne and Zurich.

The agencies assist the SNB offices by distributing and redeeming cash in their regions. In order to do this, the agencies have access to cash belonging to the SNB. With the opening of the Geneva agency, the SNB now has 14 agencies.

Turnover at agencies

The agencies' turnover (incoming and outgoing) amounted to CHF 13.8 billion (2011: CHF 11.5 billion). The share of agency turnover in the SNB's overall turnover was 12.1% (2011: 9.3%).

Cash deposit facilities

Since 2003, cash processing operators may apply for cash deposit facilities with the SNB. These storage facilities contain stocks of notes and coins. The SNB sets up the facilities with third parties, while retaining their ownership. The facilities are managed by the cash processing operators, in that they exchange cash deposit holdings for their sight deposits at the National Bank. Cash deposit facilities reduce the number of incoming and outgoing banknotes at the SNB, as well as the number of transports made by the operators of cash deposit facilities, which makes for a more efficient supply and distribution of cash. In 2012, three cash deposit facilities were managed by cash processing operators.

3.3 BANKNOTES

Mandate

Pursuant to art. 7 of the Federal Act on Currency and Payment Instruments (CPIA), the SNB issues banknotes commensurate with demand for payment purposes and takes back any banknotes which are worn, damaged or surplus to requirements due to seasonal fluctuations. It also determines the denomination and design of the notes. Particular attention is paid to their security. Given the speed at which counterfeiting technology advances, the effectiveness of the security features on the banknotes must be continuously checked and, if necessary, adapted.

Banknote circulation

Persistent uncertainty on the financial markets and low interest rates contributed to ensuring that demand for banknotes remained high in 2012. Banknote circulation averaged CHF 54.7 billion, which was considerably above the CHF 49.3 billion recorded in the previous year. The demand for large-denomination notes increased at an above-average rate. The total number of notes in circulation averaged 357.9 million (2011: 336.3 million).

Issue and disposal

In 2012, the National Bank put 69.7 million freshly printed banknotes (2011: 63.7 million) with a face value of CHF 4.4 billion into circulation (2011: CHF 4.2 billion), and destroyed 56.8 million damaged or recalled notes (2011: 67.4 million) with a face value of CHF 3.4 billion (2011: CHF 4.1 billion).

Counterfeits

Approximately 4,300 counterfeit banknotes were confiscated in Switzerland in 2012 (2011: 3,700). This corresponds to 12 counterfeit notes per million Swiss franc notes in circulation (2011: 11). By international standards, this is a modest figure.

Status of new banknote series

The development of the new banknote series began in 2005 with a design competition. Integrating and combining security features involving new technologies that have not previously been used for banknotes presented a special challenge to all participants. It has been estimated that just the technical feasibility assessment of these security features will take several years.

In the planning phase for technical feasibility and during initial production tests in 2010, it became evident that the complexity of the new security features necessitated a postponement of the issue date to autumn 2012. During an early phase of the serial production, technical difficulties arose which had not been discernible in the testing phase, whose results were positive. In February 2012, the SNB therefore announced that the new banknote series would again have to be postponed.

In the wake of the announcement, the SNB, together with the industrial partners producing the new banknotes, conducted a comprehensive reassessment of the entire project, and defined and implemented an array of measures. These measures are to ensure that the high standards on security and quality and the production implementation aspects which apply to the new banknote series can be fulfilled, and that the series can go into long-term industrial production. The decision was therefore taken to produce a further test series. The time required for these measures is about one year. Afterwards, a complete issue of the first banknote denomination, the CHF 50 note, will be produced. Together with the necessary logistical preparations for the issue, this will amount to almost another two years. For these reasons, the issue of the first new banknote series may be expected in 2015 at the earliest. The issue date will be announced as soon as production of the first banknote denomination has been completed.

NUMBER OF BANKNOTES IN CIRCULATION

In millions

- CHF 10s: **70**
- CHF 20s: **77**
- CHF 50s: **45**
- CHF 100s: **95**
- CHF 200s: **38**
- CHF 1000s: **33**

Annual average for 2012

The SNB is committed to maintaining the highest standards of quality for its new banknote series, and therefore accepted the postponement of the new issue. This decision was rendered all the easier because the banknotes currently in circulation continue to offer a high standard of security.

3.4 COINS

Mandate

The SNB is entrusted by the Confederation with the task of coin circulation. Its role is defined in art. 5 CPIA. It takes over the coins minted by Swissmint and puts into circulation the number required for payment purposes. Coins that are surplus to requirements are taken back against reimbursement of their face value. The SNB's coinage services are not remunerated, as they constitute part of its mandate to supply the country with cash.

Coin circulation

In 2012, the value of coins in circulation averaged CHF 2,847 million (2011: CHF 2,784 million), which corresponds to 5,006 million coins (2011: 4,886 million).

4
Facilitating and securing cashless payments

4.1 BACKGROUND

Mandate

In accordance with art. 5 para. 2 (c) of the National Bank Act (NBA), the Swiss National Bank (SNB) facilitates and secures the operation of cashless payment systems. Art. 9 of the NBA empowers the SNB to keep accounts (SNB sight deposit accounts) for banks and other financial market participants.

SIC: a real-time gross settlement system

A large part of the cashless payment transactions of banks and other eligible financial market participants are settled via the Swiss Interbank Clearing (SIC) system. SIC is a real-time gross settlement system. This means payment orders are executed irrevocably and individually in real time through the participants' settlement accounts and are therefore equivalent to cash payments. The prerequisite for participating in SIC is the opening of an SNB sight deposit account.

SNB steers SIC

The SNB steers the SIC system and ensures that there is sufficient liquidity by granting, when necessary, intraday loans to banks against collateral (cf. chapter 6.5 for more information on the oversight of the SIC system). It transfers liquidity from the sight deposit accounts at the SNB to the settlement accounts in the SIC system at the start of each settlement day and transfers the balances from the SIC settlement accounts back to the sight deposit accounts at the end of the settlement day. Legally, the two accounts form a unit. The settlement day in SIC starts at 5.00 pm on the previous evening and ends at 4.15 pm on the corresponding calendar day.

Operation by SIX Interbank Clearing Ltd

The SNB has transferred the operation of the SIC system to SIX Interbank Clearing Ltd, a subsidiary of SIX. The SIC agreement, concluded between the SNB and SIX Interbank Clearing Ltd, governs the provision of data processing services for the SIC system by the latter. The relationship between the SNB and the holders of sight deposit accounts is governed by the SIC giro agreement.

Involvement in SIC

Based on the SIC agreement, the SNB requests and approves modifications and upgrades to SIC. Furthermore, it has a seat on the Board of Directors of SIX Interbank Clearing Ltd, and also exerts its influence by participating in various payment system bodies.

The National Bank grants access to the SIC system to banks, but also to other financial market participants. These include PostFinance, securities dealers, insurance companies and institutions which play a significant part either in the processing of payments (such as cash processing operators) or in the implementation of monetary policy. Subject to certain conditions, banks domiciled abroad can also gain access to the SIC system. While all SIC system participants must hold a sight deposit account at the SNB, some SNB sight deposit account holders are not connected to the SIC system.

Eligibility for SIC

4.2 THE SIC SYSTEM IN 2012

In 2012, SIC settled a daily average of roughly 1.6 million transactions amounting to CHF 120 billion. Compared to the previous year, this represents a 2.7% increase in the number of transactions and a 19.5% decrease in the value of transactions. On peak days, up to 4.8 million transactions were settled and turnovers of up to CHF 228 billion achieved.

Transactions and turnover

KEY FIGURES ON SIC

	2008	2009	2010	2011	2012
Number of transactions					
Daily average (in thousands)	1,468	1,508	1,542	1,585	1,628
Peak daily value for year (in thousands)	4,350	4,788	5,056	5,477	4,755
Value of transactions[1]					
Average daily turnover (in CHF billions)	224	169	154	149	120
Peak daily turnover for year (in CHF billions)	337	360	357	255	228
Average value per transaction (in CHF thousands)	152	112	100	94	74
Average liquidity					
Sight deposits at end of day (in CHF millions)	8,522	57,886	50,489	101,189	272,952
Intraday liquidity (in CHF millions)	9,515	6,362	7,211	5,237	2,161

1 The transaction volumes are now calculated without beginning of day holdings and are thus not comparable with the figures previously reported.

Participants in SIC

The SNB had 490 holders of sight deposit accounts as at 31 December 2012 (2011: 494). Of these, 378 participated in the SIC system (2011: 380). The majority of SIC participants are domiciled in Switzerland (260, as in the previous year), and of these, 24 belong to the category 'other financial market participants' (2011: 21). This includes six domestic insurance companies.

4.3 DEVELOPMENTS IN FINANCIAL MARKET INFRASTRUCTURE

New SIC architecture

The SIC system, which began operations in 1986, is being redeveloped to keep pace with technological advances. The main goal of the SIC4 project is to redesign the technical architecture of the SIC system. The project is being managed by SIX Interbank Clearing Ltd, with the involvement of the SNB and the banks.

Swiss financial market infrastructure

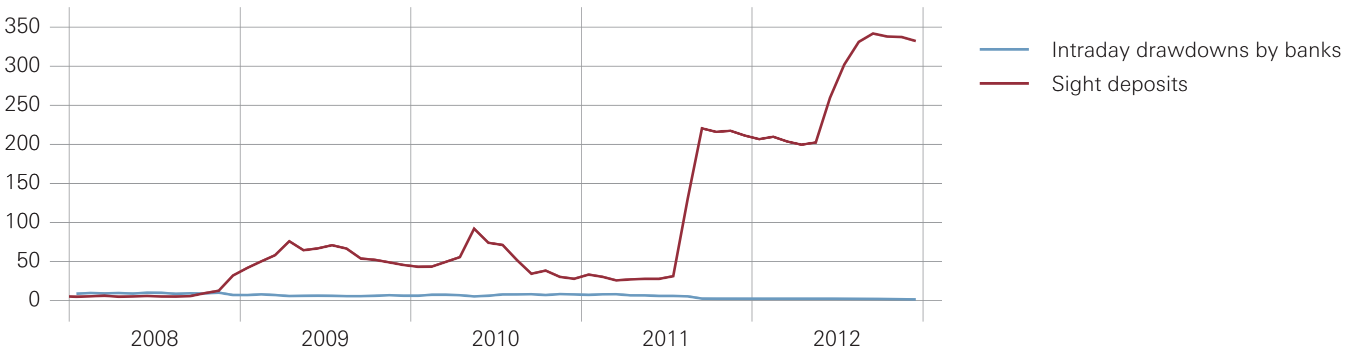
The SIC system is steered by the SNB and is a key element of the Swiss financial market infrastructure, which originated as a joint enterprise among Swiss banks. The Swiss financial market infrastructure is operated by SIX and covers the entire value chain, comprising securities trading (stock exchange), securities services (including securities settlement), payment services (including the SIC system) and financial information. A well-functioning, secure and efficient financial market infrastructure is of crucial importance to the SNB in fulfilling its statutory mandate, particularly in providing the money market with liquidity as well as facilitating and securing cashless payments.

Dialogue with SIX and banks

The financial market infrastructure providers have been subject to increased international competition and regulatory transformation for some time now. In view of these challenges and the importance of the financial market infrastructures, the SNB held comprehensive dialogues with SIX and the Swiss banks during 2012, covering the scope, organisation and operation of the Swiss financial market infrastructure.

LIQUIDITY IN SIC

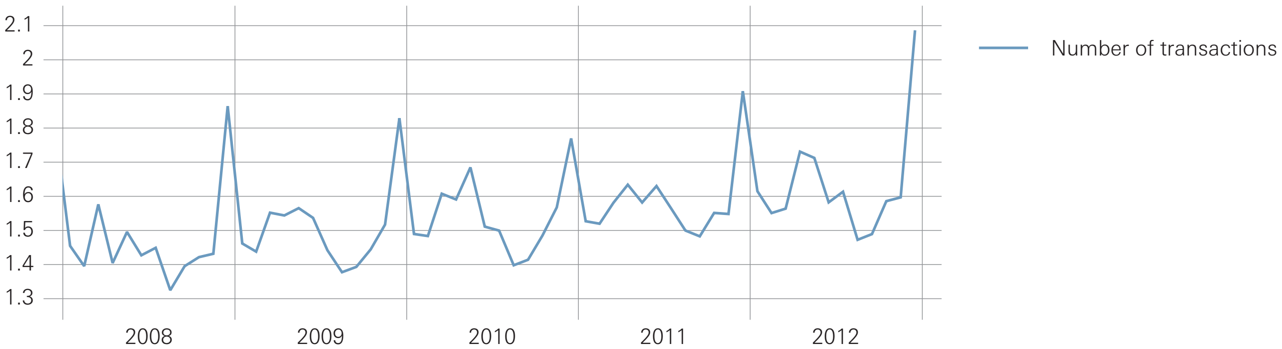
Monthly averages of daily figures, in CHF billions



Source: SNB

TRANSACTIONS IN SIC

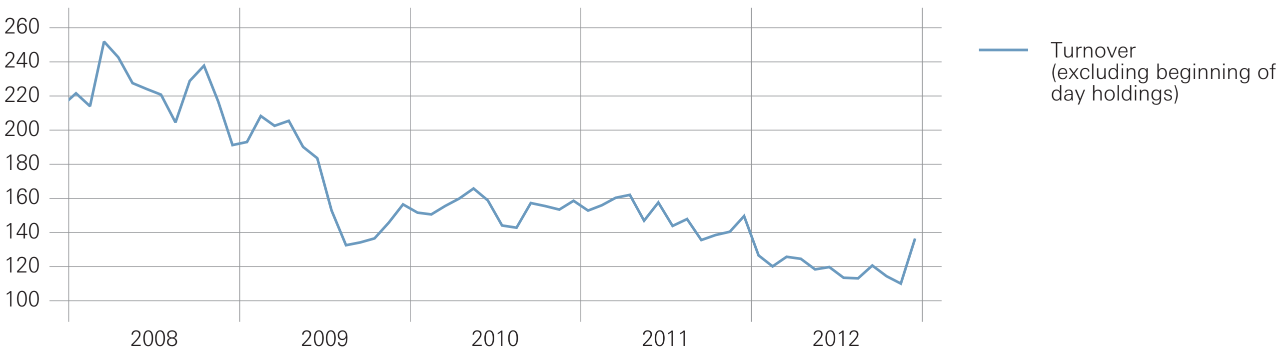
Monthly averages of daily figures, transactions in millions



Source: SNB

TURNOVER IN SIC

Monthly averages of daily figures, in CHF billions



Source: SNB

5 Asset management

5.1 BACKGROUND AND OVERVIEW

Mandate

The assets of the Swiss National Bank (SNB) fulfil important monetary policy functions. They consist of foreign currency assets, gold and, to a lesser extent, financial assets in Swiss francs. Their size and composition are determined by the established monetary order and the requirements of monetary policy. Under art. 5 para. 2 of the National Bank Act (NBA), the SNB is responsible for managing the currency reserves, part of which must be held in the form of gold (art. 99 para. 3 Federal Constitution).

Currency reserves

The National Bank's currency reserves are held primarily in the form of foreign currency investments and gold. The currency reserves also include international payment instruments and the reserve position in the International Monetary Fund (IMF), but not the loan to the stabilisation fund.

The National Bank requires currency reserves to ensure that it has room for manoeuvre in its monetary policy at all times. These reserves serve to build confidence, and to prevent and overcome potential crises. At present, the level of the currency reserves is a direct result of the implementation of monetary policy, in other words the enforcement of the minimum exchange rate.

Financial assets in Swiss francs

The financial assets in Swiss francs are made up of Swiss franc bonds and sometimes also claims from repo transactions. At the end of 2012, there were no outstanding claims from repo transactions.

Loan to stabilisation fund

The purpose of the loan to the stabilisation fund was to finance the acquisition in 2008 of illiquid assets from UBS. The objective of the stabilisation fund managed by the SNB is to successively liquidate the assets acquired. Income from the stabilisation fund portfolio (interest, sales and repayments of principal) is used primarily to repay the loan (cf. chapter 6.7).

Primacy of monetary policy

Asset management is governed by the primacy of monetary policy and is carried out in accordance with the criteria of security, liquidity and return. Assets are selected and managed according to generally accepted asset management principles, while taking into account the specific requirements of the SNB. When selecting assets, care is taken to avoid potential conflicts with the conduct of monetary policy, which is the SNB's core mandate.

Investment criteria and restrictions

The investment policy is based on requirements specific to central banks as well as comprehensive risk/return analyses. The SNB has high standards with regard to the security and liquidity of its assets. It therefore invests a substantial portion of its currency reserves in highly liquid foreign government bonds denominated in the major currencies, as well as in gold. This ensures that it retains its freedom of action even in a crisis. In order for the currency reserves to continue performing their intended function over the longer term, they need to keep their value over time. Appropriate diversification, i.e. the inclusion of additional currencies and asset classes such as equities, corporate bonds and inflation-linked bonds, helps the SNB to achieve this goal.

Challenges for investment policy

The currency reserves grew in 2012 by CHF 171 billion to around CHF 485 billion. This growth in volume was accompanied by greater demands on currency reserve management and heightened financial risk. The expansion in its portfolio prompted the National Bank to explore ways to diversify its investments further. It decided to include the South Korean won as an investment currency. Compared to a year earlier, the share of the US dollar and the pound sterling in the foreign exchange reserves increased, while that of the euro declined. The share of equities in the foreign exchange reserves also grew. As a result of rapid and large inflows due to foreign currency purchases carried out to enforce the minimum exchange rate, the effective allocation across the various currencies and asset classes briefly diverged from the desired allocation. Because the volume of currency inflows was high at times, these divergences were only corrected gradually. The SNB took care to avoid its investments having any impact on the markets and currency developments in other countries. The capacity of individual markets to rapidly absorb high volumes is an important criterion for investing currency inflows. For this reason, the SNB placed part of these inflows with other central banks. The opening of a branch in Singapore in mid-2013 will ensure a more efficient management of the SNB's assets in the Asia-Pacific region through the local presence of an internal portfolio management team.

5.2 INVESTMENT AND RISK CONTROL PROCESS

Responsibilities of Bank Council and Risk Committee

The NBA defines the SNB's responsibilities and describes in detail its mandate with regard to asset management. The Bank Council is charged with the integral oversight of the investment and risk control process. Its role is to assess the underlying principles and monitor compliance with them. The Risk Committee – which is composed of three members of the Bank Council – supports the Bank Council in this task. In particular, it monitors risk management. Internal risk management reporting is addressed to the Governing Board and the Risk Committee.

Responsibilities of Governing Board

The Governing Board defines the principles of the investment policy. In particular, it sets out the requirements with regard to the security, liquidity and return of the investments, as well as the eligible currencies, investment categories, instruments and debtor categories. In addition, it decides on the composition of the currency reserves and other assets, and defines the foreign currency investment strategy. The investment strategy encompasses the allocation to the different portfolios and the guidelines for their management, in particular the allocation to different currencies and investment categories, and the determination of the scope for active management at operational level.

Responsibilities of Investment Committee and Portfolio Management

An internal committee, the Investment Committee, determines the tactical allocation of the foreign currency investments at operational level. Within the strategically prescribed range, it adjusts currency weightings, bond durations and allocation to the different investment categories, to take account of changed market conditions. The management of the portfolios is the responsibility of Portfolio Management. The majority of investments are managed internally. External asset managers are used mainly for benchmarking the internal portfolio management. To avoid conflicts of interest, operational responsibilities for monetary policy and investment policy operations are largely kept separate.

Responsibilities of Risk Management

Risk is managed and mitigated by means of a system of reference portfolios, guidelines and limits. All relevant financial risks on investments are identified, assessed and monitored continuously. Risk measurement is based on standard risk indicators and procedures. In addition to these procedures, sensitivity analyses and stress tests are carried out on a regular basis.

The SNB's comparatively long-term investment horizon is taken into account in all of these risk analyses. To manage and assess credit risk, information from major rating agencies, market indicators and in-house analyses are used. Credit limits are set on the basis of this information, and adjusted whenever the assessment of counterparty risk changes. With a few exceptions, the replacement values of derivatives are collateralised by securities. Concentration and reputational risks are also factored in when determining risk limits. Risk indicators are aggregated across all investments. Compliance with the guidelines and limits is monitored daily. The results of risk management activities are submitted to the Governing Board and the Bank Council's Risk Committee in quarterly risk reports.

5.3 CHANGES IN AND BREAKDOWN OF ASSETS

Changes in assets

At the end of 2012, the SNB's balance sheet total was CHF 499 billion, which was CHF 153 billion higher than a year earlier (2011: CHF 346 billion). This is mainly due to the growth in the currency reserves, which rose by CHF 171 billion to CHF 485 billion in the space of a year. The bulk of this growth resulted from foreign currency purchases, although valuation gains on the currency reserves also contributed. By contrast, at the end of 2012, the SNB no longer held any foreign exchange from swaps. Holdings of Swiss franc assets declined, because at the end of 2012 there were no outstanding claims from repo transactions in Swiss francs. The loan to the stabilisation fund decreased further, as a result of repayments, coupons and asset sales. At the end of 2012, it was down to just over CHF 4 billion, compared to CHF 8 billion a year previously. The loan is denominated in various currencies, with interest being paid at the one-month Libor for the respective currency plus 2.5 percentage points.

Investment categories

At the end of 2012, the bond portfolios in the foreign currency investments and the Swiss franc bond portfolio contained government and quasi-government bonds as well as bonds issued by supranational organisations, local authorities, financial institutions (mainly covered bonds) and other corporations. A portion of the foreign currency investments was placed on accounts at other central banks and with the Bank for International Settlements (BIS).

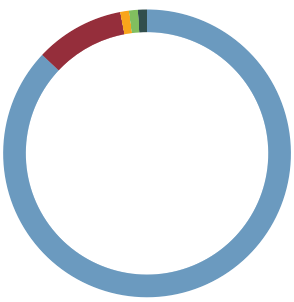
The equity portfolios are made up of shares from medium-sized and large corporations in advanced economies. The SNB takes care to ensure that its equity management, too, has no impact on the markets. Furthermore, it does not regard itself as a strategic investor. Thus, equities are managed passively and according to a set of rules, and on the basis of a strategic benchmark comprising a combination of equity indices in various currencies. This results in a globally well-diversified equity portfolio of around 1,600 individual stocks. The close replication of indices ensures that no active positions can be accumulated in individual sectors or companies. Equity holdings that are managed in this way improve both the potential return and the risk profile of the assets.

Asset management instruments

The management of foreign currency investments also made use of derivatives. These included foreign exchange forwards and foreign exchange options used to manage the currency breakdown of foreign currency investments. Interest rate risks were managed using derivative instruments such as interest rate swaps and interest rate futures. Stock index futures were used to manage the equity investments. A small number of credit default swaps were concluded to manage corporate bonds.

BREAKDOWN OF SNB ASSETS

In percent



- Foreign currency investments **87**
- Gold reserves **10**
- Swiss franc securities **1**
- Loan to stabilisation fund **1**
- Monetary institutions **1**

Total: CHF 499 billion
At year-end 2012

BREAKDOWN OF FOREIGN CURRENCY INVESTMENTS AND SWISS FRANC BOND INVESTMENTS AT YEAR-END

	2012 Foreign currency investments	2012 CHF bonds	2011 Foreign currency investments	2011 CHF bonds
Currency allocation (in percent, incl. derivatives positions)				
CHF		100		100
EUR	49		52	
USD	28		26	
JPY	8		9	
GBP	7		5	
CAD	4		4	
Other [1]	4		4	
Investment categories (in percent)				
Investments with banks	0	–	0	–
Government bonds [2]	82	35	83	34
Other bonds [3]	6	65	8	66
Equities	12	–	9	–
Breakdown of bonds (in percent)				
AAA-rated [4]	78	79	83	78
AA-rated [4]	17	21	12	21
A-rated [4]	2	0	3	1
Other	3	–	2	–
Investment duration (years)	3.3	6.6	4.0	6.1

1 AUD, DKK, SEK, SGD, KRW.
2 Government bonds in own currency, deposits with central banks and the BIS; in the case of CHF investments, also bonds issued by Swiss cantons and municipalities.
3 Government bonds in foreign currency as well as bonds issued by foreign local authorities and supranational organisations, covered bonds, corporate bonds, etc.
4 Average rating, calculated from the ratings of the three major credit rating agencies.

Changes in asset structure

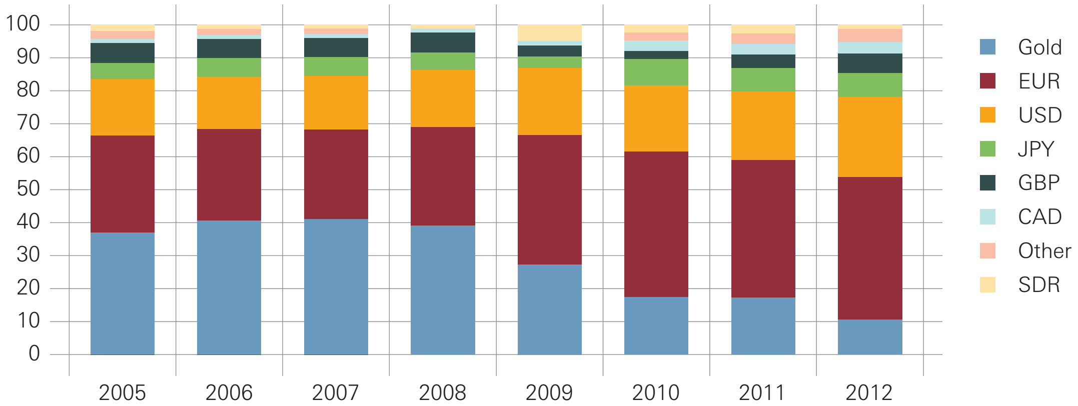
There were only very slight year-on-year changes in the investment structure of the foreign currency investments and Swiss franc bonds. The principles of currency and asset class diversification continued to be observed. At the end of 2012, the share of the main investment currencies, the euro and the US dollar, amounted to 49% and 28% respectively. Over 20% of fixed-income investments were held as sight deposits at other central banks. The share of equities was increased from 9% to 12%.

Sovereign wealth fund

Against the background of the strong rise in currency reserves, a public debate has arisen in which the possible creation of a sovereign wealth fund has been mooted. This could, it is argued, bring about an improved risk/return structure, reduce exchange rate risk and support Switzerland's strategic interests. This argument overlooks the fact that the SNB's investment needs are currently a direct consequence of the enforcement of the minimum exchange rate for monetary policy purposes, and of the associated foreign currency purchases. Therefore, when engaging in investment activities, the SNB must take account of monetary policy needs, and retain the flexibility to define the size and composition of its balance sheet. Moreover, a sovereign wealth fund would face the same exchange rate exposure as the SNB's currency reserves; even a much higher proportion of 'real' investments such as equities would offer no protection against value fluctuations. And if one were to go so far as to couple the investment of the SNB's currency reserves with Switzerland's strategic interests, this could create conflicts of interest and potentially threaten the SNB's independence. In extremis, this could hamper the SNB in the fulfilment of its core mandate. By investing part of the currency reserves in a well-diversified range of equities and corporate bonds, the SNB is able to exploit the positive contribution of these asset classes to the risk/return profile. At the same time, it retains the flexibility to adjust its monetary and investment policies to changing requirements.

BREAKDOWN OF CURRENCY RESERVES

In percent, excluding investments and liabilities from foreign exchange swaps against CHF



Source: SNB

5.4 RISKS TO ASSETS

Risk profile …

The main risk to the assets is market risk, in particular risks related to exchange rates, the gold price, share prices and interest rates. In addition, investments are exposed to liquidity risk and, to a lesser extent, credit risk. As a result of the substantial growth in currency reserves, risk increased markedly. The risk of loss on foreign currency investments resulting from a possible appreciation of the Swiss franc cannot be reduced using investment policy measures (such as hedging with foreign exchange forwards), as this would have a direct impact on monetary policy. Market risk is principally managed by diversifying across currencies and asset classes. The SNB counters liquidity risk by holding a considerable part of its investments in the world's most liquid currencies and markets. The risk associated with the loan to the stabilisation fund has fallen considerably as repayments have continued. This is discussed in greater detail in chapter 6.7 of the accountability report and in the section 'Financial information on the stabilisation fund' of the financial report.

… of currency reserves

The gold price and exchange rates were the most important risk factors for the currency reserves. The growth in foreign currency investments caused exchange rate risk to rise sharply. As a result, even minor changes in the Swiss franc exchange rate can lead to substantial fluctuations in investment income, and thus in the SNB's equity. By contrast, given a 12% proportion of shares and an average duration of over three years for fixed-interest investments, the contribution of share price risk and interest rate risk to total risk was small.

… of Swiss franc bonds

The Swiss franc bond portfolio contained first and foremost bonds issued by the Confederation, the cantons and foreign borrowers, as well as Swiss Pfandbriefe. The duration of the portfolio was six-and-a-half years. The Swiss franc portfolio is managed passively.

Credit and liquidity risks

The SNB was exposed to credit risk through bond investments relating to various borrowers and borrower categories. These included bonds issued by public and supranational borrowers as well as covered bonds and similar instruments. In addition, corporate bonds totalling some CHF 12 billion were held in the foreign currency investments. Credit risk arising from non-tradable instruments with respect to banks was very low. Replacement values of derivatives were hedged with counterparties, in accordance with the ISDA (International Swaps and Derivatives Association) agreements in force. Investments mainly take the form of government bonds or holdings at central banks; the bulk of these are in highly liquid bonds issued by euro area core countries and by the US. The large majority of fixed-income investments (78%) bore the highest rating (AAA). Investments with central banks are generally awarded the same rating as that of the country concerned. In all, over 95% of bonds were rated AA or higher.

Balance sheet growth and equity

Owing to the strong growth in currency reserves during 2012, the share of equity in the balance sheet total declined further, to just under 12% at the end of the year. This figure is low by historical standards, and it should be borne in mind that the value of currency reserves can fluctuate considerably. The SNB's loss-absorbing capital is composed mainly of the provisions for currency reserves and the distribution reserve, and rose by CHF 5 billion as a result of positive returns on assets. Of this amount, CHF 3.6 billion was allocated to the provisions for currency reserves; the remainder after the profit distribution to the Confederation and the cantons was allocated to the distribution reserve. At year-end, equity after appropriation of profit amounted to CHF 57 billion.

5.5 INVESTMENT PERFORMANCE

Positive return on investments

Investment performance is calculated for foreign currency investments, gold and Swiss franc bonds. Costs arising from and yields on foreign exchange swaps and repo transactions carried out for monetary policy purposes as well as SNB debt certificates (SNB Bills) are not considered in the return calculation.

In 2012, the overall return on currency reserves was 2.3%. The Swiss franc value of the gold reserves rose by 2.8% due to the rise in the price of gold. The return on foreign currency investments, measured in terms of Swiss francs, was 2.2%. Favourable stock market developments and declining interest rates contributed to this result. The exchange rate return on foreign currency investments was negative, at –2.3%, as a result of the Swiss franc appreciation. The return on Swiss franc bonds amounted to 3.7%.

RETURN ON INVESTMENTS

Cumulated, time-weighted daily returns in percent

	Currency reserves [1]					CHF bonds
	Total	Gold	Foreign currency investments			Total
			Total	Exchange rate return	Return in local currency	
2002	1.4	3.4	0.5	–9.1	10.5	10.0
2003	5.0	9.1	3.0	–0.4	3.4	1.4
2004	0.5	–3.1	2.3	–3.2	5.7	3.8
2005	18.9	35.0	10.8	5.2	5.5	3.1
2006	6.9	15.0	1.9	–1.1	3.0	0.0
2007	10.1	21.6	3.0	–1.3	4.4	–0.1
2008	–6.0	–2.2	–8.7	–8.9	0.3	5.4
2009	11.0	23.8	4.8	0.4	4.4	4.3
2010	–5.4	15.3	–10.1	–13.4	3.8	3.7
2011	4.9	12.3	3.1	–0.8	4.0	5.6
2012	2.3	2.8	2.2	–2.3	4.7	3.7

1 In this table, they correspond to gold and foreign currency investments, excluding IMF Special Drawing Rights.

6 Contribution to financial system stability

6.1 BACKGROUND

Mandate

Art. 5 para. 2 (e) of the National Bank Act (NBA) confers upon the Swiss National Bank (SNB) the mandate of contributing to the stability of the financial system. Financial stability means that financial system participants, i.e. financial intermediaries (particularly banks) and infrastructures (payment and securities settlement systems), can perform their functions and are able to withstand potential disturbances. It is an important prerequisite for economic development and effective monetary policy implementation.

In the area of financial stability, the SNB fulfils this mandate by analysing sources of risk to the financial system and identifying areas where action is needed. In addition, it helps to create and implement a regulatory framework for the financial sector, and oversees systemically important payment and securities settlement systems. In a crisis, the SNB fulfils its mandate by acting as lender of last resort to provide domestic banks with emergency liquidity assistance where necessary, in cases where such banks are no longer able to refinance themselves on the market and where their insolvency would have a severe impact on financial system stability (cf. chapter 2.6).

Collaboration with FINMA, FDF and foreign authorities

At national level, the SNB works together with the Swiss Financial Market Supervisory Authority (FINMA) and the Federal Department of Finance (FDF) to create a regulatory environment that promotes stability. The SNB addresses the issue mainly from a systemic perspective, and its focus is therefore on the macroprudential aspects of regulation. For its part, FINMA is responsible, among other things, for the monitoring of individual institutions, i.e. microprudential supervision. At international level, the SNB participates in the design of the regulatory framework through its membership of the Financial Stability Board (FSB), the Basel Committee on Banking Supervision (BCBS) and the Committee on Payment and Settlement Systems (CPSS). In the oversight of cross-border payment and securities settlement systems, the SNB liaises closely with foreign authorities.

6.2 MAIN ACTIVITIES IN 2012

Implementation of 'too big to fail' legislation

In 2012, the SNB was involved in various activities relating to the implementation of the 'too big to fail' legislation. The main focus was on work surrounding the determination of systemically important banks and bank functions, as well as the drafting of the associated decrees for both the big banks.

Countercyclical capital buffer

As part of a package of measures aimed at reducing risk on the mortgage market, the Federal Council announced that the legal provisions on the introduction of a countercyclical capital buffer would enter into force on 1 July 2012. The countercyclical capital buffer is a macroprudential instrument that temporarily raises capital requirements for banks in Switzerland, depending on the magnitude of the imbalances on the Swiss lending market. The SNB played an active role in the design of this instrument. The decisions on the activation, deactivation and level of the buffer will be made by the Federal Council, upon the proposal of the SNB. The SNB consults FINMA before submitting its proposal to the Federal Council.

Oversight of payment and securities settlement systems

As part of the oversight of systemically important payment and securities settlement systems, the SNB provided feedback on a number of projects set up by the system operators, in particular on the planned participation of SIX SIS Ltd in TARGET2-Securities (T2S) and on the clearing links between SIX x-clear and other central counterparties. In addition, the SNB launched the revision of the National Bank Ordinance's (NBO) minimum requirements for operators of payment and securities settlement systems.

6.3 MONITORING THE FINANCIAL SYSTEM

Financial Stability Report

In its annual *Financial Stability Report*, published in June 2012, the SNB assessed developments and risks in the economic environment as a whole and in the Swiss banking sector. It reported that, overall, economic and financial conditions for the Swiss banking sector had deteriorated. It attributed this to the escalation of the European debt crisis, the loss of momentum in global economic growth, the growing tensions in the international banking system and the build-up of imbalances on the Swiss mortgage and real estate markets.

With regard to the capitalisation of the Swiss big banks, the SNB noted that, despite the fact that progress had been achieved, their loss-absorbing capital was still below the level needed to ensure sufficient resilience given the high risks in the environment. It therefore concluded that the big banks' importance for the Swiss economy and for financial stability required that they further strengthen their resilience. Specifically, the SNB recommended that UBS continue with this process – which entailed, in particular, a policy of dividend restraint. It recommended that Credit Suisse expand its loss-absorbing capital base significantly during the course of 2012. Credit Suisse subsequently took appropriate measures.

As regards domestically focused commercial banks primarily engaged in lending activities, the SNB noted that average capitalisation relative to regulatory requirements was high. At the same time, it emphasised that the resilience of some of these banks – including some larger ones – should be further strengthened, in view of their risk profile.

In addition, the SNB pointed out that, given the growing risks in the Swiss mortgage and real estate markets, a temporary raising of system-wide capital requirements might have to be considered (cf. chapter 6.4.2).

In the second half of 2012, both big banks increased their resilience further. Progress was particularly marked at Credit Suisse. In addition to retaining profits, this was mainly attributable to the capital measures it announced in July, most of which were implemented in the months that followed. The SNB welcomed the big banks' efforts to increase their resilience, although it noted that capital levels still needed to be improved on an ongoing basis.

Monitoring of mortgage and real estate markets

The SNB continued to monitor developments on the domestic mortgage and real estate markets closely. It considered that the potential for a further build-up of imbalances and the associated risks to financial stability were still high. While there were isolated indications of a slowdown in market momentum during the year, overall the market continued to be extremely dynamic, against a background of historically low interest rates, and most real estate price indices rose sharply again. This led to growing signs of overvaluation for residential property in certain regions, and for the owner-occupied apartment segment throughout Switzerland. In addition, mortgage lending volumes, which – relative to GDP – were already high by historical standards, increased further. Finally, the quarterly mortgage lending survey conducted since the beginning of 2011 suggested that banks' risk appetite continued to be high.

6.4 MEASURES TO STRENGTHEN FINANCIAL STABILITY

6.4.1 IMPLEMENTATION OF BASEL III

Capital standards

Together with FINMA, the National Bank supported the FDF in finalising the comprehensive revision of the Ordinance on Capital Adequacy and Risk Diversification for Banks and Securities Dealers (Capital Adequacy Ordinance), which integrates the Basel III international standards into Swiss law. On 1 June 2012, the Federal Council adopted the revised Capital Adequacy Ordinance, which entered into force on 1 January 2013. The Ordinance requires all banks to hold better-quality capital and sets out additional capital requirements for systemically important banks (cf. chapter 6.4.3). The legislative provisions on the countercyclical capital buffer, which also forms part of the Basel III framework and is set down in the Capital Adequacy Ordinance, already entered into force on 1 July 2012 (cf. chapter 6.4.2).

In addition, the SNB took part in the FINMA-led working group charged with revising FINMA's circulars related to the Capital Adequacy Ordinance.

Liquidity standards

In order to integrate the Basel III international liquidity standards into Swiss legislation, a working group headed by FINMA was set up at the end of 2011. The SNB was also represented in the working group, which focused in particular on the new Ordinance on Liquidity for Banks (Liquidity Ordinance), which will be phased in from early 2013. The Liquidity Ordinance combines the existing liquidity provisions with new additional qualitative requirements for banks' liquidity management. It also authorises FINMA to introduce a comprehensive reporting requirement for the liquidity coverage ratio (LCR) from 2013 onwards. The LCR is one of the two main liquidity standards under Basel III, and is due to come into effect in Switzerland on 1 January 2015. A pilot reporting exercise was carried out with a sample of Swiss banks in 2012.

6.4.2 REDUCING RISK ON MORTGAGE MARKET

Risk weights and self-regulation rules

On 1 June 2012, the Federal Council announced three measures aimed at reducing risk on the mortgage market. The first related to the adjustment of the risk weights set down in the Capital Adequacy Ordinance for high loan-to-value mortgage loans. It entered into force on 1 January 2013. The second measure was a further revision of the self-regulation rules on mortgage lending by banks, which took effect in July 2012.

Countercyclical capital buffer

The third measure, introduced by the Federal Council with effect from 1 July 2012, is the countercyclical cyclical buffer, in whose design the SNB played a major role. This instrument allows capital requirements for banks to be temporarily raised, depending on the magnitude of the imbalances on the Swiss lending market. First, the aim is to protect the banking sector from the consequences of excessive lending growth, because the buffer increases banks' loss absorbency. Second, it leans against the build-up of such excesses by increasing the cost of lending. The countercyclical capital buffer is a macroprudential instrument, and as such constitutes a key component of the Basel III framework; most countries are planning to introduce it over the next few years. In view of the growing imbalances on the Swiss mortgage and real estate markets, the SNB advocated that this instrument be made available in Switzerland as soon as possible.

The countercyclical capital buffer is activated if there are growing signs of imbalances. The division of responsibilities is such that the Federal Council decides on the activation, deactivation and level of the buffer, upon the proposal of the SNB. The National Bank consults FINMA before submitting its proposal to the Federal Council. More detailed information on the design and implementation of the buffer can be found on the SNB's website.

Since 2010, the SNB had repeatedly warned of the build-up of risks on the Swiss mortgage and real estate markets, and the associated risks for financial stability. In the third quarter of 2012, it carried out its first assessment on whether to activate the countercyclical capital buffer. Although the momentum on domestic mortgage and real estate markets continued to be strong, the SNB decided not to propose that the buffer be activated. One reason for this was that there were some indications of a possible slowdown of this momentum (cf. chapter 6.3). Moreover, in June 2012, the Federal Council had announced further measures aimed at dampening mortgage and real estate price growth. The SNB emphasised that its decision should not be interpreted as an all-clear. The risk of a further build-up of imbalances remained high, and the SNB would regularly reassess the need to activate the buffer.

In December, during its six-monthly news conference, the SNB noted that the measures taken so far had not yet led to a significant trend reversal in mortgage and real estate markets. It stressed that, due to the exceptionally low interest rates, there was a considerable risk that imbalances would continue to build up.

6.4.3 Implementation of 'too big to fail' legislation

Revision of Banking Act

The 'too big to fail' legislation is aimed at strengthening the stability of the financial system by subjecting systemically important banks to additional regulatory requirements. Systemically important banks are those whose failure would have a severe impact on financial system stability. A bank is deemed to be systemically important if it is of a certain size, if it is closely interconnected with the financial system and the economy, and if the services it provides are hard to substitute at short notice. The SNB considers 'too big to fail' to be a key issue, and was closely involved in the drafting of the corresponding legislation. The associated revision of the Banking Act (the 'Too Big to Fail' Bill) was passed by parliament in September 2011, and took effect on 1 March 2012.

It was then necessary to amend the relevant ordinances and decrees implementing the Banking Act (including the Capital Adequacy Ordinance), and to determine systemically important banks and functions. The SNB played a major role in these efforts.

Determining systemically important banks and bank functions

The revised Banking Act gives the SNB the authority to determine which banks and bank functions are systemically important, following consultation with FINMA. The SNB carries out the requisite assessment as part of a formal process. This process culminates in the issuance of a decree. In November, the SNB issued decrees designating Credit Suisse Group and UBS as financial groups of systemic importance under the terms of the Banking Act.

Amendments to ordinances and FINMA circulars

In October 2012, parliament approved amendments to the implementing ordinances for the new Banking Act. The amendments to the Banking Ordinance and the Capital Adequacy Ordinance, as well as the associated FINMA circulars, include special provisions relating to the capital adequacy and organisation of systemically important banks, as well as changes to the requirements on risk diversification. These latter requirements, in particular, contain a reduction of the ceiling for maximum permissible concentrations of risk exposure to systemically important banks; this is aimed at reducing interconnectedness within the financial industry. As a result of efforts by the SNB, this ceiling also holds for very short positions.

In addition to the amendments to the Banking Ordinance and the Capital Adequacy Ordinance, the liquidity agreements concluded between FINMA and the big banks in March 2010 were also incorporated into the new Liquidity Ordinance. These special provisions for systemically important banks within the Liquidity Ordinance still need to be approved by parliament.

6.4.4 REGULATION OF OTC DERIVATIVES TRADING AND THE FINANCIAL MARKET INFRASTRUCTURE

At the request of a working group headed by the State Secretariat for International Financial Matters, in which the SNB participated, the Federal Council set the FDF the task of drawing up new legislation on over-the-counter (OTC) derivatives trading, and amending the regulations on the financial market infrastructure by spring 2013.

OTC derivatives trading

The new legislation on OTC derivatives trading is designed to implement the recommendations – agreed by the G20 and drafted by the FSB – on increasing the transparency, integrity and stability of the derivatives market in Switzerland. In particular, it is planned to oblige market participants, wherever possible, to trade all standardised derivatives via electronic platforms and clear them through central counterparties, and to report all derivatives transactions to a trade repository.

Financial market infrastructure

As regards financial market infrastructure, the legal framework for the authorisation of Swiss-domiciled central counterparties, central securities depositories and trade repositories is to be set up or enhanced. Furthermore, it is planned to establish a recognition regime for foreign financial market infrastructures wishing to provide services to a Swiss stock exchange or Swiss financial institutions. It is also planned to adjust the regulatory requirements for financial market infrastructure operators, in order to bring them into line with new international standards and the regulatory requirements of the EU. This last initiative is a prerequisite for Swiss financial market infrastructures to be able to continue providing services to EU markets and financial institutions.

6.5 OVERSIGHT OF PAYMENT AND SECURITIES SETTLEMENT SYSTEMS

6.5.1 BACKGROUND

Mandate

The NBA (art. 5 and arts. 19–21) requires the SNB to oversee systems for the clearing and settlement of payments (payment systems) and transactions involving financial instruments, especially securities (securities settlement systems). It empowers the SNB to impose minimum requirements on the operation of systems that might pose a risk for the stability of the financial system and to work in cooperation with FINMA and, if necessary, with foreign supervisory and oversight authorities. The NBO lays down the details of system oversight.

At present, the systems that could harbour risks for the stability of the financial system include the Swiss Interbank Clearing (SIC) payment system, the SECOM securities settlement system and the central counterparty SIX x-clear. The operators of these systems, SIX Interbank Clearing Ltd, SIX SIS Ltd and SIX x-clear Ltd – all subsidiaries of SIX – must meet the minimum requirements set out in the NBO. The SNB has developed a set of system-specific control objectives which set out these minimum requirements in greater detail.

Focus on systemically important systems

Other systems that are important for the stability of the Swiss financial system are the Continuous Linked Settlement (CLS) foreign exchange settlement system and the central counterparties LCH.Clearnet Ltd (LCH) and Eurex Clearing. The operators of these systems are domiciled in the US, the UK and Germany. The systems are exempted from the obligation to meet the minimum requirements, as they are already subject to adequate oversight by the regulators in these countries and there is a smooth exchange of information with the SNB.

Cooperation with FINMA

SIX SIS Ltd and SIX x-clear Ltd both hold banking licences and are subject to prudential supervision by FINMA as well as to system oversight by the SNB. While prudential supervision aims primarily at protecting individual creditors, system oversight focuses on the functioning of the financial system and the risks to which it is exposed. Although FINMA and the SNB exercise their supervisory and oversight powers separately, they coordinate their activities.

Cooperation with foreign authorities

The SNB cooperates with foreign authorities in the oversight of cross-border payment and securities settlement systems. In the case of the central counterparty SIX x-clear, which offers its services to various European markets and has clearing links with other central counterparties, the SNB cooperates with the central banks and supervisory authorities in Denmark, Finland, the Netherlands, Sweden and the UK.

For the oversight of the systems domiciled abroad – CLS, Eurex Clearing and LCH – the SNB has concluded memoranda of understanding or similar agreements with the relevant authorities. As regards LCH SwapClear, a division of LCH responsible for the clearing of OTC interest rate derivatives, the British financial regulator drew up a specific multilateral oversight agreement in 2012, into which the SNB also entered. The purpose of agreements with foreign authorities is to ensure that the SNB receives relevant system-related information at all times, that it is informed of assessments by local regulators, and that it can, if necessary, influence oversight activities. Finally, the SNB participates – together with the other central banks in the Group of Ten (G10) and under the leadership of the Belgian central bank – in the oversight of the Belgium-based Society for Worldwide Interbank Financial Telecommunication (SWIFT), which operates a global network for the transmission of financial information.

6.5.2 MAIN FOCUS OF OVERSIGHT

High degree of compliance with regulatory requirements

In 2012, the SNB assessed compliance with regulatory requirements by the system operators SIX Interbank Clearing Ltd, SIX SIS Ltd and SIX x-clear Ltd. The SNB concluded that compliance with the requirements was high in all areas assessed. The system operators are appropriately structured, well managed, and have adequate internal control systems. They have rules and procedures in place which limit settlement risk, and they satisfy the high requirements with respect to information and IT security. Some of the main focal points of oversight in 2012 are summarised below.

Information and IT security

To assess the systems' information and IT security, the SNB relies mainly on external auditors. In 2012, the audits – whose scope and degree of detail are determined by the SNB – focused on the physical security of the system operators and on the operation of the system. The audits revealed that the majority of the measures and controls adopted by the system operators are well suited to achieving the prescribed control objectives.

SIX SIS Ltd intends to participate in the T2S securities settlement system, which is currently being developed by the European Central Bank and is set to go live in 2015. In response to a corresponding enquiry from SIX SIS Ltd, the SNB confirmed that, from a regulatory perspective, there is no reason why the T2S framework agreement should not be signed. It asked SIX SIS Ltd to resolve the pending issues before T2S goes into operation.

T2S framework agreement

The SNB conducted an in-depth evaluation with SIX SIS Ltd and SIX x-clear Ltd regarding the provisions they have in place should a participant no longer fulfil the conditions for participation. Using a fictitious scenario, the analysis showed that both system operators have appropriate procedures and instruments to exclude a participant quickly, if necessary, and to limit the financial risks to themselves.

Provisions for possible exclusion of participants

Over the past few years, SIX x-clear Ltd has established clearing links with the central counterparties LCH, European Central Counterparty Limited (EuroCCP) and European Multilateral Clearing Facility N.V. (EMCF). This interoperability allows market participants to clear trades at different markets via the same central counterparty. The clearing links grew in importance following the expansion of SIX x-clear services to include other European trading platforms. Together with the relevant authorities from the UK and the Netherlands, the SNB concluded that the provisions currently in place to collateralise risk positions arising between central counterparties meet the regulatory requirements. This notwithstanding, the authorities advised the central counterparties to improve selected provisions and to periodically check their contractual agreements, and adapt them where necessary.

Clearing links between central counterparties

Central counterparty
A central counterparty is an institution which interposes itself between buyers and sellers on a market, acting as seller to every buyer and as buyer to every seller. Accordingly, this gives rise to two contractual relationships, namely between the central counterparty and each of the two market participants. The central counterparty is responsible for the management and performance of the contracts. Most notably, it assumes the counterparty risk, i.e. the risk that a contracting party cannot meet the obligations arising from the contract. Should one of the parties fail to meet its obligations, the central counterparty must have sufficient financial resources and liquidity to cover potential losses and meet its payment and delivery obligations on time. A central counterparty must therefore have an exceptionally robust risk management framework, particularly with regard to the management of credit and liquidity risks.

Implementing new international principles for financial market infrastructures

The National Bank intends to implement in Switzerland the new international principles for financial market infrastructures, which have been revised by the CPSS in collaboration with the International Organization of Securities Commissions (IOSCO). This will necessitate a revision of the minimum requirements stipulated in the NBO. In 2012, the SNB commenced work on this project, with the aim that the new minimum requirements enter into force in the second quarter of 2013.

6.6 INTERNATIONAL COOPERATION ON FINANCIAL MARKET REGULATION

At international level, the SNB participates in a number of different bodies in the area of financial market regulation. It is a member of the FSB, the BCBS and the CPSS (cf. chapter 7.3).

Financial Stability Board

The FSB brings together the national authorities responsible for financial stability (central banks, oversight authorities, ministries of finance), international organisations and standard-setting bodies. Switzerland is represented on the FSB by the National Bank and the FDF. In addition, the SNB is a member of the FSB Steering Committee. In April 2009, the G20 gave the FSB a mandate to promote financial stability and formulate appropriate regulatory and oversight measures. As part of this mandate, the FSB has since drawn up a number of reform proposals. Switzerland's position is developed in close collaboration between the FDF, FINMA and the SNB.

Wide range of topics at FSB

In 2012, the FSB addressed a broad range of topics. From a financial stability perspective, the most important areas of focus were, on the one hand, the work undertaken in connection with the methodology used to determine global and domestic systemically important banks; an initiative led by the BCBS (cf. section 'Principles for domestic systemically important banks' below). In November, on the basis of this assessment methodology, the FSB published a list of banks which it designated as being global systemically important financial institutions. On the other hand, the FSB concerned itself with recovery and resolution planning for global systemically important banks and formulated more detailed requirements with regard to these plans. Furthermore, in 2012, it monitored the implementation of the OTC derivatives market reforms and published two corresponding progress reports (cf. chapter 6.4.4).

Basel Committee on Banking Supervision

The BCBS brings together high-ranking representatives of banking supervisory authorities and central banks from 27 countries, including Switzerland. It develops recommendations and sets standards in the area of banking supervision, most notably the Basel Capital Accord (Basel I) and its successors, the Basel II and Basel III capital adequacy frameworks.

Principles for domestic systemically important banks

In 2012, the BCBS focused, among other things, on the formulation of rules for domestic systemically important banks. More specifically, it developed a set of principles on the assessment methodology and higher loss absorbency (HLA) requirements for these banks, and issued the framework in conjunction with the FSB in October 2012. In contrast to the rules for global systemically important banks, which the BCBS published in November 2011, the principles for domestic institutions do not set any requirements as regards the level of HLA. The 'too big to fail' legislation introduced in Switzerland is in line with both the rules for global systemically important banks and the principles for domestic systemically important banks.

6.7 STABILISATION FUND

Purpose of stabilisation fund

The SNB stabilisation fund was established in autumn 2008 as part of the package of measures adopted by the Federal Council, the Swiss Federal Banking Commission (now FINMA) and the SNB to strengthen the Swiss financial system. It was set up to take over illiquid assets from UBS in order to provide the big bank with liquidity and restore the confidence that had been lost as a result of the crisis.

The stabilisation fund is structured as a limited partnership for collective investment. Between December 2008 and April 2009, it took over assets from UBS totalling USD 38.7 billion. The asset transfer was financed by an SNB loan accounting for 90% of the transfer; the remaining 10% was financed by UBS. Detailed explanations of the provisions governing the operation of the fund, its organisation and its legal structure can be found in earlier editions of the SNB's *Annual Report*.

Business activity and results

The stabilisation fund's overall risk for the SNB was reduced from USD 9.0 billion at the end of 2011 to USD 5.6 billion at the end of 2012. This reduction was largely due to interest payments and repayments on stabilisation fund investments as well as to asset sales.

The 2012 business results are discussed in detail in the 'Financial information on the stabilisation fund' chapter of the financial report.

STABILISATION FUND PORTFOLIO BY CATEGORY

In percent

As at 31 December 2012

Prices on securitisation markets picked up further in 2012. The higher-risk segments of these markets benefited in particular from the search for yield in an environment of exceptionally low interest rates. In addition, there were growing signs that the US housing market might have bottomed out. This buoyed the market for private US mortgage-backed securities. In the UK, prices for real estate in non-prime locations declined slightly. Prices for commercial real estate in London, meanwhile, almost returned to their 2007 level.

Market developments

The management of the portfolio continues to be essentially based on the liquidation strategy established in 2009 by the stabilisation fund's Board of Directors (cf. the SNB's 2009 *Annual Report*). Owing to the positive financial market situation in 2012, substantial asset sales were again possible. In this regard, care was taken to ensure that not only assets with higher liquidity and credit ratings were sold, but also that assets of a lower quality were liquidated, provided they were close to their intrinsic values. Given the favourable market conditions, sales increased over the course of the year. Furthermore, risks were gradually reduced further thanks to repayments and interest payments.

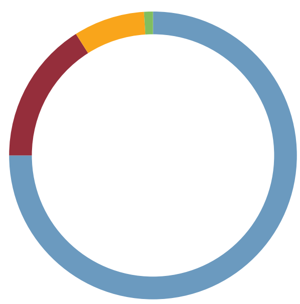
Further reduction in risk

Overall, assets worth USD 1.0 billion net were sold, of which USD 0.1 billion was accounted for by the euro area and the UK. Furthermore, the portfolio benefited from considerable interest and principal repayments amounting to USD 2.4 billion.

Significant sales and stable cash flows from investments

STABILISATION FUND PORTFOLIO BY INSTRUMENT

In percent



Securities **75**
Loans **16**
Derivatives **8**
Real estate **1**

As at 31 December 2012

SNB loan and overall risk

The table below shows the contribution made by various factors to the reduction of risk. The overall risk for the SNB is divided between the loan and contingent liabilities. The loan outstanding fell from USD 8.1 billion at the end of 2011 to USD 4.8 billion at the end of 2012. During the same period, the overall risk for the SNB was reduced by USD 3.4 billion to USD 5.6 billion.

LOAN TO STABILISATION FUND

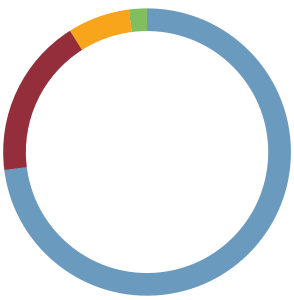
In USD billions

	Funded	Contingent liabilities	Overall risk
Total as at 31 December 2011	**8.1**	**0.9**	**9.0**
Interest on SNB loan	0.2	–	0.2
Sales [1]	–1.0	–0.3	–1.3
Repayments	–1.9	0.0	–1.9
Interest received	–0.5	–	–0.5
Other factors	–0.1	0.2	0.1
Total as at 31 December 2012	**4.8**	**0.8**	**5.6**

1 Including active liquidation of CDS (net).

STABILISATION FUND PORTFOLIO BY CURRENCY

In percent



USD **73**
GBP **18**
EUR **7**
JPY **2**

As at 31 December 2012

7
Involvement in international monetary cooperation

7.1 BACKGROUND

Mandate

Art. 5 para. 3 of the National Bank Act (NBA) stipulates that the Swiss National Bank (SNB) shall participate in international monetary cooperation. The objective of this cooperation is to promote the functioning and stability of the international monetary system and help overcome crises. As a globally integrated economy, Switzerland derives particular benefit from these aims.

Participation in different institutions

Together with the Confederation, the SNB is involved in international monetary cooperation through its participation in the International Monetary Fund (IMF), on the Financial Stability Board (FSB) and in the Organisation for Economic Co-operation and Development (OECD). Furthermore, it is a member of the Bank for International Settlements (BIS).

7.2 INTERNATIONAL MONETARY FUND

Participation in the IMF

The SNB works in collaboration with the Confederation on IMF projects and decisions. Switzerland exercises its influence through its representation on the Board of Governors, in the International Monetary and Financial Committee (IMFC) and on the Executive Board of the IMF.

European sovereign debt crisis a central point

The European financial and sovereign debt crisis was once again a focal point of the IMF's activities in 2012. Together with the European Commission and the European Central Bank, the IMF remained committed to its activities with regard to the critically affected European countries and made financial contributions to the economic adjustment programmes concerned. The aim of these programmes is to use structural adjustments to put state budgets on a more sustainable footing. The IMF also called for a strengthening of the financial system through the recapitalisation and restructuring of weak banks.

Persistently high lending

With the continuing financial and sovereign debt crisis, IMF lending to members in economic difficulties remained at a high level. Over the course of the year, the IMF Executive Board approved seven new regular (non-concessional) loan agreements totalling SDR 77.1 billion. At the end of 2012, the IMF had regular loan programmes in 21 countries amounting to a total of SDR 152.2 billion, SDR 74.4 billion of which were accounted for by insurance credit lines (mainly the Flexible Credit Line), which make it easier for countries, under certain conditions, to access IMF resources. A total of SDR 90.0 billion were outstanding on regular credit arrangements at the end of 2012.

Switzerland in the IMF

The IMF is the central institution for international monetary cooperation. It works to promote the stability of the international monetary system as well as macroeconomic and financial stability in its member countries. Its main fields of activity are surveillance, granting loans to countries faced with balance of payments difficulties, and technical assistance.

Switzerland is jointly represented by the SNB and the Federal Department of Finance (FDF) in the IMF. The Chairman of the SNB's Governing Board is a member of the IMF's highest decision-making body, the Board of Governors, which consists of a representative from each member country. The Head of the FDF is one of the 24 members of the International Monetary and Financial Committee (IMFC), the IMF's most important advisory body.

The IMF has 188 member countries. Switzerland has been a member since 1992 and is part of a voting group (constituency) whose other members are Azerbaijan, Kazakhstan, the Kyrgyz Republic, Poland, Serbia, Tajikistan and Turkmenistan. Switzerland currently occupies the post of the executive director, who holds one of the 24 seats on the Executive Board, the IMF's most important operational body. The post of executive director is held alternately by a representative of the FDF and the SNB. The FDF and the SNB determine Switzerland's policy in the IMF and support the Swiss executive director in his or her activities.

The unit of account used by the IMF is the Special Drawing Right (SDR). It is calculated on the basis of weighted exchange rates for the US dollar, euro, yen and pound sterling. At the end of 2012, one SDR was equivalent to CHF 1.40 or USD 1.54.

IMF financing

The IMF finances its lending primarily through the quotas assigned to each member country and through the New Arrangements to Borrow (NAB). However, the IMF can only draw on quotas from or credit arrangements with countries that are not beneficiaries of an IMF facility and that are not confronted with balance of payments difficulties. From total quotas amounting to SDR 238.1 billion in 2012, the IMF therefore had only SDR 198.3 billion available for lending.

Exceptional increase of IMF resources

As a result of the strong rise in demand for loans, the Board of Governors decided in 2010 to provide the IMF with more funds and to double the quotas. Since the implementation of the quota increase requires a certain amount of time, a temporary expansion of the NAB was agreed in 2011. In addition, after the crisis in the euro area had grown more acute and the stability of the international currency and financial system came under threat, an exceptional, temporary increase of IMF resources through bilateral borrowing was approved at the Spring Meeting in April 2012. At the end of 2012, commitments to these exceptional funds, some of which have yet to be approved by the national authorities, amounted to USD 461 billion.

Switzerland's participation

Switzerland has a strong interest in finding a solution for the European sovereign debt crisis. At the 2012 Spring Meeting, Switzerland pledged a USD 10 billion participation towards the exceptional increase of the IMF's resources, subject to approval by the two chambers of Swiss parliament. The SNB will then open a temporary credit line in this amount for the IMF. As the upper limit for monetary assistance is currently set at CHF 2.5 billion, in summer 2012, the Federal Council issued a dispatch concerning a credit facility of CHF 15 billion to be granted for a period of five years to continue the international monetary assistance. The new credit facility not only enables the Confederation to guarantee the SNB's credit line of USD 10 billion to the IMF, including any necessary adjustments for exchange rate fluctuations, but also allows it to create additional reserves for any future measures. The National Council dealt with the proposal as primary council in December and limited the credit facility to CHF 10 billion. The Council of States will address the proposal in the spring session of 2013.

Quota and governance reform

The decision to double the quotas to a total of SDR 476.8 billion is expected to become effective only in 2013, since the measure still requires ratification by some of the relevant national authorities of the individual member countries. It is part of a comprehensive package of quota and governance reforms and involves a major realignment of quota shares in favour of emerging economies and developing countries. The reform package also aims to reduce the number of executive directors representing advanced European economies by two. In Switzerland, participation in the IMF's quota increase requires the approval of the Federal Assembly. Parliament approved the quota and governance reform in the 2012 summer session.

Implications for Switzerland

For Switzerland, the proposed augmentation and realignment of the quota resources will mean an increase in its quota from approximately SDR 3.5 billion to SDR 5.8 billion, and a decrease in its quota share from 1.45% to 1.21%. However, owing in particular to the fact that Poland and Kazakhstan's quota shares will increase, the overall quota of the Swiss-led constituency will hardly change. In future, Switzerland will share its seat on the Executive Board with Poland as part of the IMF's aim to reduce the number of executive directors representing advanced European economies. Both countries will take it in turns to appoint an executive director every two years. This rotation will only be implemented if the governance reform actually enters into force. The earliest the rotation can be introduced is when the executive directors are elected in 2014. As the rotation will begin with Switzerland, Poland will not appoint an executive director until 2016. Switzerland will continue to represent the constituency in the IMFC.

Quota

When a country joins the IMF, it is assigned a quota based broadly on its relative position in the world economy. The quota is expressed in Special Drawing Rights, the unit of account used by the IMF. GDP, the degree of economic and financial openness, the degree to which trade and capital flows are prone to fluctuations, and reserve positions are all used in the formula to calculate the quota. The quota fulfils three important functions. Firstly, a member's quota subscription determines the maximum amount of financial resources the member is obliged to provide to the IMF. Secondly, the quota largely determines a member's voting power in IMF decisions. Thirdly, the amount of financing a member can obtain from the IMF is based on its quota. The quota is thus decisive for the financial and organisational relationship between a member country and the IMF. Quotas are reviewed at regular intervals and adjusted as necessary. At the end of 2010, it was decided to review the calculation of quotas once again so as to better reflect the increasing weight of the emerging markets in the global economy. This review is not yet concluded.

A temporary expansion of the NAB entered into effect in March 2011, increasing the number of lenders from 26 to 40 member countries and extending the maximum amount of resources available for lending from SDR 34 billion to SDR 370 billion. For the SNB, this meant an increase in its maximum lending commitment from SDR 1.54 billion to SDR 10.9 billion. Proportionally, however, its share fell from around 4.5% to 2.9%. The intention is to reduce the NAB to SDR 182 billion once the quota increase has been implemented. The SNB's maximum lending commitment will thus decrease to SDR 5.5 billion, a share of 3.0%.

Temporary expansion of NAB

GAB and NAB

The New Arrangements to Borrow (NAB) form a financial safety net for the IMF. Following the most recent increase, the IMF can currently be provided with up to SDR 370 billion in addition to its regular resources by means of the NAB. The NAB are activated for a specified period (six months at most) and a specified amount. The amount activated is based on an estimate by the IMF of the expected contingent liabilities. There are now 40 member countries participating in the NAB. The SNB is the institution representing Switzerland.

In an exceptional crisis and in the event of a shortage of funds, the General Arrangements to Borrow (GAB) permit the IMF to borrow funds in the amount of SDR 17 billion from the Group of Ten (G10) countries according to a distribution key agreed upon. The GAB can only be activated if agreement has not been reached under the NAB. The SNB is also the institution representing Switzerland in the GAB.

In November 2012, the IMF decided to extend the GAB by a further five years. In Switzerland, participation in the extension of the GAB is subject to approval by the Federal Assembly. The Federal Council proposed the relevant dispatch to parliament on 30 November 2012.

Renewal of GAB

Concessional lending facilities

The IMF supports concessional, i.e. subsidised, lending facilities in low-income countries. Pledges for these loans amounted to a total of SDR 3.1 billion at the end of 2012. To finance its concessional lending facilities, the IMF can avail itself of the Poverty Reduction and Growth Trust (PRGT). In June 2009, the IMF Executive Board decided to augment the PRGT's loan resources by SDR 10.8 billion. By the end of 2012, 14 countries had committed to provide loans to the PRGT totalling SDR 9.8 billion for this purpose, SDR 500 million of which was pledged by Switzerland. The loan to the Trust is granted by the SNB and guaranteed by the Confederation. Switzerland is also involved in financing the interest subsidy for these loans. This participation is guaranteed by the Confederation.

Switzerland's reserve position

Both Switzerland's IMF quota and the NAB are funded by the SNB. The portion of the quota remitted to the IMF and the NAB funds drawn on together equal Switzerland's reserve position in the IMF. This reserve position represents a liquid asset of the SNB vis-à-vis the IMF and thus forms part of the currency reserves. At the end of 2011, Switzerland's reserve position amounted to SDR 1,998.4 million, compared with SDR 2,176.6 million a year earlier.

SNB'S FINANCIAL COMMITMENT TO THE IMF

In CHF millions

		End-2012
	Maximum	Drawn down
Quota	4,853	998
GAB and NAB	15,301	1,806
Concessional lending facilities [1] (PRGT)	980	279
SDR [2]	2,307	–364

1 With federal guarantee.
2 The SDR is not only a unit of account, but also a means of international payment. As part of the two-way arrangement with the IMF, the SNB has committed itself to purchase (+) or sell (–) SDRs against foreign currencies (USD, EUR) up to an agreed maximum.

Within the context of the Article IV consultations, the IMF regularly reviews the economic policy of its member countries and issues recommendations. On 2 May 2012, the IMF Executive Board concluded the annual Article IV consultation with Switzerland. The IMF commented that the Swiss economy is fundamentally strong, but that some challenges still lie ahead. The biggest risk for the Swiss economy, according to the IMF, is a worsening of the euro crisis. The IMF considers that the introduction of the minimum exchange rate for the euro against the Swiss franc was an appropriate policy response to the sharp economic contraction at the time and the threat of deflation caused by the franc's appreciation. It recommended the SNB to return to a free floating exchange rate regime as soon as economic conditions normalise. Given the environment of persistently low interest rates, the IMF sees a growing risk of a real estate bubble in parts of the real estate market. Against this backdrop, the IMF considers it advisable to immediately introduce the countercyclical capital buffer and the additional capital requirements for the mortgage lending business. Moreover, the big banks should raise high-quality capital as soon as possible.

Article IV consultation

In May 2012, the SNB and the IMF jointly hosted a conference on the reform of the international monetary system for the third time. The event brought together high-level central bank representatives, senior policymakers, as well as leading academics and commentators.

Conference on international monetary system

To celebrate its 20th anniversary, a meeting of the Swiss constituency in the IMF and World Bank took place in Montreux in September 2012. The event brought together high-level representatives from central banks and governments of the member countries as well as management from the IMF and World Bank. The discussions focused primarily on the repercussions of the crisis on the member countries. Participants underlined the value and mutual benefit of the 20 years of cooperation, which made it possible for Switzerland, in particular, to gain a seat on the Executive Board of the IMF and the World Bank.

Constituency celebrates 20-year anniversary

7.3 BANK FOR INTERNATIONAL SETTLEMENTS

BIS as bank and forum for central banks

The Bank for International Settlements (BIS) is an international organisation that has its head office in Basel. It fosters international monetary and financial cooperation and serves as bank and forum for central banks. The SNB has occupied one of the seats (currently 19) on the BIS Board of Directors since its foundation.

The governors of member central banks convene for several meetings every two months to discuss developments in the global economy and the international financial system, and also to administer and oversee the work of the various committees. The SNB participates in four standing committees of the BIS: the Basel Committee on Banking Supervision, the Committee on Payment and Settlement Systems, the Committee on the Global Financial System and the Markets Committee.

Basel Committee on Banking Supervision

The Basel Committee on Banking Supervision serves as a platform for regular cooperation in matters of banking supervision. Its activities are described in greater detail in chapter 6.6.

Committee on Payment and Settlement Systems

The Committee on Payment and Settlement Systems (CPSS) is concerned with developments in national and international financial market infrastructures. In 2012, the CPSS – in collaboration with the International Organization of Securities Commissions (IOSCO) – published new standards for payment systems, central securities depositories, securities settlement systems, central counterparties and trade repositories. Other focal points of CPSS activities included the restructuring or wind-down of financial market infrastructures and continuing work towards implementing reform in the over-the-counter (OTC) derivatives market. The CPSS also published a report on innovations in retail payments.

Committee on the Global Financial System

The Committee on the Global Financial System (CGFS) monitors developments in the international financial markets and analyses their impact on financial stability. In 2012, the Committee addressed questions of global liquidity, in particular, and the use of ratings by central banks. The CGFS published two reports. The first deals with the use of macroprudential instruments, which are not targeted at banks, but at the impact of their interconnection in the system. The second report describes improving the BIS international banking statistics.

Markets Committee

The Markets Committee serves as a platform for central bank officials responsible for monetary policy operations. It examines current developments in money, currency, capital and commodity markets, as well as the functioning of these markets. In 2012, the impact of the European debt crisis and the increased use of unconventional monetary policy measures on the financial markets were discussed in particular. Consideration was also given to the importance of reference rates on international money markets (particularly Libor).

7.4 OECD

Participation in the OECD

Switzerland is a founding member of the Organisation for Economic Co-operation and Development (OECD). On the organisation's inter-governmental committees, it works to promote the development of relations among the 34 member countries with regard to economic, social and development policies.

Together with the federal government, the SNB represents Switzerland on the Economic Policy Committee (EPC), the Committee on Financial Markets (CFM) and the Statistics Committee (CSTAT). On a political and academic level, the EPC and its working groups deal with current developments in the global economy as well as with structural policy. The CFM analyses ongoing developments in the international financial markets and examines regulatory issues. The CSTAT drafts standards for the national accounts in association with other international organisations.

Every two years, the OECD performs a detailed analysis of the economy of every member country. The Swiss economy will once again be subject to an in-depth evaluation, which, as always, will be done in close cooperation with the Confederation and the SNB. The OECD also publishes its *Economic Outlook* twice a year, a report which always includes a forecast summary of the growth outlook and economic policy for Switzerland. In its November report, the OECD recommended that, in view of weak underlying price pressures, interest rates should be kept close to the zero bound. It recognised that the appreciation of the Swiss franc continues to pose difficulties for companies. It was critical of the rise in real estate prices and the growth in mortgage loans, and suggested that macroprudential measures should be envisaged, especially for the cantonal banks, which are highly exposed to the housing sector. In the light of the continuing global financial market risks, the loss-absorbing capital of the two big banks should be increased.

7.5 TECHNICAL ASSISTANCE

Principles

The SNB provides technical assistance upon request to the central banks of developing countries and emerging economies. Technical assistance includes the transfer of knowledge specific to central banks and contributes to maintaining the good relations between central banks worldwide. The SNB primarily provides assistance to the central banks from the group of countries with which it forms a constituency in the IMF and the World Bank (cf. chapter 7.2).

Main focus of technical assistance

As in recent years, the SNB again provided a large proportion of its technical assistance during 2012 to the National Bank of the Kyrgyz Republic (NBKR). It supported the NBKR in introducing a new trading platform and provided continued assistance to existing projects in the areas of monetary policy, risk management and banking operations. In-depth discussions took place with the National Bank of Kazakhstan, covering the subjects of banking operations, asset management, information technology and statistics, and internal auditing. The Central Bank of the Republic of Azerbaijan again received advice on the subject of monetary policy and also on banking operations. A sporadic exchange concerning asset management was held with the central banks of Serbia and Tajikistan. The SNB also continued to foster its relationship with the Central Bank of Turkmenistan.

Outside the constituency, the SNB provided support to the central banks of Armenia, Mozambique and Vietnam.

International events

In cooperation with the National Bank of Poland (NBP), the SNB held a seminar in May for central bankers from Eastern Europe, the Caucasus and Central Asia. The seminar – held for the ninth time – took place in the NBP's training centre close to Warsaw and dealt with the importance of global capital flows to monetary policy and financial stability.

Study Center Gerzensee

The Study Center Gerzensee, an SNB foundation for the training of central bankers, bankers and business specialists from Switzerland and abroad, organised seven courses on the subjects of monetary policy and financial markets for employees of foreign central banks in 2012. The courses were attended by a total of 170 participants from 87 countries (2011: 149 participants from 81 countries).

8
Banking services for the Confederation

Mandate

The Swiss National Bank (SNB) provides banking services to the Swiss Confederation (art. 5 para. 4 and art. 11 of the National Bank Act).

Remuneration for banking services

The SNB provides these banking services to the Swiss Confederation in return for adequate compensation. However, they are provided free of charge if they facilitate the implementation of monetary policy. Services subject to remuneration comprise: payment transactions, liquidity management, the custody of securities and the issue of money market debt register claims (MMDRCs) and Confederation bonds. Details of the services to be provided and the remuneration are laid down in an agreement concluded between the Confederation and the SNB.

Issuing activities

In 2012, the National Bank issued both MMDRCs and Confederation bonds on behalf of and for the account of the Confederation. MMDRCs amounting to CHF 191.4 billion were subscribed (2011: CHF 108.8 billion), of which CHF 44.7 billion was allocated (2011: CHF 33.4 billion). The corresponding figures for Confederation bonds were CHF 11.6 billion and CHF 6.8 billion respectively. As on previous occasions, the issues were effected by auction via an electronic trading platform.

Negative MMDRC yields continue

In 2012, money market rates on the Swiss franc money market remained at exceptionally low levels, and, in some cases, at levels well into negative territory. On 26 June, the issue yield on three-month MMDRCs dropped to –0.85%, thereby reaching a new low point. In the second half of the year, MMDRC yields increased somewhat. Taken over the whole year, the yields ranged from 0.00% to –0.85%.

Payments

In mid-May, the Confederation changed over to a standardised transmission of payment data via the SWIFT global network, as part of its payments management project. The SNB carried out roughly 70,000 payments in Swiss francs and approximately 19,000 payments in foreign currencies on behalf of the Confederation.

9 Statistics

9.1 BACKGROUND

Purpose of activities in field of statistics

The Swiss National Bank (SNB) collects the statistical data it requires to fulfil its statutory mandate on the basis of art. 14 of the National Bank Act (NBA). It collects data for the conduct of monetary policy and the oversight of payment and securities settlement systems, for safeguarding the stability of the financial system and preparing both the balance of payments and the statistics on the international investment position. Statistical data compiled for purposes relating to international monetary cooperation are transmitted to international organisations. The National Bank Ordinance (NBO) lays down the details of the SNB's activities in the field of statistics.

Institutions required to provide data

Banks, stock exchanges, securities dealers and investment funds are required to provide the SNB with figures on their activities (art. 15 NBA). The SNB may also collect statistical data on the business activities of other private individuals or legal entities where this is necessary to analyse trends in the financial markets, obtain an overview of payment transactions or prepare the balance of payments or the statistics on Switzerland's international investment position. This applies in particular to insurance companies, occupational pension institutions, investment and holding companies, and operators of payment and securities settlement systems as well as Swiss Post.

Survey activity kept to minimum

The SNB limits the number and type of surveys to what is strictly necessary. It seeks to minimise the demands placed on those required to provide information.

Confidentiality and exchange of data

The SNB is required to ensure the confidentiality of the data it collects and may only publish them in aggregated form. However, the data may be supplied to the relevant Swiss financial market supervisory authorities.

9.2 PRODUCTS

Surveys and statistics

The SNB conducts statistical surveys in the areas of banking statistics, collective investment statistics, the balance of payment and payment transactions, as well as in connection with PostFinance. An overview is contained in the appendix to the NBO and on the SNB website. The SNB publishes the results of its surveys in the form of statistics. It also maintains a data bank with 5.7 million time series in the fields of banking, financial markets and economics.

A large proportion of the statistics are published in the *Monthly Statistical Bulletin*, the *Monthly Bulletin of Banking Statistics*, and in *Banks in Switzerland*, which appears annually. The SNB also publishes data in its publications on the balance of payments, the international investment position, direct investment, and on the financial accounts and household wealth in Switzerland. The SNB's statistical publications appear in German, French and English, and can also be accessed on the SNB website. In some cases, more extensive versions are provided online. Data are also available online as Excel or text files, generally with longer time series than in the printed publications.

Statistical publications

The SNB publishes monthly data on its website in line with the International Monetary Fund's Special Data Dissemination Standard (SDDS). The data include information on the monetary aggregates and the reserve assets. Key balance sheet positions are also posted on the website on a monthly basis.

Special data dissemination standard

9.3 PROJECTS

In 2012, a revised version of the survey on cross-border trade in services (serviceBOP) was introduced. Since the first quarter, around 1,000 companies have been supplying detailed data each quarter on their services exports and imports. In addition, work continued on the revision of the surveys in connection with financial flows (investmentBOP). Both surveys aim, inter alia, to meet the requirements of the bilateral statistical agreement between Switzerland and the EU.

Balance of payments

The survey on cross-border trade in services is the SNB's first statistical survey to be carried out via an internet platform (eSurvey). Other surveys are to follow suit in future. Working with the platform simplifies both the communication with the companies required to report data and the processing of the supplied data at the SNB.

eSurvey platform

9.4 COLLABORATION

Reporting institutions

With regard to organisational and procedural issues, and when new surveys are introduced or existing ones modified, the reporting institutions – together with their associations – are given the opportunity to comment.

Group of experts

The SNB is advised on the content of its banking surveys by the banking statistics committee. This committee is made up of representatives of the Swiss commercial banks, the Swiss Bankers Association and the Swiss Financial Market Supervisory Authority (FINMA). A group of experts under the direction of the SNB participates in the compilation of the balance of payments. It comprises representatives from manufacturing, banking, insurance, various federal agencies and the KOF Swiss Economic Institute at ETH Zurich. In 2012, the group of experts gave special attention to the investmentBOP project.

Public institutions

In compiling statistical data, the SNB collaborates with the relevant federal government bodies, particularly the Swiss Federal Statistical Office (SFSO) and FINMA, as well as with the authorities of other countries and international organisations.

Swiss Federal Statistical Office

The SNB has a close working relationship with the SFSO. Reciprocal data access is governed by a data exchange agreement; this agreement also covers the collaboration between the two authorities in drawing up the Swiss financial accounts. Moreover, the SNB belongs to a number of bodies that work with Swiss federal statistics. These include the federal statistics commission (*Bundesstatistikkommission/Commission de la statistique fédérale*) and the group of experts for economic statistics (*Expertengruppe für Wirtschaftsstatistik/Groupe d'experts de statistique économique*).

Federal Office for Housing

The SNB collects quarterly data on mortgage rates from about 80 banks on behalf of the Federal Office for Housing (FOH). Based on these data, the FOH calculates the reference interest rate for tenancies. The sole responsibility for the contents of this survey lies with the FOH, which also publishes the reference interest rate.

Under the agreement with FINMA on the reciprocal exchange of data in the financial sector, the SNB collects information, including data on the capital base, liquidity and interest rate risk of banks and securities dealers. The year 2012 was marked by preparations for the start of Basel III and its modified capital adequacy requirements for banks.

FINMA

The SNB also surveys Liechtenstein-based companies when preparing its balance of payments figures and its statistics on Switzerland's international investment position. It works with the relevant authorities in Liechtenstein (the Office of Economic Affairs and the financial market supervision authority).

Principality of Liechtenstein

SNB collaboration with the EU is based on the bilateral statistical agreement that came into effect in 2007. It covers the financial accounts, parts of the banking statistics as well as, since 2010, the balance of payments. The SNB plays a role in various bodies of the EU statistical office (Eurostat).

EU

In the area of statistics, the National Bank works closely with the Bank for International Settlements (BIS), the Organisation for Economic Co-operation and Development (OECD) and the International Monetary Fund (IMF). This collaboration is aimed at harmonising statistical survey methods and analyses. In 2012, the SNB participated in several international working groups concerned with filling data gaps in financial market statistics. Improving the statistical basis will help identify undesirable trends (such as those that developed prior to the financial crisis in 2008) at an early stage.

Other international organisations