Preface

Ladies and Gentlemen

The Swiss National Bank (SNB) conducts the country's monetary policy as an independent central bank, on the basis of the Federal Constitution and the National Bank Act (NBA). The first part of this *107th Annual Report* comprises the SNB's accountability report to the Federal Assembly, and provides information about how the SNB has fulfilled its mandate – in particular its conduct of monetary policy and contribution to the stability of the financial system.

The second part of the *Annual Report* comprises the financial report, which is submitted for approval, first to the Federal Council and then to the General Meeting of Shareholders. The financial report provides information on organisational and operational developments as well as the financial result of the SNB. The financial report includes the business report and the annual financial statements of the SNB, which contain the balance sheet, income statement and profit distribution, changes in equity, cash flow statement and notes.

The year 2014 presented a mixed picture. The global economy continued to recover, although growth was generally weak and unevenly distributed. Whereas the US economy increasingly gathered momentum, growth in Japan and Europe was sluggish. Geopolitical tensions related to the conflict between Russia and Ukraine, as well as the slow progress in implementing reforms, inhibited investment activity in Europe. While China continued to be a mainstay of the global economy, many other emerging economies registered only modest growth. Inflation rates around the world declined as a result of the sharp drop in oil prices.

The Swiss economy performed well in a difficult environment. At 2.0%, the expansion in real GDP in 2014 was slightly greater than in the previous year, and unemployment decreased slightly. The mortgage and real estate markets remained a focus of attention for the SNB. Acting on the SNB's proposal, the Federal Council increased the sectoral countercyclical capital buffer in January 2014. Together with the other measures taken to dampen momentum on the mortgage and real estate markets, the increase in the capital buffer helped to stabilise lending growth and ensured that imbalances on these markets hardly increased thereafter.

Monetary policy in 2014 operated in an environment in which inflation was close to zero and interest rates were very low. Against this background, the minimum exchange rate of CHF 1.20 per euro continued to be the SNB's key instrument for ensuring appropriate monetary conditions in Switzerland. Over the course of the year, there were growing signs of a divergence between the monetary policies in the US and the euro area. While the minimum exchange rate did not come under pressure initially, this changed in the final weeks of the year. On 18 December, the SNB announced the introduction of negative interest on sight deposit account balances held at the SNB by banks and other financial market participants. The aim was to increase the interest rate differential to other currencies, thereby rendering Swiss franc investments less attractive and supporting the enforcement of the minimum exchange rate. In addition, the SNB expanded the target range for the three-month Libor into negative territory.

After a brief period of calm, pressure on the minimum exchange rate increased very significantly during the first half of January 2015. Overall, the euro weakened once again, and it became evident that the minimum exchange rate could only be enforced through ongoing intervention in the foreign exchange market. This would have resulted in an uncontrollable expansion of the balance sheet, to a level that might even have been several times Swiss GDP. At an extraordinary monetary policy meeting, the SNB concluded that a minimum exchange rate of CHF 1.20 per euro had become unsustainable, and was therefore no longer justified from a monetary policy point of view. On 15 January 2015, the SNB therefore decided to discontinue the EUR / CHF minimum exchange rate. At the same time, it lowered the interest rate on sight deposit account balances to –0.75% as of 22 January 2015, and moved the target range for the three-month Libor downwards by 0.5 percentage points to between –1.25% and –0.25%.

Had it maintained the minimum exchange rate, the exceptional increase in foreign currency purchases would have meant that the SNB risked losing control of its balance sheet and, as a result, of monetary conditions, in the long term. Against the backdrop of changing international conditions, enforcement of the minimum exchange rate was no longer justifiable. Had the SNB maintained the EUR / CHF minimum exchange rate despite this realisation, it would have put the long-term fulfilment of its mandate at risk.

Once the SNB had reached this conclusion, the timing of the discontinuation had to be addressed. Swift action was necessary. Waiting and continuing to intervene in the foreign exchange market would have increased pressure on the minimum exchange rate because of the speculation that would have ensued. In the event of a later discontinuation of the minimum exchange rate following substantial further interventions, the turmoil on the financial markets would not have been any less severe and the losses on the SNB's balance sheet would have been exorbitant. The costs of maintaining the minimum exchange rate of CHF 1.20 per euro would have been out of all proportion to the benefits for the economy.

In 2014, the annual financial statements of the SNB closed with a profit of CHF 38.3 billion, following a loss of CHF 9.1 billion in the previous year. The positive annual result was mainly attributable to profits of CHF 34.5 billion on foreign currency positions and CHF 4.1 billion on gold holdings.

The allocation to the provisions for currency reserves amounts to CHF 2.0 billion. The balancing of the negative distribution reserve absorbs CHF 6.8 billion of the profit. With the remaining profit, a dividend of CHF 1.5 million shall be paid to the shareholders, and the ordinary distribution of profits of CHF 1 billion shall be made to the Confederation and the cantons. Thus, the distribution reserve after appropriation of profit would amount to CHF 28.5 billion. According to the profit distribution agreement between the Federal Department of Finance (FDF) and the SNB, the distribution to the Confederation and the cantons is increased if the distribution reserve exceeds CHF 10 billion after profit appropriation. The SNB and the FDF agreed to a supplementary distribution of CHF 1 billion, so that the total distribution to the Confederation and the cantons for 2014 will amount to CHF 2 billion.

We wish to thank our employees for their hard work and valuable support over the past year.

Berne and Zurich, 27 February 2015

JEAN STUDER
President of the Bank Council

THOMAS J. JORDAN
Chairman of the Governing Board