

Speech

SCHWEIZERISCHE NATIONALBANK
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SWISS NATIONAL BANK 

Embargo:
26 April 2013, 10 am

The dual challenges of 2012

Address by Jean Studer,
President of the Bank Council,
to the General Meeting of Shareholders
of the Swiss National Bank, 26 April 2013

Swiss National Bank
26 April 2013
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Dear Shareholders
Ladies and Gentlemen
Dear Guests

Introduction

I am very pleased to welcome you to the General Meeting of Shareholders of the Swiss National Bank. This is the first time that I am attending as President of the SNB Bank Council. My first presidential year has been a busy one, and I have found it both rewarding and satisfying. In my new post, I have learned even more about this institution, the variety of fields in which it is active, its operational structures and processes, and last but not least, the people behind the work. The fact that I have been a member of the Bank Council since 2007, and am therefore already familiar with our institution, has stood me in good stead.

2012 – two major challenges to face

The SNB was presented with two major challenges last year. The first was in the area of monetary policy. Events in the international arena caused such intense pressure on the Swiss franc to appreciate that huge purchases of foreign currency were necessary in order to enforce the minimum exchange rate of CHF 1.20 against the euro. The Chairman of the Governing Board, Thomas Jordan, will look in more detail at this challenge, and thus too at current monetary policy and economic developments, in his own speech.

The second challenge that arose in 2012 was to the institution itself. I am referring to the resignation of the previous Governing Board Chairman in January last year, which took place in unusual circumstances. We reacted swiftly and resolutely to this difficult and unprecedented situation: The necessary personnel-related decisions were taken immediately, the staff regulations – especially those relating to private financial transactions – were tightened, and the compliance function was strengthened. This ensured that the SNB was able to focus on fulfilling its mandate without distraction.

Thus, as regards both the monetary policy challenge and the institutional challenge, we can say: In 2012, the SNB retained full freedom of action at all times, despite a difficult environment, both externally and internally. It continued to carry out its mandate in the interests of the country as a whole. Today, the SNB is stronger, both institutionally and in terms of its personnel.

Strengthening internal regulations and the compliance function

Over the past year, the SNB devoted particular attention both to its internal regulations and to compliance with them. To give you a better idea of what exactly the SNB did in this area, I will just cite a few examples. In response to the events at the beginning of last year, the National Bank issued new regulations on private financial investments and financial transactions by members of SNB management, which considerably restricted the assets that they could hold. Furthermore, the regulations on the employment relationship of Governing Board members and their deputies were revised, with a special focus on restricting their activities after they leave the SNB. In addition, the SNB reviewed a number of regulations that relate to all staff. For example, the Code of Conduct for staff and the directive on staff members' private financial investments and financial transactions were tightened and disclosure requirements were expanded.

Finally, new directives aimed at improving the internal control system entered into force. In this way, the National Bank strengthened its compliance structure and created an independent Compliance unit with a direct reporting line to the Bank Council. The new unit also acts as a contact point to which staff can report irregularities and infringements of regulations. The role of Compliance is to identify, prevent or reduce the legal and reputational risks to the SNB which may arise out of the non-observance of statutory or internal regulations and standards. In addition, the Bank Council is itself now subject to an explicit Code of Conduct for the first time. All these measures demonstrate the importance of a comprehensive and modern set of regulations for the internal workings of the institution. In particular, the measures took account of the strong expansion of the SNB's scope of activities in recent years. The guidelines and regulations governing the conduct of management and staff are available on our website. The SNB is thereby ensuring transparency and reflecting in a contemporary way the great importance we have always attached to orderly operating procedures.

All these improvements to internal regulations ultimately have one aim: To provide an environment in which the SNB can concentrate unhindered on fulfilling its statutory mandate, which is to conduct monetary policy in the interests of the country as a whole. At the same time, the SNB is aware that no controls can ever be completely watertight. As such, the regulations lay the foundations on which a culture of trust can develop and thrive. For

although it is important to observe the letter of regulation, the attitude and integrity of staff are even more important.

Adapting operating resources in response to challenges

The SNB must have appropriate resources – qualified staff, suitable premises and other operating resources. This applies particularly with regard to the enforcement of the minimum exchange rate, the management of investments and risks – which have grown in tandem with the expansion of the SNB's balance sheet – and new tasks in the area of financial stability, such as combating imbalances on the real estate market. The Bank Council has therefore approved the requisite adjustment in headcount and other resources. However, it continues to oversee the disciplined, responsible and reasonable use of operating resources. The public relies on the SNB to continue working in the prudent manner typical of Switzerland.

Here I would like to mention two operational highlights of 2012. First, the purchase of the Metropol building, just around the corner from the Zurich head office, which has enabled us to optimise our real estate portfolio. Second, the decision to open a branch office in Singapore, which will allow us to more efficiently manage the SNB's Asian investments by having a local presence. Moreover, it facilitates round-the-clock foreign exchange market operations in connection with the minimum exchange rate.

Balance sheet and income statement against the background of the minimum exchange rate

The sheer size of the balance sheet and income statement makes items such as fixed assets and personnel expenses appear almost negligible by comparison. Monetary policy in 2012 was the main factor behind the growth in the SNB's balance sheet and income statement. Year-on-year, the balance sheet total increased from CHF 346 billion to nearly CHF 500 billion, thus continuing and reinforcing the trend of recent years. By way of comparison, it is worth remembering that, at the end of 2006, the balance sheet total amounted to CHF 112 billion. With the rise in foreign currency assets has come a significant rise in financial risk. The SNB had to assume this risk for monetary policy reasons, in order to fulfil its mandate. Even after the investments have been diversified across various currencies and instruments, the level of risk remains very high. Dealing with this risk places great emphasis, not only on risk management in connection with asset management activities, but also on the build-up of

equity capital and provisions for currency reserves. The Bank Council therefore devoted considerable attention to such topics in the past year.

A key focus in this regard was the appropriate regulation of the profit distribution to the public sector. The 2011 financial year was the first in which the new agreement between the Federal Department of Finance and the SNB on the profit distribution was applied. Under the new agreement, instead of an annual CHF 2.5 billion, the Confederation and the cantons now receive 'only' CHF 1 billion. In 2012, our stock of income-generating foreign currency investments once again grew substantially in connection with the enforcement of the minimum exchange rate. Nevertheless, the Confederation and the cantons are still going to receive 'only' CHF 1 billion. Is this not a contradiction? As a former cantonal government member and finance director, who always eagerly received the annual transfer from the SNB, this question is naturally close to my heart. But the answer is still 'no'. The stock of investments may have grown, but we are currently in an environment of low interest rates, and interest income is likely to be lower than in the past. Moreover – and this is the key point – risk has risen markedly. Increased risk requires increased provisions, and results in correspondingly modest profit distributions. The strengthening of provisions, which the Bank Council has pursued for a number of years, and the current profit distribution agreement are a reflection of this.

It is worth pointing out here that profit distributions are merely a by-product of monetary policy. A forward-looking policy brings benefits not just for the general population and the economy, but also for the Confederation and the cantons – and it does so in a number of different ways.

If price stability is ensured, this makes it easier to, for example, service debts, because interest rates trend lower and fluctuate less. Monetary policy can also contribute to a smoother economic cycle, more secure employment and good utilisation of industrial capacity. The benefit of good monetary policy for the public sector manifests itself in affordable debt service, attractive tax revenue and manageable social welfare expenditure. These factors carry considerably more weight with the Confederation and the cantons than the difference between CHF 2.5 billion and CHF 1 billion. In addition, it should be noted that the distributable profit corresponds to income minus allocations to provisions. Undistributed profits are allocated to the distribution reserve. On the one hand, this increases the SNB's capacity to absorb

potential losses. On the other, if these profits prove to be sustained and no losses are incurred, the potential for higher future distributions grows. So, if we are over-cautious today, we can pay out more in the future, and vice versa. A healthy balance sheet is a prerequisite for the SNB having sufficient room for manoeuvre over the long term, to enable it to fulfil its mandate. Sound public finances are another important criterion. Conversely, as a glance abroad shows, ailing public finances carry the risk that monetary policy will become overstretched. The SNB is therefore grateful to the Confederation and the cantons for the budgetary restraint they have shown.

Concluding remarks

My remarks have no doubt reminded you how unique, in many respects, the SNB is as an institution as it goes about its special mission. And, indeed, the general public certainly seem to acknowledge this. The SNB enjoys a high degree of public confidence, and its words and deeds are highly credible; this is of crucial importance for monetary policy. This ‘trust bonus’ is based primarily on the fact that the SNB can be relied upon to always make its decisions completely independently, and that the monetary policy which it pursues in the interests of the country as a whole is an indispensable public service. The SNB’s independence is firmly anchored in our constitutional democracy. Even during these last few trying years, its independence and freedom of action have never been called into question, and monetary policy’s focus on stability has never been doubted. This must remain so in the future if the SNB is to continue conducting a sound monetary policy.

Over the past few years, central banks worldwide have taken on new tasks as part of efforts to manage the crisis. They are operating in a changed environment, and are more visible and active than before. So it is not surprising that questions are increasingly being posed about the responsibilities and accountability of central banks. For a central bank, this debate provides an opportunity to explain its motivation and actions even more clearly to the general public. If it can seize this opportunity, confidence in the institution and its credibility will both improve – which in turn will further reinforce the independence of monetary policy.

Against this background, it is especially important for the SNB to continue focusing its deliberations and efforts entirely on its democratically legitimised and publicly conferred mandate. It must act in a forward-looking way, with respect for the great task it has been given and for the powers and resources with which it has been endowed, while exercising

discretion and caution. The new Governing Board appointed last year has carried out its special responsibilities fully and competently at all times. I look forward to a continued close and collegial collaboration between the Bank Council and the Governing Board.

Finally, I would like to extend special thanks to you, our shareholders, for your confidence in us. Thanks are also due to my Bank Council colleagues for their huge efforts in the service of our institution. I would also like to thank the staff of the SNB for their commitment to the interests of our country.

Thank you for your attention.