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Introductory remarks by Bruno Gehrig, Member of the Governing Board of the Swiss National Bank

Steering concept

The change of concept will also bear on the operations area. In implementing monetary policy, we will henceforth target the interest rate level on the money market rather than the amount of liquidity. Our steering concept consists of three elements:

- The first element is a clearly defined reference interest rate: we will use the 3-month LIBOR (London Interbank Offered Rate), the economically most important money market rate for Swiss franc investments. We will publish it daily in the major financial data services and on our website.
- The second element of monetary control is the target range for the 3-month LIBOR, which establishes the guidelines for practical monetary policy and - supplementing the long-term inflation forecast - serves the market as an orientation framework. The target range has a spread of one percentage point (corresponding to 100 basis points). We publish the location of the target range and check it on an ongoing basis.
- Thirdly, we will also announce in what area within the target range we expect the 3-month LIBOR to be. It is not our intention to exercise precise control over the LIBOR. We will continue to tolerate certain market-induced fluctuations. We will, however, take action should any development of the LIBOR have an undesirable monetary policy effect.

The LIBOR target range will lie between 1.25% and 2.25% in the near term. We plan to allow a moderate increase in the LIBOR towards the middle of the target range. This intention refers to the development after the transition to the new year. Current interest rates exhibiting a strong upward distortion due to the end-of-month effect will settle in at a normal level after the turn of the year.

We are convinced that this steering concept promotes transparency and thus the efficiency of monetary policy without compromising the indispensable room for manoeuvre.

Why the LIBOR?

The LIBOR, the interest rate for three-month investments in the interbank market, is the most frequently used Swiss franc money market rate. It is fixed and published daily in the London market according to a transparent mechanism. The LIBOR reflects money market conditions and is a central parameter for the refinancing of first-rate banks and companies. It is more important economically than the short-term repo rates which we use for daily monetary transactions. There are two additional qualities which favour the LIBOR as a monetary policy reference interest rate. Firstly, it does not react too violently to short-term imbalances on the money market, is thus less prone to incidental fluctuations and as such is well-suited as a monetary bellwether. Secondly, it reacts more quickly than the repo rate to economically relevant interest rate effects influencing our money market from abroad or from the capital market, thus enhancing its role as an indicator. Experience has shown that the LIBOR is more closely interconnected to the entire interest rate and economic structure and fluctuates to a much lesser degree than, for example, the call money rate (graph in annex).

When interpreting the LIBOR it must be borne in mind that it cannot be compared directly with the repo rates. It tends to be higher for two reasons. One aspect is that it applies to the longer maturity of three months. The second is that it refers to unsecured interbank loans and therefore includes a risk premium. Repo rates, by contrast, are zero-risk interest rates with underlying loans secured by securities. It is impossible to determine the risk premium exactly since no instruments with similar liquidity are available for the zero-risk money market rate (yet). Our experience with repo transactions this year has shown that depending on maturity and market conditions, repo rates can be up to one half percentage point lower than the three-month LIBOR.

Steering technique and signalling effect

We will take a flexible approach in steering the LIBOR and not react to short-term swings. As a general rule, we will chart the course of the LIBOR indirectly, i.e. via short-term repo transactions. Any undesirable upturns in interest rates can be corrected by injecting more liquidity or, conversely, by draining liquidity, we can induce an upward movement of interest rates.

While we communicate our long-term monetary stance with the inflation forecast, the target range serves as an indicator for our intentions in the shorter term. As a rule, we will assess this indicator every quarter and justify any changes. Moreover, we will make a statement as to the position of the reference rate within the target range. Short-term repo rates, by contrast, do not serve as a monetary indicator. Contrary to the practice of the ECB, we will in principle act daily in the market and take a flexible approach in setting the repo rates. More often than not, they vary not because of the monetary course but due to liquidity distribution aspects within the system or due to short-term distortions.

In supplying the market with liquidity, we rely on the proven monetary policy instruments, centring on repo transactions with maturities ranging from one day to several weeks. At currently approximately 20 billion Swiss francs, they correspond to roughly half the monetary base. In addition, we can place federal government funds with the banks or conclude foreign exchange swaps should the need arise. In case of unforeseen liquidity bottlenecks, advances against securities (lombard loans) are still available. Furthermore, since October, banks have been able to use intraday liquidity on a repo basis to speed up payment transactions. This new facility serves to facilitate the settlement of payments within the Swiss Interbank Clearing system (SIC). Monetary policy is not affected, however.

Discount rate no longer used

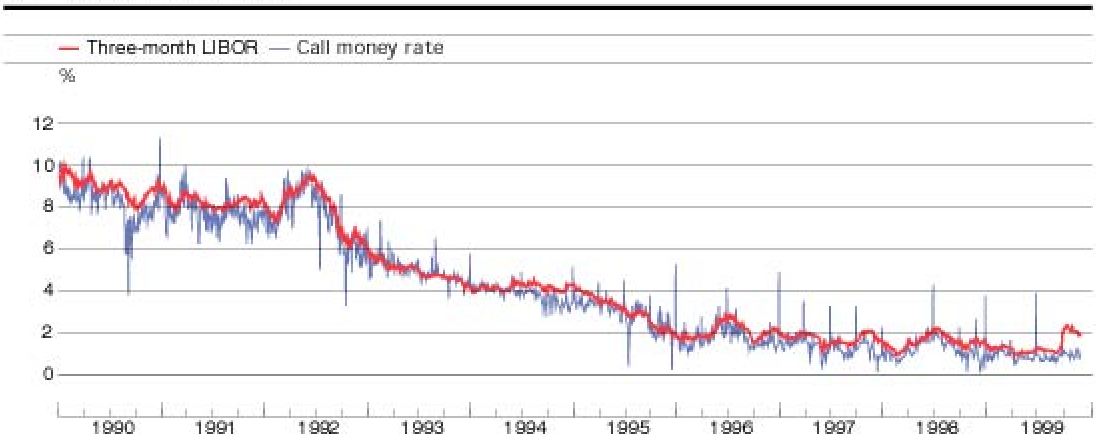
Discount business - a classical instrument of the National Bank - has become increasingly insignificant over the last decades. The National Bank has not concluded a single discount transaction since 1993. The discount rate still had a certain significance as a monetary indicator, however. In the new steering concept the target range for the LIBOR will assume this role, rendering the discount rate obsolete also in this respect. Consequently, starting in January 2000, we will no longer fix and publish a discount rate. There are no provisions in the National Bank Law which would prohibit such a step. The rules governing the lombard rate remain unchanged.

Ready for the millennium change

The Swiss financial centre is very well prepared for the millennium change. Everything reasonably feasible has been done. The relevant systems have been successfully tested and the necessary preparations made. Even in the most unlikely event of a crisis there is a plan of action in place for the whole financial centre. In spite of the well-founded confidence all the parties concerned are still called upon to stand ready to take action at any time during the turn of the year and to carry out the numerous test and control jobs with the utmost care.

With regard to supplying the market with liquidity, we plan to have a regular presence in the market also in the coming weeks and to make our contribution to a century rollover without disruptions.

CHF Money market rates



Annex

LIBOR

The London Interbank Offered Rate (LIBOR) is the rate fixed every business day at 11:00 o'clock (London time) by the British Bankers' Association. It is the rate at which major banks are prepared to grant unsecured money market loans to each other. The LIBOR is fixed according to a clearly defined procedure for different currencies and maturities. The Swiss franc LIBOR corresponds to the average of the current interest rates of six leading banks.

Repo rate

The repo rate is the interest rate used for repo transactions. In a repo (repurchase agreement) the cash taker sells securities to the cash provider with the understanding to repurchase securities of the same type and quantity at a later date. The repo rate is owed for the amount loaned and is generally lower than the interest rate for unsecured money market loans.

The National Bank uses this instrument for the steering of liquidity. In principle, it is willing to purchase any securities from the "SNB basket" and the "German GC basket".