



Speech

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Is the SNB's institutional framework still appropriate to our times?

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of the Swiss National Bank

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Dear Shareholders
Ladies and Gentlemen
Dear Guests

I am sure you will agree that we can look back on a very eventful year from an international perspective. As is customary at our General Meeting, it will be up to the Chairman of the Governing Board, Thomas Jordan, to explain in his speech how the Swiss National Bank has managed to maintain a steady monetary policy course in turbulent times, and to provide an outlook for the future.

Periods of uncertainty influence economic and financial developments, which in turn impact the activities of institutions such as the SNB. Under such circumstances, it is not surprising that the SNB and the institutional framework within which it operates are in the focus of public interest. In the first part of my speech today, I will therefore concentrate on the SNB's institutional framework. My second topic will be the appropriation of profit, or, to be more precise, the rules governing the calculation and distribution of SNB profits. This is of particular importance to you as shareholders.

Institutional aspects

Ladies and gentlemen, the institutional aspects regarding the SNB are subject to rules that are laid down in the National Bank Act (NBA). In 2015, several parliamentary procedural requests were submitted to the national government in this connection. The Federal Council looked closely into the various issues and summarised its response in its monetary policy report published at the end of December 2016. The fundamental question is whether the rules governing the SNB are still appropriate to our times. And without further ado, I can reveal to you that after a thorough assessment of the matter, the Federal Council came to the conclusion that the institutional framework has proved its worth, that there is no need for any modification, and that the SNB is able to fulfil its mandate effectively on the existing legal basis.

Three aspects came under particular scrutiny in the Federal Council's report: the SNB's independence, its transparency, and the size of the Governing Board. Since all three are highly significant for the SNB and for the fulfilment of its mandate, I would like to go into them in greater detail. Independence basically means that, in the conduct of its monetary policy, the SNB is not allowed to ask for or accept any instructions, be it from the Federal Council, the Federal Assembly or any other outside party. The main reason for this is that the time horizon involved in monetary policy is relatively long because there is generally a lag in the effect of monetary policy measures on the real economy. Besides, history and experience have shown that an independent central bank is far better able to ensure price stability than one that is obliged to follow political instructions. From its very beginning, the SNB was given a legal structure reflecting this independence to make sure that it can truly take decisions autonomously within the scope of its competences. As you know, the SNB is constituted as a

special-statute joint-stock company, and you as shareholders embody an important part of its independence.

Doubts are sometimes expressed as to whether the SNB's independent monetary policy is sufficiently legitimised from a democratic point of view. One reason for this is probably the fact that central banks, among them the SNB, have been forced to take unconventional measures in recent years in order to fulfil their monetary policy mandate. In the case of Switzerland, examples include the introduction and discontinuation of the minimum exchange rate and the adoption of a negative interest rate. These interventions and their consequences have had a far-reaching effect, which meant that the SNB has been in the public eye to a greater extent than before. However, Swiss legislators have provided for situations like these. As a counterbalance to the independence granted, the law makes the SNB accountable to the Federal Council, to parliament and to the public. The SNB is therefore obliged to assume responsibility for its actions, and to explain its policy and decisions on a regular basis. In its report, the Federal Council concludes that this provides sound democratic legitimisation for the independence of the SNB and ensures that its activities are transparent.

And speaking of transparency: I have already noted on earlier occasions that, in an international comparison, the SNB ranks among the most transparent central banks. Besides the aforementioned duty of accountability, our General Meeting is a further important pillar in this respect. The General Meeting gives the SNB an opportunity to provide you, who are present here, and the public in general, with information on its monetary policy activities. Moreover, the SNB regularly publishes a wide array of information, and members of the Governing Board use public appearances to explain what the SNB does and why. The SNB is aware that especially high demands are placed on its reporting at times like these when exceptional instruments are applied in monetary policy.

As you may know, there are voices calling for the minutes of meetings relating to monetary policy decisions to be published, as they are in several other countries. Just as the Federal Council did, I would like to emphasise that certain, specifically Swiss characteristics need to be taken into account in this context. In particular, we have the deeply rooted principle of collegiality in our political culture, a principle to which the Governing Board also adheres, even though it is obliged to speak in a single voice in public. Moreover, the SNB's Governing Board is a small body by international standards, so that if the minutes were published, attributing certain statements to one of the three members would be fairly easy. Knowing that the minutes were to be published would hamper the exchange of thoughts and opinions and the decision-making process within the Governing Board and thus impair the quality of the SNB's monetary policy. Once a monetary policy decision has been taken, the decision itself and the reasons behind are explained in a comprehensive way. Publishing the minutes would not provide any added benefit. On the contrary, it would be detrimental to our country.

As mentioned before, the Governing Board consists of three members. Would monetary policy decisions not be more broad-based if the Governing Board were expanded? Reality shows that already now there are differing viewpoints flowing into the decision-making

process. Besides, the three deputy members of the Governing Board have an advisory role in the process, and relevant specialists from the areas of economics, financial stability, money market and foreign exchange are also consulted. Ultimately, the SNB's record speaks for itself. Even in the difficult years following the onset of the financial crisis, it managed to fulfil its mandate, i.e. to conduct a monetary policy geared to stability in the interests of Switzerland as a whole. Bearing the specific characteristics of Switzerland in mind, we can therefore agree with the position maintained by the Federal Council: an enlargement of the Governing Board would bring no advantages, but would expose it to the risk of politicisation.

Adjustments in the appropriation of profit

As previously mentioned, the second part of my presentation will focus on the topic of profit appropriation. The rules governing the calculation and distribution of SNB profits also constitute a component of the institutional framework. They are laid down in the NBA and are intended to maintain the SNB's ability to conduct monetary policy in the long term. The principal legislation and the key goals remain unchanged for the current appropriation of profit. Nevertheless, taking account of the latest developments, a few adjustments have been necessary. They will apply to the 2016 financial year and I would like to outline them here.

As you know, the allocation to the provisions for currency reserves is the first step in the appropriation of the annual result. These provisions represent the most important component of the SNB's equity capital. They act as a buffer against all forms of loss risk, in particular the risk of valuation losses on currency reserves. In principle, the provisions serve to maintain the currency reserves at the level necessary for monetary policy. It should be noted that the allocation to the provisions is made irrespective of the annual result.

The level of this allocation is calculated on the basis of economic developments in Switzerland. Provisions will, in accordance with existing rules, continue to be increased by double the average nominal GDP growth rate over the previous five years. In December 2016, we additionally stipulated that a minimum annual allocation of 8% of the existing provisions will now apply. As a result, the allocation for the 2016 financial year will be roughly twice as much as it would have been without this change.

What is the reason for this change? Foreign exchange market interventions by the SNB aimed, when necessary, at countering excessive upward pressure on the Swiss franc have resulted in a considerable expansion of the balance sheet. As a result, the capital ratio has declined significantly and loss exposure increased. To take account of this development, we are aiming for a more substantial build-up of the SNB's equity capital, in other words a larger cushion of reserves. The minimum allocation rule of 8% ensures that sufficient allocations are made to the provisions even in periods of low nominal GDP growth.

The part of the annual result remaining after allocation to the provisions for currency reserves is the distributable profit. Together with the distribution reserve, i.e. earnings or losses of the previous year brought forward, this amount is available for dividend payment and for the profit distribution to the Confederation and the cantons. The NBA specifies a maximum

dividend of 6% of the share capital, i.e. CHF 15 per share, and stipulates an annual profit distribution to the Confederation and the cantons. The amount of the distribution is to be smoothed over the medium term by means of an agreement between the Federal Department of Finance (FDF) and the SNB. In November 2016, the agreement governing the 2016 to 2020 financial years was concluded.

As in the past, an annual distribution of CHF 1 billion is to be made so long as this does not render the distribution reserve negative. In future, omitted or reduced distributions will be compensated for in subsequent years provided that the distribution reserve allows this, in other words that it does not become negative as a result. A further change assures that a supplementary distribution of a maximum of CHF 1 billion is made if the distribution reserve does not thereby fall below CHF 20 billion. The previous agreement permitted an increase in the distribution, provided the distribution reserve did not drop below CHF 10 billion. This threshold has thus been raised. The main reason for this is that SNB's future annual results are likely to fluctuate more widely given the considerable expansion of its balance sheet. As a final change, the supplementary distribution is now defined in the agreement and is capped at CHF 1 billion. Previously, the FDF and the SNB jointly determined the level of any supplementary distribution.

You may well ask yourself how these adjustments will impact shareholders, the cantons and the Confederation or – in other words – how dividend payments and the profit distribution will be affected.

For the cantons and the Confederation, there are two positive aspects: first, the guarantee that omitted distributions can be taken into account in the distribution calculations of subsequent years, and second, the advantages of having the level of the supplementary distribution already defined in the agreement. In both cases, however, funds will be distributed only if the distribution reserve is high enough. Moreover, the introduction of a minimum annual allocation to the provisions for currency reserves tends to reduce the distributable profit, thus lowering the amount available for distribution.

This last point also concerns the shareholders. As mentioned earlier, the allocation to provisions for currency reserves, the first step in the profit appropriation process, is made irrespective of the annual result. Should there be a loss or an insufficient profit, the shortfall will be taken from the distribution reserve, which will thereby decline. The distribution reserve may even become negative, precluding a dividend payment, as was the case after the 2013 financial year.

As to adjustments in the appropriation of profit, let me reiterate, ladies and gentlemen, that the goal is to strengthen the SNB's capital base. This is a crucial prerequisite for ensuring our institution's ability to conduct monetary policy over the long term.

Concluding remarks

Let me now return to the question posed in the title: is the SNB's institutional framework still appropriate to our times? The answer is yes. The applicable legal basis laid down in the NBA is still up to date. The NBA provides for sufficient flexibility in view of the changing requirements of our times, in particular when it comes to making adjustments in the profit distribution agreement. On the one hand, the institutional framework gives the SNB the necessary scope to be able to fulfil its mandate in the interests of Switzerland as a whole – also in an unsettled environment. On the other hand, this framework also imposes on the SNB the duty to render account and to assume responsibility for its actions. Bear in mind that the demands in this respect are, not surprisingly, especially high in this day and age.

At the same time, we are well advised to look ahead and make sure that the SNB's ability to conduct monetary policy remains intact.

In this context, let me emphasise the importance I attribute to a substantive public debate. A constructive dialogue is essential for the citizens of our country to retain confidence in our institution and give it the necessary support in the fulfilment of its mandate.

With this in mind, dear shareholders, I would like to thank you for engaging in this debate and for your loyalty to our institution.

Thank you for your attention.