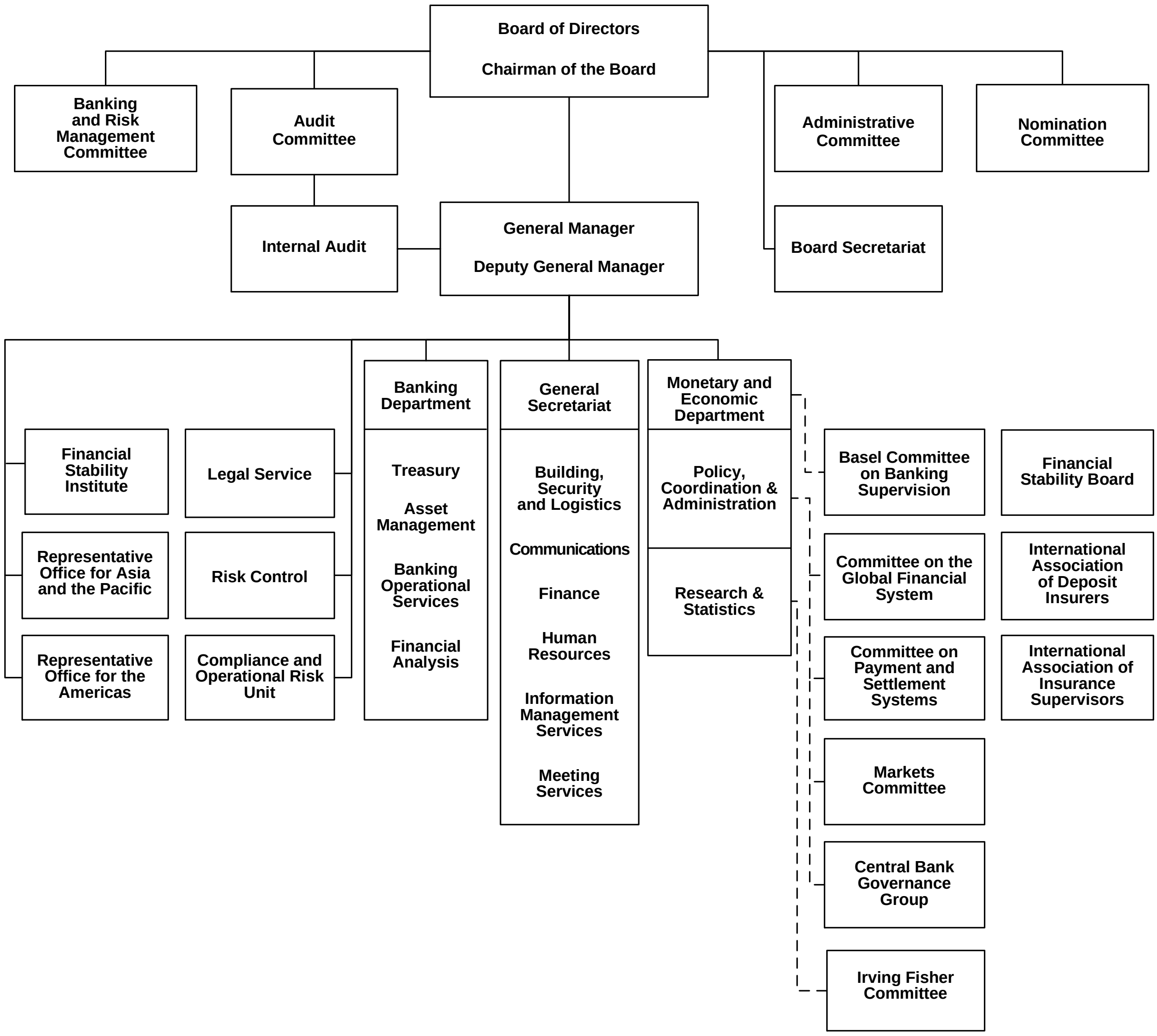



Organisation of the BIS as at 31 March 2011

# The BIS: mission, activities, governance and financial results

The mission of the Bank for International Settlements (BIS) is to serve central banks in their pursuit of monetary and financial stability, to foster international cooperation in those areas and to act as a bank for central banks.

In the light of the Bank's mission, this chapter reviews the activities of the BIS, and the groups it hosts, for the financial year 2010/11; describes the institutional framework that supports their work; and presents the year's financial results.

In broad outline, the BIS pursues its mission by:

- promoting discussion and facilitating collaboration among central banks;
- supporting dialogue with other authorities that are responsible for promoting financial stability;
- conducting research on policy issues confronting central banks and financial supervisory authorities;
- acting as a prime counterparty for central banks in their financial transactions; and
- serving as an agent or trustee in connection with international financial operations.

The BIS promotes international cooperation on monetary and financial policy through its meetings programmes for central bank officials and through the Basel Process – hosting international committees and standard-setting bodies and facilitating their interaction.

In particular, the BIS hosts the Financial Stability Board and supports its mandate: to coordinate at the international level the work of national financial authorities and international standard-setting bodies in order to develop and promote the implementation of effective regulatory, supervisory and other financial sector policies.

The BIS research and statistics function addresses the needs of monetary and supervisory authorities for data and policy insight.

The BIS banking function provides prime counterparty, agent and trustee services appropriate to the BIS mission.

## The meetings programmes and the Basel Process

The BIS promotes international financial and monetary cooperation in two major ways:

- through hosting bimonthly and other meetings of central bank officials; and
- through the Basel Process, which facilitates cooperation of the committees and standard-setting bodies hosted by the BIS in Basel.

## *Bimonthly meetings and other regular consultations*

At bimonthly meetings, normally held in Basel, Governors and other senior officials of BIS member central banks discuss current developments and the outlook for the world economy and financial markets. They also exchange views and experiences on issues of special and topical interest to central banks. In addition to the bimonthly meetings, the Bank regularly hosts gatherings that variously include public and private sector representatives and the academic community.

The two principal bimonthly meetings are the Global Economy Meeting and the All Governors' Meeting.

### *Global Economy Meeting*

The Global Economy Meeting (GEM) comprises the Governors from 30 BIS member central banks in major advanced and emerging market economies that account for about four fifths of global GDP. Governors from another 15 central banks attend the GEM as observers.[1] The GEM has two main roles: (i) monitoring and assessing developments, risks and opportunities in the world economy and the global financial system; and (ii) providing guidance to the Basel-based central bank committees, especially the main three – the Committee on the Global Financial System, the Committee on Payment and Settlement Systems and the Markets Committee. The GEM also receives reports from the chairs of those committees and decides on publication.

As the Global Economy Meeting is quite large, it is supported by an informal group called the Economic Consultative Committee (ECC). Limited to 18 participants, the ECC includes all BIS Board member Governors, the central bank Governors from India and Brazil, and the BIS General Manager. The ECC assembles proposals for consideration by the GEM. In addition, the ECC Chairman initiates recommendations to the GEM on the appointment of chairs of the main central bank committees and on the composition and organisation of those committees.

Jean-Claude Trichet, President of the ECB, has been elected by the BIS Board as Chairman of both the GEM and the ECC.

### *All Governors' Meeting*

The All Governors' Meeting comprises the Governors of all BIS member central banks and is chaired by the BIS Chairman. It gathers during the bimonthly meetings to discuss selected topics of general interest to its members. In 2010/11, the topics discussed were:

- strategies for exit from unconventional central bank balance sheet policies;
- the reform proposals of the Basel Committee on Banking Supervision;

[1] The members of the GEM are the central bank Governors of Argentina, Australia, Belgium, Brazil, Canada, China, France, Germany, Hong Kong SAR, India, Indonesia, Italy, Japan, Korea, Malaysia, Mexico, the Netherlands, Poland, Russia, Saudi Arabia, Singapore, South Africa, Spain, Sweden, Switzerland, Thailand, Turkey, the United Kingdom and the United States and also the President of the European Central Bank and the President of the Federal Reserve Bank of New York. The Governors attending as observers are from Algeria, Austria, Chile, the Czech Republic, Denmark, Finland, Greece, Hungary, Ireland, Israel, New Zealand, Norway, the Philippines, Portugal and Romania.

- statistics needed for financial stability analysis;
- managing inflation expectations following the financial crisis;
- implications of the expansion of central bank balance sheets in Asia; and
- the role of central banks in government debt markets since the beginning of the financial crisis.

In agreement with the BIS Board and the GEM, the All Governors' Meeting guides the work of the Central Bank Governance Group, which also meets during the bimonthly meetings, and the Irving Fisher Committee on Central Bank Statistics. The All Governors' Meeting is better suited than the GEM for this responsibility because the membership of the two groups goes beyond the participants in the GEM.

*Other regular consultations*

During the bimonthly meetings, Governors of central banks in (i) major emerging markets and (ii) small open economies gather to discuss themes of special relevance to their economies.

The Bank hosts regular meetings of the Group of Central Bank Governors and Heads of Supervision (GHOS), which oversees the work of the Basel Committee on Banking Supervision. The GHOS met three times during the year to consider the Basel III reform package being developed by the BCBS to strengthen the regulation, supervision and risk management of the banking sector. At its meetings, the GHOS agreed on key design elements of the package, on calibration of the capital and liquidity measures, and on the pace of transition to the implementation phases of the plan.

The Bank regularly arranges informal discussions among public and private sector representatives that focus on their shared interests in promoting a sound and well functioning international financial system. In addition, the Bank organises various other meetings for senior central bank officials on a regular or ad hoc basis, to which other financial authorities, the private financial sector and the academic community are invited to contribute. These meetings include:

- the meetings of the working parties on domestic monetary policy, held in Basel but also hosted at a regional level by a number of central banks in Asia, central and eastern Europe, and Latin America;
- the meeting of Deputy Governors of emerging market economies; and
- the high-level meetings organised by the Financial Stability Institute in various regions of the world for Deputy Governors and other senior-level supervisors.

## *The Basel Process*

The Basel Process refers to the facilitative role of the BIS in hosting and supporting the work of the international secretariats engaged in standard setting and the pursuit of financial stability. A key example of the Basel Process is the support the BIS provides to the Financial Stability Board (FSB), which coordinates the work of national financial authorities and international standard-setting bodies and whose work programme has been endorsed by the G20 heads of state and government. Another aspect of the Basel Process is the mandate given by the BIS to its own Financial Stability Institute (FSI), namely to assist financial sector supervisory authorities worldwide in strengthening oversight of their financial systems.

*Features of the Basel Process*

The Basel Process is based on four key features: (i) the synergies of co-location; (ii) flexibility and openness in the exchange of information; (iii) support from the economic research expertise and banking experience of the BIS; and (iv) the dissemination of work.

*Synergies*. The BIS hosts the secretariats of nine groups, including the FSB, that contribute to the pursuit of financial stability. The agendas of the following six are set by the global community of central banks and/or supervisory authorities:

- the Basel Committee on Banking Supervision (BCBS): addresses supervision at the level of individual institutions and its relation to macroprudential supervision;
- the Committee on the Global Financial System (CGFS): monitors and analyses macrofinancial stability issues;
- the Committee on Payment and Settlement Systems (CPSS): analyses and sets standards for the payment, clearing and settlement infrastructure;
- the Markets Committee: examines the functioning of financial markets;
- the Central Bank Governance Group: examines issues related to the design and operation of central banks; and
- the Irving Fisher Committee on Central Bank Statistics (IFC): addresses statistical issues of concern to central banks, including those relating to economic, monetary and financial stability.

The remaining three groups hosted at the BIS have separate governance and reporting lines:

- the FSB;
- the International Association of Deposit Insurers (IADI); and
- the International Association of Insurance Supervisors (IAIS).

The physical proximity of these groups at the BIS creates synergies that, regardless of the variation in governance arrangements, produce a broad and fruitful exchange of ideas.

*Flexibility*. The limited size of these groups leads to flexibility and openness in the exchange of information, thereby enhancing the coordination of their work on financial stability issues and avoiding overlaps and gaps in their work programmes. At the same time, their output is much larger than their limited size would suggest, as they are able to leverage the expertise of the international community of central bankers, financial regulators and supervisors, and other international and national public authorities.

*Supportive BIS expertise and experience*. The work of the Basel-based committees is informed by the BIS's economic research and banking experience. The latter is derived from the BIS Banking Department's working relationships with market participants and its implementation of regulatory standards and financial controls for the conduct of its banking operations.

*Dissemination*. Dissemination of the standard-setting bodies' work to official organisations is facilitated by the FSI.

## Activities of BIS-hosted groups in 2010/11

The following pages review the year's principal activities of the nine groups hosted at the BIS.

### *Financial Stability Board*

The Financial Stability Board (FSB) coordinates the work of national financial authorities and international standard-setting bodies and develops policies to enhance global financial stability. It closely monitors whether implementation of these policies takes place in a full and consistent manner.[2]

More specifically, under its mandate from the G20, the FSB:

- assesses vulnerabilities affecting the global financial system and identifies and reviews the regulatory, supervisory and related actions needed to address them, including the outcomes of those actions;
- promotes coordination and information exchange among authorities responsible for financial stability;
- monitors and advises on market developments and their implications for regulatory policy;
- monitors and advises on best practice in meeting regulatory standards;
- undertakes joint strategic reviews of the international standard-setting bodies to ensure that their policy development work is timely, coordinated and focused on priorities, and that it addresses gaps;
- sets guidelines for and supports the establishment of supervisory colleges;
- supports contingency planning for cross-border crisis management, particularly with respect to systemically important firms; and
- collaborates with the IMF to conduct early warning exercises.

The membership of the FSB consists of senior officials from finance ministries, central banks and financial regulators and supervisors of 24 countries and territories (the country members of the G20 plus Hong Kong SAR, the Netherlands, Singapore, Spain and Switzerland) as well as from the ECB and the European Commission. It also includes representatives of international financial institutions and of international standard-setting and central bank bodies.[3] The FSB is chaired by Mario Draghi, Governor of the Bank of Italy.

[2] The FSB was established by the G20 Leaders (heads of state and government) at their April 2009 London Summit. The G20 comprises 19 countries and the European Union. The charter setting out the objectives, mandate, membership and organisational processes of the FSB took effect in September 2009, when it was endorsed by the G20 Leaders at their Pittsburgh Summit.

[3] The international financial institutions are the BIS, the IMF, the OECD and the World Bank. The international standard-setting and central bank bodies are the BCBS, the CGFS, the CPSS, the International Accounting Standards Board (IASB), the IAIS and the International Organization of Securities Commissions (IOSCO).

The FSB operates through plenary meetings of its membership and through the following groups:

- a Steering Committee, chaired by Mario Draghi;
- a Standing Committee on Assessment of Vulnerabilities, chaired by Jaime Caruana, General Manager of the BIS;
- a Standing Committee on Supervisory and Regulatory Cooperation, chaired by Adair Turner, Chairman of the UK Financial Services Authority; and
- a Standing Committee on Standards Implementation, chaired by Tiff Macklem, Senior Deputy Governor of the Bank of Canada.

Through work at the plenary meetings in June, September and October 2010, the FSB and its members further developed the international regulatory reform programme aimed at creating a sounder financial system and reducing systemic risk globally. Two central elements of that programme were endorsed by the Seoul Summit of the G20 in November 2010: (i) a strengthened global framework for bank capital and liquidity; and (ii) a comprehensive policy framework to address the moral hazard associated with institutions that are too big or too complex to fail. In addition, during the past year the FSB set out principles and timetables, and monitored implementation, in a wide range of other areas, as detailed below.

*Strengthening the global capital and liquidity framework for banks*

The FSB and the Basel Committee, in collaboration with the BIS and the IMF, jointly assessed the macroeconomic implications of the transition to the new capital and liquidity reform proposals in Basel III. The resulting transitional arrangements have been designed to ensure that the implementation does not harm the economic recovery.

*Reducing the moral hazard posed by systemically important financial institutions (SIFIs)*

In October 2010, the FSB adopted a policy framework as well as work processes and timelines for addressing the systemic risks and moral hazard posed by SIFIs.[4] The framework comprises action in five areas:

- improvements to resolution regimes to ensure that any financial institution can be resolved without disruption to the financial system and without taxpayer support;
- a requirement that SIFIs and initially in particular G-SIFIs have additional loss absorption capacity beyond the Basel III standards to reflect the greater risks these institutions pose to the global financial system;
- more intensive supervisory oversight for financial institutions that may pose systemic risk;
- stronger robustness standards for the core financial infrastructure to reduce contagion risks from the failure of individual institutions;[5] and

[4] A SIFI is a firm whose disorderly failure would cause significant disruption to the wider financial system and to overall economic activity because of its size, complexity and systemic interconnectedness. Global SIFIs (G-SIFIs) are SIFIs that are systemically important in a global context.

[5] The core financial market infrastructure includes elements such as payment systems, securities settlement systems and central counterparties.

- assessment, by an FSB Peer Review Council, of the effectiveness and consistency of national policy measures for G-SIFIs, beginning by end-2012.

In November 2011, the FSB will finalise a package of measures covering: an identification methodology for G-SIFIs; the amounts of additional going-concern and gone-concern loss absorbency that G-SIFIs will need and the instruments by which that can be met; and improvements to resolution tools and regimes. Draft proposals for these measures and their phase-in periods will be issued for public comment.

*Improving the OTC and commodity derivatives markets*

In October 2010, the FSB published 21 recommendations for implementing – in an internationally consistent and non-discriminatory way – the G20 commitments for improving by end-2012 the functioning, transparency and oversight of the over-the-counter (OTC) derivatives market. The G20 commitments relate to increased standardisation, central clearing, organised platform trading, and reporting of all trades to trade repositories.

The FSB has planned a series of six-month reports – derived from a survey of FSB members – on progress in reforming OTC derivatives markets. The report scheduled for release in April 2011 found that major implementation projects are under way in the largest OTC derivatives markets, and international policy development is proceeding according to timetable. Nevertheless, the FSB expressed concern that many jurisdictions may not meet the end-2012 deadline unless they take substantial, concrete steps towards implementation immediately. It saw inconsistencies in approaches between jurisdictions emerging in some areas. The FSB will continue to monitor developments to check whether progress on implementation is on track and to identify any further emerging inconsistencies that should be addressed.

At their Seoul Summit, the G20 Leaders called for a report from IOSCO on the regulation, supervision and transparency of commodity derivatives markets and the financial market for oil, and for the FSB to consider next steps. IOSCO's report, scheduled for April 2011, was to cover the work being undertaken in the short term in these areas; consider a broadened mandate to include other commodities, including agricultural and soft commodities; and outline the medium- to longer-term work being considered. The FSB supports those actions and in October 2011 will again consider next steps on the basis of a further IOSCO report.

*Strengthening the oversight and regulation of shadow banking*

As the recent financial crisis has shown, the "shadow banking system" – credit intermediation involving entities and activities outside the regulated banking system – can be a source of systemic risk both directly and through its interconnectedness with the regular banking system. Shadow banks can also create opportunities for arbitrage that might undermine stricter bank regulation and lead to a build-up of additional leverage and risks in the financial system as a whole. The FSB is therefore developing recommendations to strengthen the oversight and regulation of the shadow banking system. It scheduled the release of a background note on its work for April 2011.

*Reducing reliance on credit rating agencies (CRAs)*

The use of CRA ratings in regulatory regimes for banks and other financial institutions contributes to a mechanistic market reliance on ratings. Because of such reliance, a downgrading by a CRA can push the rating of a securities issuer below a threshold rating level and thereby create a "cliff effect" of widespread disinvestment in the securities of that issuer, leading to sharp price declines and further disinvestment. Such cliff effects amplify procyclicality and can generate systemic disruptions. In October 2010, the FSB issued principles for reducing the reliance of market participants on ratings from CRAs and requested standard setters and regulators to consider next steps to translate the principles into more specific policy actions. The principles are applicable to central bank operations, the prudential supervision of banks, internal limits and investment policies of investment managers, private sector margin agreements, and disclosures by issuers of securities. The FSB is monitoring progress on the translation of the principles into policy actions.

*Developing macroprudential frameworks and tools*

The financial crisis exposed gaps in the public policy toolkit for dealing with systemic risk, and it has intensified the official sector's interest in strengthening the macroprudential aspect of current policy arrangements. The FSB, the IMF and the BIS are working on a joint report, to be delivered at the November 2011 G20 Summit, outlining both international and national advances in the design of macroprudential frameworks and tools. To survey experience, the three organisations scheduled two meetings for 2011: a high-level conference to be held in Washington in April and a roundtable to be held in Basel in June.

*Addressing data gaps*

The FSB is developing a template of metrics and procedures that would improve consistency in the collection and sharing of data on the interconnectedness and common exposures of SIFIs. The project is part of a broader exercise by the IMF and the FSB, set out in their November 2009 report, *The financial crisis and information gaps*, which proposed improvements to data collection to better capture the build-up of risk in the financial sector.

*Strengthening accounting standards*

The FSB supports the development of a single set of high-quality global accounting standards. To that end, it continues to encourage the IASB and the United States' Financial Accounting Standards Board to complete their convergence project by the end of 2011.

*Strengthening adherence to international standards*

The FSB is fostering a "race to the top" by encouraging all jurisdictions to raise their level of adherence to international financial standards. It has updated its Compendium of Standards, including the 12 key standards that it designates as deserving of priority implementation. FSB member jurisdictions will lead by example by implementing the standards and disclosing their level of adherence to them.

Under a programme of country and thematic peer reviews that began in 2010, FSB member jurisdictions are evaluating each other's implementation of internationally agreed standards and policies. The FSB has now completed country peer reviews of Italy, Mexico and Spain and thematic peer reviews of compensation practices, of mortgage underwriting and origination, and of risk disclosures for structured credit products and other exposures. A country peer review of Australia is under way, and reviews of Canada and Switzerland will be launched in the second half of 2011. The FSB is conducting a second review of the implementation of sound compensation practices and will conduct a thematic review of deposit insurance systems during the second half of 2011.

Using a network of national experts, the FSB is closely monitoring implementation of its post-crisis policy recommendations to strengthen financial stability. The FSB scheduled the release of detailed information on national implementation for April 2011, and in November 2011 it will publish updated information based on a further survey.

The FSB is also encouraging jurisdictions throughout the world to follow international financial standards, including through an initiative to evaluate jurisdictions' adherence to standards for supervisory and regulatory cooperation and information exchange. By November 2011, the FSB will publish a list of all jurisdictions evaluated.

*Advancing consumer finance protection*

At the request of the G20, the FSB is collaborating with the OECD and other international organisations in a study of options for advancing consumer finance protection, including the development of common principles. A report is scheduled for release by November 2011.

*Financial stability in emerging market and developing economies*

The FSB, the IMF and the World Bank are jointly writing a report to the G20 identifying and examining financial stability issues of particular relevance to emerging market and developing economies. The report will include policy recommendations that could be taken forward by national authorities and international standard-setting bodies.

*Regional consultative groups*

To facilitate its interaction with a wider group of countries, the FSB is setting up six regional consultative groups that will bring together the members of the FSB and more than 60 jurisdictions outside the FSB's membership. The regional groups – covering the Americas; Asia; the Commonwealth of Independent States; Europe; the Middle East and North Africa; and sub-Saharan Africa – will provide the opportunity to discuss vulnerabilities affecting the regional and global financial systems and the financial stability initiatives of the FSB and of the various jurisdictions. The first meetings will take place in 2011. In addition, the FSB intends to conduct outreach as needed concerning its policy initiatives with an even wider range of interested countries.

*FSB capacity, resources and governance*

The demands on the FSB have grown since its establishment in 2009. To help the FSB keep pace with these demands, the G20 has asked it to make proposals for strengthening its capacity, resources and governance. These will be reviewed at the G20's October 2011 meeting.

FSB: www.financialstabilityboard.org

## *Basel Committee on Banking Supervision*

The Basel Committee on Banking Supervision seeks to improve supervisory understanding and the quality of banking supervision worldwide. It supports supervisors by providing a forum for exchanging information on national supervisory arrangements, improving the effectiveness of techniques for supervising international banks, and setting minimum supervisory standards.

The Committee, which generally meets four times a year, consists of senior representatives of bank supervisory authorities and central banks responsible for banking supervision or financial stability issues in the Committee's member countries.[6] The Group of Governors and Heads of Supervision (GHOS) is the governing body of the Basel Committee and consists of central bank governors and (non-central bank) heads of supervision from member countries. Nout Wellink, President of the Netherlands Bank, is chairman of the Basel Committee.

On 16 December 2010, the Basel Committee published a set of global standards to address both firm-specific risks and broader, systemic threats so as to promote a more resilient banking sector. The framework, "Basel III", responded to the core of the global financial reform agenda and was endorsed by the G20 Leaders at their 2010 Seoul Summit. Basel III, together with the underlying Basel II framework and the reforms approved by the Committee in July 2009,[7] represents a major step in strengthening bank soundness and financial stability.

Over the course of 2010, the Committee also released a number of standards and proposals to enhance risk management and supervision in concert with the higher standards in Basel III.

*The Basel III framework*

Basel III strengthens international prudential requirements for capital and liquidity. It raises the minimum amount of capital that banks must hold against

[6] The Committee comprises representatives from Argentina, Australia, Belgium, Brazil, Canada, China, France, Germany, Hong Kong SAR, India, Indonesia, Italy, Japan, Korea, Luxembourg, Mexico, the Netherlands, Russia, Saudi Arabia, Singapore, South Africa, Spain, Sweden, Switzerland, Turkey, the United Kingdom and the United States. Observers on the Basel Committee are: the European Banking Authority, the European Central Bank, the European Commission, the Financial Stability Institute and the International Monetary Fund.

[7] *Enhancements to the Basel II framework*; *Revisions to the Basel II market risk framework*; and *Guidelines for computing capital for incremental risk in the trading book – final version*.

risk-weighted assets and requires capital of greater loss-absorbing capacity. Further, Basel III improves the risk coverage of the regulatory framework. It also introduces an overall leverage ratio that will apply against unweighted assets and off-balance sheet exposures to provide another check on excessive credit expansion at the level of the firm. In addition, Basel III addresses the liquidity aspect of the recent crisis by requiring a larger stock of liquid reserves and a reduction in maturity mismatches.

The GHOS agreed on transitional arrangements for implementing the new standards. These will help ensure that the banking sector can meet the higher standards through reasonable amounts of earnings retention and new capital without impairing lending activity.

*Bank capital*

*Improving its quality*. An essential element of Basel III is its stricter definition of regulatory capital. Higher-quality capital means more loss-absorbing capacity, which will allow banks to better withstand periods of stress. A key aspect of the new capital definition is its greater focus on common equity, the highest-quality component of a bank's capital. Credit losses and writedowns come directly out of retained earnings, which are part of a bank's common equity. The Basel III capital framework defines common equity more narrowly than does the present rule. In a move that further extracts lower-quality capital from required capital, the new rules require regulatory adjustments from the capital base to be made against common equity rather than, as is done currently, against the rest of Tier 1 or against Tier 2 capital.

During the financial crisis, taxpayers were exposed to loss when the public sector injected capital into a number of large, internationally active banks that were in distress. The extra funds rescued them from failure and hence supported their depositors, but the infusion allowed investors in the banks' Tier 2 capital instruments (mainly subordinated debt) and in some Tier 1 instruments to avoid loss. Therefore, the Basel III definition of capital issued in December 2010 was supplemented by the GHOS in January 2011 with additional minimum requirements to ensure that, before taxpayers are exposed to loss, all classes of bank capital fully absorb losses at the point when the firm becomes non-viable.

*Requiring higher amounts*. The Basel III reforms increase the minimum requirement of (now higher-quality) common equity from 2% to 4.5% of risk-weighted assets. In addition, Basel III introduces a macroprudential overlay requiring additional capital buffers (see below).

*Expanding risk coverage of the framework*. By itself, the new definition of capital constitutes a significant improvement in the global capital regime. The regime will be enhanced further by better risk coverage. The Basel III framework introduces measures to strengthen capital requirements for counterparty credit exposures arising from banks' derivative, repo and securities financing activities. The reforms will increase the capital required to back those exposures, reduce procyclicality and provide additional incentives to move the trading of OTC derivative contracts to central counterparties, thus helping reduce systemic risk across the financial system. The reforms also provide incentives to strengthen the risk management of counterparty credit exposures. In addition, as part of its July 2009 reforms, the Committee adopted higher capital requirements for trading and for derivative and securitisation activities, to become effective at the end of 2011. The better risk coverage adopted in December 2010 reinforces those requirements as well as the stronger definition of capital.

*Introducing a leverage ratio*. Basel III introduces a non-risk-based leverage ratio to serve as a backstop to the risk-based capital requirement. The use of this supplementary measure will help contain the build-up of excessive leverage in the system. It will also serve as an additional safeguard against attempts to "game" the risk-based requirements and will help address model risk.

*Liquidity*

*Introducing global standards*. Strong capital requirements are necessary to the stability of the banking sector, but they are not sufficient. A strong liquidity base reinforced through robust supervisory standards is of equal importance, but until now no internationally harmonised liquidity standards have been adopted. Basel III introduces two such supervisory standards – a liquidity coverage ratio (LCR) and a net stable funding ratio (NSFR) – whose purpose is to improve banks' liquidity risk management and risk profile. The LCR is designed to make banks more resilient to short-term disruptions in their access to funding, while the NSFR addresses longer-term structural liquidity mismatches in bank balance sheets.

The new liquidity framework includes a common set of monitoring metrics to assist supervisors in identifying and analysing liquidity risk at both the bank and system level. The metrics should be considered as the minimum information that supervisors should use in monitoring liquidity risk profiles.

*Macroprudential framework*

*Introducing capital buffers*. A macroprudential element of the Basel III capital framework is the requirement that, in good times, banks should build up buffers – specifically, a *capital conservation buffer* and a *countercyclical buffer* – that can be drawn down in periods of stress. This approach promotes the goal of mitigating procyclicality both in banking and in the broader financial system. These buffers are in addition to the minimum capital requirements.

Losses that begin to reduce a bank's capital conservation buffer, set initially at 2.5% of common equity, would trigger constraints on its ability to make discretionary distributions of capital. The constraints become progressively tighter as the bank's capital level moves closer to the minimum requirement.

The countercyclical buffer, to be maintained at 0–2.5% of common equity or other fully loss-absorbing capital, is aimed at the broader macroprudential goal of protecting the banking sector in periods of excess aggregate credit growth; such periods have often been associated with the accumulation of system-wide risk. In December 2010, the Committee issued *Guidance for* *national authorities operating the countercyclical capital buffer* as a supplement to the requirements set out in the Basel III rules text. In addition to providing supervisory guidance, that document should help banks themselves understand and anticipate buffer-related decisions in jurisdictions to which they have credit exposures.

*Addressing systemically important institutions*. During the crisis, when procyclicality amplified shocks over time, excessive interconnectedness among systemically important banks transmitted shocks across the financial system and wider economy. To address the latter issue, the Basel Committee and the FSB are developing an integrated approach to systemically important financial institutions, which could include combinations of capital surcharges, contingent capital and bail-in debt. As part of this effort, the Committee developed a proposal on a provisional methodology to assess the systemic importance of financial institutions at the global level. The framework to address systemically important institutions will be finalised over the course of 2011.

*Calibrating Basel III standards and assessing the impact*

In developing Basel III, the Committee engaged in a four-month public consultation on the proposed reform measures. As an important input to the calibration of the new capital and liquidity standards, the Committee conducted a comprehensive quantitative study to estimate the effects of the requirements on individual banks, the results of which were published in December 2010. It complemented this "bottom up" approach with an empirical assessment of the overall level of capital that should be maintained within the banking system (*Calibrating regulatory minimum capital requirements and capital buffers: a top-down approach*). The top-down assessment, published in October 2010, helped inform the calibration of the common equity and Tier 1 risk-based ratios and the Tier 1 leverage ratio, as well as of the regulatory buffers above the minimum.

The Committee also conducted an assessment of the long-term economic impact of the reforms and estimated the costs associated with transitioning to higher capital and liquidity requirements. Its August 2010 report on that work (*An assessment of the long-term economic impact of stronger capital and liquidity requirements*) found clear net long-term economic benefits to higher regulatory standards: the higher standards raise the safety and soundness of the global banking system, which in turn reduces both the probability of financial crises and the output losses associated with such crises. And those benefits substantially exceed the potential output costs for a range of higher capital and liquidity requirements. In addition, the Committee and the FSB established the Macroeconomic Assessment Group (MAG), an international team of researchers tasked with studying the macroeconomic impact of the transition to the higher standards. The MAG study is summarised in its December 2010 *Final report: assessing the macroeconomic impact of the transition to stronger capital and liquidity requirements*. It concludes that the transition is likely to have only a modest impact on aggregate output.

*Risk management and supervision*

The stronger capital and liquidity standards in Basel III must be accompanied by better risk management and supervision, particularly given the international environment of fast-paced financial innovation. In 2010, the Basel Committee issued standards and proposals and continued studies to meet that need.

*Improving cross-border bank resolution*. In March 2010, the Basel Committee issued 10 recommendations on effective cross-border resolution. The Committee continues to work on the topic with the FSB, including monitoring how the Committee's recommendations are being implemented and where additional work is needed to address conflicts across resolution regimes. The Committee is conducting a comprehensive analysis and will review the results in the first half of 2011. They will be used by the FSB and other standard setters to formulate standards and guidance that countries can use to reform their national resolution regimes and make them more consistent with each other.

*Addressing operational risk*. The regulatory capital adequacy framework envisages a gradual convergence of the operational risk discipline towards a narrower band of effective risk management and measurement practices. In December 2010, the Committee issued two consultative documents on operational risk. *Sound practices for the management and supervision of operational risk* updates the Committee's 2003 guidance on the basis of current industry best practice and supervisory experience in three areas: governance, risk management and disclosure. The second consultative document, *Operational risk – supervisory guidelines for the advanced measurement approaches*, covers governance, data and modelling. Also dealing with advanced measurement is the Committee's October 2010 publication, *Recognising the risk-mitigating impact of insurance in operational risk modelling*, which also more broadly discusses the potential benefits and shortcomings of insurance to mitigate operational risk.

*Aligning remuneration and risk*. The Committee's October 2010 consultative report *Range of methodologies for risk and performance alignment of remuneration* analyses methods for incorporating risk and performance in compensation schemes, including bonus pools, with the aim of furthering the practice. The report notes practical and technical issues that complicate the alignment effort and offers some clarifications on design options. The Committee's December 2010 consultative document *Pillar 3 disclosure requirements for remuneration*, developed in consultation with the FSB, is aimed at promoting consistency of disclosure. Such consistency would support market discipline by helping market participants better assess the quality of bank compensation practices.

*Strengthening backtesting*. Banks that are permitted to calculate their regulatory capital with internal models are required to frequently validate their models, and backtesting is integral to the process. In its December 2010 guidance *Sound practices for backtesting counterparty credit risk models*, the Committee addresses weaknesses in backtesting that were revealed by the financial crisis.

*Improving supervisory colleges*. The financial crisis highlighted the importance of improving supervisory colleges to better support the effective supervision of international banking groups. On the basis of the crisis experience, the Committee issued a set of principles that aim to promote and strengthen the colleges. The paper *Good practice principles on supervisory colleges* supplements broader guidance issued by the Basel Committee on cross-border cooperation and information-sharing. The principles are designed to provide the flexibility needed to implement the guidance for a wide range of banks across jurisdictions.

*Enhancing corporate governance*. Drawing on the lessons of the crisis, and following a public consultation, the Committee in October 2010 updated and reinforced its guidance on corporate governance, last issued in 2006. The new document, *Principles for enhancing corporate governance*, sets out revised statements of best practice in key areas and urges regular supervisory evaluation of banks' corporate governance practices and their consistency with the Committee's principles.

*Addressing microfinance*. In August 2010, the Basel Committee issued the final version of its paper *Microfinance activities and the Core Principles for Effective Banking Supervision*, which provides guidance on the range of practices employed in the regulation and supervision of microfinance activities.

*Assessing the impact on trade finance*. As announced in December 2010, the Committee is assessing the specific impact of the regulatory regime on the capital treatment of trade finance, particularly in low-income countries.

*Accounting and transparency*

The Committee analyses and submits written comments on all consultative drafts issued by standard setters on international accounting and auditing issues relevant to banks and supervisors. During the year, the Committee developed a concrete proposal to make operational an expected loss approach to provisioning as an input to the IASB's reform efforts in that area.

More broadly, the Committee is promoting the development of a single set of high-quality global accounting standards, and towards that end it supports the convergence of accounting standards of the IASB and those established in the United States by the Financial Accounting Standards Board. In response to the financial crisis, the two boards have created accounting projects on several topics, including financial instruments and fair value measurements, to which the Committee has contributed.

Basel Committee: www.bis.org/bcbs

### *Committee on the Global Financial System*

The Committee on the Global Financial System (CGFS) monitors financial market developments and analyses their implications for financial stability. The chair of the CGFS is Mark Carney, Governor of the Bank of Canada, who succeeded Donald L Kohn, then Vice Chairman of the Board of Governors of the Federal Reserve System, on 1 July 2010. Committee members consist of the Deputy Governors and other senior officials from the central banks of 23 advanced and emerging market economies and the Economic Adviser of the BIS.

Assessment of the recent sovereign debt problems in the euro area and their effects on financial stability and bank funding shaped much of the Committee's discussions. Committee members also examined the global implications of monetary stimulus programmes in the major advanced economies, particularly their effects on portfolio flows to emerging market economies.

To deepen its understanding of current policy issues, the Committee organised a number events bringing together representatives of financial institutions and central banks:

- meetings with market participants on the outlook for investments in bank debt given the prospective phasing-out of public sector support for banks and the proposed changes in bank regulation;
- a workshop for central banks, hosted by the People's Bank of China, to assess the implications of capital flows for financial stability and the role of monetary policy and exchange rates in dealing with capital flow pressures; and
- discussions with representatives from insurance firms and pension funds on the new international accounting standards and ongoing regulatory initiatives as they might affect their demand for fixed income assets and the functioning of financial markets generally.

The Committee established a study group on macroprudential polices to address build-ups of systemic financial risk in the light of the recent crisis. Other groups worked on international banking issues, including changes in banks' management of funding and liquidity in response to the crisis, and on the implications of sovereign debt management for central bank operations and monetary and financial stability.

The Committee participated in global policy forums to discuss the broader implications of the recent financial reform agenda. These included a high-level workshop it co-sponsored with IOSCO and the CPSS related to access to central counterparties (CCPs) in OTC derivatives markets; another such forum was a joint workshop with the CPSS and the Markets Committee examining the issue of liquidity for CCPs. The CGFS also further developed its plans to close gaps in statistical data, focusing particularly on enhancements to the BIS international banking statistics.

CGFS: www.bis.org/cgfs

### *Committee on Payment and Settlement Systems*

The Committee on Payment and Settlement Systems (CPSS) contributes to the strengthening of financial market infrastructure by promoting safe and efficient payment, clearing and settlement arrangements. The Committee also facilitates cooperation among non-CPSS central banks on payment, clearing and settlement issues and provides support and expertise to meetings it organises in cooperation with regional central banks. The CPSS is chaired by William C Dudley, President and Chief Executive Officer of the Federal Reserve Bank of New York.

*Review of standards*

In March 2011, the CPSS and IOSCO jointly released a consultative report, *Principles for financial market infrastructures*. The document proposes new international standards to govern systemically important financial market infrastructures (FMIs) – payment systems, central securities depositories, securities settlement systems, CCPs and trade repositories. The proposals reflect the lessons learned from the recent financial crisis as well as the experience gained from applying the existing standards during the past decade.

When finalised, the new principles will replace the three existing sets of CPSS and CPSS-IOSCO standards, namely the *Core principles for systemically important payment systems* (2001); the *Recommendations for securities settlement systems* (2001); and the *Recommendations for central counterparties* (2004). The CPSS and IOSCO believe that a single set of principles will provide greater consistency in the oversight and regulation of FMIs worldwide.

Compared with the existing standards, the new principles introduce more demanding requirements. Perhaps the most crucial of those concern the financial resources and risk management procedures through which an FMI copes with the default of a participant; the mitigation of operational risk; and the links and other interdependencies among FMIs through which operational and financial risks can spread. Moreover, the new principles address issues that are not covered by the existing standards, for example segregation and portability, tiered participation and general business risk.

The consultation period ends on 29 July 2011, and the CPSS and IOSCO will publish a final report in early 2012.

*Market structure in the clearing industry*

A November 2010 CPSS report, *Market structure developments in the clearing industry: implications for financial stability*, assesses how far recent developments have given rise to new risks and outlines practical issues that regulators and overseers may wish to consider, either as part of their oversight role or in the context of their broader financial stability mandate. The report also examines two other topics: whether changes in market structure or ownership might affect the expansion of central clearing services, and the effect of ownership on CCPs' incentives to manage counterparty risk.

*Clearing and settling repos*

During the recent financial crisis, some markets for repurchase agreements (repos) proved to be less reliable than expected as a source of funding liquidity. In September 2010, the Committee published the report *Strengthening repo clearing and settlement arrangements*. Based on a survey of selected CPSS member countries, it identifies issues concerning clearing and settlement arrangements for repos that could undermine the resilience of repo markets and outlines ways in which these issues can be addressed.

*Other activities*

In January 2011, the Committee co-sponsored with IOSCO and the CGFS a high-level workshop to discuss issues related to access to CCPs in OTC derivatives markets. In March 2011, it held a joint workshop with the CGFS and the Markets Committee to take stock of issues related to the liquidity needs of CCPs.

CPSS: www.bis.org/cpss

## *Markets Committee*

The Markets Committee, chaired by Hiroshi Nakaso, Assistant Governor of the Bank of Japan, is a forum for senior central bank officials to jointly monitor developments in financial markets and assess their implications for central bank liquidity management operations. Currently, 21 central banks are represented on the Committee.

Turmoil in sovereign debt markets, the continued use of unconventional policies and ongoing financial sector reforms provided the backdrop for the Committee's discussions. The Committee closely followed developments in the euro area government bond markets and banking sector and examined their impact on funding markets and central bank operations. It also considered related technical issues such as the current practice of using credit support annexes in derivative transactions between public and private sector entities.

Renewed market turmoil and slower than expected economic recovery in 2010 held back the exit of major central banks from unconventional policies and prompted additional actions in some cases. The effects of such policies on the targeted markets and on the risk-taking behaviour of investors across asset classes constituted another key theme in the Committee's deliberations.

The Committee paid increasing attention to the financial market implications of post-crisis reform initiatives that were approaching or entering the implementation stage. These included the introduction of new liquidity standards in the Basel III framework and the push towards greater use of CCPs. The Committee held a joint workshop with the CGFS and the CPSS in March 2011 to take stock of issues related to the liquidity needs of CCPs.

In March 2011, the Markets Committee set up a small group of central bank experts to conduct a fact-finding study on high-frequency trading in foreign exchange markets. Its purpose is to inform, among other things, the interpretation of the results of the April 2010 BIS Triennial Central Bank Survey of Foreign Exchange and Derivatives Market Activity.

Markets Committee: www.bis.org/markets

## *Central Bank Governance*

The Central Bank Governance Group, comprising representatives from nine central banks and chaired by Stanley Fischer, Governor of the Bank of Israel, serves as a venue for the exchange of views on the design and operation of central banks as public policy institutions. In addition, it prioritises work on this topic which is then carried out through the BIS and the Central Bank Governance Network, consisting of more than 50 central banks. During the past year, the Governance Group examined the implications of central banks' changing financial stability responsibilities and initiated work on the financial strength that central banks need in order to be effective in the post-crisis world.

### *Irving Fisher Committee on Central Bank Statistics*

The Irving Fisher Committee on Central Bank Statistics (IFC) provides a forum for central bank economists and statisticians to address statistical topics related to monetary and financial stability. Seventy-two central banks and relevant international and regional organisations are members of the Committee, which is chaired by Manuel Marfán, Deputy Governor of the Central Bank of Chile. The Committee's fifth conference at the BIS convened in August to review work to resolve data gaps revealed by the financial crisis. Attendees also discussed the findings of a survey of the Committee's membership on data initiatives related to financial stability.

The IFC organised workshops on:

- the use of business surveys by central banks (with the National Bank of Ukraine);
- data requirements for monitoring derivatives market activity (with the People's Bank of China);
- inflation measurement (one with the Saudi Arabian Monetary Agency and one with the Center for Latin American Monetary Studies and the Central Bank of Peru); and
- residency versus nationality views of financial positions (with the Inter-Agency Group on Economic and Financial Statistics).

It also organised two training events, one on national accounts (with the National Bank of Belgium) and one on statistical challenges for the European System of Central Banks (with the ECB). In November, the IFC presented its first annual report to the BIS All Governors' Meeting.

IFC: www.bis.org/ifc

### *International Association of Deposit Insurers*

The International Association of Deposit Insurers (IADI) provides a forum for deposit insurers, central banks and international organisations to enhance the effectiveness of deposit insurance and bank resolution systems and cooperate on related financial stability issues. Currently, 82 organisations, including 63 deposit insurers, are IADI members or participants. IADI draws upon its membership to provide guidance on the establishment or enhancement of effective deposit insurance systems as well as on training, outreach, educational programmes and research.

In June 2009, IADI together with the Basel Committee on Banking Supervision issued the final version of *Core principles for effective deposit* *insurance systems*. The principles are designed to guide jurisdictions in strengthening existing systems as well as in creating deposit insurance systems where they do not currently exist. During 2010, a methodology for assessing compliance with the core principles was developed jointly by IADI, the BCBS, the IMF, the World Bank, the European Forum of Deposit Insurers (EFDI) and the European Commission. The FSB has included the core principles in its *Compendium of standards* and in 2011 will include them in its list of "key standards for sound financial systems". Efforts are under way for the core principles and the associated assessment methodology to be included in the IMF and World Bank Financial Sector Assessment Program (FSAP) and for the FSB and the G20 to use them in their peer review programme to assess and improve national deposit insurance systems.

IADI's Training and Conference Committee developed a comprehensive training programme on a wide variety of topics critical to effective practice for deposit insurers. IADI strengthened its partnerships with the FSI, EFDI and the South East Asian Central Banks (SEACEN) Research and Training Centre to deliver these training programmes. IADI and the FSI jointly developed five deposit insurance e-learning tutorials and modules to present to all FSI Connect subscribers, including IADI members.

IADI held its Ninth Annual General Meeting and Conference in Tokyo on 26–28 October 2010. More than 240 participants from over 50 countries attended the conference, entitled "Financial safety-nets: Going forward". In addition, IADI's seven regional committees and 12 partner organisations brought together professionals throughout the year for specialised and region-focused events such as "Bank insolvency in the Caribbean: Law and best practice"; a seminar on "Resolution of problem banks" and another on "Claims management: Reimbursement to insured depositors"; a Latin American seminar, "The role of banks in economic stability and growth"; a regional conference, "The benefits of deposit insurance in Africa"; and an Asia-Pacific conference, "Lessons learned and challenges of the deposit insurers in dealing with crisis".

IADI's Research and Guidance Committee (RGC) established a Financial Inclusion and Innovation Subcommittee to focus on deposit insurance issues related to financial inclusion and to formally engage on the topic with interested entities such as the G20 Financial Inclusion Experts Group (FIEG). In February 2011, the subcommittee held a Financial Inclusion Workshop at the BIS for IADI members in cooperation with the World Bank Consultative Group to Assist the Poor (CGAP) and the Basel Committee.

IADI: www.iadi.org

### *International Association of Insurance Supervisors*

The International Association of Insurance Supervisors (IAIS) is the international standard-setting body for prudential supervision of the insurance industry. The mission of the IAIS is to promote effective and globally consistent regulation and supervision of the insurance industry in order to develop and maintain fair, safe and stable insurance markets for the benefit of policyholders; and to contribute to global financial stability.

The IAIS is actively involved in assessing the regulatory reforms recommended by the FSB. An important issue that the IAIS Financial Stability Committee is considering is the indicators that should be used in assessing the systemic importance of insurers. The committee is also considering macroprudential tools and developing proposals on macroprudential surveillance.

*Insurance core principles*

In February 2011, the IAIS concluded a two-year review of its supervisory material with the release of a comprehensive draft revision for a 60-day consultation period. The draft incorporates lessons of the financial crisis, addresses FSB recommendations and reflects the evolution of supervisory and industry practices. It organises the supervisory material into a hierarchy with insurance core principles (ICPs) at the top, standards for implementation of the ICPs at the next level and guidance third. The IAIS plans to submit a final draft for adoption at its general meeting on 1 October 2011.

*Accounting*

The IAIS has a strong interest in ensuring high-quality financial reporting that offers a meaningful, economically sound portrayal of insurers' financial health. It closely monitors the international financial reporting developments that will most influence the overall accounting model for regulated insurance enterprises. In July 2010, the IASB released a consultative draft regarding insurance contracts. The IAIS provided extensive comments and continues to provide input to the IASB on the matter.

*Group-wide supervision*

Responding to recommendations by the G20, the FSB and the Joint Forum,[8] the IAIS adopted a *Guidance paper on treatment of non-regulated entities in group-wide supervision* in April 2010 to address key regulatory gaps observed from the crisis and to minimise opportunities for regulatory arbitrage. The paper calls for appropriate consideration of the complexity of group structures and the full spectrum of risks posed by non-regulated entities through measures such as capital adequacy and governance requirements.

*Internationally active insurance groups*

The IAIS is developing the Common Framework for the Supervision of Internationally Active Insurance Groups (ComFrame), a multilateral framework reaching beyond the regulatory approaches of individual jurisdictions and regions. ComFrame should lead to more consistency regarding each jurisdiction's supervision of internationally active insurance groups. The IAIS plans to conclude its development of ComFrame by mid-2013, after which it will undertake an impact assessment.

[8] The Joint Forum was established in 1996 under the aegis of the Basel Committee on Banking Supervision, IOSCO and the IAIS to deal with issues common to the banking, securities and insurance sectors, including the regulation of financial conglomerates. Membership consists of senior supervisors from the three sectors (www.bis.org/bcbs/jointforum.htm).

*Reinsurance*

Global reinsurers – firms that, for a fee or premium, agree to indemnify an insurer against losses on one or more contracts – are important for the efficient functioning of sound insurance markets. Reinsurance bolsters the ultimate security of ceding insurers, thereby protecting customers and contributing to overall financial stability.

The December 2010 issue of the IAIS's twice-yearly *Global reinsurance market report* showed that reinsurers were profitable in 2009, benefiting from sound management of asset portfolios and diversification of insurance risks as well as from a moderate year for claims arising from catastrophes. The August 2010 mid-year edition discussed macroprudential surveillance in insurance and reinsurance.

*Multilateral Memorandum of Understanding*

The IAIS Multilateral Memorandum of Understanding (MMoU), which became operational in June 2009, is a framework for cooperation and exchange of information with an overall goal of improving the effectiveness of cross-border supervision of insurance companies. It is also expected to contribute to the global efforts to enhance the regulation of systemically important financial institutions. Participation in the MMoU has grown to 14 signatories as of February 2011, and another 23 applications are being validated.

*Standards observance*

In October 2010, the IAIS established a Standards Observance Subcommittee to support the implementation of standards through the development of self-assessment and peer review mechanisms. The subcommittee will coordinate closely with the FSB to ensure the fulfilment of FSB recommendations for the insurance industry.

In addition, and more broadly, the IAIS organises regional seminars and workshops to assist insurance supervisors in implementing its principles, standards and guidance material in collaboration with the FSI, national insurance supervisory authorities and other bodies.

IAIS: www.iaisweb.org

## *Financial Stability Institute*

The Financial Stability Institute (FSI) supports global financial stability by disseminating supervisory standards and sound practices and assisting in their implementation.

*High-level meetings, seminars and conferences*

The FSI conducts a well established series of high-level meetings, seminars and conferences. The 47 events held in 2010 for banking and insurance supervisors, many conducted in partnership with regional groups of supervisors, focused on current regulatory reforms and drew more than 1,700 participants. In particular, the FSI's meetings for Deputy Governors of central banks and heads of supervisory authorities took place this year in Africa, Latin

America, the Middle East and, in partnership with the IMF, in Washington for a global audience. These meetings addressed the ongoing development of supervisory reforms in response to the financial crisis as well as the implementation of existing standards.

*FSI Connect*

FSI Connect is an online information resource and learning tool provided by the FSI for financial sector supervisors at all levels of experience and expertise. Through FSI Connect, close to 8,500 users at more than 225 subscribing institutions have access to more than 200 tutorials on banking, insurance, deposit insurance, and payment and settlement systems. The FSI is revising the tutorials related to bank capital to ensure that they are consistent with the regulatory developments contained in Basel III. In addition, the FSI is continuing to expand FSI Connect's coverage of insurance risks and related supervisory issues and techniques.

*Other major initiatives*

In 2010, the FSI finalised its latest survey on Basel II implementation around the world. In addition, it awarded its fifth biennial FSI Award for research on an issue of importance to the global supervisory community.

## Research and statistics

The BIS carries out research and analysis on issues of interest to central banks and, increasingly, financial supervisory authorities. Most of this work appears in the Bank's regular outlets, such as the *Annual Report*, the *Quarterly Review* and the *BIS Papers* and *Working Papers* series, as well as in external professional publications and on the Bank's website (www.bis.org). In addition, the research function develops background material for meetings of senior central bankers and provides secretariat and analytical services to the various groups hosted by the BIS in Basel. It also collects, analyses and disseminates statistical information for central banks and the general public on key elements of the international financial system.

The FSB and the IMF have made recommendations to the G20 regarding data gaps and the financial crisis. Those recommendations, a number of them involving the BIS and some of the Basel-based committees, were endorsed by the G20 in November 2009, and progress and plans for completion were reported back to the G20 by the FSB and the IMF in May 2010.

### *Research focus*

In line with the Bank's mission, the focus of BIS research is on monetary and financial stability. As in the previous year, a principal theme of the work was the policy implications of the global financial crisis. A major strand of this analysis addressed the implications of the crisis for bank regulation and supervision and economic activity. The analysis explored the short-term and long-term implications of Basel III for the real economy as well as the design of the macroprudential overlay of the new standards, including the identification of systemically important banks and options for countercyclical capital schemes. This work was largely carried out in support of the Basel Committee on Banking Supervision, but some of the more technical analyses were also released in the *BIS Working Papers* series.

A second strand of the crisis-related work explored possible improvements in financial statistics that could strengthen the monitoring of systemic risks. Several studies examined how the BIS international banking statistics could help in this context and provided the basis for data collection exercises under the aegis of the CGFS. The release of the 2010 Triennial Central Bank Survey of Foreign Exchange and Derivatives Market Activity supported several studies that examined major structural changes in these markets.

A third strand assessed the implications of the financial crisis for the functioning of the financial system, post-crisis macroeconomic trends and monetary policy. Work analysed the behaviour of markets under stress, notably the foreign exchange swap market; the provision of central bank liquidity assistance to markets and institutions; the need for balance sheet and operational restructuring in the financial industry; the deleveraging of private sector balance sheets; and changes in the transmission mechanism of monetary policy.

The BIS research function annually organises a number of conferences and workshops in which participation bridges the worlds of policy, research and business. The leading event, the BIS Annual Conference, brings together senior policymakers, leading academics and market participants. In June 2010, the Ninth BIS Annual Conference addressed the future of central bank governance under post-crisis mandates.

## *International statistical initiatives*

This year, the few remaining BIS member central banks that had not been supplying national data to the BIS Data Bank started to report key macroeconomic statistics on a regular basis. The coverage of the Data Bank continued to expand in areas related to financial stability, including debt issuance by major sectors of the economy and financial positions of non-bank financial institutions. With the approval of the respective central banks, data on residential property prices are posted on the BIS public website.

In June 2010, additional data were reported by central banks from major financial centres to the semiannual collection of statistics on OTC derivatives, including on transactions cleared with central counterparties. Some additional centres will start contributing to this data collection, for which much more detail will become available at the end of the year. More than 50 central banks participated in the 2010 Triennial Central Bank Survey of Foreign Exchange and Derivatives Market Activity; a special effort was made to improve the timeliness of the publication of the data. In May 2011, the BIS was scheduled to release a new online database on its website to better disseminate its international banking statistics.

The Inter-Agency Group on Economic and Financial Statistics, which consists of the BIS, the ECB, Eurostat, the IMF, the OECD, the United Nations and the World Bank, has been tasked to follow up on a number of the recommendations made by the FSB and the IMF – and endorsed by the G20 in November 2009 – regarding data gaps revealed by the financial crisis.

In May 2010, the Working Group on Securities Databases, which consists of the BIS, the ECB and the IMF, released the second part of a *Handbook on Securities Statistics*, which covers holdings of debt securities.

The BIS is represented in a number of other international committees focused on statistics. All these groups worked during the year to address the information gaps revealed by the financial turmoil. Together with the IMF, the OECD and the World Bank, the BIS maintains the Joint External Debt Hub, which consolidates information on external debt from creditor and debtor sources. The BIS co-sponsors the Statistical Data and Metadata Exchange (SDMX) programme, which produces and maintains technical standards and content-oriented guidelines for the dissemination of statistical information. The BIS, other international organisations and various central banks are using SDMX to provide their statistics on their websites in standardised electronic formats and to efficiently exchange data bilaterally.

## Other central bank initiatives to which the BIS lends support

The BIS contributes to the activities of regional central bank groupings by providing speakers with relevant expertise for their meetings. During the past year, such speakers, including those from the secretariats of the Basel-based groups and the BIS Representative Offices, contributed to events organised by:

- the Center for Latin American Monetary Studies (inflation measurement, monetary policy, payment systems, reserve management);
- the South East Asian Central Banks (SEACEN) Research and Training Centre (payment systems, risk management, macroeconomic and monetary policy management, central bank communication strategy, asset price inflation, financial markets, reserve management);
- the Southern African Development Community central banks (capital flows);
- the Macroeconomic and Financial Management Institute of Eastern and Southern Africa (financial market development, payment systems, portfolio management); and
- the Centre Africain d'Études Supérieures en Gestion (Masters in Banking and Finance programme).

BIS experts also contributed to events organised by:

- the Deutsche Bundesbank;
- the Bank of France's International Banking and Finance Institute;
- the Bank of England's Centre for Central Banking Studies; and
- the Bank of Japan.

## Financial services of the Bank

The BIS offers a wide range of financial services tailored specifically to assist central banks and other official monetary authorities in the management of their foreign reserves. Some 140 such institutions, as well as a number of international organisations, make active use of these services.

Safety and liquidity are the key features of the BIS's credit intermediation services, which are supported by a rigorous internal risk management framework. In accordance with best practice, a separate risk control unit reporting directly to the Deputy General Manager monitors the Bank's credit, liquidity and market risks. Similarly, a compliance and operational risk unit controls the Bank's operational risks.

### *Scope of services*

In response to the diverse – and constantly evolving – needs of central banks, the BIS offers an extensive array of investment possibilities in terms of currency denomination, maturity and liquidity. In addition to traditional money market placements such as sight/notice accounts and fixed-term deposits, the Bank offers tradable instruments (Fixed-Rate Investments at the BIS – FIXBIS, and Medium-Term Instruments – MTIs), in maturities ranging from one week to five years, and structured products with embedded optionality. The BIS also provides short-term liquidity facilities and extends credit to central banks, usually on a collateralised basis. The Bank also acts as trustee and collateral agent (see below).

The Bank transacts foreign exchange and gold on behalf of its customers, providing access to a large liquidity base in the context of, for example, regular rebalancing of reserve portfolios or major changes in reserve currency allocation. The foreign exchange services of the Bank encompass spot transactions in major currencies and Special Drawing Rights (SDR), as well as swaps, outright forwards, options and dual currency deposits (DCDs). In addition, the Bank provides gold services such as sight accounts, fixed-term deposits, earmarked accounts, upgrading and refining, and location exchanges.

The BIS provides asset management services in sovereign securities and high-grade credit fixed income instruments. These may take the form of either a dedicated portfolio mandate negotiated between the BIS and a customer or an open-end fund structure – the BIS Investment Pool (BISIP) – allowing customers to invest in a common pool of assets. Both investment structures are offered as either single currency or multicurrency mandates in the world's major reserve currencies: the US dollar, euro, sterling and yen. For multicurrency mandates, the investor can choose from portfolios that are either hedged back into the base currency or left unhedged.

Dedicated mandates are designed according to each customer's preferences with regard to investment guidelines and benchmarks. In contrast, BISIPs are similar to mutual funds or unit trust funds but specifically cater to the investment criteria typical of central banks and international institutions. The two Asian Bond Funds, ABF1 and ABF2, are administered by the BIS under the BISIP umbrella: ABF1 is managed by the BIS and ABF2 by a group of external fund managers.

BIS financial services are provided from two linked trading rooms: one in Basel, at the Bank's head office, and one in Hong Kong SAR, at its Asian Office.

The Banking Department of the BIS also hosts global and regional meetings, seminars and workshops on reserve management issues. These meetings facilitate the exchange of knowledge and experience among reserve managers and promote the development of investment and risk management capabilities in central banks and international organisations.

## *Financial operations in 2010/11*

In 2010/11, financial markets started to settle into a calmer mode despite some bouts of high volatility and weak investor confidence. Against this steadier background, the Bank's customer currency deposit base reached SDR 207.1 billion at the end of 2010/11, representing an increase of SDR 11.3 billion during the financial year.

The total balance sheet of the BIS increased by SDR 2.2 billion, following a marginal increase of SDR 3.5 billion in the previous year. As a result, the balance sheet total at 31 March 2011 was SDR 261.1 billion.

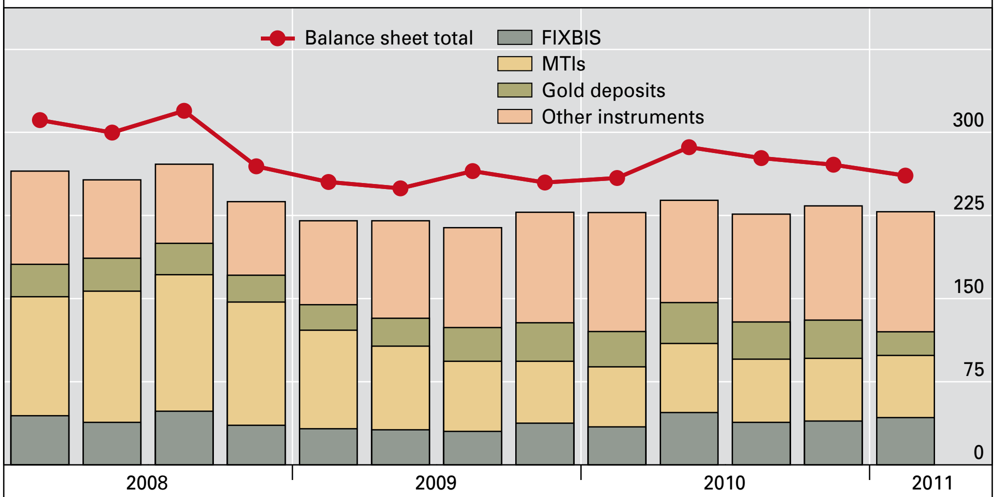
### *Liabilities*

Customer currency and gold placements constitute the largest share of total liabilities (see graph). On 31 March 2011, customer placements (excluding repurchase agreements) amounted to SDR 228.4 billion, compared with SDR 227.8 billion at the end of 2009/10. This net increase resulted from the combined effect of a decrease in gold deposits and an increase in customer currency deposits.

Around 91% of customer placements are denominated in currencies, with the remainder in gold. Currency deposits increased from SDR 195.8 billion a year ago to SDR 207.1 billion at end-March 2011. That balance represents some 3.1% of the world's total foreign exchange reserves of nearly SDR 6.2 trillion, up from SDR 5.7 trillion at end-March 2010.[9] The share of currency placements

Balance sheet total and customer placements by product

End-quarter figures, in billions of SDR




The sum of the bars indicates total customer placements.

[9] Funds placed by institutions for which foreign exchange reserves data are not available are excluded from the calculation.

denominated in US dollars was 68%, while euro- and sterling-denominated funds accounted for 19% and 5%, respectively.

The net increase in customer currency placements resulted mainly from the combined increases of 14%, 25% and 4% in investments in fixed-term deposits, FIXBIS and MTIs, respectively, and a decrease of 38% in sight and notice accounts.

Gold deposits amounted to SDR 21.3 billion at end-March 2011, a decrease of SDR 10.8 billion over the financial year.

A breakdown of placements with the BIS by geographical region shows that Asian customers account for the highest share.

### *Assets*

Most of the assets held by the BIS consist of government and quasi-government securities, including reverse repurchase agreements and, to an extent similar to that in the previous financial year, investments with highly rated commercial banks of international standing. In addition, the Bank owned 119 tonnes of fine gold at 31 March 2011. The Bank's credit exposure is managed in a conservative manner, with almost all of it rated A– or higher at 31 March 2011 (see note 3. "Credit risk", in the "Risk management" section of the financial statements).

The Bank's holdings of currency assets totalled SDR 209.3 billion on 31 March 2011, up from SDR 199.0 billion at the end of the previous financial year (see note 5 to the financial statements).

The Bank uses various derivative instruments to manage its assets and liabilities efficiently (see note 7 to the financial statements).

## *Trustee for international government loans*

In conformity with the agreements in force, the Bank continued to perform its functions as trustee for the funding bonds 1990–2010 of the Dawes and Young Loans (for details, see the BIS's *63rd Annual Report* of June 1993).

For all funding bonds 1990–2010, the financial year 2009/10 ended on 3 October 2010, on which date all the outstanding funding bonds fell due for redemption.

The Deutsche Bundesbank, as paying agent, notified the Bank that in 2010 the Bundesamt für zentrale Dienste und offene Vermögensfragen (BADV – Federal Office for Central Services and Unresolved Property Issues) had arranged for payment of approximately €90.4 million, covering interest payments for the maturity dates of 3 April 2010 and 3 October 2010 and the final redemption due on 3 October 2010. Redemption values and other details were published by the BADV in the *Bundesanzeiger* (Federal Gazette).

The following table shows the position with regard to both loans upon final redemption.

Drawings and final redemption payments were made for the most part in euros at the Deutsche Bundesbank, Frankfurt am Main, in its capacity as principal paying agent.

| Loans[1] | | Issue of bonds in 1990 | Drawings 1996–2009 | Final redemption on 3 October 2010 |
|---|---|---|---|---|
| Dawes Loan | | | | |
| Pound sterling tranches: | | | | |
| Belgian/Dutch/French/Swiss[2] | GBP | 1,500,000 | 525,000 | 975,000 |
| American | USD | 15,400,000 | 5,390,000 | 10,010,000 |
| British[2] | GBP | 2,400,000 | 840,000 | 1,560,000 |
| Swedish | SEK | 4,100,000 | 1,435,000 | 2,665,000 |
| Swiss | CHF | 3,500,000 | 1,225,000 | 2,275,000 |
| Young Loan | | | | |
| American | USD | 16,300,000 | 2,852,500 | 13,447,500 |
| Belgian | BEF | 45,000,000 | 7,875,000 | 37,125,000 |
| British | GBP | 4,600,000 | 805,000 | 3,795,000 |
| Dutch | NLG | 14,000,000 | 2,450,000 | 11,550,000 |
| French | FRF | 86,000,000 | 15,050,000 | 70,950,000 |
| German | DEM | 8,500,000 | 1,487,500 | 7,012,500 |
| Swedish | SEK | 24,000,000 | 4,200,000 | 19,800,000 |
| Swiss | CHF | 16,500,000 | 2,887,500 | 13,612,500 |

[1] All amounts are nominal values. [2] The pound sterling issues existed in two tranches: one for the Belgian, Dutch, French and Swiss issues, and one for the British.

Over the period 1996–2009, a total of 14 redemptions were made by means of drawings. Thus, with an annual redemption rate of 2.5% (1.25%) of the issue value of the Dawes Loan (Young Loan) funding bonds, a total of 35% (17.5%) of the issue value had been redeemed by 3 October 2009. Accordingly, the final redemption due in the following year on 3 October 2010 amounted to 65% (82.5%) of the issue value.[10]

## Representative Offices

The BIS has a Representative Office for Asia and the Pacific (the Asian Office), located in the Hong Kong Special Administrative Region of the People's Republic of China; and a Representative Office for the Americas (the Americas Office), located in Mexico City. The Representative Offices promote cooperation within each region by organising meetings, conducting policy research and fostering the exchange of information and data. The Asian Office also provides banking services to the region's monetary authorities.

### *The Asian Office*

With strong support from the BIS shareholding central banks in the Asia-Pacific region, the Asian Office took on a new research programme while continuing to co-organise high-level policy meetings in the region and to offer its specialised banking services.

[10] See the BIS's *50th Annual Report* of June 1980 with respect to the Bank's reservations regarding the application by the BADV of the exchange guarantee clause for the Young Loan, which reservations also extend to the funding bonds 1990–2010.

*The Asian Consultative Council*

The Asian Consultative Council (ACC), comprising the Governors of the 12 BIS shareholding central banks in the region,[11] helps guide the activities of the Asian Office and reports to the BIS Board on those activities. In October, Zeti Akhtar Aziz, Governor of the Central Bank of Malaysia, completed her term as chair of the ACC, and the BIS Board appointed Masaaki Shirakawa, Governor of the Bank of Japan, to serve as chair for the next two years.

At its semiannual meeting in June 2010, the Council endorsed a BIS proposal for a two-year research strategy to be carried out by the Asian Office. At its January 2011 meeting, the Council discussed the progress of the research and offered suggestions to help the Office pursue the strategy more effectively.

*Two-year research strategy for the Asian Office*

The research strategy addresses two themes of high relevance to ACC central banks: on the monetary side, the role of central bank balance sheets in monetary policy and exchange rate issues; and on the financial side, property prices. Much of this work is being carried out in collaboration with academics and central bank researchers, and the effort will culminate in research conferences.

The research on the implications of the size and structure of central bank balance sheets addresses four topics: (i) the implications of prolonged intervention in currency markets; (ii) modelling the balance sheet transmission mechanism; (iii) international spillovers of monetary policy; and (iv) the use of reserve requirements. The conference to present this research is scheduled for late 2011.

The research on property markets in the region covers four broad issues: (i) measurement and valuation; (ii) housing finance systems; (iii) the relationship of property markets to the health of the banking sector; and (iv) the ability of various policy instruments to influence property prices and market activity. A research workshop will be held jointly with the Monetary Authority of Singapore in September 2011, and the conference to present completed work is scheduled for late 2012.

The Asian Office has engaged in collaborative research with most BIS shareholding central banks in the region as well as with regional organisations of central banks. The work has fed into the numerous meetings organised by the Asian Office and produced several articles in refereed journals and the major BIS publications.

*The Special Governors' Meeting and other high-level meetings in Asia*

The Asian Office organised 14 high-level policy meetings in the region during the period. Each meeting was held jointly with a central bank in the region or with a regional body of central banks, such as the Executives' Meeting of East Asia-Pacific Central Banks (EMEAP) and the South East Asian Central Banks (SEACEN) Research and Training Centre.

[11] The central banks of Australia, China, Hong Kong SAR, India, Indonesia, Japan, Korea, Malaysia, New Zealand, the Philippines, Singapore and Thailand.

The annual Special Governors' Meeting was organised jointly with the Bank of Japan and held in Kyoto in January 2011. The event gathered together the Governors of the major central banks in the region and other Governors from around the world. The Governors discussed the domestic and international implications of the expansion of central bank balance sheets in Asia. For the first time, the event also included a meeting of the Governors with the chief executive officers of large financial institutions in the region, in which views were exchanged on the evolving business models of banking in Asia.

Other high-level events included the June 2010 meeting of the Working Party on Monetary Policy in Asia, co-hosted by the People's Bank of China in Xi'an; the September 2010 BIS meeting on Monetary Policy Operating Procedures, co-hosted by the Bangko Sentral ng Pilipinas in Manila; the November 2010 Sixth High-Level Seminar on Financial Markets, co-hosted by the Bank of Japan in Hong Kong; the January 2011 BOK-BIS Conference on Macroprudential Regulation and Policy, co-hosted by the Bank of Korea in Seoul; and the January 2011 SEACEN-BIS Exco Seminar, co-hosted by the National Bank of Cambodia in Phnom Penh.

### *Banking activity and the Asian Bond Funds*

Ongoing concerns about the global economic and financial environment led central banks in the region to remain cautious in their reserve portfolio management and to rely especially on the short-term liquid instruments offered by the BIS Banking Department.

As fund administrator, the BIS continued to support the second Asian Bond Fund (ABF2), an EMEAP initiative to foster the development of local currency bond markets. At the end of March 2011, the combined size of the funds stood at $4.0 billion, an increase from $3.5 billion at the end of March 2010. Private sector investment amounted to $1.1 billion, of which investments in the Pan Asia Bond Index Fund (PAIF) accounted for about 86% and investments in the eight single-market funds the remainder. The total return on the PAIF from its inception on 7 July 2005 to the end of March 2011 was 50.5%, which compared favourably with the 31.9% return on a US Treasury index of similar duration.

## *The Americas Office*

The Americas Office, together with staff at the BIS head office, is monitoring the way capital inflows may be influencing regional monetary policy and how the new recommendations to enhance key supervisory standards and strengthen financial stability will affect local economies. Within the region, the Office is disseminating BIS research and analysis on these and related topics.

The Office's work with BIS member banks, non-shareholding central banks, regulatory authorities and the academic community generated several publications this year, including "Currency collapses and output dynamics: a long-run perspective", "Monetary policy in the presence of informal labor markets" and "The use of reserve requirements as a policy instrument in Latin America", all available on the Americas Office pages of the BIS website.

At the November 2010 annual meeting of the Latin American and Caribbean Economic Association (LACEA), the Americas Office and the BIS Monetary and Economic Department organised a discussion with academics, regional central bank directors and former Governors. They also sponsored a session on each of two contributed papers, one on the implications of global factors for monetary policies in emerging market economies and the other on financial stability considerations in monetary frameworks.

The Office co-organised and contributed to meetings at regional central banks, including the September 2010 meeting of the Working Party on Monetary Policy in Latin America, convened at the Central Bank of Brazil, and offered support to several training events organised by the BIS's Financial Stability Institute in cooperation with regional groupings of supervisors. In October 2010, the Office hosted and co-chaired a regional meeting of heads of internal audit from central banks in the Americas; and in December 2010, it hosted a meeting in Mexico City on the future of international banking, organised jointly by the BIS and the Bank of Spain. The Office provided speakers to, or participated in, various conferences and meetings convened by regional central banks and research organisations.

*The Consultative Council for the Americas*

The Office serves as the secretariat to the Consultative Council for the Americas (CCA). The CCA, which comprises the Governors of the six BIS member central banks in the Americas,[12] was established in May 2008 as an advisory committee to the BIS Board of Directors. Henrique de Campos Meirelles chaired the CCA from March 2010 until the end of his term as Governor of the Central Bank of Brazil, on 1 December 2010. In January 2011, the BIS Board appointed José de Gregorio, Governor of the Central Bank of Chile, to a two-year term as chair. CCA members are regularly informed of the work of the BIS and the Americas Office in the region and provide valuable guidance on current and possible future work at the BIS of interest to the Americas.

## Governance and management of the BIS

The governance and management of the Bank are conducted at three principal levels:

- the General Meeting of BIS member central banks;
- the BIS Board of Directors; and
- BIS Management.

The BIS has its head office in Basel, Switzerland. At the end of the 2010/11 financial year, the BIS employed 604 staff members from 53 countries.

### *The General Meeting of BIS member central banks*

Fifty-six central banks and monetary authorities are currently members of the BIS. These 56 institutions have rights of voting and representation at General

[12] The central banks of Argentina, Brazil, Canada, Chile, Mexico and the United States.

Meetings. The Annual General Meeting (AGM) is held no later than four months after 31 March, the end of the BIS financial year. The AGM decides the distribution of the dividend and profit of the BIS, approves the annual report and the accounts of the Bank, makes adjustments in the allowances paid to Board members and selects the Bank's external auditors.

### *The BIS Board of Directors*

Consisting of 19 members, the Board of Directors is assisted by four committees of Board members: the Administrative Committee, the Audit Committee, the Banking and Risk Management Committee, and the Nomination Committee. The main responsibilities of the Board are determining the strategic and policy direction of the BIS and supervising the Bank's Management.

Hans Tietmeyer retired from the Board of Directors at the end of his term, 31 December 2010. He had been a member of the Board since 1993 and had served as its Vice-Chairman since 2003. At its January 2011 meeting, the BIS Board elected Masaaki Shirakawa, Governor of the Bank of Japan, to succeed Mr Tietmeyer as Vice-Chairman for a three-year term commencing on 10 January 2011. At the same meeting, the Board appointed Philipp Hildebrand, Chairman of the Governing Board of the Swiss National Bank, to succeed Mr Tietmeyer as Chairman of the Bank's Administrative Committee with effect from 10 January 2011.

Henrique de Campos Meirelles stepped down as Governor of the Central Bank of Brazil, and therefore as a member of the BIS Board, at the end of December 2010. In January 2011, the Board elected Agustín Carstens, Governor of the Bank of Mexico, as a member of the Board for the remainder of Mr Meirelles' term.

In March 2011, the Board re-elected Stefan Ingves, Governor of Sveriges Riksbank, for a further period of three years ending on 31 March 2014.

Baron Guy Quaden retired as Governor of the National Bank of Belgium at the end of March 2011. Luc Coene succeeded Baron Quaden as Governor on 1 April 2011 and became an ex officio member of the Board of Directors. Mr Coene subsequently appointed Baron Quaden as a member of the Board until 31 March 2014.

Axel Weber stepped down as President of the Deutsche Bundesbank, and therefore as a member of the BIS Board, on 30 April 2011. On 1 May 2011, Jens Weidmann succeeded Mr Weber at the Deutsche Bundesbank and became an ex officio member of the Board.

Christian Noyer, Governor of the Bank of France, reappointed Jean-Pierre Landau, Second Deputy Governor of the Bank of France, as a member of the BIS Board until 31 December 2011. Mervyn King, Governor of the Bank of England, reappointed Paul Tucker, Deputy Governor of the Bank of England, as a member of the Board until 31 December 2011.

BIS shareholding institutions and members of the BIS Board of Directors are listed on the following pages.

# BIS member central banks

Bank of Algeria

Central Bank of Argentina

Reserve Bank of Australia

Central Bank of the Republic of Austria

National Bank of Belgium

Central Bank of Bosnia and Herzegovina

Central Bank of Brazil

Bulgarian National Bank

Bank of Canada

Central Bank of Chile

People's Bank of China

Croatian National Bank

Czech National Bank

National Bank of Denmark

Bank of Estonia

European Central Bank

Bank of Finland

Bank of France

Deutsche Bundesbank (Germany)

Bank of Greece

Hong Kong Monetary Authority

Magyar Nemzeti Bank (Hungary)

Central Bank of Iceland

Reserve Bank of India

Bank Indonesia

Central Bank of Ireland

Bank of Israel

Bank of Italy

Bank of Japan

Bank of Korea

Bank of Latvia

Bank of Lithuania

National Bank of the Republic of Macedonia

Central Bank of Malaysia

Bank of Mexico

Netherlands Bank

Reserve Bank of New Zealand

Central Bank of Norway

Bangko Sentral ng Pilipinas (Philippines)

National Bank of Poland

Bank of Portugal

National Bank of Romania

Central Bank of the Russian Federation

Saudi Arabian Monetary Agency

National Bank of Serbia

Monetary Authority of Singapore

National Bank of Slovakia

Bank of Slovenia

South African Reserve Bank

Bank of Spain

Sveriges Riksbank (Sweden)

Swiss National Bank

Bank of Thailand

Central Bank of the Republic of Turkey

Bank of England

Board of Governors of the Federal Reserve System (United States)

# Board of Directors

Christian Noyer, Paris
Chairman of the Board of Directors

Masaaki Shirakawa, Tokyo
Vice-Chairman

Ben S Bernanke, Washington
Mark Carney, Ottawa
Agustín Carstens, Mexico City
Luc Coene, Brussels
Mario Draghi, Rome
William C Dudley, New York
Philipp Hildebrand, Zurich
Stefan Ingves, Stockholm
Mervyn King, London
Jean-Pierre Landau, Paris
Guy Quaden, Brussels
Fabrizio Saccomanni, Rome
Jean-Claude Trichet, Frankfurt am Main
Paul Tucker, London
Jens Weidmann, Frankfurt am Main
Nout H E M Wellink, Amsterdam
Zhou Xiaochuan, Beijing

*Alternates*

Mathias Dewatripont or Jan Smets, Brussels
Andreas Dombret or Karlheinz Bischofberger, Frankfurt am Main
Paul Fisher or Michael Cross, London
Pierre Jaillet or Christian Durand, Paris
Ignazio Visco, Rome
Janet L Yellen or D Nathan Sheets, Washington

*Committees of the Board of Directors*

Administrative Committee, chaired by Philipp Hildebrand
Audit Committee, chaired by Mark Carney
Banking and Risk Management Committee, chaired by Stefan Ingves
Nomination Committee, chaired by Christian Noyer

## *BIS Management*

BIS Management is under the overall direction of the General Manager, who is responsible to the Board of Directors for the conduct of the Bank. The General Manager is advised by the Executive Committee of the BIS, which consists of the General Manager as chair, the Deputy General Manager, the Heads of the three BIS departments – the General Secretariat, the Banking Department and the Monetary and Economic Department – and the General Counsel.

Other senior officials are the Deputy Heads of the departments and the Chairman of the Financial Stability Institute.

| | |
|---|---|
| General Manager | Jaime Caruana |
| Deputy General Manager | Hervé Hannoun |
| Secretary General and Head of General Secretariat | Peter Dittus |
| Economic Adviser and Head of Monetary and Economic Department | Stephen G Cecchetti |
| Head of Banking Department | Günter Pleines |
| General Counsel | Diego Devos |
| Deputy Secretary General | Jim Etherington |
| Deputy Head of Banking Department | Louis de Montpellier |
| Deputy Head of Monetary and Economic Department (Research and Statistics) | Claudio Borio |
| Deputy Head of Monetary and Economic Department (Policy, Coordination and Administration) | Philip Turner |
| Chairman, Financial Stability Institute | Josef Tošovský |

Deputy Secretary General Jim Etherington and Deputy Head of Banking Department Louis de Montpellier were each reappointed for a five-year period.

### *Bank budget policy*

The process of formulating the Bank's expenditure budget for the next financial year starts about six months in advance with the setting by Management of a broad business orientation and financial framework. Within this context, business areas specify their plans and the corresponding resource requirements. The process of reconciling detailed business plans, objectives and overall resource availability culminates in a draft financial budget. The budget must be approved by the Board before the start of the financial year.

The budget distinguishes between administrative and capital expenditures. In common with organisations similar to the BIS, Management and staff expenditure – including remuneration, pensions, and health and accident insurance – amounts to around 70% of administrative expenditure. The other major expenditure categories, each accounting for about 10% of administrative spending, are information technology (IT), telecommunications, and building and equipment. Capital spending mainly relates to building expenses and IT investment and can vary significantly from year to year. Most of the Bank's administrative and capital expenditure is incurred in Swiss francs.

Administrative expenditure before depreciation[13] for the financial year 2010/11 amounted to 253.7 million Swiss francs, 3.0% below the budget of 261.6 million Swiss francs, while capital expenditure, at 21.7 million Swiss francs, was 1.8 million under budget. The largest sources of the underspending in administrative expenditure were lower than budgeted management and staff costs and IT and telecommunications spending.

Administrative and capital expenditure in 2010/11 reflected the main priority in the budget, which was to further reinforce the Bank's response to the global financial crisis in the following areas:

- Human and financial resources devoted to financial stability issues were increased by the creation of additional staff positions to support the work of the Financial Stability Board (FSB), the Basel Committee on Banking Supervision (BCBS) and the Committee on the Global Financial System (CGFS). A key achievement was the completion of the new Basel III reform package and its endorsement by the G20. This was the outcome of major efforts by the BCBS, the FSB and the BIS's Monetary and Economic Department.
- In the Banking Department and the Risk Control, Finance and Compliance units, dealing with the aftermath of the financial crisis was the main priority. Work in the banking business was oriented towards carefully managing the balance sheet and enhancing risk management, valuation, operational controls and management accounting.

Also in 2010/11, the Banking Department started work on the asset management infrastructure project, which will further enhance data management, compliance checking, portfolio analysis, order management and trade processing.

In March 2011, the Board approved a 2.6% increase in the administrative budget for the financial year 2011/12, to 268.5 million Swiss francs. It approved an increase of 3.1 million Swiss francs in the capital budget, to 26.6 million.

The Bank's business plan, on which the proposed administrative budget for 2011/12 is based, builds on the achievements in 2010/11 and gives priority to further enhancing financial stability activities. It allocates additional human and financial resources to deal with the expanding financial stability workload, particularly in the FSB, the BCBS and the Committee on Payment and Settlement Systems. The additional work includes disseminating the Basel III package to the global community of central banks and financial supervisors

[13] The Bank's budgetary accounting is cash-based and excludes certain financial accounting adjustments, principally relating to retirement benefit obligations, which take into account financial market and actuarial developments. These additional factors are included under "Operating expense" disclosed in the profit and loss account (see "Net profit and its distribution").

and enhancing the Bank's statistical capacity for the monitoring of financial markets and institutions.

Strengthening the resilience of BIS banking activities based on appropriate levels of profitability and financial risk from a medium-term perspective will be the main priority of the Banking Department and the Risk Control, Finance and Compliance units. Additional resources were also made available in the budget to complete the asset management infrastructure project started in 2010/11.

*Bank remuneration policy*

The jobs performed by BIS staff members are assessed on the basis of a number of objective criteria, including qualifications, experience and responsibilities, and are classified into distinct job grades. The job grades are associated with a structure of salary ranges. Every three years, a comprehensive survey benchmarks BIS salaries against compensation in comparable institutions and market segments. When benchmarking BIS salaries against comparators, the Bank focuses on the upper half of market compensation in order to attract highly qualified staff. The analysis takes into account differences in the taxation of compensation for the staff of the surveyed institutions. The most recent survey took place in the second half of 2010. As of 1 July 2011, it will result in an alignment of the midpoints of the Bank's salary ranges with the observed market benchmarks.

In years between comprehensive salary surveys, the salary structure is adjusted on the basis of the rate of inflation in Switzerland and the weighted average change in real wages in advanced economies. In view of the negative inflation and real salary growth in the reference period, the salary structure was reduced by 1% on 1 July 2010. Movements of salaries of individual staff members within the ranges of the salary structure are based on performance.

Through the Bank, BIS staff members have access to a contributory health insurance plan and a contributory defined benefit pension plan. Non-locally hired, non-Swiss staff members recruited for a position at the Bank's headquarters, including senior officials, are entitled to an expatriation allowance. It currently amounts to 14% of annual salary for unmarried staff members and 18% for married staff members, subject to a ceiling. Expatriate staff members are also entitled to receive an education allowance for their children subject to certain conditions. In the Representative Offices, the BIS makes a distinction between staff members on an international assignment from the headquarters and staff members recruited directly for a position in a Representative Office. The employment conditions of the former are determined in accordance with the Bank's international assignment policy. For staff recruited directly, employment conditions are aligned with those in the market in which the Office is located, but they include access to the same health insurance and pension plans available to staff engaged at the Bank's headquarters.

The salaries of senior officials are regularly benchmarked against compensation in comparable institutions and market segments. As with the survey for other staff, the most recent executive compensation survey took place in the second half of 2010. The results confirmed the appropriateness of the current practice of annually adjusting the salaries of senior officials for the rate of Swiss inflation.

As of 1 July 2010, the annual remuneration of senior officials, before expatriation allowances, is based on the following salary structure:

- General Manager[14] 758,600 Swiss francs
- Deputy General Manager 641,900 Swiss francs
- Heads of Department 583,550 Swiss francs

The Annual General Meeting approves the remuneration of members of the Board of Directors, with adjustments taking place every three years. The total fixed annual remuneration paid to the Board of Directors was 1,049,520 Swiss francs as at 1 April 2011. In addition, Board members receive an attendance fee for each Board meeting in which they participate. Assuming the full Board is represented in all Board meetings, the annual total of these attendance fees amounts to 973,788 Swiss francs.

## Net profit and its distribution

The Bank recorded a net profit of SDR 816.0 million for the 81st financial year, ended 31 March 2011. This result represents a return to a more normal level of profitability in comparison with the exceptionally high profit of SDR 1,859.8 million recorded for the preceding financial year, which was achieved against the background of recovery in global financial markets, particularly in the credit markets, where many spreads against Libor had narrowed back to pre-September 2008 levels. The principal factors behind the 2010/11 result are discussed below.

### *Principal factors behind the 2010/11 profit*

The financial year 2010/11 was marked by changeable global financial market conditions. In the first quarter of the financial year, tensions in the euro zone credit markets resulted in widened credit spreads against Libor for the debt instruments in the Bank's borrowed funds credit portfolios. In the second quarter, the tensions eased and credit spreads narrowed somewhat. This quarterly pattern of change in euro zone tensions and credit spreads in the first half of the financial year was repeated in the second half. Money market and foreign exchange spreads were, however, more stable than in the previous three financial years.

Net interest income amounted to SDR 1,465.4 million in 2010/11, compared with SDR 1,431.2 million in the preceding financial year. This increase was mainly attributable to:

- a 2.7% increase in the average volume of currency deposits from customers; and

[14] In addition to the basic salary, the General Manager receives an annual representation allowance and enhanced pension rights.

- the impact of early repurchases of Medium-Term Instrument (MTI) liabilities and the associated hedging arrangements. This increase is offset by an equivalent loss within net valuation movements.[15]

The impact of these positive factors was reduced by narrowing intermediation margins in the second half of the financial year.

Net valuation movements amounted to a loss of SDR 509.2 million in contrast to a gain of SDR 520.5 million last year.

The valuation loss in 2010/11 was mainly attributable to:

- the impact of MTI hedging mentioned above; and
- widening credit spreads on euro zone debt instruments held by the Bank's credit portfolios.

Operating expense (see note 24 to the financial statements) amounted to SDR 205.0 million, 7.4% above the preceding year's figure of SDR 190.8 million. Expressed in Swiss francs, the currency in which most of the Bank's administrative expenditure is incurred, operating expense rose by 1.1%. Administrative expense before depreciation, at SDR 190.8 million, exceeded the previous year's figure of SDR 177.7 million by 7.4%. The depreciation charge of SDR 14.2 million was 9.2% above the previous year's level of SDR 13.1 million.

After taking into account the above factors, the Bank's operating profit amounted to SDR 738.5 million, SDR 1,015.9 million below the SDR 1,754.4 million recorded in 2009/10.

Over the past two financial years, the Bank sold investment securities to align the portfolio with its benchmark duration of three years. The 2010/11 operation, which involved securities that had been acquired when interest rates were higher, produced a net gain of SDR 55.7 million. The sales in 2009/10 generated a net gain of SDR 105.4 million.

The Bank gained SDR 21.8 million on the sale of one tonne of its gold investment assets. The Bank made no such sales in 2009/10.

As a result of these factors, the net profit for 2010/11 amounted to SDR 816.0 million, SDR 1,043.8 million below the preceding year's SDR 1,859.8 million.

### *Movements in equity*

The Bank's revaluation accounts, one for investment securities and one for gold, form part of the Bank's equity. They consist of net realised gains or losses – which are transferred to the profit and loss account – and net unrealised gains or losses.

The securities revaluation account decreased by SDR 197.3 million because of net unrealised losses on investment securities (–SDR 141.6 million),

[15] Holders of MTIs may sell these financial instruments back to the BIS at their current market value. When an MTI is repurchased by the BIS, the corresponding assets and hedging arrangements are retained and are normally refinanced through the issue of new liability financial instruments with similar market risk characteristics. Recent repurchases have taken place in a period when interest rates have been lower than when the repurchased MTIs were originally issued. As a result, the Bank's interest accrual margin has widened because the interest rates paid on the refinanced liabilities are lower than on the original MTIs. This has produced a higher net interest income, but this benefit is offset by a correspondingly lower net valuation movement as the assets and hedging arrangements converge to par value at maturity.

incurred as interest yields began to rise in the second half of the financial year; and, as noted above, because of the transfer to the profit and loss account of realised gains (–SDR 55.7 million) on sales.

The gold revaluation account increased by SDR 650.4 million because of net unrealised gains (+SDR 672.2 million) on the Bank's own gold investment assets, which were attributable to the year-on-year appreciation of gold; and, as noted above, because of the transfer to the profit and loss account of realised gains (–SDR 21.8 million) on the sale of one tonne of gold.

After taking these gains into account, the Bank's total return[16] for 2010/11 was SDR 1,269.1 million. This represented a return of 7.8% on average equity of SDR 16,238 million. In 2009/10, the total return was SDR 2,204.1 million, or 14.9%, on average equity of SDR 14,795 million. Taking into account the payment of the dividend of SDR 374.1 million for 2009/10, the Bank's equity increased by SDR 895.0 million during the year ended 31 March 2011.

## *Proposed dividend*

The Board's review of the BIS dividend policy in 2009/10 took into consideration the Bank's capital needs and the interests of BIS shareholders in obtaining a fair and sustainable return on their investments in BIS shares. In framing the dividend policy, the Board adopted a number of governing principles, which are:

- First, the need for the Bank to maintain a strong capital base at all times, including during financial stress.
- Second, the dividend should be relatively stable, set at a sustainable level and changing in a predictable manner each year.
- Third, while the Bank's dividend policy should provide guidance for the medium term, the dividend should continue to reflect the prevailing financial circumstances of the Bank and should remain an annual decision of the Board.

The dividend policy takes into account the Bank's capital adequacy and leverage ratio requirements. The policy, which is due to be reviewed again in 2014/15, incorporates:

- a normal sustainable dividend, decided ex ante in conformity with the medium-term dividend policy, which would increase by SDR 10 per annum; and
- a supplementary dividend, which would be decided ex post, while keeping leverage and economic capital within desired ranges.

The policy ensures that earnings are retained to augment the Bank's capital at a sufficient rate to support the Bank's business and maintain its capital position relative to the size of the balance sheet and its economic capital requirements. In normal circumstances, it results in a steady progression in annual dividends while retaining the flexibility to be operable in years of low or high profits. In addition, the final approval of the dividend each May coincides with the outcome of the annual economic capital allocation process

[16] The total return is shown as "Total comprehensive income" in the table entitled "Statement of comprehensive income" on page 146 in the financial statements.

(see note 2 of the capital adequacy section of the financial statements), enabling the Board to pay an appropriate dividend while ensuring that the Bank's capital base remains strong.

Consistent with this dividend policy, it is proposed for the financial year 2010/11 to declare a normal dividend of SDR 295 per share, SDR 10 above the normal dividend for 2009/10. Last year, a supplementary dividend of SDR 400 per share was paid in recognition of the exceptionally high net profit. Given the return to a more normal level of profit, no supplementary dividend will be proposed for 2010/11.

## *Proposed distribution of the net profit for the year*

On the basis of Article 51 of the Statutes, the Board of Directors recommends to the Annual General Meeting that the net profit of SDR 816.0 million for the financial year 2010/11 be applied by the General Meeting in the following manner:

(a) SDR 161.1 million to be paid as a normal dividend of SDR 295 per share;

(b) SDR 65.5 million to be transferred to the general reserve fund;[17]

(c) SDR 6.0 million to be transferred to the special dividend reserve fund; and

(d) SDR 583.4 million, representing the remainder of the available net profit, to be transferred to the free reserve fund.

If approved, the dividend could be paid out on 1 July 2011 in any constituent currency of the SDR, or in Swiss francs, according to the instructions of each shareholder named in the Bank's share register on 31 March 2011.

The number of issued and paid-up shares is 547,125. Of these shares, 1,000, namely the suspended shares of the Albanian issue, were held in treasury at 31 March 2011. No dividend will be paid on treasury shares; therefore, the dividend will be paid on 546,125 shares.

## *Report of the auditors*

The Bank's financial statements have been duly audited by Deloitte AG, who have confirmed that they give a true and fair view of the Bank's financial position at 31 March 2011 and the results of its operations for the year then ended. Their report is to be found immediately following the financial statements.

[17] The general reserve fund exceeded four times the Bank's paid-up capital at 31 March 2011. Article 51 of the Bank's Statutes requires that 10% of the profit after payment of the dividend be paid into the general reserve fund until its balance equals five times the paid-up capital.

# Financial statements

as at 31 March 2011

The financial statements on pages 144–208 for the financial year ended 31 March 2011 were approved on 9 May 2011 for presentation to the Annual General Meeting on 26 June 2011. They are presented in a form approved by the Board of Directors pursuant to Article 49 of the Bank's Statutes and are subject to approval by the shareholders at the Annual General Meeting.

| | |
|---|---|
| Jaime Caruana | Hervé Hannoun |
| General Manager | Deputy General Manager |

# Balance sheet

As at 31 March

| *SDR millions* | Notes | **2011** | 2010 |
|---|---|---|---|
| **Assets** | | | |
| Cash and sight accounts with banks | 3 | 329.8 | 1,516.2 |
| Gold and gold loans | 4 | 36,637.2 | 43,039.8 |
| Treasury bills | 5 | 76,932.1 | 84,714.8 |
| Securities purchased under resale agreements | 5 | 51,464.0 | 42,305.9 |
| Loans and advances | 6 | 24,170.4 | 19,288.6 |
| Government and other securities | 5 | 56,987.9 | 53,687.7 |
| Derivative financial instruments | 7 | 5,790.3 | 10,114.7 |
| Accounts receivable | 8 | 8,616.3 | 4,035.7 |
| Land, buildings and equipment | 9 | 190.8 | 189.9 |
| **Total assets** | | **261,118.8** | 258,893.3 |
| **Liabilities** | | | |
| Currency deposits | 10 | 207,085.6 | 195,755.1 |
| Gold deposits | 11 | 21,269.9 | 32,064.1 |
| Derivative financial instruments | 7 | 6,959.5 | 4,187.4 |
| Accounts payable | 12 | 8,758.1 | 10,792.4 |
| Other liabilities | 13 | 375.4 | 319.0 |
| **Total liabilities** | | **244,448.5** | 243,118.0 |
| **Shareholders' equity** | | | |
| Share capital | 14 | 683.9 | 683.9 |
| Statutory reserves | 15 | 12,154.4 | 10,668.7 |
| Profit and loss account | | 816.0 | 1,859.8 |
| Less: shares held in treasury | 16 | (1.7) | (1.7) |
| Other equity accounts | 17 | 3,017.7 | 2,564.6 |
| **Total equity** | | **16,670.3** | 15,775.3 |
| **Total liabilities and equity** | | **261,118.8** | 258,893.3 |

# Profit and loss account

For the financial year ended 31 March

| *SDR millions* | Notes | **2011** | 2010 |
|---|---|---|---|
| Interest income | 19 | 3,324.4 | 4,051.9 |
| Interest expense | 20 | (1,859.0) | (2,620.7) |
| **Net interest income** | | **1,465.4** | 1,431.2 |
| | | | |
| Net valuation movement | 21 | (509.2) | 520.5 |
| **Net interest and valuation income** | | **956.2** | 1,951.7 |
| | | | |
| Net fee and commission income | 22 | 3.1 | 10.7 |
| Net foreign exchange loss | 23 | (15.8) | (17.2) |
| **Total operating income** | | **943.5** | 1,945.2 |
| | | | |
| Operating expense | 24 | (205.0) | (190.8) |
| **Operating profit** | | **738.5** | 1,754.4 |
| | | | |
| Net gain on sales of securities available for sale | 25 | 55.7 | 105.4 |
| Net gain on sales of gold investment assets | 26 | 21.8 | – |
| | | | |
| **Net profit for the financial year** | | **816.0** | 1,859.8 |

| | | | |
|---|---|---|---|
| **Basic and diluted earnings per share (in SDR per share)** | 27 | **1,494.2** | 3,405.4 |

# Statement of comprehensive income

For the financial year ended 31 March

| *SDR millions* | Notes | **2011** | 2010 |
|---|---|---|---|
| **Net profit for the financial year** | | **816.0** | 1,859.8 |
| Unrealised loss on securities available for sale | 17A | (197.3) | (112.5) |
| Unrealised gain on gold investment assets | 17B | 650.4 | 456.8 |
| **Total comprehensive income for the financial year** | | **1,269.1** | 2,204.1 |

# Statement of cash flows

For the financial year ended 31 March

| *SDR millions* | Notes | **2011** | 2010 |
|---|---|---|---|
| **Cash flow from / (used in) operating activities** | | | |
| Interest and similar income received | | 3,591.1 | 4,875.0 |
| Interest and similar expenses paid | | (1,769.2) | (2,522.8) |
| Net fee and commission income | 22 | 3.1 | 10.7 |
| Foreign exchange transaction gain | 23 | 21.5 | 0.3 |
| Operating expenses paid | | (190.8) | (177.6) |
| **Non-cash flow items included in operating profit** | | | |
| Valuation movements on operating assets and liabilities | 21 | (509.2) | 520.5 |
| Foreign exchange translation loss | 23 | (37.3) | (17.5) |
| Change in accruals and amortisation | | (356.5) | (921.2) |
| **Change in operating assets and liabilities** | | | |
| Currency deposit liabilities held at fair value through profit and loss | | 17,500.9 | 3,220.0 |
| Currency banking assets | | (10,882.2) | 6,472.1 |
| Sight and notice deposit account liabilities | | (11,022.2) | (2,839.8) |
| Gold deposit liabilities | | (10,794.2) | 9,012.0 |
| Gold and gold loan banking assets | | 7,042.6 | (17,170.5) |
| Accounts receivable | | 1.5 | (0.7) |
| Other liabilities / accounts payable | | (332.7) | 339.9 |
| Net derivative financial instruments | | 7,096.5 | 1,005.0 |
| **Net cash flow from / (used in) operating activities** | | **(637.1)** | 1,805.4 |
| | | | |
| **Cash flow from / (used in) investment activities** | | | |
| Net change in currency investment assets available for sale | 5B | (829.8) | (606.4) |
| Net change in currency investment assets held at fair value through profit and loss | | (82.9) | 131.1 |
| Net change in gold investment assets | 4B | 32.2 | 3.7 |
| Net purchase of land, buildings and equipment | 9 | (15.1) | (12.1) |
| **Net cash flow from / (used in) investment activities** | | **(895.6)** | (483.7) |

| *SDR millions* | Notes | **2011** | 2010 |
|---|---|---|---|
| **Cash flow from / (used in) financing activities** | | | |
| Dividends paid | | (374.1) | (144.7) |
| **Net cash flow from / (used in) financing activities** | | **(374.1)** | (144.7) |
| | | | |
| **Total net cash flow** | | **(1,906.8)** | 1,177.0 |
| | | | |
| Net effect of exchange rate changes on cash and cash equivalents | | 178.4 | 49.8 |
| Net movement in cash and cash equivalents | | (2,085.2) | 1,127.2 |
| **Net change in cash and cash equivalents** | | **(1,906.8)** | 1,177.0 |
| | | | |
| **Cash and cash equivalents, beginning of year** | 28 | **2,488.8** | 1,311.8 |
| **Cash and cash equivalents, end of year** | 28 | **582.0** | 2,488.8 |

## Movements in the Bank's equity

For the financial year ended 31 March

| *SDR millions* | Notes | Share capital | Statutory reserves | Profit and loss | Shares held in treasury | Other equity accounts | Total equity |
|---|---|---|---|---|---|---|---|
| **Equity at 31 March 2009** | | **683.9** | **10,367.3** | **446.1** | **(1.7)** | **2,220.3** | **13,715.9** |
| Total comprehensive income | 17 | – | – | 1,859.8 | – | 344.3 | 2,204.1 |
| Payment of 2008/09 dividend | | – | – | (144.7) | – | – | (144.7) |
| Allocation of 2008/09 profit | | – | 301.4 | (301.4) | – | – | – |
| **Equity at 31 March 2010** | | **683.9** | **10,668.7** | **1,859.8** | **(1.7)** | **2,564.6** | **15,775.3** |
| Total comprehensive income | 17 | – | – | 816.0 | – | 453.1 | 1,269.1 |
| Payment of 2009/10 dividend – normal | | – | – | (155.6) | – | – | (155.6) |
| Payment of 2009/10 dividend – supplementary | | – | – | (218.5) | – | – | (218.5) |
| Allocation of 2009/10 profit | | – | 1,485.7 | (1,485.7) | – | – | – |
| **Equity at 31 March 2011 per balance sheet before proposed profit allocation** | | **683.9** | **12,154.4** | **816.0** | **(1.7)** | **3,017.7** | **16,670.3** |
| Proposed dividend | 14 | – | – | (161.1) | – | – | (161.1) |
| Proposed transfers to reserves | | – | 654.9 | (654.9) | – | – | – |
| **Equity at 31 March 2011 after proposed profit allocation** | | **683.9** | **12,809.3** | **–** | **(1.7)** | **3,017.7** | **16,509.2** |

At 31 March 2011 statutory reserves included share premiums of SDR 811.7 million (2010: SDR 811.7 million).

## Statement of proposed profit allocation

For the financial year ended 31 March

| *SDR millions* | Notes | 2011 |
|---|---|---|
| **Net profit for the financial year** | | **816.0** |
| Transfer to legal reserve fund | 15 | – |
| | | |
| **Proposed dividend:** | | |
| SDR 295 per share on 546,125 shares | | **(161.1)** |
| | | |
| **Proposed transfers to reserves:** | | |
| | | |
| General reserve fund | 15 | (65.5) |
| Special dividend reserve fund | 15 | (6.0) |
| Free reserve fund | 15 | (583.4) |
| | | |
| **Balance after allocation to reserves** | | **–** |

The proposed profit allocation is in accordance with Article 51 of the Bank's Statutes.

## Movements in the Bank's statutory reserves

For the financial year ended 31 March

| | | | | | | 2011 |
|---|---|---|---|---|---|---|
| *SDR millions* | Notes | Legal reserve fund | General reserve fund | Special dividend reserve fund | Free reserve fund | Total statutory reserves |
| **Balance at 31 March 2010** | | **68.3** | **3,079.9** | **154.0** | **7,366.5** | **10,668.7** |
| Allocation of 2009/10 profit | 15 | – | 148.6 | 12.0 | 1,325.1 | 1,485.7 |
| | | | | | | |
| **Balance at 31 March 2011 per balance sheet before proposed profit allocation** | | **68.3** | **3,228.5** | **166.0** | **8,691.6** | **12,154.4** |
| Proposed transfers to reserves | 15 | – | 65.5 | 6.0 | 583.4 | 654.9 |
| | | | | | | |
| **Balance at 31 March 2011 after proposed profit allocation** | | **68.3** | **3,294.0** | **172.0** | **9,275.0** | **12,809.3** |

# Accounting policies

The accounting policies set out below have been applied to both of the financial years presented unless otherwise stated.

## 1. Scope of the financial statements

These financial statements contain all assets and liabilities that are controlled by the Bank and in respect of which the economic benefits as well as the rights and obligations lie with the Bank.

Assets and liabilities in the name of but not controlled by the Bank and in respect of which the economic benefits as well as the rights and obligations do not lie with the Bank are not included in these financial statements. Information on off-balance sheet assets and liabilities is disclosed in note 31.

## 2. Functional and presentation currency

The functional and presentation currency of the Bank is the Special Drawing Right (SDR) as defined by the International Monetary Fund (IMF).

The SDR is calculated from a basket of major trading currencies according to Rule O–1 as adopted by the Executive Board of the IMF on 30 December 2010 and effective 1 January 2011. As currently calculated, one SDR is equivalent to the sum of USD 0.660, EUR 0.423, JPY 12.1 and GBP 0.111. Prior to 1 January 2011, one SDR was equivalent to the sum of USD 0.632, EUR 0.410, JPY 18.4 and GBP 0.0903. The change in the composition of the SDR basket was such that the values of the SDR under the old and new baskets were equivalent at 31 December 2010 and no significant gains or losses resulted from the change in the weights of the currencies. The composition of the SDR currency basket is subject to review every five years by the IMF; the next review is due to be undertaken in December 2015.

All figures in these financial statements are presented in SDR millions unless otherwise stated.

## 3. Currency translation

Monetary assets and liabilities are translated into SDR at the exchange rates ruling at the balance sheet date. Other assets and liabilities are recorded in SDR at the exchange rates ruling at the date of the transaction. Profits and losses are translated into SDR at an average rate. Exchange differences arising from the retranslation of monetary assets and liabilities and from the settlement of transactions are included as net foreign exchange gains or losses in the profit and loss account.

## 4. Designation of financial instruments

Upon initial recognition the Bank allocates each financial instrument to one of the following categories:

- Loans and receivables
- Financial assets and financial liabilities held at fair value through profit and loss
- Available for sale financial assets
- Financial liabilities measured at amortised cost

The allocation to these categories is dependent on the nature of the financial instrument and the purpose for which it was entered into, as described in Section 5 below.

The resulting designation of each financial instrument determines the accounting methodology that is applied, as described in the accounting policies below. Where the financial instrument is designated as held at fair value through profit and loss, the Bank does not subsequently change this designation.

## 5. Asset and liability structure

Assets and liabilities are organised into two sets of portfolios:

### *A. Banking portfolios*

These comprise currency and gold deposit liabilities and related banking assets and derivatives.

The Bank operates a banking business in currency and gold on behalf of its customers. In this business the Bank takes limited gold price, interest rate and foreign currency risk.

The Bank designates all currency financial instruments in its banking portfolios (other than cash and sight and notice accounts with banks, and sight and notice deposit account liabilities) as held at fair value through profit and loss. The use of fair values in the currency banking portfolios is described in Section 9 below.

All gold financial assets in these portfolios are designated as loans and receivables and all gold financial liabilities are designated as financial liabilities measured at amortised cost.

***B. Investment portfolios***

These comprise assets, liabilities and derivatives relating principally to the investment of the Bank's equity.

The Bank holds most of its equity in financial instruments denominated in the constituent currencies of the SDR, which are managed using a fixed duration benchmark of bonds.

Except for the currency assets described in the next paragraph, currency assets (other than cash and sight and notice accounts with banks) are designated as available for sale. Related securities sold under repurchase agreements are designated as financial liabilities measured at amortised cost.

In addition, the Bank maintains some of its equity in more actively traded portfolios. The currency investment assets in these portfolios are trading assets and as such are designated as held at fair value through profit and loss.

The remainder of the Bank's equity is held in gold. The Bank's own gold holdings are designated as available for sale.

## 6. Cash and sight accounts with banks

Cash and sight accounts with banks are included in the balance sheet at their principal value plus accrued interest where applicable.

## 7. Notice accounts

Notice accounts are short-term monetary assets. They typically have notice periods of three days or less and are included under the balance sheet heading "Loans and advances". They are considered to be cash equivalents for the purposes of the cash flow statement.

Due to their short-term nature, these financial instruments are designated as loans and receivables. They are included in the balance sheet at their principal value plus accrued interest. Interest is included in interest income on an accruals basis.

## 8. Sight and notice deposit account liabilities

Sight and notice deposit accounts are short-term monetary liabilities. They typically have notice periods of three days or less and are included under the balance sheet heading "Currency deposits".

Due to their short-term nature, these financial instruments are designated as financial liabilities measured at amortised cost. They are included in the balance sheet at their principal value plus accrued interest. Interest is included in interest expense on an accruals basis.

## 9. Use of fair values in the currency banking portfolios

In operating its currency banking business, the Bank acts as a market-maker in certain of its currency deposit liabilities. As a result of this activity the Bank incurs realised profits and losses on these liabilities.

In accordance with the Bank's risk management policies, the market risk inherent in this activity is managed on an overall fair value basis, combining all the relevant assets, liabilities and derivatives in its currency banking portfolios. The realised and unrealised profits or losses on currency deposit liabilities are thus largely offset by realised and unrealised losses or profits on the related currency banking assets and derivatives, or on other currency deposit liabilities.

To reduce the accounting inconsistency that would arise from recognising realised and unrealised gains and losses on different bases, the Bank designates the relevant assets, liabilities and derivatives in its currency banking portfolios as held at fair value through profit and loss.

## 10. Currency deposit liabilities held at fair value through profit and loss

As described above, all currency deposit liabilities, with the exception of sight and notice deposit account liabilities, are designated as held at fair value through profit and loss.

These currency deposit liabilities are initially included in the balance sheet on a trade date basis at cost. The subsequent accrual of interest to be paid and amortisation of premiums received and discounts paid are included under the profit and loss account heading "Interest expense" on an effective interest rate basis.

After trade date, the currency deposit liabilities are revalued to fair value, with all realised and unrealised movements in fair value included under "Net valuation movement".

## 11. Currency assets held at fair value through profit and loss

Currency assets include treasury bills, securities purchased under resale agreements, loans and advances, and government and other securities.

As described above, the Bank designates all of the relevant assets in its currency banking portfolios as held at fair value through profit and loss. In addition, the Bank maintains certain actively traded investment portfolios. The currency investment assets in these portfolios are trading assets and as such are designated as held at fair value through profit and loss.

These currency assets are initially included in the balance sheet on a trade date basis at cost. The subsequent accrual of interest and amortisation of premiums paid and discounts received are included in the profit and loss account under "Interest income" on an effective interest rate basis.

After trade date, the currency assets are revalued to fair value, with all realised and unrealised movements in fair value included under "Net valuation movement".

## 12. Currency investment assets available for sale

Currency assets include treasury bills, securities purchased under resale agreements, loans and advances, and government and other securities.

As described above, the Bank designates as available for sale all of the relevant assets in its currency investment portfolios, except for those assets in the Bank's more actively traded investment portfolios.

These currency investment assets are initially included in the balance sheet on a trade date basis at cost. The subsequent accrual of interest and amortisation of premiums paid and discounts received are included in the profit and loss account under "Interest income" on an effective interest rate basis.

After trade date, the currency investment assets are revalued to fair value, with unrealised gains or losses included in the securities revaluation account, which is reported under the balance sheet heading "Other equity accounts". The movement in fair value is included in the statement of comprehensive income under the heading "Unrealised loss on securities available for sale". Realised profits on disposal are included in the profit and loss account under "Net gain on sales of securities available for sale".

## 13. Short positions in currency assets

Short positions in currency assets are included in the balance sheet under the heading "Other liabilities" at fair value on a trade date basis.

## 14. Gold

Gold comprises gold bar assets held in custody at central banks and sight accounts denominated in gold. Gold is considered by the Bank to be a financial instrument.

Gold is included in the balance sheet at its weight in gold (translated at the gold market price and USD exchange rate into SDR). Purchases and sales of gold are accounted for on a settlement date basis. Forward purchases or sales of gold are treated as derivatives prior to the settlement date.

The treatment of realised and unrealised gains or losses on gold is described in Section 17 below.

## 15. Gold loans

Gold loans comprise fixed-term gold loans. Gold loans are included in the balance sheet on a trade date basis at their weight in gold (translated at the gold market price and USD exchange rate into SDR) plus accrued interest.

Accrued interest on gold loans is included in the profit and loss account under "Interest income" on an effective interest rate basis.

## 16. Gold deposits

Gold deposits comprise unallocated sight and fixed-term deposits of gold from central banks.

Unallocated gold deposits provide customers with a general claim on the Bank for delivery of gold of the same weight and quality as that delivered by the customer to the Bank, but do not provide the right to specific gold bars. Unallocated gold deposits are included in the balance sheet on a trade date basis at their weight in gold (translated at the gold market price and USD exchange rate into SDR) plus accrued interest. Accrued interest on gold deposits is included in the profit and loss account under "Interest expense" on an effective interest rate basis.

Allocated (or "earmarked") gold deposits provide depositors with a claim for delivery of the specific gold bars deposited by the customer with the Bank on a custody basis. Beneficial ownership and risk remain with the customer. As such, allocated gold deposit liabilities and the related gold bar assets are not included on the Bank's balance sheet. They are disclosed as off-balance sheet items (see note 31).

## 17. Realised and unrealised gains or losses on gold

The treatment of realised and unrealised gains or losses on gold depends on the designation as described below:

### *A. Banking portfolios, comprising gold deposits and related gold banking assets*

The Bank designates gold loans in its banking portfolios as loans and receivables and gold deposits as financial liabilities measured at amortised cost. The gold derivatives included in the portfolios are designated as held at fair value through profit and loss.

Gains or losses on these transactions in gold are included in the profit and loss account under "Net foreign exchange gain / (loss)" as net transaction gains or losses.

Gains or losses on the retranslation of the net position in gold in the banking portfolios are included under "Net foreign exchange gain / (loss)" as net translation gains or losses.

### *B. Investment portfolios, comprising gold investment assets*

The Bank's own holdings of gold are designated and accounted for as available for sale assets.

Unrealised gains or losses on the Bank's gold investment assets over their deemed cost are taken to the gold revaluation account in equity, which is reported under the balance sheet heading "Other equity accounts". The movement in fair value is included in the statement of comprehensive income under the heading "Unrealised gain on gold investment assets".

For gold investment assets held on 31 March 2003 (when the Bank changed its functional and presentation currency from the gold franc to the SDR) the deemed cost is approximately SDR 151 per ounce, based on the value of USD 208 that was applied from 1979 to 2003 following a decision by the Bank's Board of Directors, translated at the 31 March 2003 exchange rate.

Realised gains or losses on disposal of gold investment assets are included in the profit and loss account as "Net gain / (loss) on sales of gold investment assets".

## 18. Securities sold under repurchase agreements

Where these liabilities are associated with the management of currency assets held at fair value through profit and loss, they are designated as financial instruments held at fair value through profit and loss. Where these liabilities are associated with currency assets available for sale, they are designated as financial liabilities measured at amortised cost.

They are initially included in the balance sheet on a trade date basis at cost. The subsequent accrual of interest is included in the profit and loss account under "Interest expense" on an effective interest rate basis.

After trade date, those liabilities that are designated as held at fair value through profit and loss are revalued to fair value, with unrealised gains or losses included under "Net valuation movement".

## 19. Derivatives

Derivatives are used either to manage the Bank's market risk or for trading purposes. They are designated as financial instruments held at fair value through profit and loss.

Derivatives are initially included in the balance sheet on a trade date basis at cost. The subsequent accrual of interest and amortisation of premiums paid and discounts received are included in the profit and loss account under "Interest income" on an effective interest rate basis.

After trade date, derivatives are revalued to fair value, with all realised and unrealised movements in value included under "Net valuation movement".

Derivatives are included as either assets or liabilities, depending on whether the contract has a positive or a negative fair value for the Bank.

Where a derivative contract is embedded within a host contract which is not accounted for as held at fair value through profit and loss, it is separated from the host contract for accounting purposes and treated as though it were a standalone derivative as described above.

## 20. Valuation policy

The Bank's valuation policy has been approved by the Board of Directors. In this policy the Bank defines how financial instruments are designated, which determines their valuation basis and accounting treatment. This policy is supplemented with detailed valuation procedures.

The majority of the financial instruments on the balance sheet are included at fair value. The Bank defines the fair value of a financial instrument as the amount at which the instrument could be exchanged between knowledgeable, willing parties in an arm's length transaction.

The use of fair values ensures that the financial reporting to the Board and shareholders reflects the way in which the banking business is managed and is consistent with the risk management and economic performance figures reported to Management.

The Bank considers published price quotations in active markets as the best evidence of fair value. Where no published price quotations exist, the Bank determines fair values using a valuation technique appropriate to the particular financial instrument. Such valuation techniques may involve using market prices of recent arm's length market transactions in similar instruments or may make use of financial models. Where financial models are used, the Bank aims at making maximum use of observable market inputs (eg interest rates and volatilities) as appropriate, and relies as little as possible on its own estimates. Such valuation models comprise discounted cash flow analyses and option pricing models.

Where valuation techniques are used to determine fair values, the valuation models are subject to initial approval and periodic review in line with the requirements of the Bank's model validation policy.

The Bank has an independent valuation control function which periodically reviews the value of its financial instruments, taking into account both the accuracy of the valuations and the valuation methodologies used. Other valuation controls include the review and analysis of daily profit and loss.

The Bank values its assets at the bid price and its liabilities at the offer price. Derivative financial instruments are valued on a bid-offer basis, with valuation reserves, where necessary, included in derivative financial liabilities. Financial assets and liabilities that are not valued at fair value are included in the balance sheet at amortised cost.

## 21. Impairment of financial assets

Financial assets, other than those designated as held at fair value through profit and loss, are assessed for indications of impairment at each balance sheet date. A financial asset is impaired when there is objective evidence that the estimated future cash flows of the asset have been reduced as a result of one or more events that occurred after the initial recognition of the asset. Evidence of impairment could include significant financial difficulty, default, or probable bankruptcy / financial reorganisation of the counterparty or issuer.

Impairment losses are recognised to the extent that a decline in fair value below amortised cost is considered other than temporary. Impairment of currency assets is included in the profit and loss account under "Net valuation movement", with impairment of gold loans included under "Interest income". If the amount of the impairment loss decreases in a subsequent period, the previously recognised impairment loss is reversed through profit and loss to the extent that the carrying amount of the investment does not exceed that which it would have been had the impairment not been recognised.

## 22. Accounts receivable and accounts payable

Accounts receivable and accounts payable are principally very short-term amounts relating to the settlement of financial transactions. They are initially recognised at fair value and subsequently included in the balance sheet at amortised cost.

## 23. Land, buildings and equipment

The cost of the Bank's buildings and equipment is capitalised and depreciated on a straight line basis over the estimated useful lives of the assets concerned, as follows:

- Buildings – 50 years
- Building installations and machinery – 15 years
- Information technology equipment – up to 4 years
- Other equipment – 4 to 10 years

The Bank's land is not depreciated. The Bank undertakes an annual review of impairment of land, buildings and equipment. Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down to that amount.

## 24. Provisions

Provisions are recognised when the Bank has a present legal or constructive obligation as a result of events arising before the balance sheet date and it is probable that economic resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation. Best estimates and assumptions are used when determining the amount to be recognised as a provision.

## 25. Post-employment benefit obligations

The Bank operates three post-employment benefit arrangements for staff pensions, Directors' pensions, and health and accident insurance for current and former staff members. An independent actuarial valuation is performed annually for each arrangement.

### *A. Staff pensions*

The Bank provides a final salary defined benefit pension arrangement for its staff, based on a fund without separate legal personality, out of which benefits are paid. The fund assets are administered by the Bank for the sole benefit of current and former members of staff who participate in the arrangement. The Bank remains ultimately liable for all benefits due under the arrangement.

The liability in respect of the staff pension fund is based on the present value of the defined benefit obligation at the balance sheet date, less the fair value of the fund assets at the balance sheet date, together with adjustments for unrecognised actuarial gains and losses and past service costs. The defined benefit obligation is calculated using the projected unit credit method. The present value of the defined benefit obligation is determined from the estimated future cash outflows. The rate used to discount the cash flows is determined by the Bank based on the market yield of highly rated corporate debt securities in Swiss francs which have terms to maturity approximating the terms of the related liability.

The amount charged to the profit and loss account represents the sum of the current service cost of the benefits accruing for the year under the scheme, and interest at the discount rate on the defined benefit obligation. In addition, actuarial gains and losses arising from experience adjustments (where the actual outcome is different from the actuarial assumptions previously made), changes in actuarial assumptions and amendments to the pension fund regulations are charged to the profit and loss account over the service period of staff concerned in accordance with the "corridor accounting" methodology described below. The resulting liabilities are included under the heading "Other liabilities" in the balance sheet.

#### *B. Directors' pensions*

The Bank provides an unfunded defined benefit arrangement for Directors' pensions. The liability, defined benefit obligation and amount charged to the profit and loss account in respect of the Directors' pension arrangement are calculated on a similar basis to that used for the staff pension fund.

#### *C. Post-employment health and accident benefits*

The Bank provides an unfunded post-employment health and accident benefit arrangement for its staff. The liability, benefit obligation and amount charged to the profit and loss account in respect of the health and accident benefit arrangement are calculated on a similar basis to that used for the staff pension fund.

#### *D. Corridor accounting*

Actuarial gains or losses arise from experience adjustments (where the actual outcome is different from the actuarial assumptions previously made), changes in actuarial assumptions and amendments to the pension fund regulations. Where the cumulative unrecognised actuarial gains or losses exceed the higher of the benefit obligation or any assets used to fund the obligation by more than a corridor of 10%, the resulting excess outside the corridor is amortised over the expected remaining service period of the staff concerned.

### 26. Cash flow statement

The Bank's cash flow statement is prepared using an indirect method. It is based on the movements in the Bank's balance sheet, adjusted for changes in financial transactions awaiting settlement.

Cash and cash equivalents consist of cash and sight and notice accounts with banks, which are very short-term financial assets that typically have notice periods of three days or less.

# Notes to the financial statements

## 1. Introduction

The Bank for International Settlements (BIS, "the Bank") is an international financial institution which was established pursuant to the Hague Agreements of 20 January 1930, the Bank's Constituent Charter and its Statutes. The headquarters of the Bank are at Centralbahnplatz 2, 4002 Basel, Switzerland. The Bank maintains representative offices in the Hong Kong Special Administrative Region of the People's Republic of China (for Asia and the Pacific) and in Mexico City, Mexico (for the Americas).

The objectives of the BIS, as laid down in Article 3 of its Statutes, are to promote cooperation among central banks, to provide additional facilities for international financial operations and to act as trustee or agent for international financial settlements. Fifty-six central banks are currently members of the Bank. Rights of representation and voting at General Meetings are exercised in proportion to the number of BIS shares issued in the respective countries. The Board of Directors of the BIS is composed of the Governors and appointed Directors from the Bank's founding central banks, being those of Belgium, France, Germany, Italy, the United Kingdom and the United States of America, as well as the Governors of the central banks of Canada, China, Japan, Mexico, the Netherlands, Sweden and Switzerland, and the President of the European Central Bank.

## 2. Use of estimates

The preparation of the financial statements requires the Bank's Management to make some estimates in arriving at the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of income and expenses during the financial year. To arrive at these estimates, Management uses available information, makes assumptions and exercises judgment.

Assumptions include forward-looking estimates, for example relating to the valuation of assets and liabilities, the assessment of post-employment benefit obligations and the assessment of provisions and contingent liabilities.

Judgment is exercised when selecting and applying the Bank's accounting policies. The judgments relating to the designation and valuation of financial instruments are another key element in the preparation of these financial statements.

Subsequent actual results could differ materially from those estimates.

### *A. The valuation of financial assets and liabilities*

There is no active secondary market for certain of the Bank's financial assets and financial liabilities. Such assets and liabilities are valued using valuation techniques which require judgment to determine appropriate valuation parameters. Changes in assumptions about these parameters could materially affect the reported fair values. The valuation impact of a 1 basis point change in spread assumptions is shown in the table below:

For the financial year ended 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Treasury bills | 0.2 | 0.3 |
| Securities purchased under resale agreements | 0.3 | 0.1 |
| Loans and advances | 0.5 | 0.3 |
| Government and other securities | 10.2 | 9.8 |
| Currency deposits | 14.3 | 15.0 |
| Derivative financial instruments | 4.3 | 5.6 |

### *B. Impairment provision on financial assets*

Gold loans include a provision of SDR 29.0 million following an impairment review as at 31 March 2011 (31 March 2010: SDR 23.5 million). The impairment review was conducted at an individual counterparty level, identifying those counterparties which were experiencing significant financial difficulties at the balance sheet date. The increase in the provision during the financial year ended 31 March 2011 is due to changes in gold prices and exchange rates, which are included under the profit and loss account heading "Net foreign exchange loss". No additional impairment charge was recognised during the financial year (2010: nil). Impairment charges, when recognised, are included in the profit and loss account under the heading "Net interest income".

### *C. Actuarial assumptions*

The valuation of the Bank's pension fund and health care arrangements relies on actuarial assumptions which include expectations of inflation, interest rates, medical cost inflation and retirement age and life expectancy of participants. Changes to these assumptions have an impact on the valuation of the Bank's pension fund liabilities and the amounts recognised in the financial statements.

## 3. Cash and sight accounts with banks

Cash and sight accounts with banks consist of cash balances with central banks and commercial banks that are available to the Bank on demand.

## 4. Gold and gold loans

### *A. Total gold holdings*

The composition of the Bank's total gold holdings was as follows:

As at 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Gold | 35,401.7 | 41,596.9 |
| Gold loans | 1,235.5 | 1,442.9 |
| **Total gold and gold loan assets** | **36,637.2** | 43,039.8 |
| Comprising: | | |
| Gold investment assets | 3,451.2 | 2,811.2 |
| Gold and gold loan banking assets | 33,186.0 | 40,228.6 |

Included in "Gold" is SDR 11,940.5 million (409 tonnes) of gold (2010: SDR 8,160.1 million; 346 tonnes) that the Bank holds in connection with its gold swap contracts. Under such contracts the Bank exchanges currencies for physical gold, and has an obligation to return the gold at the end of the contract. See note 7 for more details on gold swap transactions.

### *B. Gold investment assets*

The Bank's gold investment assets are included in the balance sheet at their weight in gold (translated at the gold market price and USD exchange rate into SDR) plus accrued interest. The excess of this value over the deemed cost value is included in the gold revaluation account which is reported under the balance sheet heading "Other equity accounts"; the movement in this value is included in the statement of comprehensive income under the heading "Unrealised gain on gold investment assets". Realised gains or losses on the disposal of gold investment assets are recognised in the profit and loss account under the heading "Net gain on sales of gold investment assets".

Note 17B provides further analysis of the gold revaluation account. Note 26 provides further analysis of the net gain on sales of gold investment assets.

The table below analyses the movements in the Bank's gold investment assets:

For the financial year ended 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Balance at beginning of year | 2,811.2 | 2,358.1 |
| | | |
| **Net change in gold investment assets** | | |
| Disposals of gold | (26.7) | – |
| Impairment, sight account and other net movements | (5.5) | (3.7) |
| | (32.2) | (3.7) |
| | | |
| Gold price movement | 672.2 | 456.8 |
| **Balance at end of year** | **3,451.2** | 2,811.2 |

At 31 March 2011 the Bank's gold investment assets amounted to 119 tonnes of fine gold (2010: 120 tonnes).

## 5. Currency assets

### *A. Total holdings*

Currency assets comprise treasury bills, securities purchased under resale agreements, fixed-term loans and advances, and government and other securities.

Currency assets held at fair value through profit and loss comprise those currency banking assets that represent the reinvestment of currency deposit liabilities along with currency investment assets that are part of more actively traded portfolios. The remaining part of the Bank's currency investment assets are categorised as available for sale and, together with the gold investment assets, largely represent the investment of the Bank's equity.

*Treasury bills* are short-term debt securities issued by governments on a discount basis.

*Securities purchased under resale agreements* ("reverse repurchase agreements") are usually short-term transactions under which the Bank makes a fixed-term loan to a counterparty which provides collateral in the form of securities. The rate on the loan is fixed at the beginning of the transaction, and there is an irrevocable commitment to return the equivalent securities subject to the repayment of the loan. During the term of the agreement the Bank monitors the fair value of the collateral securities and may call for additional collateral or be required to return collateral based on the movement in its market value.

*Fixed-term loans* are primarily investments made with commercial banks. Also included in this category are investments made with central banks, international institutions and other public sector organisations. This includes advances made as part of committed and uncommitted standby facilities. These loans are recognised in the balance sheet total "Loans and advances", which also includes notice accounts (see note 6).

*Government and other securities* are debt securities issued by governments, international institutions, other public sector institutions, commercial banks and corporates. They include commercial paper, certificates of deposit, fixed and floating rate bonds, covered bonds and asset-backed securities.

The tables below analyse the Bank's holdings of currency assets:

| **As at 31 March 2011** | Banking assets | Investment assets | | | **Total currency assets** |
|---|---|---|---|---|---|
| *SDR millions* | Held at fair value through profit and loss | Available for sale | Held at fair value through profit and loss | Total | |
| **Treasury bills** | **76,739.3** | **–** | **192.8** | **192.8** | **76,932.1** |
| **Securities purchased under resale agreements** | **51,464.0** | **–** | **–** | **–** | **51,464.0** |
| **Fixed-term loans and advances** | **23,918.2** | **–** | **–** | **–** | **23,918.2** |
| **Government and other securities** | | | | | |
| Government | 11,498.1 | 11,083.5 | – | 11,083.5 | 22,581.6 |
| Financial institutions | 18,933.2 | 226.9 | 601.6 | 828.5 | 19,761.7 |
| Other | 13,808.6 | 836.0 | – | 836.0 | 14,644.6 |
| | **44,239.9** | **12,146.4** | **601.6** | **12,748.0** | **56,987.9** |
| **Total currency assets** | **196,361.4** | **12,146.4** | **794.4** | **12,940.8** | **209,302.2** |

| As at 31 March 2010 | Banking assets | Investment assets | | | Total currency assets |
|---|---|---|---|---|---|
| *SDR millions* | Held at fair value through profit and loss | Available for sale | Held at fair value through profit and loss | Total | |
| **Treasury bills** | 84,652.5 | – | 62.3 | 62.3 | 84,714.8 |
| **Securities purchased under resale agreements** | 42,305.9 | – | – | – | 42,305.9 |
| **Fixed-term loans and advances** | 18,316.0 | – | – | – | 18,316.0 |
| **Government and other securities** | | | | | |
| Government | 7,863.1 | 9,563.8 | 8.9 | 9,572.7 | 17,435.8 |
| Financial institutions | 18,878.3 | 677.7 | 543.2 | 1,220.9 | 20,099.2 |
| Other | 14,838.0 | 1,314.7 | – | 1,314.7 | 16,152.7 |
| | 41,579.4 | 11,556.2 | 552.1 | 12,108.3 | 53,687.7 |
| **Total currency assets** | 186,853.8 | 11,556.2 | 614.4 | 12,170.6 | 199,024.4 |

***B. Currency investment assets available for sale***

The Bank's currency investment assets relate principally to the investment of its equity. They are designated as available for sale unless they are part of an actively traded portfolio.

The table below analyses the movements in the Bank's currency investment assets available for sale:

For the financial year ended 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Balance at beginning of year | 11,556.2 | 10,859.3 |
| | | |
| **Net change in currency investment assets available for sale** | | |
| Additions | 5,299.8 | 5,233.1 |
| Disposals | (2,996.5) | (3,941.1) |
| Other net movements | (1,473.5) | (685.6) |
| | 829.8 | 606.4 |
| | | |
| Net change in transactions awaiting settlement | (98.0) | 97.6 |
| Fair value and other movements | (141.6) | (7.1) |
| | | |
| **Balance at end of year** | **12,146.4** | 11,556.2 |

## 6. Loans and advances

Loans and advances comprise fixed-term loans to commercial banks, advances and notice accounts. Advances relate to committed and uncommitted standby facilities which the Bank provides for its customers. Notice accounts are very short-term financial assets, typically having a notice period of three days or less.

Fixed-term loans and advances are designated as held at fair value through profit and loss. Notice accounts are designated as loans and receivables and are included in the balance sheet at amortised cost.

As at 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Fixed-term loans and advances | 23,918.2 | 18,316.0 |
| Notice accounts | 252.2 | 972.6 |
| | | |
| **Total loans and advances** | **24,170.4** | 19,288.6 |

The amount of the change in fair value recognised in the profit and loss account on fixed-term loans and advances is SDR 12.3 million (2010: SDR –11.6 million).

## 7. Derivative financial instruments

The Bank uses the following types of derivative instruments for economic hedging and trading purposes.

*Interest rate and bond futures* are contractual agreements to receive or pay a net amount based on changes in interest rates or bond prices on a future date. Futures contracts are settled daily with the exchange. Associated margin payments are settled by cash or marketable securities.

*Currency and gold options* are contractual agreements under which the seller grants the purchaser the right, but not the obligation, to either buy (call option) or sell (put option), by or on a set date, a specific amount of a currency or gold at a predetermined price. In consideration, the seller receives a premium from the purchaser.

*Currency and gold swaps, cross-currency interest rate swaps and interest rate swaps* are bilateral contractual agreements to exchange cash flows related to currencies, gold or interest rates (for example, fixed rate for floating rate). Cross-currency interest rate swaps involve the exchange of cash flows related to a combination of interest rates and foreign exchange rates. Except for certain currency and gold swaps and cross-currency interest rate swaps, no exchange of principal takes place.

*Currency and gold forwards* are bilateral contractual agreements involving the exchange of foreign currencies or gold at a future date. This includes undelivered spot transactions.

*Forward rate agreements* are bilateral interest rate forward contracts that result in cash settlement at a future date for the difference between a contracted rate of interest and the prevailing market rate.

*Swaptions* are bilateral options under which the seller grants the purchaser the right, but not the obligation, to enter into a currency or interest rate swap at a predetermined price by or on a set date. In consideration, the seller receives a premium from the purchaser.

In addition, the Bank sells products to its customers which contain embedded derivatives (see notes 10 and 11). Where the host contract is not accounted for as held at fair value, embedded derivatives are separated from the host contract for accounting purposes and treated as though they are regular derivatives. As such, the gold currency options embedded in gold dual currency deposits are included within derivatives as currency and gold options.

The table below analyses the fair value of derivative financial instruments:

| As at 31 March | **2011** | | | 2010 | | |
|---|---|---|---|---|---|---|
| | Notional amounts | Fair values | | Notional amounts | Fair values | |
| *SDR millions* | | Assets | Liabilities | | Assets | Liabilities |
| Bond futures | 1,095.0 | 0.5 | (0.4) | 754.9 | 0.8 | – |
| Cross-currency interest rate swaps | 1,597.0 | 4.8 | (314.8) | 345.8 | 56.1 | (401.9) |
| Currency and gold forwards | 2,747.7 | 13.6 | (25.2) | 736.2 | 2.7 | (1.1) |
| Currency and gold options | 3,430.0 | 43.7 | (43.8) | 6,034.1 | 47.9 | (47.2) |
| Currency and gold swaps | 128,060.9 | 766.9 | (3,711.9) | 108,476.1 | 3,282.5 | (199.8) |
| Forward rate agreements | 18,945.7 | 6.3 | (5.1) | 7,975.6 | 0.7 | (2.9) |
| Interest rate futures | 7,559.2 | 0.1 | – | 2,015.9 | – | – |
| Interest rate swaps | 304,357.4 | 4,954.4 | (2,853.3) | 309,000.7 | 6,721.1 | (3,532.8) |
| Swaptions | 773.4 | – | (5.0) | 845.2 | 2.9 | (1.7) |
| **Total derivative financial instruments at end of year** | **468,566.3** | **5,790.3** | **(6,959.5)** | 436,184.5 | 10,114.7 | (4,187.4) |
| **Net derivative financial instruments at end of year** | | | **(1,169.2)** | | | 5,927.3 |

## 8. Accounts receivable

| As at 31 March | | |
|---|---|---|
| *SDR millions* | **2011** | 2010 |
| Financial transactions awaiting settlement | 8,606.0 | 4,023.9 |
| Other assets | 10.3 | 11.8 |
| **Total accounts receivable** | **8,616.3** | 4,035.7 |

"Financial transactions awaiting settlement" relates to short-term receivables (typically due in three days or less) where transactions have been effected but cash has not yet been transferred. This includes assets that have been sold and liabilities that have been issued.

## 9. Land, buildings and equipment

| For the financial year ended 31 March | | | | 2011 | 2010 |
|---|---|---|---|---|---|
| *SDR millions* | Land | Buildings | IT and other equipment | Total | Total |
| Historical cost | | | | | |
| Balance at beginning of year | **41.2** | **243.9** | **88.6** | **373.7** | 361.6 |
| Capital expenditure | – | 6.3 | 8.8 | 15.1 | 12.1 |
| Disposals and retirements | – | – | (4.5) | (4.5) | – |
| **Balance at end of year** | **41.2** | **250.2** | **92.9** | **384.3** | 373.7 |
| Depreciation | | | | | |
| Balance at beginning of year | **–** | **115.2** | **68.6** | **183.8** | 170.6 |
| Depreciation | – | 7.8 | 6.4 | 14.2 | 13.1 |
| Disposals and retirements | – | – | (4.5) | (4.5) | – |
| **Balance at end of year** | **–** | **123.0** | **70.5** | **193.5** | 183.7 |
| **Net book value at end of year** | **41.2** | **127.2** | **22.4** | **190.8** | 189.9 |

The depreciation charge for the financial year ended 31 March 2011 includes an additional charge of SDR 1.0 million for IT and other equipment following an impairment review (2010: SDR 0.6 million).

## 10. Currency deposits

Currency deposits are book entry claims on the Bank. The currency deposit instruments are analysed in the table below:

As at 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| **Deposit instruments repayable at one to two days' notice** | | |
| Medium-Term Instruments (MTIs) | 54,453.9 | 52,420.8 |
| Callable MTIs | 1,556.7 | 1,717.3 |
| Fixed Rate Investments of the BIS (FIXBIS) | 42,751.3 | 34,223.7 |
| | **98,761.9** | 88,361.8 |
| **Other currency deposits** | | |
| Floating Rate Investments of the BIS (FRIBIS) | 962.8 | 116.9 |
| Fixed-term deposits | 89,550.9 | 78,434.1 |
| Dual Currency Deposits (DCDs) | 85.7 | 95.8 |
| Sight and notice deposit accounts | 17,724.3 | 28,746.5 |
| | **108,323.7** | 107,393.3 |
| **Total currency deposits** | **207,085.6** | 195,755.1 |
| Comprising: | | |
| Designated as held at fair value through profit and loss | 189,361.3 | 167,008.6 |
| Designated as financial liabilities measured at amortised cost | 17,724.3 | 28,746.5 |

*Medium-Term Instruments (MTIs)* are fixed rate investments at the BIS for quarterly maturities of up to 10 years.

*Callable MTIs* are MTIs that are callable at the option of the Bank at an exercise price of par, with call dates between June 2011 and December 2011 (2010: June 2010 and December 2010). The balance sheet total for callable MTIs includes the fair value of the embedded interest rate option.

*FIXBIS* are fixed rate investments at the Bank for any maturities between one week and one year.

*FRIBIS* are floating rate investments at the Bank with maturities of one year or longer for which the interest rate is reset in line with prevailing market conditions.

*Fixed-term deposits* are fixed rate investments at the BIS, typically with a maturity of less than one year.

*Dual Currency Deposits (DCDs)* are fixed-term deposits that are repayable on the maturity date either in the original currency or at a fixed amount in a different currency at the option of the Bank. The balance sheet total for DCDs includes the fair value of the embedded foreign exchange option. These deposits all mature between 4 April 2011 and 9 May 2011 (2010: between 21 April 2010 and 12 May 2010).

*Sight and notice deposit accounts* are very short-term financial liabilities, typically having a notice period of three days or less. They are designated as financial liabilities measured at amortised cost.

The Bank acts as the sole market-maker in certain of its currency deposit liabilities and has undertaken to repay at fair value some of these financial instruments, in whole or in part, at one to two business days' notice.

### *A. Valuation of currency deposits*

Currency deposits (other than sight and notice deposit accounts) are included in the balance sheet at fair value. This value differs from the amount that the Bank is contractually obliged to pay at maturity to the holder of the deposit. The amount the Bank is contractually obliged to pay at maturity in respect of its total currency deposits (including accrued interest to 31 March 2011) is SDR 206,432.4 million (2010: SDR 193,896.3 million).

The Bank uses valuation techniques to estimate the fair value of its currency deposits. These valuation techniques comprise discounted cash flow models and option pricing models. The discounted cash flow models value the expected cash flows of financial instruments using discount factors that are partly derived from quoted interest rates (eg Libor and swap rates) and partly based on assumptions about spreads at which each product is offered to and repurchased from customers.

The spread assumptions are based on recent market transactions in each product. Where the product series has been closed to new investors (and thus there are no recent market transactions) the Bank uses the latest quoted spread for the series as the basis for determining the appropriate model inputs.

The option pricing models include assumptions about volatilities that are derived from market quotes.

***B. Impact of changes in the Bank's creditworthiness***

The fair value of the Bank's liabilities would be affected by any change in its creditworthiness. If the Bank's creditworthiness deteriorated, the value of its liabilities would decrease, and the change in value would be reflected as a valuation movement in the profit and loss account. The Bank regularly assesses its creditworthiness as part of its risk management processes. The Bank's assessment of its creditworthiness did not indicate a change which could have had an impact on the fair value of the Bank's liabilities during the period under review.

## 11. Gold deposits

Gold deposits placed with the Bank originate entirely from central banks. They are all designated as financial liabilities measured at amortised cost.

## 12. Accounts payable

Accounts payable consist of financial transactions awaiting settlement, relating to short-term payables (typically payable within three days or less) where transactions have been effected but cash has not yet been transferred. This includes assets that have been purchased and liabilities that have been repurchased.

## 13. Other liabilities

The Bank's other liabilities consist of:

As at 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Post-employment benefit obligations (see note 18) | | |
| Staff pensions | 22.7 | 12.1 |
| Directors' pensions | 5.9 | 5.2 |
| Health and accident benefits | 258.3 | 217.5 |
| Short positions in currency assets | 65.7 | 66.0 |
| Payable to former shareholders | 0.6 | 0.5 |
| Other | 22.2 | 17.7 |
| **Total other liabilities** | **375.4** | 319.0 |

## 14. Share capital

The Bank's share capital consists of:

As at 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Authorised capital: 600,000 shares, each of SDR 5,000 par value, of which SDR 1,250 is paid up | 3,000.0 | 3,000.0 |
| Issued capital: 547,125 shares | 2,735.6 | 2,735.6 |
| **Paid-up capital (25%)** | **683.9** | 683.9 |

The number of shares eligible for dividend is:

| As at 31 March | **2011** | 2010 |
|---|---|---|
| Issued shares | 547,125 | 547,125 |
| Less: shares held in treasury | (1,000) | (1,000) |
| **Outstanding shares eligible for full dividend** | **546,125** | 546,125 |

## 15. Statutory reserves

The Bank's Statutes provide for application of the Bank's annual net profit by the Annual General Meeting on the proposal of the Board of Directors to three specific reserve funds: the legal reserve fund, the general reserve fund and the special dividend reserve fund; the remainder of the net profit after payment of any dividend is generally allocated to the free reserve fund.

*Legal reserve fund.* This fund is currently fully funded at 10% of the Bank's paid-up capital.

*General reserve fund.* After payment of any dividend, 10% of the remainder of the Bank's annual net profit currently must be allocated to the general reserve fund. When the balance of this fund equals five times the Bank's paid-up capital, (see note 14), such annual contribution will decrease to 5% of the remainder of the annual net profit.

*Special dividend reserve fund.* A portion of the remainder of the annual net profit may be allocated to the special dividend reserve fund, which shall be available, in case of need, for paying the whole or any part of a declared dividend. Dividends are normally paid out of the Bank's net profit.

*Free reserve fund.* After the above allocations have been made, any remaining unallocated net profit is generally transferred to the free reserve fund.

Receipts from the subscription of the Bank's shares are allocated to the legal reserve fund as necessary to keep it fully funded, with the remainder being credited to the general reserve fund.

The free reserve fund, general reserve fund and legal reserve fund are available, in that order, to meet any losses incurred by the Bank. In the event of liquidation of the Bank, the balances of the reserve funds (after the discharge of the liabilities of the Bank and the costs of liquidation) would be divided among the Bank's shareholders.

## 16. Shares held in treasury

| For the financial year ended 31 March | **2011** | 2010 |
|---|---|---|
| Number of shares at beginning of year | 1,000 | 1,000 |
| Movements during the year | – | – |
| **Number of shares at end of year** | **1,000** | 1,000 |

The shares held in treasury consist of 1,000 shares of the Albanian issue which were suspended in 1977.

## 17. Other equity accounts

Other equity accounts represent the revaluation accounts of the currency assets available for sale and gold investment assets, which are further described in notes 4 and 5.

Other equity accounts comprise:

As at 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Securities revaluation account | 121.3 | 318.6 |
| Gold revaluation account | 2,896.4 | 2,246.0 |
| **Total other equity accounts** | **3,017.7** | 2,564.6 |

### *A. Securities revaluation account*

This account contains the difference between the fair value and the amortised cost of the Bank's currency assets available for sale.

The movements in the securities revaluation account were as follows:

For the financial year ended 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Balance at beginning of year | 318.6 | 431.1 |
| **Net valuation movement** | | |
| Net gain on sales | (55.7) | (105.4) |
| Fair value and other movements | (141.6) | (7.1) |
| | (197.3) | (112.5) |
| **Balance at end of year** | **121.3** | 318.6 |

The table below analyses the balance in the securities revaluation account, which relates to government and other securities:

| SDR millions | Fair value of assets | Historical cost | Securities revaluation account | Gross gains | Gross losses |
|---|---|---|---|---|---|
| **As at 31 March 2011** | 12,146.4 | 12,025.1 | **121.3** | 190.4 | (69.1) |
| As at 31 March 2010 | 11,556.2 | 11,237.6 | 318.6 | 322.2 | (3.6) |

### *B. Gold revaluation account*

This account contains the difference between the book value and the deemed cost of the Bank's gold investment assets. For gold investment assets held on 31 March 2003 (when the Bank changed its functional and presentation currency from the gold franc to the SDR) the deemed cost is approximately SDR 151 per ounce, based on the value of USD 208 that was applied from 1979 to 2003 in accordance with a decision by the Bank's Board of Directors, translated at the 31 March 2003 exchange rate.

The movements in the gold revaluation account were as follows:

For the financial year ended 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Balance at beginning of year | 2,246.0 | 1,789.2 |
| | | |
| **Net valuation movement** | | |
| Net gain on sales | (21.8) | – |
| Gold price movement | 672.2 | 456.8 |
| | 650.4 | 456.8 |
| | | |
| **Balance at end of year** | **2,896.4** | 2,246.0 |

## 18. Post-employment benefit obligations

The Bank operates three post-employment arrangements:

1. A final salary defined benefit pension arrangement for its staff. The pension arrangement is based on a fund without separate legal personality, out of which benefits are paid. The fund assets are administered by the Bank for the sole benefit of current and former members of staff who participate in the arrangement. The Bank remains ultimately liable for all benefits due under the arrangement.

2. An unfunded defined benefit arrangement for its Directors, whose entitlement is based on a minimum service period of four years.

3. An unfunded post-employment health and accident benefit arrangement for its staff. Entitlement to this arrangement is based in principle on the employee remaining in service up to 50 years of age and the completion of a minimum service period of 10 years.

All arrangements are valued annually by independent actuaries.

### *A. Amounts recognised in the balance sheet*

| As at 31 March | | | Staff pensions | | |
|---|---|---|---|---|---|
| *SDR millions* | **2011** | 2010 | 2009 | 2008 | 2007 |
| Present value of obligation | (1,039.1) | (913.1) | (747.4) | (709.7) | (653.7) |
| Fair value of fund assets | 881.9 | 762.4 | 619.6 | 714.3 | 648.6 |
| Funded status | (157.2) | (150.7) | (127.8) | 4.6 | (5.1) |
| Unrecognised actuarial losses | 134.5 | 138.6 | 125.4 | 41.2 | 47.3 |
| Unrecognised past service cost | – | – | – | (45.8) | (42.2) |
| **Liability at end of year** | **(22.7)** | (12.1) | (2.4) | – | – |

| As at 31 March | | | Directors' pensions | | |
|---|---|---|---|---|---|
| *SDR millions* | **2011** | 2010 | 2009 | 2008 | 2007 |
| Present value of obligation | (7.2) | (6.5) | (5.7) | (5.4) | (4.6) |
| Fair value of fund assets | – | – | – | – | – |
| Funded status | (7.2) | (6.5) | (5.7) | (5.4) | (4.6) |
| Unrecognised actuarial losses | 1.3 | 1.3 | 0.9 | 0.6 | 0.3 |
| Unrecognised past service cost | – | – | – | – | – |
| **Liability at end of year** | **(5.9)** | (5.2) | (4.8) | (4.8) | (4.3) |

| As at 31 March | | | Post-employment health and accident benefits | | |
|---|---|---|---|---|---|
| *SDR millions* | **2011** | 2010 | 2009 | 2008 | 2007 |
| Present value of obligation | (316.7) | (284.2) | (225.4) | (208.0) | (186.3) |
| Fair value of fund assets | – | – | – | – | – |
| Funded status | (316.7) | (284.2) | (225.4) | (208.0) | (186.3) |
| Unrecognised actuarial losses | 63.3 | 72.3 | 40.1 | 30.3 | 42.0 |
| Unrecognised past service cost | (4.9) | (5.6) | (6.3) | (7.7) | (7.8) |
| **Liability at end of year** | **(258.3)** | (217.5) | (191.6) | (185.4) | (152.1) |

*B. Present value of defined benefit obligation*

The reconciliation of the opening and closing amounts of the present value of the benefit obligation is as follows:

| As at 31 March | Staff pensions | | | Directors' pensions | | | Post-employment health and accident benefits | | |
|---|---|---|---|---|---|---|---|---|---|
| *SDR millions* | **2011** | 2010 | 2009 | **2011** | 2010 | 2009 | **2011** | 2010 | 2009 |
| Present value of obligation at beginning of year | 913.1 | 747.4 | 709.7 | 6.5 | 5.7 | 5.4 | 284.2 | 225.4 | 208.0 |
| Current service cost | 40.1 | 32.0 | 29.8 | 0.3 | 0.2 | 0.2 | 9.4 | 8.5 | 7.9 |
| Employee contributions | 5.2 | 4.5 | 3.9 | – | – | – | – | – | – |
| Interest cost | 25.6 | 24.5 | 24.9 | 0.2 | 0.2 | 0.2 | 8.1 | 7.5 | 7.4 |
| Actuarial loss / (gain) | (11.8) | 84.3 | 29.3 | – | – | 0.3 | (11.9) | 30.2 | 11.5 |
| Benefit payments | (29.0) | (28.3) | (24.5) | (0.4) | (0.3) | (0.3) | (2.5) | (2.2) | (1.9) |
| Exchange differences | 95.9 | 48.7 | (25.7) | 0.6 | 0.7 | (0.1) | 29.4 | 14.8 | (7.5) |
| **Present value of obligation at end of year** | **1,039.1** | 913.1 | 747.4 | **7.2** | 6.5 | 5.7 | **316.7** | 284.2 | 225.4 |

*C. Fair value of fund assets for staff pensions*

The reconciliation of the opening and closing amounts of the fair value of fund assets for the staff pension arrangement is as follows:

For the financial year ended 31 March

| *SDR millions* | **2011** | 2010 | 2009 |
|---|---|---|---|
| Fair value of fund assets at beginning of year | 762.4 | 619.6 | 714.3 |
| Expected return on fund assets | 39.4 | 31.8 | 34.0 |
| Actuarial gain / (loss) | 0.9 | 74.4 | (99.3) |
| Employer contributions | 22.0 | 20.0 | 18.3 |
| Employee contributions | 5.2 | 4.5 | 3.9 |
| Benefit payments | (29.0) | (28.3) | (24.5) |
| Exchange differences | 81.0 | 40.4 | (27.1) |
| **Fair value of fund assets at end of year** | **881.9** | 762.4 | 619.6 |

*D. Amounts recognised in the profit and loss account*

| For the financial year ended 31 March | Staff pensions | | | Directors' pensions | | | Post-employment health and accident benefits | | |
|---|---|---|---|---|---|---|---|---|---|
| *SDR millions* | **2011** | 2010 | 2009 | **2011** | 2010 | 2009 | **2011** | 2010 | 2009 |
| Current service cost | 40.1 | 32.0 | 29.8 | 0.3 | 0.2 | 0.2 | 9.4 | 8.5 | 7.9 |
| Interest cost | 25.6 | 24.5 | 24.9 | 0.2 | 0.2 | 0.2 | 8.1 | 7.5 | 7.4 |
| Less: expected return on fund assets | (39.4) | (31.8) | (34.0) | – | – | – | – | – | – |
| Less: past service cost | – | – | – | – | – | – | (1.2) | (1.1) | (6.3) |
| Net actuarial losses recognised in year | 4.2 | 4.4 | – | 0.1 | 0.1 | – | 3.5 | 1.4 | – |
| **Total included in operating expense** | **30.5** | 29.1 | 20.7 | **0.6** | 0.5 | 0.4 | **19.8** | 16.3 | 9.0 |

The Bank expects to make a contribution to its post-employment arrangements of SDR 26.9 million in 2011/12.

*E. Major categories of fund assets as a percentage of total fund assets*

| As at 31 March | | |
|---|---|---|
| *Percentages* | **2011** | 2010 |
| European equities | 14.6 | 7.1 |
| Other equities | 32.0 | 33.4 |
| European fixed income | 16.3 | 18.5 |
| Other fixed income | 30.1 | 30.9 |
| Other assets | 7.0 | 10.1 |
| Actual return on fund assets | **4.9%** | 14.4% |

The staff pension fund does not invest in financial instruments issued by the Bank.

*F. Principal actuarial assumptions used in these financial statements*

| As at 31 March | 2011 | 2010 |
|---|---|---|
| **Applicable to all three post-employment benefit arrangements** | | |
| Discount rate – market rate of highly rated Swiss corporate bonds | 2.75% | 2.75% |
| **Applicable to staff and Directors' pension arrangements** | | |
| Assumed increase in pensions payable | 1.50% | 1.50% |
| **Applicable to staff pension arrangement only** | | |
| Expected return on fund assets | 5.00% | 5.00% |
| Assumed salary increase rate | 4.10% | 4.10% |
| **Applicable to Directors' pension arrangement only** | | |
| Assumed Directors' pensionable remuneration increase rate | 1.50% | 1.50% |
| **Applicable to post-employment health and accident benefit arrangement only** | | |
| Long-term medical cost inflation assumption | 5.00% | 5.00% |

The assumed increases in staff salaries, Directors' pensionable remuneration and pensions payable incorporate an inflation assumption of 1.5% at 31 March 2011 (2010: 1.5%).

The expected rate of return on fund assets is based on long-term expectations for inflation, interest rates, risk premia and asset allocations. The estimate takes into consideration historical returns and is determined in conjunction with the fund's independent actuaries.

The assumption for medical inflation has a significant effect on the amounts recognised in the profit and loss account. A 1% change in the assumption for medical inflation compared to that used for the 2010/11 calculation would have the following effects:

For the financial year ended 31 March

| *SDR millions* | 2011 | 2010 |
|---|---|---|
| Increase / (decrease) of the total service and interest cost | | |
| 6% medical inflation | 7.1 | 5.2 |
| 4% medical inflation | (5.2) | (3.9) |

As at 31 March

| *SDR millions* | 2011 | 2010 |
|---|---|---|
| Increase / (decrease) of the benefit obligation | | |
| 6% medical inflation | 88.9 | 70.0 |
| 4% medical inflation | (67.5) | (53.1) |

## 19. Interest income

For the financial year ended 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| **Currency assets available for sale** | | |
| Government and other securities | 299.9 | 317.7 |
| | **299.9** | 317.7 |
| **Currency assets held at fair value through profit and loss** | | |
| Treasury bills | 335.6 | 529.9 |
| Securities purchased under resale agreements | 188.3 | 156.7 |
| Loans and advances | 123.9 | 101.7 |
| Government and other securities | 838.7 | 959.1 |
| | **1,486.5** | 1,747.4 |
| **Assets designated as loans and receivables** | | |
| Sight and notice accounts | 2.8 | 2.0 |
| Gold investment assets | 1.2 | 2.7 |
| Gold banking assets | 2.2 | 3.1 |
| | **6.2** | 7.8 |
| **Derivative financial instruments held at fair value through profit and loss** | **1,531.8** | 1,979.0 |
| **Total interest income** | **3,324.4** | 4,051.9 |

## 20. Interest expense

For the financial year ended 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| **Liabilities held at fair value through profit and loss** | | |
| Currency deposits | 1,811.0 | 2,573.8 |
| **Liabilities designated as financial liabilities measured at amortised cost** | | |
| Sight and notice deposit accounts | 46.6 | 44.9 |
| Gold deposits | 1.4 | 2.0 |
| | **48.0** | 46.9 |
| **Total interest expense** | **1,859.0** | 2,620.7 |

## 21. Net valuation movement

The net valuation movement arises entirely on financial instruments designated as held at fair value through profit and loss.

For the financial year ended 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| **Currency assets held at fair value through profit and loss** | | |
| Unrealised valuation movements on currency assets | (473.7) | 698.6 |
| Realised gains on currency assets | 108.5 | 53.2 |
| | **(365.2)** | 751.8 |
| **Currency liabilities held at fair value through profit and loss** | | |
| Unrealised valuation movements on financial liabilities | 646.4 | 1,977.4 |
| Realised losses on financial liabilities | (292.4) | (928.4) |
| | **354.0** | 1,049.0 |
| **Valuation movements on derivative financial instruments** | **(498.0)** | (1,280.3) |
| **Net valuation movement** | **(509.2)** | 520.5 |

## 22. Net fee and commission income

For the financial year ended 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Fee and commission income | 12.1 | 18.8 |
| Fee and commission expense | (9.0) | (8.1) |
| **Net fee and commission income** | **3.1** | 10.7 |

## 23. Net foreign exchange loss

For the financial year ended 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Net transaction gain | 21.5 | 0.3 |
| Net translation loss | (37.3) | (17.5) |
| **Net foreign exchange loss** | **(15.8)** | (17.2) |

## 24. Operating expense

The following table analyses the Bank's operating expense in Swiss francs (CHF), the currency in which most expenditure is incurred:

For the financial year ended 31 March

| *CHF millions* | **2011** | 2010 |
|---|---|---|
| **Board of Directors** | | |
| Directors' fees | 2.2 | 2.3 |
| Pensions to former Directors | 0.6 | 0.6 |
| Travel, external Board meetings and other costs | 1.2 | 1.3 |
| | **4.0** | 4.2 |
| **Management and staff** | | |
| Remuneration | 120.4 | 118.8 |
| Pensions | 50.8 | 51.8 |
| Other personnel-related expense | 48.3 | 44.2 |
| | **219.5** | 214.8 |
| **Office and other expense** | **71.3** | 73.7 |
| **Administrative expense in CHF millions** | **294.8** | 292.7 |
| Administrative expense in SDR millions | 190.8 | 177.7 |
| Depreciation in SDR millions | 14.2 | 13.1 |
| **Operating expense in SDR millions** | **205.0** | 190.8 |

The average number of full-time equivalent employees during the financial year ended 31 March 2011 was 547 (2010: 540).

## 25. Net gain on sales of securities available for sale

For the financial year ended 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Disposal proceeds | 3,038.7 | 3,941.1 |
| Amortised cost | (2,983.0) | (3,835.7) |
| **Net gain on sales of securities available for sale** | **55.7** | 105.4 |
| Comprising: | | |
| Gross realised gains | 69.9 | 107.7 |
| Gross realised losses | (14.2) | (2.3) |

## 26. Net gain on sales of gold investment assets

For the financial year ended 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Disposal proceeds | 26.7 | – |
| Deemed cost (see note 17B) | (4.9) | – |
| **Net gain on sales of gold investment assets** | **21.8** | – |

## 27. Earnings and dividends per share

| For the financial year ended 31 March | **2011** | 2010 |
|---|---|---|
| Net profit for the financial year (SDR millions) | 816.0 | 1,859.8 |
| Weighted average number of shares entitled to dividend | 546,125 | 546,125 |
| **Basic and diluted earnings per share (SDR per share)** | **1,494.2** | 3,405.4 |
| **Dividends per share (SDR per share)** | | |
| Normal | **295** | 285 |
| Supplementary | – | 400 |
| **Total** | **295** | 685 |

The Bank's dividend policy incorporates two elements: a normal sustainable dividend that is intended to change in a predictable manner from year to year, and a supplementary dividend that is appropriate when profits are high and the Bank's capital requirements are met.

## 28. Cash and cash equivalents

The cash and cash equivalents in the cash flow statement comprise:

As at 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Cash and sight accounts with banks | 329.8 | 1,516.2 |
| Notice accounts | 252.2 | 972.6 |
| **Total cash and cash equivalents** | **582.0** | 2,488.8 |

## 29. Taxes

The Bank's special legal status in Switzerland is set out principally in its Headquarters Agreement with the Swiss Federal Council. Under the terms of this document the Bank is exempted from virtually all direct and indirect taxes at both federal and local government level in Switzerland.

Similar agreements exist with the government of the People's Republic of China for the Asian Office in Hong Kong SAR and with the Mexican government for the Americas Office.

## 30. Exchange rates

The following table shows the principal rates and prices used to translate balances in foreign currency and gold into SDR:

| | Spot rate as at 31 March | | Average rate for the financial year ended | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| USD | **0.631** | 0.658 | **0.654** | 0.644 |
| EUR | **0.895** | 0.889 | **0.864** | 0.909 |
| JPY | **0.00762** | 0.00704 | **0.00764** | 0.00694 |
| GBP | **1.013** | 0.998 | **1.016** | 1.027 |
| CHF | **0.689** | 0.625 | **0.647** | 0.606 |
| Gold (in ounces) | **907.5** | 732.9 | **844.9** | 657.4 |

## 31. Off-balance sheet items

Fiduciary transactions are effected in the Bank's name on behalf of, and at the risk of, the Bank's customers without recourse to the other assets of the Bank. They are not included in the Bank's balance sheet and comprise:

As at 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Safe custody arrangements | 11,260.6 | 11,115.6 |
| Collateral pledge agreements | 33.9 | 88.8 |
| Portfolio management mandates | 10,507.9 | 8,981.2 |
| Gold bars held under earmark | 8,671.1 | 5,003.9 |
| **Total** | **30,473.5** | 25,189.5 |

The above table includes the nominal value of securities held under safe custody and collateral pledge arrangements, and the net asset value of portfolio management mandates. Portfolio management mandates include BIS Investment Pools (BISIPs), which are collective investment arrangements for central banks, and dedicated mandates for single central bank investors.

Gold bars held under earmark comprise specific gold bars which have been deposited with the Bank on a custody basis. They are included at their weight in gold (translated at the gold market price and the USD exchange rate into SDR). At 31 March 2011 gold bars held under earmark amounted to 297 tonnes of fine gold (2010: 212 tonnes).

The financial instruments held under the above arrangements are deposited with external custodians, either central banks or commercial institutions.

In addition to the off-balance sheet items listed above, the Bank also manages portfolios of BIS currency deposits on behalf of its customers. These totalled SDR 5,776.7 million at 31 March 2011 (2010: SDR 5,713.0 million). The assets in these portfolios are included in the balance sheet under the heading "Currency deposits".

## 32. Commitments

The Bank provides a number of committed standby facilities for its customers on a collateralised or uncollateralised basis. As at 31 March 2011 the outstanding commitments to extend credit under these committed standby facilities amounted to SDR 2,287.7 million (2010: SDR 4,919.8 million), of which SDR 189.4 million was uncollateralised (2010: SDR 2,420.7 million).

## 33. The fair value hierarchy

The Bank categorises its financial instrument fair value measurements using a hierarchy that reflects the significance of inputs used in measuring fair value. The valuation is categorised at the lowest level of input that is significant to the fair value measurement in its entirety. The fair value hierarchy used by the Bank comprises the following levels:

Level 1 – unadjusted quoted prices in active markets for identical financial instruments.

Level 2 – inputs other than those in level 1 which are observable for the financial instrument either directly (ie as a price) or indirectly (ie derived from prices for similar financial instruments). This includes observable interest rates, spreads and volatilities.

Level 3 – inputs that are not observable in financial markets.

### *A. Assets measured at fair value*

**As at 31 March 2011**

| *SDR millions* | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| **Financial assets held at fair value through profit and loss** | | | | |
| Treasury bills | 71,198.0 | 5,734.2 | – | 76,932.1 |
| Securities purchased under resale agreements | – | 51,464.0 | – | 51,464.0 |
| Fixed-term loans | – | 23,918.2 | – | 23,918.2 |
| Government and other securities | 18,401.2 | 26,376.2 | 64.1 | 44,841.5 |
| Derivative financial instruments | 5.5 | 5,784.8 | – | 5,790.3 |
| **Financial assets designated as available for sale** | | | | |
| Government and other securities | 11,862.1 | 284.4 | – | 12,146.4 |
| **Total financial assets accounted for at fair value** | **101,466.7** | **113,561.7** | **64.1** | **215,092.5** |
| **Financial liabilities held at fair value through profit and loss** | | | | |
| Currency deposits | – | (189,361.3) | – | (189,361.3) |
| Derivative financial instruments | (16.5) | (6,943.0) | – | (6,959.5) |
| Other liabilities (short positions in currency assets) | – | (65.7) | – | (65.7) |
| **Total financial liabilities accounted for at fair value** | **(16.5)** | **(196,370.0)** | **–** | **(196,386.5)** |

As at 31 March 2010

| *SDR millions* | Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| **Financial assets held at fair value through profit and loss** | | | | |
| Treasury bills | 62,644.6 | 22,070.2 | – | 84,714.8 |
| Securities purchased under resale agreements | – | 42,305.9 | – | 42,305.9 |
| Fixed-term loans | – | 18,316.0 | – | 18,316.0 |
| Government and other securities | 13,354.7 | 28,685.4 | 91.4 | 42,131.5 |
| Derivative financial instruments | 2.5 | 10,112.2 | – | 10,114.7 |
| **Financial assets designated as available for sale** | | | | |
| Government and other securities | 10,699.4 | 856.8 | – | 11,556.2 |
| **Total financial assets accounted for at fair value** | 86,701.2 | 122,346.5 | 91.4 | 209,139.1 |
| **Financial liabilities held at fair value through profit and loss** | | | | |
| Currency deposits | – | (167,008.6) | – | (167,008.6) |
| Derivative financial instruments | (12.6) | (4,174.8) | – | (4,187.4) |
| Other liabilities (short positions in currency assets) | – | (66.0) | – | (66.0) |
| **Total financial liabilities accounted for at fair value** | (12.6) | (171,249.4) | – | (171,262.0) |

The Bank considers published price quotations in active markets as the best evidence of fair value. The financial instruments valued using active market quotes are categorised as level 1.

Where reliable published price quotations are not available for a financial instrument, the Bank determines fair value by using market standard valuation techniques. These valuation techniques include the use of discounted cash flow models as well as other standard market valuation methods. Where financial models are used, the Bank aims at making maximum use of observable market inputs. The financial instruments valued in this manner are categorised as level 2.

A small percentage of the Bank's financial instruments valuations are produced using valuation techniques that utilise significant unobservable inputs. The financial instruments valued in this manner are categorised as level 3. The financial instruments categorised as level 3 at 31 March 2010 and 2011 comprise illiquid corporate bonds.

The accuracy of the Bank's valuations is ensured through an independent price verification exercise performed by the valuation control function.

***B. Reconciliation of assets and liabilities measured at fair value level 3***

**As at 31 March 2011**

| *SDR millions* | Financial assets held at fair value through profit and loss | Financial assets designated as available for sale | **Total** |
|---|---|---|---|
| Balance at beginning of year | 91.4 | – | 91.4 |
| Gains in profit or loss | 0.7 | – | 0.7 |
| Gains in equity | – | – | – |
| **Total gains** | **0.7** | – | **0.7** |
| Disposals | (11.4) | – | (11.4) |
| Transfers out of level 3 | (31.7) | – | (31.7) |
| Transfers into level 3 | 15.1 | – | 15.1 |
| **Balance at end of year** | **64.1** | – | **64.1** |
| Gains in profit or loss for assets and liabilities held at end of year | 1.0 | – | 1.0 |

As at 31 March 2010

| *SDR millions* | Financial assets held at fair value through profit and loss | Financial assets designated as available for sale | **Total** |
|---|---|---|---|
| Balance at beginning of year | 566.6 | 28.5 | 595.1 |
| Gains in profit or loss | 109.0 | – | 109.0 |
| Gains in equity | – | 1.0 | 1.0 |
| **Total gains** | 109.0 | 1.0 | 110.0 |
| Disposals | (40.5) | – | (40.5) |
| Transfers out of level 3 | (617.5) | (29.5) | (647.0) |
| Transfers into level 3 | 73.8 | – | 73.8 |
| **Balance at end of year** | 91.4 | – | 91.4 |
| Gains in profit or loss for assets and liabilities held at end of year | 28.2 | – | 28.2 |

## 34. Effective interest rates

The effective interest rate is the rate that discounts the expected future cash flows of a financial instrument to the current book value.

The tables below summarise the effective interest rate by major currency for applicable financial instruments:

**As at 31 March 2011**

| *Percentages* | USD | EUR | GBP | JPY | Other currencies |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| Gold loans | – | – | – | – | 0.46 |
| Treasury bills | 0.26 | 0.93 | 0.60 | 0.11 | 0.82 |
| Securities purchased under resale agreements | 0.08 | 0.60 | 0.53 | 0.04 | – |
| Loans and advances | 0.28 | 0.94 | 0.68 | 0.10 | 0.16 |
| Government and other securities | 1.54 | 2.64 | 2.08 | 0.51 | 5.07 |
| **Liabilities** | | | | | |
| Currency deposits | 0.82 | 1.02 | 1.06 | 0.04 | 0.56 |
| Gold deposits | – | – | – | – | 0.38 |
| Short positions in currency assets | 4.53 | – | – | – | – |

As at 31 March 2010

| *Percentages* | USD | EUR | GBP | JPY | Other currencies |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| Gold loans | – | – | – | – | 0.49 |
| Treasury bills | 0.31 | 0.72 | 0.49 | 0.11 | 2.19 |
| Securities purchased under resale agreements | 0.12 | 0.21 | 0.47 | 0.05 | – |
| Loans and advances | 0.41 | 0.40 | 0.51 | 0.07 | 0.07 |
| Government and other securities | 1.96 | 2.66 | 2.19 | 0.66 | 4.75 |
| **Liabilities** | | | | | |
| Currency deposits | 1.03 | 0.73 | 1.34 | 0.12 | 0.28 |
| Gold deposits | – | – | – | – | 0.42 |
| Short positions in currency assets | 1.68 | – | – | – | – |

## 35. Geographical analysis

### *A. Total liabilities*

As at 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Africa and Europe | 76,200.4 | 93,697.7 |
| Asia-Pacific | 105,303.5 | 100,001.4 |
| Americas | 48,847.3 | 40,988.6 |
| International organisations | 14,097.3 | 8,430.3 |
| **Total** | **244,448.5** | 243,118.0 |

### *B. Off-balance sheet items*

As at 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Africa and Europe | 7,652.0 | 6,107.7 |
| Asia-Pacific | 18,918.4 | 17,911.3 |
| Americas | 3,903.1 | 1,170.5 |
| **Total** | **30,473.5** | 25,189.5 |

Note 31 provides further analysis of the Bank's off-balance sheet items. A geographical analysis of the Bank's assets is provided in the "Risk management" section below (note 3B).

### *C. Credit commitments*

As at 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Africa and Europe | 179.1 | 2,861.7 |
| Asia-Pacific | 2,108.6 | 2,058.1 |
| Americas | – | – |
| **Total** | **2,287.7** | 4,919.8 |

Note 32 provides further analysis of the Bank's credit commitments.

## 36. Related parties

The Bank considers the following to be its related parties:

- the members of the Board of Directors;
- the senior officials of the Bank;
- close family members of the above individuals;
- enterprises which could exert significant influence over a member of the Board of Directors or senior official, and enterprises over which one of these individuals could exert significant influence;
- the Bank's post-employment benefit arrangements; and
- central banks whose Governor is a member of the Board of Directors and institutions that are connected with these central banks.

A listing of the members of the Board of Directors and senior officials is shown in the section of the Annual Report entitled "Board of Directors and senior officials". Note 18 provides details of the Bank's post-employment benefit arrangements.

### *A. Related party individuals*

The total compensation of senior officials recognised in the profit and loss account amounted to:

For the financial year ended 31 March

| *CHF millions* | **2011** | 2010 |
|---|---|---|
| Salaries, allowances and medical cover | 7.7 | 6.9 |
| Post-employment benefits | 2.2 | 1.9 |
| **Total compensation in CHF millions** | **9.9** | 8.8 |
| SDR equivalent | 6.8 | 5.5 |

Note 24 provides details of the total compensation of the Board of Directors.

The Bank offers personal deposit accounts for all staff members and its Directors. The accounts bear interest at a rate determined by the Bank based on the rate offered by the Swiss National Bank on staff accounts. The movements and total balance on personal deposit accounts relating to members of the Board of Directors and the senior officials of the Bank were as follows:

For the financial year ended 31 March

| *CHF millions* | **2011** | 2010 |
|---|---|---|
| Balance at beginning of year | 19.7 | 12.8 |
| Deposits taken including interest income (net of withholding tax) | 4.2 | 8.6 |
| Withdrawals | (2.2) | (1.7) |
| **Balance at end of year in CHF millions** | **21.7** | 19.7 |
| SDR equivalent | 15.0 | 12.3 |
| Interest expense on deposits in CHF millions | 0.5 | 0.4 |
| SDR equivalent | 0.3 | 0.2 |

Balances related to individuals who are appointed as members of the Board of Directors or as senior officials of the Bank during the financial year are included in the table above along with other deposits taken. Balances related to individuals who cease to be members of the Board of Directors or senior officials of the Bank during the financial year are included in the table above along with other withdrawals.

In addition, the Bank operates a blocked personal deposit account for certain staff members who were previously members of the Bank's savings fund, which closed on 1 April 2003. The terms of these blocked accounts are such that staff members cannot make further deposits or withdrawals and the balances are paid out when they leave the bank. The accounts bear interest at a rate determined by the Bank based on the rate offered by the Swiss National Bank on staff accounts plus 1%. The total balance of blocked accounts at 31 March 2011 was SDR 20.9 million (2010: SDR 20.0 million). They are reported under the balance sheet heading "Currency deposits".

### *B. Related party central banks and connected institutions*

The BIS provides banking services to its customers, who are predominantly central banks, monetary authorities and international financial institutions. In fulfilling this role, the Bank in the normal course of business enters into transactions with related party central banks and connected institutions. These transactions include making advances, and taking currency and gold deposits.

It is the Bank's policy to enter into transactions with related party central banks and connected institutions on similar terms and conditions to transactions with other, non-related party customers.

*Currency deposits from related party central banks and connected institutions*

For the financial year ended 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Balance at beginning of year | 57,512.6 | 50,475.4 |
| Deposits taken | 362,877.5 | 356,011.2 |
| Maturities, repayments and fair value movements | (370,954.6) | (351,789.4) |
| Net movement on notice accounts | (2,279.2) | 2,815.4 |
| **Balance at end of year** | **47,156.3** | 57,512.6 |
| Percentage of total currency deposits at end of year | 22.8% | 29.4% |

*Gold deposit liabilities from related central banks and connected institutions*

For the financial year ended 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Balance at beginning of year | 27,688.7 | 19,468.7 |
| Deposits taken | – | 40.8 |
| Net withdrawals and gold price movements | – | (40.8) |
| Net movement on gold sight accounts | (12,152.7) | 8,220.0 |
| **Balance at end of year** | **15,536.0** | 27,688.7 |
| Percentage of total gold deposits at end of year | 73.0% | 86.4% |

*Securities purchased under resale transactions with related party central banks and connected institutions*

For the financial year ended 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Balance at beginning of year | 4,942.7 | 4,602.5 |
| Collateralised deposits placed | 1,176,076.2 | 903,642.0 |
| Maturities and fair value movements | (1,175,071.9) | (903,301.8) |
| **Balance at end of year** | **5,947.0** | 4,942.7 |
| Percentage of total securities purchased under resale agreements at end of year | 11.6% | 11.7% |

*Other balances with related party central banks and connected institutions*

The Bank maintains sight accounts in currencies with related party central banks and connected institutions, the total balance of which was SDR 314.6 million as at 31 March 2011 (2010: SDR 1,417.9 million). Gold held with related party central banks and connected institutions totalled SDR 35,383.0 million as at 31 March 2011 (2010: SDR 41,575.7 million).

*Derivative transactions with related party central banks and connected institutions*

The BIS enters into derivative transactions with related party central banks and connected institutions, including foreign exchange deals and interest rate swaps. The total nominal value of these transactions with related party central banks and connected institutions during the year ended 31 March 2011 was SDR 35,893.0 million (2010: SDR 19,431.3 million).

## 37. Contingent liabilities

In the opinion of the Bank's Management there were no material contingent liabilities at 31 March 2011.

# Capital adequacy

## 1. Capital

The table below shows the composition of the Bank's Tier 1 and total capital.

As at 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Share capital | 683.9 | 683.9 |
| Statutory reserves per balance sheet | 12,154.4 | 10,668.7 |
| Less: shares held in treasury | (1.7) | (1.7) |
| **Tier 1 capital** | **12,836.6** | 11,350.9 |
| Profit and loss account | 816.0 | 1,859.8 |
| Other equity accounts | 3,017.7 | 2,564.6 |
| **Total equity** | **16,670.3** | 15,775.3 |

The Bank assesses its capital adequacy continuously. The assessment is supported by an annual capital and business planning process.

The Bank has implemented a risk framework that is consistent with the revised *International Convergence of Capital Measurement and Capital Standards* (Basel II Framework) issued by the Basel Committee on Banking Supervision in June 2006. The implementation includes all three pillars of the Framework, and takes the particular scope and nature of the Bank's activities into account. Since the Bank is not subject to national banking supervisory regulation, the application of Pillar 2 is limited to the Bank's own assessment of capital adequacy. This assessment is based primarily on an economic capital methodology which is more comprehensive and geared to a substantially higher solvency level than the minimum Pillar 1 capital level required by the Basel II Framework.

## 2. Economic capital

The Bank's own assessment of its capital adequacy is performed on the basis of its economic capital frameworks for market risk, credit risk, operational risk and other risks. These are designed to determine the amount of equity needed to absorb losses arising from its exposures to a statistical level of confidence consistent with the objective of maintaining superior credit quality. The Bank's economic capital frameworks measure economic capital to a 99.995% confidence level assuming a one-year horizon, except for other risks. The amount of economic capital set aside for other risks is based on Management's assessment of risks which are not, or not fully, reflected in the Bank's economic capital calculations.

The following table summarises the Bank's economic capital utilisation for credit risk, market risk, operational risk and other risks:

As at 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| Credit risk | 5,974.2 | 5,659.8 |
| Market risk | 2,836.5 | 2,708.7 |
| Operational risk | 700.0 | 475.0 |
| Other risks | 300.0 | 300.0 |
| **Total economic capital utilisation** | **9,810.7** | 9,143.5 |

### 3. Risk-weighted assets and minimum capital requirements under the Basel II Framework

The Basel II Framework includes several approaches for calculating risk-weighted assets and the corresponding minimum capital requirements. In principle, the minimum capital requirements are determined by taking 8% of the risk-weighted assets.

The following table summarises the relevant exposure types and approaches as well as the risk-weighted assets and related minimum capital requirements for credit risk, market risk and operational risk.

| As at 31 March | | 2011 | | | 2010 | | |
|---|---|---|---|---|---|---|---|
| *SDR millions* | Approach used | Amount of exposure | Risk-weighted assets (A) | Minimum capital requirement (B) | Amount of exposure | Risk-weighted assets (A) | Minimum capital requirement (B) |
| **Credit risk** | | | | | | | |
| Exposure to sovereigns, banks and corporates | Advanced internal ratings-based approach, where (B) is derived as (A) x 8% | 158,491.3 | 7,538.3 | 603.1 | 207,871.9 | 9,027.4 | 722.2 |
| Securitisation exposures, externally managed portfolios and other assets | Standardised approach, where (B) is derived as (A) x 8% | 2,256.6 | 1,190.0 | 95.2 | 2,820.7 | 1,159.5 | 92.8 |
| **Market risk** | | | | | | | |
| Exposure to foreign exchange risk and gold price risk | Internal models approach, where (A) is derived as (B) / 8% | – | 10,806.2 | 864.5 | – | 10,768.1 | 861.4 |
| **Operational risk** | Advanced measurement approach, where (A) is derived as (B) / 8% | – | 3,760.4 | 300.8 | – | 2,256.3 | 180.5 |
| **Total** | | | **23,294.9** | **1,863.6** | | 23,211.3 | 1,856.9 |

For credit risk, the Bank has adopted the advanced internal ratings-based approach for the majority of its exposures. Under this approach, the risk weighting for a transaction is determined by the relevant Basel II risk weight function using the Bank's own estimates for key inputs. For certain exposures, the Bank has adopted the standardised approach. Under this approach, risk weightings are mapped to exposure types.

Risk-weighted assets for market risk are derived following an internal models approach. For operational risk, the advanced measurement approach is used. Both these approaches rely on value-at-risk (VaR) methodologies. The minimum capital requirements are derived from the VaR figures and are translated into risk-weighted assets taking into account the 8% minimum capital requirement.

More details on the assumptions underlying the calculations are provided in the sections on credit risk, market risk and operational risk.

## 4. Tier 1 capital ratio

The capital ratio measures capital adequacy by comparing the Bank's Tier 1 capital with its risk-weighted assets. The table below shows the Bank's Tier 1 capital ratio, consistent with the Basel II Framework.

As at 31 March

| *SDR millions* | **2011** | 2010 |
|---|---|---|
| **Tier 1 capital (A)** | **12,836.6** | 11,350.9 |
| Total risk-weighted assets (B) | 23,294.9 | 23,211.3 |
| **Tier 1 capital ratio (A) / (B)** | **55.1%** | 48.9% |

As required by the Basel II Framework, expected loss is calculated for credit risk exposures subject to the advanced internal ratings-based approach. The expected loss is calculated at the balance sheet date taking into account the impairment provision which is reflected in the Bank's financial statements. Note 2B to the financial statements provides details of the impairment provision. In accordance with the requirements of the Basel II Framework, the expected loss is compared with the impairment provision and any shortfall is deducted from the Bank's Tier 1 capital. At 31 March 2011 the impairment provision exceeded the expected loss.

The Bank maintains a very high creditworthiness and performs a comprehensive capital assessment considering its specific characteristics. As such, it maintains a capital position substantially in excess of the minimum requirement.

# Risk management

## 1. Risks faced by the Bank

The Bank supports its customers, predominantly central banks, monetary authorities and international financial institutions, in the management of their reserves and related financial activities.

Banking activities form an essential element of meeting the Bank's objectives and, as such, ensure its financial strength and independence. The BIS engages in banking activities that are customer-related as well as activities that are related to the investment of its equity, each of which may give rise to financial risk comprising credit risk, market risk and liquidity risk. The Bank is also exposed to operational risk.

Within the risk framework defined by the Board of Directors, the Management of the Bank has established risk management policies designed to ensure that risks are identified, appropriately measured and controlled as well as monitored and reported.

## 2. Risk management approach and organisation

The Bank maintains superior credit quality and adopts a prudent approach to financial risk-taking, by:

- maintaining an exceptionally strong capital position;
- investing its assets predominantly in high credit quality financial instruments;
- seeking to diversify its assets across a range of sectors;
- adopting a conservative approach to its tactical market risk-taking and carefully managing market risk associated with the Bank's strategic positions, which include its gold holdings; and
- maintaining a high level of liquidity.

### *A. Organisation*

Under Article 39 of the Bank's Statutes, the General Manager is responsible to the Board for the management of the Bank, and is assisted by the Deputy General Manager. The Deputy General Manager is responsible for the Bank's independent risk control and compliance functions. The General Manager and the Deputy General Manager are supported by senior management advisory committees.

The key advisory committees are the Executive Committee, the Finance Committee and the Compliance and Operational Risk Committee. The first two committees are chaired by the General Manager and the third by the Deputy General Manager, and all include other senior members of the Bank's Management. The Executive Committee advises the General Manager primarily on the Bank's strategic planning and the allocation of resources, as well as on decisions related to the broad financial objectives for the banking activities and operational risk management. The Finance Committee advises the General Manager on the financial management and policy issues related to the banking business, including the allocation of economic capital to risk categories. The Compliance and Operational Risk Committee acts as an advisory committee to the Deputy General Manager and ensures the coordination of compliance matters and operational risk management throughout the Bank.

The independent risk control function for financial risks is performed by the Risk Control unit. The independent operational risk control function is shared between Risk Control, which maintains the operational risk quantification, and the Compliance and Operational Risk Unit. Both units report directly to the Deputy General Manager.

The Bank's compliance function is performed by the Compliance and Operational Risk Unit. The objective of this function is to provide reasonable assurance that the activities of the Bank and its staff conform to applicable laws and regulations, the BIS Statutes, the Bank's Code of Conduct and other internal rules, policies and relevant standards of sound practice.

The Compliance and Operational Risk Unit identifies and assesses compliance risks and guides and educates staff on compliance issues. The Head of the Compliance and Operational Risk Unit also has a direct reporting line to the Audit Committee, which is an advisory committee to the Board of Directors.

The Finance unit and the Legal Service complement the Bank's risk management. The Finance unit operates an independent valuation control function, produces the Bank's financial statements and controls the Bank's expenditure by setting and monitoring the annual budget. The objective of the independent valuation control function is to ensure that the Bank's valuations comply with its valuation policy and procedures, and that the processes and procedures which influence the Bank's valuations conform to best practice guidelines. The Finance unit has a direct reporting line to the Secretary General.

The Legal Service provides legal advice and support covering a wide range of issues relating to the Bank's activities. The Legal Service has a direct reporting line to the General Manager.

The Internal Audit function reviews internal control procedures and reports on how they comply with internal standards and industry best practices. The scope of internal audit work includes the review of risk management procedures, internal control systems, information systems and governance processes. Internal Audit has a direct reporting line to the Audit Committee and is responsible to the General Manager and the Deputy General Manager.

### *B. Risk monitoring and reporting*

The Bank's financial and operational risk profile, position and performance are monitored on an ongoing basis by the relevant units. Financial risk and compliance reports aimed at various management levels are regularly provided to enable Management to adequately assess the Bank's risk profile and financial condition.

Management reports financial and risk information to the Board of Directors on a monthly and a quarterly basis. Furthermore, the Audit Committee receives regular reports from Internal Audit, the Compliance and Operational Risk Unit and the Finance unit. The Banking and Risk Management Committee, another advisory committee to the Board, receives an annual report from the Risk Control unit. The preparation of reports is subject to comprehensive policies and procedures, thus ensuring strong controls.

### *C. Risk methodologies*

The Bank revalues virtually all of its financial assets to fair value on a daily basis and reviews its valuations monthly, taking into account necessary adjustments for impairment. It uses a comprehensive range of quantitative methodologies for valuing financial instruments and for measuring risk to its net profit and equity. The Bank reassesses its quantitative methodologies in the light of its changing risk environment and evolving best practice.

The Bank's model validation policy defines the roles and responsibilities and processes related to the implementation of new or materially changed risk models.

A key methodology used by the Bank to measure and manage risk is the calculation of economic capital based on value-at-risk (VaR) techniques. VaR expresses the statistical estimate of the maximum potential loss on the current positions of the Bank measured to a specified level of confidence and a specified time horizon.

The Bank's economic capital calculation is designed to measure the amount of equity needed to absorb losses arising from its exposures to a statistical level of confidence determined by the Bank's aim to remain of the highest creditworthiness.

The Bank assesses its capital adequacy on the basis of economic capital frameworks for market risk, credit risk, operational risk and other risks, supplemented by sensitivity and risk factor analyses. The Bank's economic capital frameworks measure economic capital to a 99.995% confidence interval assuming a one-year holding period.

The Bank allocates economic capital to the above risk categories. An additional amount of economic capital is set aside based on Management's assessment of risks which are not, or not fully, reflected in the economic capital calculations.

A comprehensive stress testing framework complements the Bank's risk assessment including its VaR and economic capital calculations for financial risk. The Bank's key market risk factors and credit exposures are stress-tested. The stress testing includes the analysis of severe historical and adverse hypothetical macroeconomic scenarios, as well as sensitivity tests of extreme but still plausible movements of the key risk factors identified. The Bank also performs stress tests related to liquidity risk.

## 3. Credit risk

Credit risk arises because a counterparty may fail to meet its obligations in accordance with the agreed contractual terms and conditions. A financial asset is considered past due when a counterparty fails to make a payment on the contractual due date.

The Bank manages credit risk within a framework and policies set by the Board of Directors and Management. These are complemented by more detailed guidelines and procedures at the level of the independent risk control function.

### *A. Credit risk assessment*

Credit risk is continuously controlled at both a counterparty and an aggregated level. As part of the independent risk control function, individual counterparty credit assessments are performed subject to a well defined internal rating process, involving 18 rating grades. As part of this process, counterparty financial statements and market information are analysed. The rating methodologies depend on the nature of the counterparty. Based on the internal rating and specific counterparty features, the Bank sets a series of credit limits covering individual counterparties and countries. Internal ratings are assigned to all counterparties. In principle, the ratings and related limits are reviewed at least annually. The main assessment criterion in these reviews is the ability of the counterparties to meet interest and principal repayment obligations in a timely manner.

Credit risk limits at the counterparty level are approved by the Bank's Management and fit within a framework set by the Board of Directors.

On an aggregated level credit risk, including default and country transfer risk, is measured, monitored and controlled based on the Bank's economic capital calculation for credit risk. To calculate economic capital for credit risk, the Bank uses a portfolio VaR model. Management limits the Bank's overall exposure to credit risk by allocating an amount of economic capital to credit risk.

### *B. Default risk*

The following tables show the exposure of the Bank to default risk, without taking into account any collateral held or other credit enhancements available to the Bank. Credit risk is further mitigated through the use of collateral and legally enforceable netting or setoff agreements. The corresponding assets and liabilities are not offset on the balance sheet.

The exposures set out in the tables below are based on the carrying value of the assets on the balance sheet as categorised by sector, geographical region and credit quality. The carrying value is the fair value of the financial instruments, including derivatives, except in the case of very short-term financial instruments (sight and notice accounts) and gold, which are shown at amortised cost net of any impairment charge. Commitments are reported at their notional amounts. Gold and gold loans exclude gold bar assets held in custody, and accounts receivable do not include unsettled liability issues, because these items do not represent credit exposures of the Bank.

The vast majority of the Bank's assets are invested in securities issued by G10 governments and financial institutions rated A– or above by at least one of the major external credit assessment institutions. Limitations on the number of high-quality counterparties in these sectors mean that the Bank is exposed to single-name concentration risk.

Gold loans include a provision of SDR 29.0 million following an impairment review as at 31 March 2011 (31 March 2010: SDR 23.5 million). The increase in the provision during the reporting period ended 31 March 2011 is due to changes in gold prices and exchange rates.

As at 31 March 2011, no financial assets were considered past due (31 March 2010: nil).

### *Default risk by asset class and issuer type*

The following tables show the exposure of the Bank to default risk by asset class and issuer type, without taking into account any collateral held or other credit enhancements available to the Bank. "Public sector" includes international and other public sector institutions.

**As at 31 March 2011**

| *SDR millions* | Sovereign and central banks | Public sector | Banks | Corporate | Securitisation | Total |
|---|---|---|---|---|---|---|
| **On-balance sheet exposures** | | | | | | |
| Cash and sight accounts with banks | 316.7 | – | 6.8 | 6.3 | – | 329.8 |
| Gold and gold loans | – | – | 1,225.1 | 29.1 | – | 1,254.2 |
| Treasury bills | 76,932.1 | – | – | – | – | 76,932.1 |
| Securities purchased under resale agreements | 5,947.0 | – | 45,517.0 | – | – | 51,464.0 |
| Loans and advances | 1,182.5 | 424.2 | 22,563.7 | – | – | 24,170.4 |
| Government and other securities | 28,467.5 | 14,375.1 | 9,206.9 | 3,589.2 | 1,349.2 | 56,987.9 |
| Derivatives | 156.2 | 31.4 | 5,602.1 | 0.6 | – | 5,790.3 |
| Accounts receivable | 2.0 | 434.9 | 131.5 | 8.0 | – | 576.4 |
| **Total on-balance sheet exposure** | **113,004.0** | **15,265.6** | **84,253.1** | **3,633.2** | **1,349.2** | **217,505.1** |
| **Commitments** | | | | | | |
| Undrawn unsecured facilities | 189.4 | – | – | – | – | 189.4 |
| Undrawn secured facilities | 2,098.3 | – | – | – | – | 2,098.3 |
| **Total commitments** | **2,287.7** | **–** | **–** | **–** | **–** | **2,287.7** |
| **Total exposure** | **115,291.7** | **15,265.6** | **84,253.1** | **3,633.2** | **1,349.2** | **219,792.8** |

As at 31 March 2010

| *SDR millions* | Sovereign and central banks | Public sector | Banks | Corporate | Securitisation | Total |
|---|---|---|---|---|---|---|
| **On-balance sheet exposures** | | | | | | |
| Cash and sight accounts with banks | 1,419.9 | – | 96.3 | – | – | 1,516.2 |
| Gold and gold loans | – | – | 1,440.6 | 23.5 | – | 1,464.1 |
| Treasury bills | 84,714.8 | – | – | – | – | 84,714.8 |
| Securities purchased under resale agreements | 4,942.7 | – | 35,497.5 | 1,865.7 | – | 42,305.9 |
| Loans and advances | 2,887.0 | 655.4 | 15,746.2 | – | – | 19,288.6 |
| Government and other securities | 24,325.0 | 12,411.4 | 12,464.5 | 2,378.4 | 2,108.4 | 53,687.7 |
| Derivatives | 48.7 | 139.1 | 9,926.1 | 0.8 | – | 10,114.7 |
| Accounts receivable | 182.6 | – | 378.8 | 9.4 | – | 570.8 |
| **Total on-balance sheet exposure** | 118,520.7 | 13,205.9 | 75,550.0 | 4,277.8 | 2,108.4 | 213,662.8 |
| **Commitments** | | | | | | |
| Undrawn unsecured facilities | 2,420.7 | – | – | – | – | 2,420.7 |
| Undrawn secured facilities | 2,499.1 | – | – | – | – | 2,499.1 |
| **Total commitments** | 4,919.8 | – | – | – | – | 4,919.8 |
| **Total exposure** | 123,440.5 | 13,205.9 | 75,550.0 | 4,277.8 | 2,108.4 | 218,582.6 |

*Default risk by geographical region*

The following tables represent the exposure of the Bank to default risk by geographical region, without taking into account any collateral held or other credit enhancements available to the Bank.

**As at 31 March 2011**

| *SDR millions* | Africa and Europe | Asia-Pacific | Americas | International institutions | Total |
|---|---|---|---|---|---|
| **On-balance sheet exposures** | | | | | |
| Cash and sight accounts with banks | 315.1 | 1.2 | 13.5 | – | 329.8 |
| Gold and gold loans | 901.8 | 58.3 | 294.1 | – | 1,254.2 |
| Treasury bills | 37,831.2 | 36,796.9 | 2,304.0 | – | 76,932.1 |
| Securities purchased under resale agreements | 45,359.2 | 5,710.0 | 394.8 | – | 51,464.0 |
| Loans and advances | 19,224.0 | 3,429.6 | 1,345.2 | 171.6 | 24,170.4 |
| Government and other securities | 31,368.7 | 3,427.6 | 13,667.5 | 8,524.1 | 56,987.9 |
| Derivatives | 4,082.8 | 175.1 | 1,532.1 | 0.3 | 5,790.3 |
| Accounts receivable | 140.6 | 0.8 | 435.0 | – | 576.4 |
| **Total on-balance sheet exposure** | **139,223.4** | **49,599.5** | **19,986.2** | **8,696.0** | **217,505.1** |
| **Commitments** | | | | | |
| Undrawn unsecured facilities | – | 189.4 | – | – | 189.4 |
| Undrawn secured facilities | 179.1 | 1,919.2 | – | – | 2,098.3 |
| **Total commitments** | **179.1** | **2,108.6** | **–** | **–** | **2,287.7** |
| **Total exposure** | **139,402.5** | **51,708.1** | **19,986.2** | **8,696.0** | **219,792.8** |

As at 31 March 2010

| *SDR millions* | Africa and Europe | Asia-Pacific | Americas | International institutions | Total |
|---|---|---|---|---|---|
| **On-balance sheet exposures** | | | | | |
| Cash and sight accounts with banks | 1,425.4 | 0.8 | 90.0 | – | 1,516.2 |
| Gold and gold loans | 967.5 | 258.8 | 237.8 | – | 1,464.1 |
| Treasury bills | 43,846.7 | 40,642.0 | 226.1 | – | 84,714.8 |
| Securities purchased under resale agreements | 37,363.3 | 4,777.9 | 164.7 | – | 42,305.9 |
| Loans and advances | 14,323.0 | 3,554.4 | 822.5 | 588.7 | 19,288.6 |
| Government and other securities | 33,323.6 | 4,219.2 | 9,656.9 | 6,488.0 | 53,687.7 |
| Derivatives | 7,106.0 | 237.3 | 2,771.4 | – | 10,114.7 |
| Accounts receivable | 99.7 | 91.6 | 379.5 | – | 570.8 |
| **Total on-balance sheet exposure** | 138,455.2 | 53,782.0 | 14,348.9 | 7,076.7 | 213,662.8 |
| **Commitments** | | | | | |
| Undrawn unsecured facilities | 2,223.4 | 197.3 | – | – | 2,420.7 |
| Undrawn secured facilities | 638.3 | 1,860.8 | – | – | 2,499.1 |
| **Total commitments** | 2,861.7 | 2,058.1 | – | – | 4,919.8 |
| **Total exposure** | 141,316.9 | 55,840.1 | 14,348.9 | 7,076.7 | 218,582.6 |

The Bank has allocated exposures to regions based on the country of incorporation of each legal entity.

### *Default risk by counterparty / issuer rating*

The following tables show the exposure of the Bank to default risk by class of financial asset, without taking into account any collateral held or other credit enhancements available to the Bank.

The ratings shown reflect the Bank's internal ratings expressed as equivalent external ratings. The vast majority of the Bank's exposure is rated equivalent to A– or above.

| **As at 31 March 2011**<br>*SDR millions* | AAA | AA | A | BBB | BB and below | Unrated | Total |
|---|---|---|---|---|---|---|---|
| **On-balance sheet exposures** | | | | | | | |
| Cash and sight accounts with banks | 315.3 | 11.7 | 2.1 | 0.3 | 0.1 | 0.3 | 329.8 |
| Gold and gold loans | – | 303.8 | 921.3 | 29.1 | – | – | 1,254.2 |
| Treasury bills | 28,360.2 | 41,532.1 | 7,039.8 | – | – | – | 76,932.1 |
| Securities purchased under resale agreements | 237.0 | 13,499.4 | 37,727.6 | – | – | – | 51,464.0 |
| Loans and advances | 1,543.6 | 7,498.1 | 15,128.7 | – | – | – | 24,170.4 |
| Government and other securities | 36,427.9 | 12,321.0 | 7,501.6 | 686.5 | 50.9 | – | 56,987.9 |
| Derivatives | 31.3 | 798.3 | 4,914.0 | 0.1 | 46.0 | 0.6 | 5,790.3 |
| Accounts receivable | 435.0 | 0.3 | 134.9 | 0.3 | 1.4 | 4.5 | 576.4 |
| **Total on-balance sheet exposure** | **67,350.3** | **75,964.7** | **73,370.0** | **716.3** | **98.4** | **5.4** | **217,505.1** |
| *Percentages* | *31.0%* | *34.9%* | *33.7%* | *0.3%* | *0.1%* | *0.0%* | *100.0%* |
| **Commitments** | | | | | | | |
| Undrawn unsecured facilities | – | – | – | 189.4 | – | – | 189.4 |
| Undrawn secured facilities | – | 710.0 | 721.8 | 419.7 | 246.8 | – | 2,098.3 |
| **Total commitments** | **–** | **710.0** | **721.8** | **609.1** | **246.8** | **–** | **2,287.7** |
| **Total exposure** | **67,350.3** | **76,674.7** | **74,091.8** | **1,325.4** | **345.2** | **5.4** | **219,792.8** |

| As at 31 March 2010<br>SDR millions | AAA | AA | A | BBB | BB and below | Unrated | Total |
|---|---|---|---|---|---|---|---|
| **On-balance sheet exposures** | | | | | | | |
| Cash and sight accounts with banks | 1,418.2 | 6.6 | 90.7 | 0.6 | – | 0.1 | 1,516.2 |
| Gold and gold loans | – | 347.4 | 1,093.2 | 23.5 | – | – | 1,464.1 |
| Treasury bills | 29,892.4 | 45,901.5 | 8,920.9 | – | – | – | 84,714.8 |
| Securities purchased under resale agreements | 164.8 | 9,935.1 | 32,206.0 | – | – | – | 42,305.9 |
| Loans and advances | 1,731.9 | 3,962.9 | 12,705.2 | 230.8 | 657.8 | – | 19,288.6 |
| Government and other securities | 33,369.9 | 12,306.2 | 7,710.4 | 301.2 | – | – | 53,687.7 |
| Derivatives | 147.4 | 1,563.4 | 8,365.3 | 1.4 | 37.2 | – | 10,114.7 |
| Accounts receivable | 467.7 | 91.6 | – | – | – | 11.5 | 570.8 |
| **Total on-balance sheet exposure** | 67,192.3 | 74,114.7 | 71,091.7 | 557.5 | 695.0 | 11.6 | 213,662.8 |
| *Percentages* | *31.4%* | *34.7%* | *33.3%* | *0.3%* | *0.3%* | *0.0%* | *100%* |
| **Commitments** | | | | | | | |
| Undrawn unsecured facilities | 2,223.4 | – | – | 197.3 | – | – | 2,420.7 |
| Undrawn secured facilities | 219.1 | 468.3 | 700.1 | 871.7 | 239.9 | – | 2,499.1 |
| **Total commitments** | 2,442.5 | 468.3 | 700.1 | 1,069.0 | 239.9 | – | 4,919.8 |
| **Total exposure** | 69,634.8 | 74,583.0 | 71,791.8 | 1,626.5 | 934.9 | 11.6 | 218,582.6 |

### *C. Credit risk mitigation*

Credit risk is mitigated through the use of collateral and legally enforceable netting or setoff agreements. The corresponding assets and liabilities are not offset on the balance sheet.

The Bank requires counterparties to provide collateral, under reverse repurchase agreements, some derivative financial instrument contracts and certain drawn-down facility agreements, to mitigate counterparty default risk in accordance with the respective policies and procedures. During the term of the agreement, the Bank monitors the fair value of the collateral securities and may call for further collateral or be required to return collateral based on the movement in its market value.

The Bank mitigates settlement risk by using established clearing centres and by settling transactions where possible through a delivery versus payment settlement mechanism. Daily settlement risk limits are monitored on a continuous basis.

The table below shows the collateral obtained by the Bank. It excludes transactions which have yet to settle (on which neither cash nor collateral has been exchanged).

| As at 31 March | **2011** | | 2010 | |
|---|---|---|---|---|
| *SDR millions* | Fair value of relevant contracts | Value of collateral | Fair value of relevant contracts | Value of collateral |
| **Collateral obtained for** | | | | |
| Securities purchased under resale agreements | 45,703.9 | 45,858.7 | 34,301.6 | 35,055.3 |
| Advances | 63.1 | 67.5 | 1,512.8 | 2,170.6 |
| Derivatives | 1,639.8 | 1,743.5 | 4,144.6 | 4,425.2 |
| **Total collateral obtained** | **47,406.8** | **47,669.7** | 39,959.0 | 41,651.1 |

The Bank is allowed to sell or pledge collateral obtained, but must deliver equivalent financial instruments upon expiry of the contract. The Bank accepts sovereign securities and cash as collateral for derivatives. Eligible collateral for reverse repurchase agreements comprises sovereign and supranational debt as well as US agency securities. Eligible collateral for loans and advances includes currency deposits with the Bank as well as units in the BIS Investment Pools (BISIPs) and securities in portfolios managed by the BIS.

As at 31 March 2011 the total amount of undrawn facilities which could be drawn down subject to collateralisation by the counterparty was SDR 2,098.3 million (2010: SDR 2,499.1 million).

The Bank did not provide collateral on any of its financial instrument contracts as at 31 March 2011 (2010: nil).

### *D. Economic capital for credit risk*

The Bank determines economic capital for credit risk using a VaR methodology on the basis of a portfolio VaR model, assuming a one-year time horizon and a 99.995% confidence interval. The table below shows the key figures of the Bank's exposure to credit risk in terms of economic capital utilisation over the past two financial years.

| For the financial year | **2011** | | | | 2010 | | | |
|---|---|---|---|---|---|---|---|---|
| *SDR millions* | Average | High | Low | At 31 March | Average | High | Low | At 31 March |
| **Economic capital utilisation for credit risk** | 5,807.1 | 6,315.0 | 5,345.7 | **5,974.2** | 5,653.2 | 6,072.9 | 5,110.5 | 5,659.8 |

### *E. Minimum capital requirements for credit risk*

#### *Exposure to sovereigns, banks and corporates*

For the calculation of risk-weighted assets for exposures to banks, sovereigns and corporates, the Bank has adopted an approach that is consistent with the advanced internal ratings-based approach.

As a general rule, under this approach risk-weighted assets are determined by multiplying the credit risk exposures with risk weights derived from the relevant Basel II risk weight function using the Bank's own estimates for key inputs. These estimates for key inputs are also relevant to the Bank's economic capital calculation for credit risk.

The credit risk exposure for a transaction or position is referred to as the exposure at default (EAD). The Bank determines the EAD as the notional amount of all on- and off-balance sheet credit exposures, except derivatives. The EAD for derivatives is calculated using an approach consistent with the internal models method proposed under the Basel II Framework. In line with this methodology, the Bank calculates effective expected positive exposures that are then multiplied by a factor alpha as set out in the Framework.

Key inputs to the risk weight function are a counterparty's estimated one-year probability of default (PD) as well as the estimated loss-given-default (LGD) and maturity for each transaction.

Due to the high credit quality of the Bank's investments and the conservative credit risk management process at the BIS, the Bank is not in a position to estimate PDs and LGDs based on its own default experience. The Bank calibrates counterparty PD estimates through a mapping of internal rating grades to external credit assessments taking external default data into account. Similarly, LGD estimates are derived from external data. Where appropriate, these estimates are adjusted to reflect the risk-reducing effects of collateral obtained giving consideration to market price volatility, remargining and revaluation frequency.

During the reporting period methodological refinements have been implemented to shift the recognition of the risk-reducing effects of collateral obtained for derivative contracts, reverse repurchase agreements and collateralised advances to the EAD. In addition, refinements have been implemented with the aim of extending the scope for the recognition of netting agreements.

The table below details the calculation of risk-weighted assets. The exposures are measured taking netting and collateral benefits into account. The total amount of exposures reported in the table as at 31 March 2011 includes SDR 463.0 million for interest rate contracts (31 March 2010: SDR 4,687.7 million) and SDR 287.5 million for FX and gold contracts (31 March 2010: SDR 6,028.4 million).

**As at 31 March 2011**

| **Internal rating grades expressed as equivalent external rating grades** *SDR millions / percentages* | Amount of exposure *SDR millions* | Exposure-weighted PD *%* | Exposure-weighted average LGD *%* | Exposure-weighted average risk weight *%* | Risk-weighted assets *SDR millions* |
|---|---|---|---|---|---|
| AAA | 63,927.4 | 0.004 | 37.8 | 1.9 | 1,197.8 |
| AA | 61,483.3 | 0.02 | 40.7 | 4.1 | 2,496.1 |
| A | 32,008.5 | 0.05 | 48.2 | 10.6 | 3,399.1 |
| BBB | 1,008.2 | 0.19 | 41.7 | 39.5 | 398.1 |
| BB and below | 63.9 | 1.00 | 42.3 | 73.7 | 47.2 |
| **Total** | **158,491.3** | | | | **7,538.3** |

As at 31 March 2010

| Internal rating grades expressed as equivalent external rating grades *SDR millions / percentages* | Amount of exposure *SDR millions* | Exposure-weighted PD *%* | Exposure-weighted average LGD *%* | Exposure-weighted average risk weight *%* | Risk-weighted assets *SDR millions* |
|---|---|---|---|---|---|
| AAA | 64,185.5 | 0.006 | 31.8 | 2.7 | 1,705.0 |
| AA | 70,006.0 | 0.02 | 28.3 | 3.8 | 2,689.4 |
| A | 70,804.3 | 0.06 | 21.0 | 5.9 | 4,147.2 |
| BBB | 1,916.2 | 0.31 | 16.9 | 12.0 | 230.8 |
| BB and below | 959.9 | 9.85 | 6.2 | 26.6 | 255.0 |
| **Total** | 207,871.9 | | | | 9,027.4 |

The table below summarises the impact of collateral arrangements on the amount of credit exposure after taking netting into account.

**As at 31 March 2011**

| *SDR millions* | Amount of exposure after taking netting into account | Benefits from collateral arrangements | Amount of exposure after taking into account netting and collateral arrangements |
|---|---|---|---|
| **Total** | 212,964.8 | 54,473.5 | **158,491.3** |

### *F. Securitisation exposures*

The Bank only invests in highly rated securitisation exposures based on traditional, ie non-synthetic, securitisation structures. Given the scope of the Bank's activities, risk-weighted assets under the Basel II Framework are determined according to the standardised approach for securitisation. Under this approach, external credit assessments of the securities are used to determine the relevant risk weights. External credit assessment institutions used for this purpose are Moody's Investors Service, Standard & Poor's and Fitch Ratings. Risk-weighted assets are then derived as the product of the notional amounts of the exposures and the associated risk weights.

The following table shows the Bank's investments in securitisation analysed by type of securitised assets:

**As at 31 March 2011**

| *SDR millions* | External rating | Amount of exposures | Risk weight | Risk-weighted assets |
|---|---|---|---|---|
| Residential mortgage-backed securities | AAA | 161.1 | 20% | 32.2 |
| Securities backed by credit card receivables | AAA | 376.3 | 20% | 75.3 |
| Securities backed by other receivables (government-sponsored) | AAA | 795.8 | 20% | 159.2 |
| **Total** | | **1,333.2** | | **266.7** |

As at 31 March 2010

| *SDR millions* | External rating | Amount of exposures | Risk weight | Risk-weighted assets |
|---|---|---|---|---|
| Residential mortgage-backed securities | AAA | 471.6 | 20% | 94.3 |
| Securities backed by credit card receivables | AAA | 857.6 | 20% | 171.5 |
| Securities backed by other receivables (government-sponsored) | AAA | 747.2 | 20% | 149.5 |
| **Total** | | 2,076.4 | | 415.3 |

## 4. Market risk

The Bank is exposed to market risk through adverse movements in market prices. The main components of the Bank's market risk are gold price risk, interest rate risk and foreign exchange risk. The Bank measures market risk and calculates economic capital based on a VaR methodology using a Monte Carlo simulation technique. Risk factor volatilities and correlations are estimated using a one-year observation period. Furthermore, the Bank computes sensitivities to certain market risk factors.

In line with the Bank's objective of maintaining its superior credit quality, economic capital is measured at the 99.995% confidence interval assuming a one-year holding period. The Bank's Management manages market risk economic capital usage within a framework set by the Board of Directors. VaR limits are supplemented by operating limits.

VaR models depend on statistical assumptions and the quality of available market data and, while forward-looking, they extrapolate from past events.

To ensure that models provide a reliable measure of potential losses over the one-year time horizon, the Bank has established a comprehensive regular backtesting framework, comparing daily performance with corresponding VaR estimates. The results are analysed and reported to Management.

The Bank also supplements its market risk measurement based on VaR modelling and related economic capital calculations with a series of stress tests. These include severe historical scenarios, adverse hypothetical macroeconomic scenarios and sensitivity tests of gold price, interest rate and foreign exchange rate movements.

### *A. Gold price risk*

Gold price risk is the exposure of the Bank's financial condition to adverse movements in the price of gold.

The Bank is exposed to gold price risk principally through its holdings of gold investment assets, which amount to 119 tonnes (2010: 120 tonnes). These gold investment assets are held in custody or placed on deposit with commercial banks. At 31 March 2011 the Bank's net gold investment assets amounted to SDR 3,451.2 million (2010: SDR 2,811.2 million), approximately 21% of its equity (2010: 18%). The Bank sometimes also has small exposures to gold price risk emerging from its banking activities with central and commercial banks. Gold price risk is measured within the Bank's VaR methodology, including its economic capital framework and stress tests.

### *B. Interest rate risk*

Interest rate risk is the exposure of the Bank's financial condition to adverse movements in interest rates including credit spreads. The Bank is exposed to interest rate risk through the interest bearing assets relating to the management of its equity held in its investment portfolios and investments relating to its banking portfolios. The investment portfolios are managed using a fixed duration benchmark of bonds.

The Bank measures and monitors interest rate risk using a VaR methodology and sensitivity analyses taking into account movements in relevant money market rates, government bonds, swap rates and credit spreads.

The tables below show the impact on the Bank's equity of a 1% upward shift in the relevant yield curve per time band:

**As at 31 March 2011**

| *SDR millions* | Up to 6 months | 6 to 12 months | 1 to 2 years | 2 to 3 years | 3 to 4 years | 4 to 5 years | Over 5 years |
|---|---|---|---|---|---|---|---|
| Euro | 2.6 | (8.6) | (16.9) | (11.0) | (27.4) | (32.1) | (29.3) |
| Japanese yen | 0.9 | (3.3) | (6.1) | (5.2) | (13.7) | (2.8) | (3.2) |
| Pound sterling | 1.8 | (2.9) | (3.5) | (12.8) | (9.5) | (9.1) | (19.9) |
| Swiss franc | (1.2) | (0.3) | (0.4) | (0.6) | (0.8) | (5.7) | 7.5 |
| US dollar | 19.4 | (15.9) | (13.5) | (47.5) | (39.4) | (26.7) | (7.3) |
| Other currencies | (0.7) | (5.6) | 0.2 | (0.6) | 0.4 | 0.3 | – |
| **Total** | **22.8** | **(36.6)** | **(40.2)** | **(77.7)** | **(90.4)** | **(76.1)** | **(52.2)** |

As at 31 March 2010

| SDR millions | Up to 6 months | 6 to 12 months | 1 to 2 years | 2 to 3 years | 3 to 4 years | 4 to 5 years | Over 5 years |
|---|---|---|---|---|---|---|---|
| Euro | (3.7) | (8.4) | (12.8) | (20.4) | (11.3) | (16.4) | (48.1) |
| Japanese yen | 0.3 | (2.6) | (6.7) | (12.2) | (16.0) | (5.8) | (0.9) |
| Pound sterling | 0.6 | (1.0) | (4.9) | (7.3) | (12.8) | (6.3) | – |
| Swiss franc | 0.2 | (0.2) | (0.4) | (0.6) | (0.7) | (2.9) | 4.6 |
| US dollar | 16.8 | (18.4) | (17.4) | (34.1) | (49.0) | (20.7) | (19.4) |
| Other currencies | 16.9 | 15.5 | (9.4) | 0.5 | (0.4) | (0.4) | – |
| **Total** | 31.1 | (15.1) | (51.6) | (74.1) | (90.2) | (52.5) | (63.8) |

### *C. Foreign exchange risk*

The Bank's functional currency, the SDR, is a composite currency comprising fixed amounts of USD, EUR, JPY and GBP. Currency risk is the exposure of the Bank's financial condition to adverse movements in exchange rates. The Bank is exposed to foreign exchange risk primarily through the assets relating to the management of its equity. The Bank is also exposed to foreign exchange risk through managing its customer deposits and through acting as an intermediary in foreign exchange transactions between central and commercial banks. The Bank reduces its foreign exchange exposures by matching the relevant assets to the constituent currencies of the SDR on a regular basis, and by limiting currency exposures arising from customer deposits and foreign exchange transaction intermediation.

Foreign exchange risk is measured and monitored based on the Bank's VaR methodology and sensitivity analyses considering movements in key foreign exchange rates.

The following tables show the Bank's assets and liabilities by currency and gold exposure. The net foreign exchange and gold position in these tables therefore includes the Bank's gold investments. To determine the Bank's net foreign exchange exposure, the gold amounts need to be removed. The SDR-neutral position is then deducted from the net foreign exchange position excluding gold to arrive at the net currency exposure of the Bank on an SDR-neutral basis.

| As at 31 March 2011<br>*SDR millions* | SDR | USD | EUR | GBP | JPY | CHF | Gold | Other currencies | Total |
|---|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | | |
| Cash and sight accounts with banks | – | 12.6 | 151.3 | 8.0 | – | 151.3 | – | 6.6 | 329.8 |
| Gold and gold loans | – | 9.0 | – | – | – | – | 36,628.2 | – | 36,637.2 |
| Treasury bills | – | 2,304.0 | 29,737.0 | 397.2 | 36,796.9 | 5,337.0 | – | 2,360.0 | 76,932.1 |
| Securities purchased under resale agreements | – | 394.8 | 37,559.5 | 7,799.6 | 5,710.0 | – | – | 0.1 | 51,464.0 |
| Loans and advances | 171.7 | 8,460.0 | 10,937.4 | 1,368.1 | 1,062.4 | 544.4 | – | 1,626.4 | 24,170.4 |
| Government and other securities | – | 29,061.1 | 21,378.5 | 3,769.8 | 1,209.5 | 35.3 | – | 1,533.7 | 56,987.9 |
| Derivative financial instruments | (36.5) | 23,335.2 | 8,337.9 | (408.9) | (26,700.9) | 327.2 | (247.0) | 1,183.3 | 5,790.3 |
| Accounts receivable | 0.1 | 6,969.2 | 684.9 | 426.6 | – | 8.0 | – | 527.5 | 8,616.3 |
| Land, buildings and equipment | 189.7 | – | – | – | – | 1.1 | – | – | 190.8 |
| **Total assets** | **325.0** | **70,545.9** | **108,786.5** | **13,360.4** | **18,077.9** | **6,404.3** | **36,381.2** | **7,237.6** | **261,118.8** |
| **Liabilities** | | | | | | | | | |
| Currency deposits | (7,691.5) | (140,478.2) | (38,882.7) | (10,083.1) | (4,667.5) | (680.8) | – | (4,601.8) | (207,085.6) |
| Gold deposits | – | (5.6) | – | – | – | – | (21,264.3) | – | (21,269.9) |
| Derivative financial instruments | 4,221.7 | 79,073.2 | (59,048.3) | 126.6 | (11,840.3) | (5,452.7) | (11,666.5) | (2,373.2) | (6,959.5) |
| Accounts payable | – | (1,964.2) | (4,761.1) | (1,491.8) | – | (275.6) | – | (265.4) | (8,758.1) |
| Other liabilities | – | (66.6) | (2.8) | – | – | (305.3) | – | (0.7) | (375.4) |
| **Total liabilities** | **(3,469.8)** | **(63,441.4)** | **(102,694.9)** | **(11,448.3)** | **(16,507.8)** | **(6,714.4)** | **(32,930.8)** | **(7,241.1)** | **(244,448.5)** |
| **Net currency and gold position** | **(3,144.8)** | **7,104.5** | **6,091.6** | **1,912.1** | **1,570.1** | **(310.1)** | **3,450.4** | **(3.5)** | **16,670.3** |
| Adjustment for gold investment assets | – | – | – | – | – | – | (3,450.4) | – | (3,450.4) |
| **Net currency position** | **(3,144.8)** | **7,104.5** | **6,091.6** | **1,912.1** | **1,570.1** | **(310.1)** | **–** | **(3.5)** | **13,219.9** |
| SDR-neutral position | 3,144.8 | (6,818.8) | (6,196.9) | (1,840.6) | (1,508.4) | – | – | – | (13,219.9) |
| **Net currency exposure on SDR-neutral basis** | **–** | **285.7** | **(105.3)** | **71.5** | **61.7** | **(310.1)** | **–** | **(3.5)** | **–** |

As at 31 March 2010

| *SDR millions* | SDR | USD | EUR | GBP | JPY | CHF | Gold | Other currencies | Total |
|---|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | | |
| Cash and sight accounts with banks | – | 92.1 | 110.2 | 6.7 | – | 1,303.0 | – | 4.2 | 1,516.2 |
| Gold and gold loans | – | 11.1 | – | – | – | – | 43,028.7 | – | 43,039.8 |
| Treasury bills | – | 226.1 | 37,727.4 | 3,309.1 | 40,642.0 | 374.8 | – | 2,435.4 | 84,714.8 |
| Securities purchased under resale agreements | – | 164.8 | 33,618.8 | 3,744.4 | 4,777.9 | – | – | – | 42,305.9 |
| Loans and advances | 474.0 | 8,424.2 | 4,049.1 | 552.6 | 460.2 | 4,492.9 | – | 835.6 | 19,288.6 |
| Government and other securities | – | 24,646.8 | 22,876.5 | 3,088.0 | 1,587.0 | 32.6 | – | 1,456.8 | 53,687.7 |
| Derivative financial instruments | 3.3 | 92,178.4 | (34,182.7) | 455.8 | (41,264.4) | (661.0) | (5,295.8) | (1,118.9) | 10,114.7 |
| Accounts receivable | 0.1 | 2,300.2 | 1,456.2 | 66.4 | 92.7 | 8.6 | – | 111.5 | 4,035.7 |
| Land, buildings and equipment | 185.8 | – | – | – | – | 4.1 | – | – | 189.9 |
| **Total assets** | 663.2 | 128,043.7 | 65,655.5 | 11,223.0 | 6,295.4 | 5,555.0 | 37,732.9 | 3,724.6 | 258,893.3 |
| **Liabilities** | | | | | | | | | |
| Currency deposits | (1,821.3) | (132,064.1) | (43,134.8) | (10,403.6) | (4,423.6) | (1,240.5) | – | (2,667.2) | (195,755.1) |
| Gold deposits | – | (7.1) | – | – | – | – | (32,057.0) | – | (32,064.1) |
| Derivative financial instruments | 12.1 | 12,211.3 | (8,789.8) | 515.2 | 99.4 | (4,305.3) | (2,867.1) | (1,063.2) | (4,187.4) |
| Accounts payable | – | (2,064.0) | (8,619.2) | (17.6) | (91.6) | – | – | – | (10,792.4) |
| Other liabilities | – | (67.2) | (0.3) | – | – | (251.5) | – | – | (319.0) |
| **Total liabilities** | (1,809.2) | (121,991.1) | (60,544.1) | (9,906.0) | (4,415.8) | (5,797.3) | (34,924.1) | (3,730.4) | (243,118.0) |
| **Net currency and gold position** | (1,146.0) | 6,052.6 | 5,111.4 | 1,317.0 | 1,879.6 | (242.3) | 2,808.8 | (5.8) | 15,775.3 |
| Adjustment for gold investment assets | – | – | – | – | – | – | (2,808.8) | – | (2,808.8) |
| **Net currency position** | (1,146.0) | 6,052.6 | 5,111.4 | 1,317.0 | 1,879.6 | (242.3) | – | (5.8) | 12,966.5 |
| SDR-neutral position | 1,146.0 | (5,866.7) | (5,145.9) | (1,272.2) | (1,827.7) | – | – | – | (12,966.5) |
| **Net currency exposure on SDR-neutral basis** | – | 185.9 | (34.5) | 44.8 | 51.9 | (242.3) | – | (5.8) | – |

### *D. Economic capital for market risk*

The Bank measures market risk based on a VaR methodology using a Monte Carlo simulation technique taking correlations between risk factors into account. Economic capital for market risk is also calculated following this methodology measured to the 99.995% confidence interval and assuming a one-year holding period. The Bank measures its gold price risk relative to changes in the USD value of gold. The foreign exchange risk component, resulting from changes in the USD exchange rate versus the SDR, is included in the measurement of foreign exchange risk. The table below shows the key figures of the Bank's exposure to market risk in terms of economic capital utilisation over the past two financial years.

| For the financial year | 2011 | | | | 2010 | | | |
|---|---|---|---|---|---|---|---|---|
| *SDR millions* | Average | High | Low | At 31 March | Average | High | Low | At 31 March |
| **Economic capital utilisation for market risk** | 2,884.2 | 3,069.2 | 2,684.0 | **2,836.5** | 2,803.0 | 3,097.8 | 2,374.1 | 2,708.7 |

The table below provides further analysis of the Bank's market risk exposure by category of risk.

| For the financial year | 2011 | | | | 2010 | | | |
|---|---|---|---|---|---|---|---|---|
| *SDR millions* | Average | High | Low | At 31 March | Average | High | Low | At 31 March |
| Gold price risk | 1,956.7 | 2,121.0 | 1,830.6 | **1,909.8** | 1,870.9 | 2,013.0 | 1,721.9 | 1,900.9 |
| Interest rate risk | 1,617.7 | 1,760.7 | 1,456.1 | **1,542.2** | 1,790.8 | 2,182.7 | 1,434.4 | 1,647.9 |
| Foreign exchange risk | 797.0 | 874.6 | 666.3 | **814.6** | 715.2 | 800.4 | 651.3 | 658.4 |
| Diversification effects | (1,487.1) | (1,711.4) | (1,352.4) | **(1,430.1)** | (1,573.9) | (1,815.3) | (1,454.9) | (1,498.5) |

### *E. Minimum capital requirements for market risk*

For the calculation of minimum capital requirements for market risk under the Basel II Framework, the Bank has adopted a banking book approach consistent with the scope and nature of its business activities. Consequently, market risk-weighted assets are determined for gold price risk and foreign exchange risk, but not interest rate risk. The related minimum capital requirement is derived using the VaR-based internal models method. Under this method, VaR calculations are performed using the Bank's VaR methodology, assuming a 99% confidence interval, a 10-day holding period and a one-year historical observation period.

The actual minimum capital requirement is derived as the higher of the VaR on the calculation date and the average of the daily VaR measures on each of the preceding 60 business days (including the calculation date) subject to a multiplication factor of three plus a potential add-on depending on backtesting results. For the period under consideration, the number of backtesting outliers observed remained within the range where no add-on is required. The table below summarises the market risk development relevant to the calculation of minimum capital requirements and the related risk-weighted assets over the reporting period.

| As at 31 March | 2011 | | | 2010 | | |
|---|---|---|---|---|---|---|
| *SDR millions* | VaR | Risk-weighted assets (A) | Minimum capital requirement (B) | VaR | Risk-weighted assets (A) | Minimum capital requirement (B) |
| **Market risk, where (A) is derived as (B) / 8%** | 288.2 | 10,806.2 | **864.5** | 287.1 | 10,768.1 | 861.4 |

## 5. Liquidity risk

Liquidity risk arises when the Bank may not be able to meet expected or unexpected current or future cash flows and collateral needs without affecting its daily operations or its financial condition.

Outstanding balances in the currency and gold deposits from central banks, international organisations and other public institutions are the key drivers of the size of the Bank's balance sheet. The Bank has undertaken to repurchase at fair value certain of its currency deposit instruments at one or two business days' notice. The Bank has developed a liquidity management framework based on a statistical model underpinned by conservative assumptions with regard to cash inflows and the liquidity of liabilities. Within this framework, the Board of Directors has set a limit for the Bank's liquidity ratio which requires liquid assets to be at least 100% of the potential liquidity requirement. In addition, liquidity stress tests assuming extreme withdrawal scenarios are performed. These stress tests specify additional liquidity requirements to be met by holdings of liquid assets. The Bank's liquidity has consistently been materially above its minimum liquidity ratio and the requirements of its stress tests.

The Bank's currency and gold deposits, principally from central banks and international institutions, comprise 93% (2010: 93%) of its total liabilities. At 31 March 2011 currency and gold deposits originated from 171 depositors (2010: 174). Within these deposits, there are significant individual customer concentrations, with four customers each contributing in excess of 5% of the total on a settlement date basis (2010: six customers).

The following tables show the maturity profile of cash flows for assets and liabilities. The amounts disclosed are the undiscounted cash flows to which the Bank is committed.

| **As at 31 March 2011**<br>*SDR millions* | Up to 1 month | 1 to 3 months | 3 to 6 months | 6 to 12 months | 1 to 2 years | 2 to 5 years | 5 to 10 years | Over 10 years | Total |
|---|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | | |
| Cash and sight accounts with banks | 329.8 | – | – | – | – | – | – | – | 329.8 |
| Gold and gold loans | 35,402.2 | 0.2 | 116.9 | 235.6 | 675.2 | 241.4 | – | – | 36,671.5 |
| Treasury bills | 20,560.7 | 34,860.3 | 9,809.3 | 11,493.0 | – | – | – | – | 76,723.3 |
| Securities purchased under resale agreements | 37,247.3 | 6,508.0 | 1,922.6 | – | – | – | – | – | 45,677.9 |
| Loans and advances | 10,979.7 | 11,508.3 | 1,159.4 | – | – | – | – | – | 23,647.4 |
| Government and other securities | 2,714.6 | 3,182.7 | 4,433.6 | 11,945.4 | 12,101.3 | 20,634.4 | 5,019.1 | 608.1 | 60,639.2 |
| **Total assets** | **107,234.3** | **56,059.5** | **17,441.8** | **23,674.0** | **12,776.5** | **20,875.8** | **5,019.1** | **608.1** | **243,689.1** |
| **Liabilities** | | | | | | | | | |
| Currency deposits | | | | | | | | | |
| Deposit instruments repayable at 1–2 days' notice | (7,108.9) | (15,075.9) | (17,684.3) | (16,343.5) | (18,205.4) | (21,450.7) | (2,331.1) | – | (98,199.8) |
| Other currency deposits | (63,470.8) | (21,510.5) | (12,675.9) | (7,303.5) | (3.2) | – | – | – | (104,963.9) |
| Gold deposits | (20,714.5) | – | – | (82.4) | (236.3) | (239.9) | – | – | (21,273.1) |
| Securities sold short | (0.4) | (0.7) | (1.1) | (2.1) | (4.2) | (12.7) | (21.4) | (71.3) | (113.9) |
| **Total liabilities** | **(91,294.6)** | **(36,587.1)** | **(30,361.3)** | **(23,731.5)** | **(18,449.1)** | **(21,703.3)** | **(2,352.5)** | **(71.3)** | **(224,550.7)** |
| **Derivatives** | | | | | | | | | |
| *Net settled* | | | | | | | | | |
| Interest rate contracts | 99.2 | 243.4 | 410.3 | 447.1 | 634.0 | 318.3 | 4.5 | – | 2,156.8 |
| *Gross settled* | | | | | | | | | |
| Exchange rate and gold price contracts | | | | | | | | | |
| Inflows | 42,049.4 | 52,875.9 | 21,374.8 | 11,771.3 | – | – | – | – | 128,071.4 |
| Outflows | (42,703.7) | (54,108.8) | (21,993.1) | (12,287.9) | – | – | – | – | (131,093.5) |
| Subtotal | (654.3) | (1,232.9) | (618.3) | (516.6) | – | – | – | – | (3,022.1) |
| Interest rate contracts | | | | | | | | | |
| Inflows | 0.8 | 50.4 | 1.4 | 39.1 | 289.4 | 1,023.5 | 25.1 | – | 1,429.7 |
| Outflows | – | (54.5) | (9.9) | (76.8) | (400.7) | (1,215.6) | (34.7) | – | (1,792.2) |
| Subtotal | 0.8 | (4.1) | (8.5) | (37.7) | (111.3) | (192.1) | (9.6) | – | (362.5) |
| **Total derivatives** | **(554.3)** | **(993.6)** | **(216.5)** | **(107.2)** | **522.7** | **126.2** | **(5.1)** | **–** | **(1,227.8)** |
| **Total future undiscounted cash flows** | **15,385.4** | **18,478.8** | **(13,136.0)** | **(164.7)** | **(5,149.9)** | **(701.3)** | **2,661.5** | **536.8** | **17,910.6** |

As at 31 March 2010

| SDR millions | Up to 1 month | 1 to 3 months | 3 to 6 months | 6 to 12 months | 1 to 2 years | 2 to 5 years | 5 to 10 years | Over 10 years | Total |
|---|---|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | | | |
| Cash and sight accounts with banks | 1,516.2 | – | – | – | – | – | – | – | 1,516.2 |
| Gold and gold loans | 41,621.2 | 188.2 | 0.2 | 233.8 | 285.6 | 743.1 | – | – | 43,072.1 |
| Treasury bills | 18,983.6 | 44,817.9 | 10,718.1 | 10,160.9 | – | – | – | – | 84,680.5 |
| Securities purchased under resale agreements | 30,810.0 | 2,779.5 | 749.9 | – | – | – | – | – | 34,339.4 |
| Loans and advances | 8,977.2 | 9,138.4 | 132.8 | 3.7 | 17.2 | 957.9 | – | – | 19,227.2 |
| Government and other securities | 1,798.3 | 3,172.6 | 5,605.1 | 10,821.8 | 9,349.3 | 18,426.1 | 7,214.9 | 533.3 | 56,921.4 |
| **Total assets** | 103,706.5 | 60,096.6 | 17,206.1 | 21,220.2 | 9,652.1 | 20,127.1 | 7,214.9 | 533.3 | 239,756.8 |
| **Liabilities** | | | | | | | | | |
| Currency deposits | | | | | | | | | |
| Deposit instruments repayable at 1–2 days' notice | (7,600.9) | (15,852.5) | (10,355.5) | (9,688.4) | (16,571.6) | (27,601.1) | (3,398.3) | – | (91,068.3) |
| Other currency deposits | (78,823.0) | (17,938.3) | (6,997.4) | (1,095.1) | – | – | – | – | (104,853.8) |
| Gold deposits | (31,382.9) | – | – | (232.7) | (66.6) | (386.5) | – | – | (32,068.7) |
| Securities sold short | (0.3) | (0.7) | (2.0) | (1.0) | (4.0) | (12.0) | (20.2) | (78.9) | (119.1) |
| **Total liabilities** | (117,807.1) | (33,791.5) | (17,354.9) | (11,017.2) | (16,642.2) | (27,999.6) | (3,418.5) | (78.9) | (228,109.9) |
| **Derivatives** | | | | | | | | | |
| *Net settled* | | | | | | | | | |
| Interest rate contracts | 863.1 | 376.2 | 625.1 | 573.6 | 899.0 | 609.7 | 36.8 | – | 3,983.5 |
| *Gross settled* | | | | | | | | | |
| Exchange rate and gold price contracts | | | | | | | | | |
| Inflows | 31,532.0 | 50,905.4 | 15,319.8 | 10,702.2 | – | – | – | – | 108,459.4 |
| Outflows | (30,879.9) | (49,419.5) | (14,768.8) | (10,284.6) | – | – | – | – | (105,352.8) |
| Subtotal | 652.1 | 1,485.9 | 551.0 | 417.6 | – | – | – | – | 3,106.6 |
| Interest rate contracts | | | | | | | | | |
| Inflows | 35.7 | 219.0 | 203.8 | 136.1 | 110.8 | 1,013.0 | 373.9 | – | 2,092.3 |
| Outflows | (42.9) | (248.5) | (253.6) | (166.4) | (139.2) | (1,148.2) | (417.0) | – | (2,415.8) |
| Subtotal | (7.2) | (29.5) | (49.8) | (30.3) | (28.4) | (135.2) | (43.1) | – | (323.5) |
| **Total derivatives** | 1,508.0 | 1,832.6 | 1,126.3 | 960.9 | 870.6 | 474.5 | (6.3) | – | 6,766.6 |
| **Total future undiscounted cash flows** | (12,592.6) | 28,137.7 | 977.5 | 11,163.9 | (6,119.5) | (7,398.0) | 3,790.1 | 454.4 | 18,413.5 |

The Bank writes options in the ordinary course of its banking business. The table below discloses the fair value of the written options analysed by exercise date:

**Written options**

| *SDR millions* | Up to 1 month | 1 to 3 months | 3 to 6 months | 6 to 12 months | 1 to 2 years | 2 to 5 years | 5 to 10 years | Over 10 years | Total |
|---|---|---|---|---|---|---|---|---|---|
| **As at 31 March 2011** | (38.6) | (0.1) | – | (5.1) | – | (5.0) | – | – | **(48.8)** |
| As at 31 March 2010 | – | (5.9) | (8.4) | (32.0) | (1.2) | (1.4) | – | – | (48.9) |

The table below shows the contractual expiry date of the credit commitments as at the balance sheet date:

**Contractual expiry date**

| *SDR millions* | Up to 1 month | 1 to 3 months | 3 to 6 months | 6 to 12 months | 1 to 2 years | 2 to 5 years | 5 to 10 years | Maturity undefined | Total |
|---|---|---|---|---|---|---|---|---|---|
| **As at 31 March 2011** | – | – | – | 268.5 | – | – | – | 1,919.2 | **2,287.7** |
| As at 31 March 2010 | 2,683.8 | – | – | 375.2 | – | – | – | 1,860.8 | 4,919.8 |

## 6. Operational risk

Operational risk is defined by the Bank as the risk of financial loss, or damage to the Bank's reputation, or both, resulting from one or more risk causes, as outlined below:

- Human factors: insufficient personnel, lack of requisite knowledge, skills or experience, inadequate training and development, inadequate supervision, loss of key personnel, inadequate succession planning, or lack of integrity or ethical standards.
- Failed or inadequate processes: a process is poorly designed or unsuitable, or is not properly documented, understood, implemented, followed or enforced.
- Failed or inadequate systems: a system is poorly designed, unsuitable or unavailable, or does not operate as intended.
- External events: the occurrence of an event having an adverse impact on the Bank but outside its control.

Operational risk includes legal risk, but excludes strategic risk.

The Bank's operational risk management framework, policies and procedures comprise the management and measurement of operational risk, including the determination of the relevant key parameters and inputs, business continuity planning and the monitoring of key risk indicators.

The Bank has established a procedure of immediate reporting for operational risk-related incidents. The Compliance and Operational Risk Unit develops action plans with the respective units and follows up on their implementation on a regular basis.

For the measurement of operational risk economic capital and operational risk-weighted assets, the Bank has adopted a VaR approach using a Monte Carlo simulation technique that is consistent with the advanced measurement approach proposed under the Basel II Framework. In line with the assumptions of the Basel II Framework, the quantification of operational risk does not take reputational risk into account. Internal and external loss data, scenario estimates and control self-assessments to reflect changes in the business and control environment of the Bank are key inputs in the calculations. In quantifying its operational risk, the Bank does not take potential protection it may obtain from insurance into account.

### *A. Economic capital for operational risk*

Consistent with the parameters used in the calculation of economic capital for financial risk, the Bank measures economic capital for operational risk to the 99.995% confidence interval assuming a one-year holding period. The table below shows the key figures of the Bank's exposure to operational risk in terms of economic capital utilisation over the past two financial years.

| For the financial year | **2011** | | | | 2010 | | | |
|---|---|---|---|---|---|---|---|---|
| *SDR millions* | Average | High | Low | At 31 March | Average | High | Low | At 31 March |
| **Economic capital utilisation for operational risk** | 643.8 | 700.0 | 475.0 | **700.0** | 460.4 | 475.0 | 450.0 | 475.0 |

### *B. Minimum capital requirements for operational risk*

In line with the key parameters of the Basel II Framework, the calculation of the minimum capital requirement for operational risk is determined assuming a 99.9% confidence interval and a one-year time horizon. The table below shows the minimum capital requirements for operational risk and related risk-weighted assets.

| As at 31 March | **2011** | | | 2010 | | |
|---|---|---|---|---|---|---|
| *SDR millions* | VaR | Risk-weighted assets (A) | Minimum capital requirement (B) | VaR | Risk-weighted assets (A) | Minimum capital requirement (B) |
| **Operational risk, where (A) is derived as (B) / 8%** | 300.8 | 3,760.4 | **300.8** | 180.5 | 2,256.3 | 180.5 |

# Independent auditor's report

to the Board of Directors and to the General Meeting
of the Bank for International Settlements, Basel

We have audited the accompanying financial statements of the Bank for International Settlements, which comprise the balance sheet as at 31 March 2011, and the profit and loss account, the statement of cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

*Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the Statutes and with the principles of valuation described under significant accounting policies in the notes, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

*Auditor's Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those Standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

*Opinion*

In our opinion, the financial statements give a true and fair view of the financial position of the Bank for International Settlements as at 31 March 2011 and of its financial performance and its cash flows for the year then ended in accordance with the accounting principles described in the notes to the financial statements and the Statutes of the Bank.

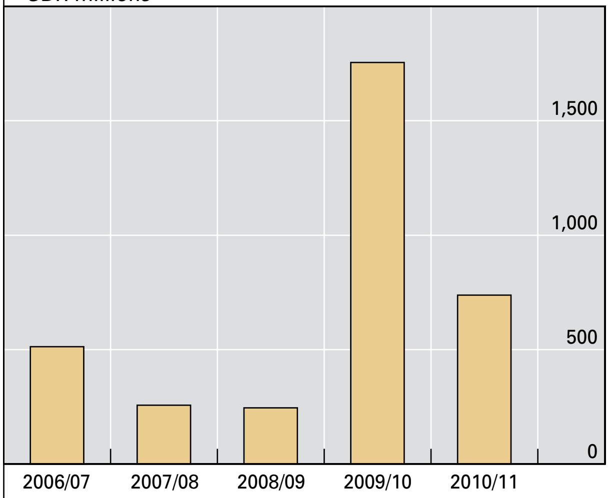
Deloitte AG

Mark D. Ward                                        Erich Schärli

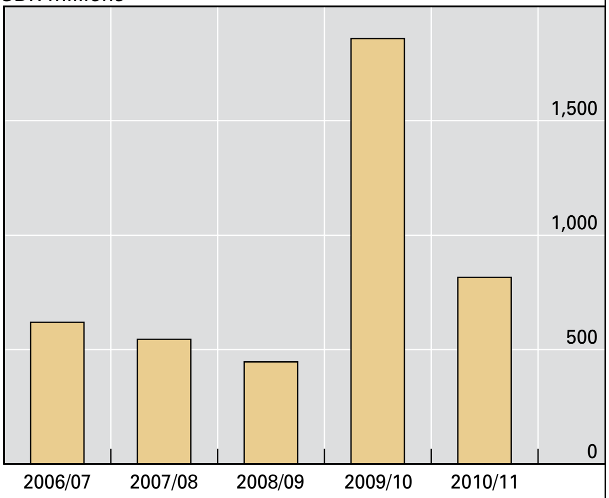
Zurich, 9 May 2011

## Five-year graphical summary

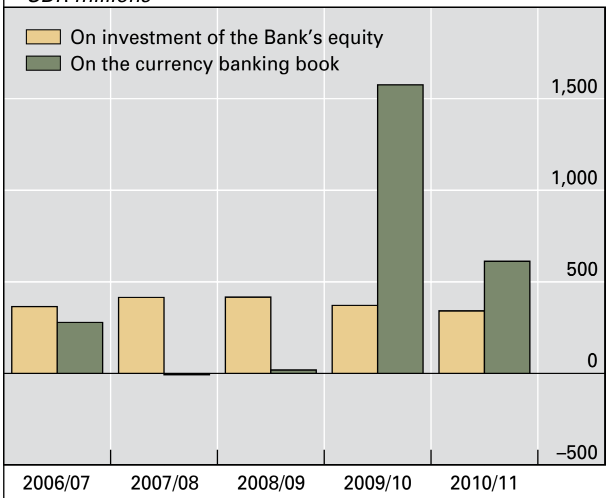
### Operating profit
*SDR millions*



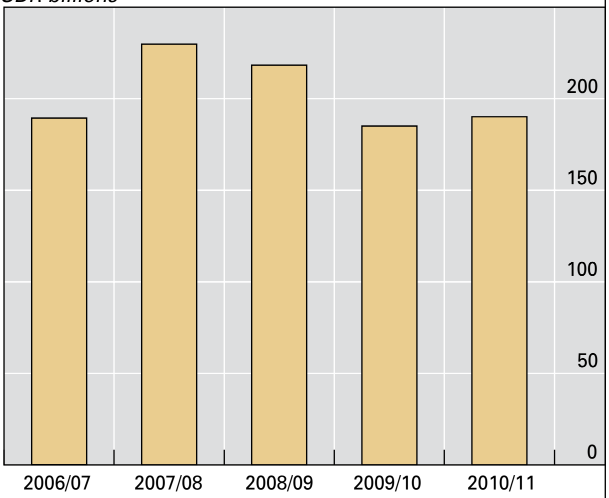

### Net profit
*SDR millions*



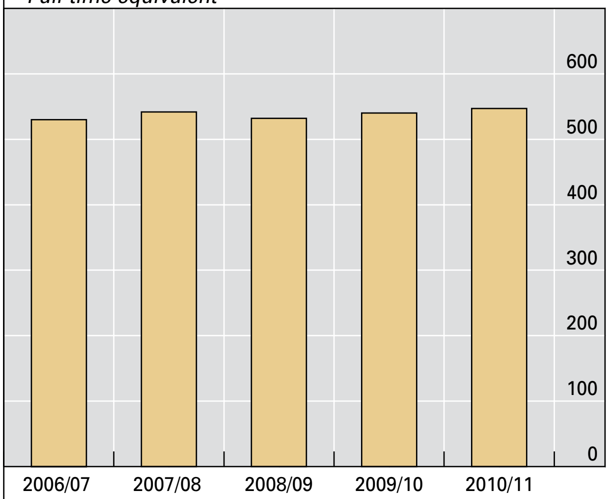

### Net interest earned on currency investments
*SDR millions*



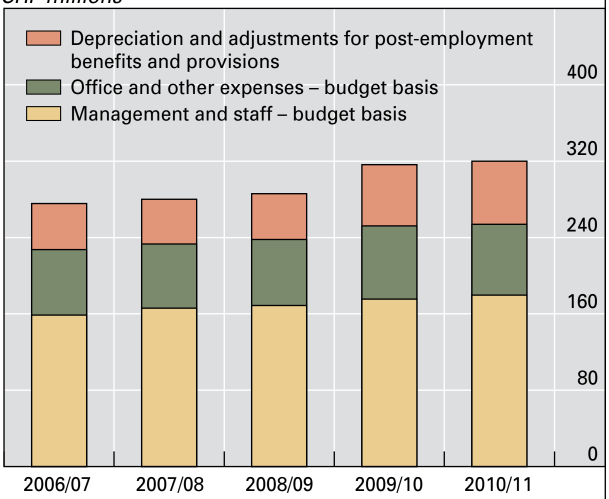

### Average currency deposits (settlement date basis)
*SDR billions*




### Average number of employees
*Full-time equivalent*




### Operating expense
*CHF millions*




The financial information in the top four panels has been restated to reflect a change in the accounting policy made in the previous years' accounts.

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