Thomas Jordan: Monetary policy in a climate of increased uncertainty

Summary of a speech by Mr Thomas Jordan, Member of the Governing Board of the Swiss National Bank, at the SNB Money Market Event, Geneva, 1 November 2007.

The complete speech can be found in German on the Swiss National Bank's website (www.snb.ch).

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Uncertainty about the extent and distribution of losses from US "subprime" mortgages has resulted in a marked squeeze on financial markets. In particular, there is considerable uncertainty concerning the true valuation of securitised assets and structured products based on subprime mortgages. Demand for liquidity has surged. In certain instances, the crisis of confidence among financial market participants was so pronounced that some markets did not function at all. The "re-pricing of risk" has caused risk premia for most financial instruments to soar.

Risk premia are important for the Swiss National Bank (SNB) for two reasons. On the one hand, they act as economic signals and should therefore be as unbiased as possible in the way they reflect underlying risks. In addition, there are certain risks attached to extreme values of risk premia. Abrupt and uncontrolled corrections could lead to instability on financial markets and interfere with their smooth functioning. On the other hand, risk premia affect the restrictiveness of monetary policy. An increase in such premia tightens monetary policy. The SNB monetary policy concept, where the three-month Libor is at the centre of the implementation of monetary policy, takes systematic account of changes in risk premia.