

Thomas Jordan: Discussions on the topic of the euro/Swiss franc minimum exchange rate

Speech by Mr Thomas Jordan, Vice-Chairman of the Governing Board of the Swiss National Bank, held at the Swiss National Bank, Zurich, 10 April 2012.

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Ladies and Gentlemen

I would like to welcome you to this discussion on the topic of the euro/Swiss franc minimum exchange rate and thank you for attending at such short notice. As you are aware, on Thursday of last week a few of the transactions in the foreign exchange market for the euro were concluded at a rate below the minimum exchange rate set by the Swiss National Bank (SNB). I consider it important that you are aware of the sequence of events, and also that I reaffirm the SNB's current policy. Since this is a specifically market-related topic, we have chosen this rather special approach involving a discussion with news agencies.

The fact that a few individual transactions at less than CHF 1.20 per euro were observed last Thursday has led to some isolated doubts being raised about the SNB's resolve to enforce its minimum exchange rate. Right from the start I want to make it quite clear that such doubts are misplaced. The Swiss National Bank is enforcing the minimum exchange rate with all the means at its disposal. We are prepared to buy foreign currency in unlimited quantities for this purpose. In this respect, our policies are totally unchanged.

What precisely occurred last Thursday? Within just a few seconds, the euro/Swiss franc exchange rate fell from 1.2020 to 1.2000. Despite SNB offers placed in the trading systems, a few isolated transactions occurred below CHF 1.20 per euro. However, at no time did the best available euro exchange rate in the market fall below the minimum exchange rate of CHF 1.20. Thus, for a short time, what is known as a segmented market could be observed, in which transactions below the best price were concluded. This situation was remedied within very few seconds, however, by means of arbitrage.

How could transactions take place on the foreign exchange market for below CHF 1.20 per euro despite the fact that the SNB was at all times present in the market? The foreign exchange market is a decentralised market. Rather than foreign exchange being traded on a bourse, forex transactions are made directly between market participants. Each bank has its own individual group of counterparties, and, in particular, banks with lower ratings only have a small number of counterparties. The exchange rates below CHF 1.20 per euro were concluded by banks that do not have an agreement relating to limits with the SNB, in other words, by banks that cannot or do not wish to trade with the SNB. The SNB was at all times prepared to buy unlimited quantities of euros at CHF 1.20 per euro. All market participants were at all times aware of this SNB purchase offer, including the banks without an agreement relating to limits. Consequently, banks which sold euros for less than CHF 1.20 did not receive the best market price and had – relatively speaking – to accept losses. Since there is no compulsion to make business transactions at the best prices, such anomalies cannot always be excluded. However, they can only be maintained for a very short period.

How is the SNB organised in operational terms for implementing the minimum exchange rate? Since the introduction of the minimum exchange rate, the SNB has monitored the foreign exchange market from market opening in Asia on Sunday evening to market closing in New York on Friday evening without any interruption. The same applies to holidays. The interbank market, which is the market of relevance for the SNB, includes its counterparties. The SNB accepts well over 100 banks with more than 700 trading desks as counterparties. Thanks to this network of contacts, the global foreign exchange market is almost completely covered. On the part of the SNB, the trading limits amount to some hundreds of billions of

euros a day. These limits can be flexibly adjusted by the SNB, should this be necessary. Via electronic trading systems, the banks have access at all times to the offers. The SNB's strategy for implementing the minimum exchange rate has proved effective – including in the last few days. On the relevant interbank market, CHF 1.20 per euro qualifies as the lowest exchange rate. Consequently, the minimum exchange rate applied at all times.

Does the minimum exchange rate continue to apply? Yes. Without any qualification. The SNB has successfully enforced the minimum exchange rate and will continue to do so, without any restrictions. The Swiss franc is still overvalued and represents a substantial challenge for the Swiss economy. The SNB continues to expect that the Swiss franc will weaken. Should the economic outlook and the risk of deflation so require, the SNB stands ready to take further measures at any time.