

Olaf Sleijpen: On the pivotal role of central bank capital

Speech by Mr Olaf Sleijpen, Executive Board Member of Monetary Affairs and Financial Stability of the Netherlands Bank, at the DNB-Risk Management workshop on "Central bank capital in turbulent times", Amsterdam, 11 April 2024.

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Good morning, esteemed participants.

This workshop convenes at a pivotal moment for central banks, and the chosen title reflects this significance. Over the past decade, the post Great Financial Crisis monetary policies followed by a global surge in inflation and subsequent monetary tightening resulted in significant losses for central banks across the globe.

Amidst widespread central bank losses, the significance of central bank capital has surged. Central bank capital plays a pivotal role as a buffer to absorb risks stemming from monetary policy operations.

Also DNB, the Dutch central bank, is experiencing a large loss due to the Eurosystem's monetary policy, estimated at 9 billion euros during the period 2023 until 2028 (a bit short of 1% of GDP).

In the recent revision of the capital policy, both DNB and the Ministry of Finance – representing the Bank's sole shareholder - reaffirmed the pivotal role of central bank capital. They emphasized the urgent need to reestablish robust buffers, especially during periods of profitability for central banks.

Indeed, if you want to achieve an effective capital policy you need to engage in a thorough and transparent dialogue with the central bank's shareholder, typically the government. Throughout the revision of DNB's capital policy, we meticulously outlined to the shareholder the sources of financial risks and the rationale behind their materialization into losses. Then we delineated how central bank capital serves to mitigate impending losses and elucidated on how future profits will contribute to rebuilding our capital position.

DNB and its shareholder have reached a consensus on a strategy to gradually rebuild buffers through the retention of future profits, rather than opting for recapitalization. This decision underscores the mutual commitment to preserving central bank independence. Furthermore, it signifies the robustness of DNB's capital position, reassuring stakeholders that the central bank policies remain effective despite the erosion of capital over the coming years.

In essence, DNB regards capital as paramount, because it ensures the central bank's ability to fulfill its mandate even amidst challenging economic conditions. This commitment to maintaining a strong capital base underscores our dedication to safeguarding price stability and preserving its capacity to navigate through uncertain economic landscapes.

The program of this workshop builds pretty much on this view. In the first session, we start by discussing the importance of central bank capital. Then, in the second session, we will discuss how future changes in monetary policy will impact central bank capital. Finally, tomorrow in the third session, we broaden the scope to the external environment. We will examine how central banks negotiate with their shareholders, and how risks outside monetary policy, such as financial stability risks and climate risk, affect central bank capital.

You all contribute to intellectual capital by sharing your diverse expertise and insights. Your contributions help central banks make informed decisions, refine capital policy frameworks, and adapt to evolving financial landscapes, ultimately strengthening the role of central banks in society.

Thank you.