

# FINANCIAL NEWS

Monday, 24 September 2012

## The currency mountain with more holes than a Swiss cheese

[William Hutchings](#)

24 Sep 2012

**Holes are a good thing when they appear in Switzerland's Emmental cheese, but a potential €200bn hole in Switzerland's foreign exchange reserves is worrying asset managers.**

Twelve months ago the Swiss National Bank, trying to counter the impact of a flight to quality by anxious investors, decided to set and maintain its euro exchange rate at a minimum of Sfr1.20.

It said it was prepared to buy foreign currency in "unlimited quantities" to make this happen.

Christopher Cruden, chief executive of Insch Capital Management, a Swiss alternative investment manager, said this intervention has lasted longer than he expected and, so far, has been successful in placing a floor on the number of Swiss francs needed to buy one euro.

However, he said: "The Swiss National Bank has taken a very considerable amount of risk in order to achieve its aim. They now pose grave danger to themselves and to wider financial markets."

In pursuit of its policy, the SNB's euro-denominated reserves, mainly in German and French treasury bonds, have now exceeded €200bn, according to Insch, while another asset manager estimates them at €210bn.

Switzerland's total foreign currency reserves now total Sfr420bn, equivalent to €340bn, which is almost three times the value of Swiss gross domestic product. Five years ago, its currency reserves equated to about 40% of GDP.

The value of these assets would be jeopardised if the eurozone broke up, especially if core economies left it.

Cruden said the SNB's policy has artificially supported euro exchange rates with its purchases of euro-denominated assets, and reversing this could create havoc: "The foreign exchange operations could send markets into uncharted turmoil and lead to a run on the euro – the very last thing the SNB would want.

The SNB may not be able to offload the pile of euros it has accumulated without suffering huge losses."

However, Thanos Papasavvas, a fixed income and currency strategist at Investec Asset Management, said the very scale of this risk – and its impact on the Swiss – made it unlikely to happen.

"The Swiss won't dump these assets, because it would take the Swiss franc to below one to the euro and ruin their economy. It's like the Chinese, who are not going to sell their US dollar holdings," he said.

He sees other risks. The Swiss National Bank is funded by the Swiss cantons, and Papasawas said: "If the SNB starts losing money, political questions will be asked. That may have unintended consequences. The other risk is of inflation."

A third asset manager, who asked not to be identified, also expressed unease about the Swiss exchange rate policy. He said: "I keep a list of artificial situations – interventions and caps and price controls – and this is one of the big ones."

These things often lead to unintended consequences. I think it's going to be a very interesting three to six months."

[Got university debt? Work at Deutsche Bank](#)

[Deutsche Bank takes knife to corporate finance](#)

[Methodists rebuke pursuit of Mammon](#)

[Danger lurks in even the most liquid products](#)

[?]