

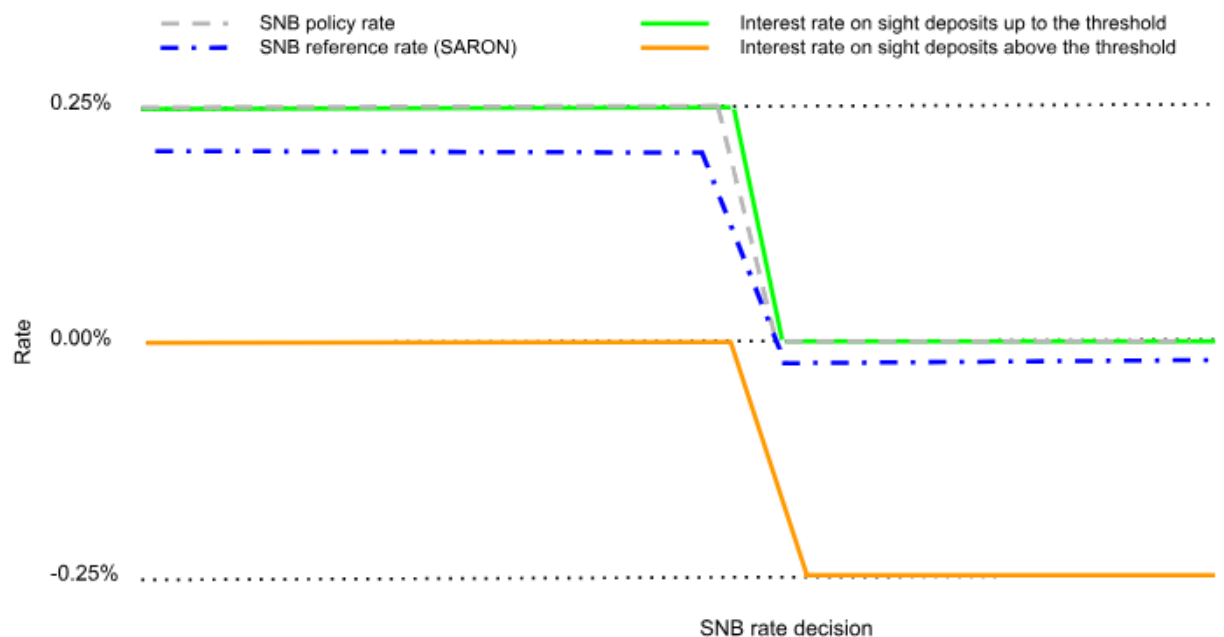
Research

Joris van Beek
Junior Economist
+31 20 522 0214
j.vanbeek@afsgroup.nl

Arne Petimezas
Director Research
+31 20 522 0244
a.petimezas@afsgroup.nl

No more subterfuge please

- The Swiss National Bank made return to negative rates today as per our expectations, but with a twist. The SNB will steer the level of bank reserves (aka sight deposits) through certificate sales and reverse repos so that SARON will settle close but below zero. That compares with our call of a settlement close but above minus 25bps. So negative rates, but only by tip-toeing into negative territory.
- To be sure, as per our call, the interest rates on reserves above the threshold was cut by 25bps to minus 25bps while the rate on reserve below the threshold – the bulk of bank reserves – was cut by 25bps to zero.
- In any case, the SNB will need to fine-tune the level of bank reserves in such a way that the arbitrage – borrowing reserves in the interbank market and then parking the proceeds at the SNB – remains profitable. Without such arbitrage by banks, SARON will lose its significance.
- The figure below graphically represents where SARON will settle from now on:



- **Given the political nature of negative interest rates, the SNB monetary policy statement relegated the mention of negative rates to the footnotes.** One expects such subterfuge from a corporate that tries to hide a profit warning, not from a renowned central bank. SNB President Martin Schlegel's remarks during the press conference that "zero is not negative" look strangely odd. And that's just an understatement.
- **On the macro side of things, a return of deflation forced the SNB to resume a cutting cycle that they thought had ended in March.** Viewing deflation largely as being of an exchange rate-driven nature, the SNB did not address our concern that what little price pressures remain, are driven by rents, a statistical artefact. In any case, the SNB expects that the recent deflation episode is only intermittent, and that marginal inflation will return. Thus, the SNB expects that there will be no further rate cuts. In any case, as per the SNB's guidance, the bar for another cut is very high. Ditto for forex intervention.
- **We believe that the SNB continues to underestimate deflationary risks.** Which, it must be emphasized, are a result of haven flows into the franc. More likely than not, the SNB will be forced to cut again, and by another 25bps. Note that theoretically, the SNB could instead steer the settlement of SARON lower within the corridor (so, closer to minus 25bps) by increasing the share of reserves that are remunerated at the negative rate. However, we think an outright cut is more likely.

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