

# 2007 | ANNUAL REPORT **BANQUE DE FRANCE**

To  
The President of the Republic  
And Parliament

By Governor Christian Noyer



## 2007 Portfolio



The photographs featured in this report mainly illustrate the Bank's banknote fitness checking and sorting activities. They were taken by Pascal Assailly and Philippe Jolivel.

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## A WORD FROM THE GOVERNOR

The euro has been our currency, and that of over 300 million Europeans with whom we share Economic and Monetary Union, for a decade now. During this period, the Banque de France, an institution of the French Republic, has been a member of the Eurosystem, the central banking system of the euro area, which manages the single currency in the same way as the Federal Reserve System manages the US dollar.

The Banque de France is first and foremost a monetary institution. Within the Eurosystem, which comprises the European Central Bank (ECB) and the national central banks (NCBs) of the euro area Member States, the Banque de France participates in attaining the primary objective assigned to us by the Treaty on European Union, i.e. maintaining price stability. By keeping inflation low, stable and predictable, the Eurosystem contributes to sound and sustainable economic growth. Monetary stability underpins economic agents' confidence in the euro, our currency. To this end, the Banque de France takes part, within the decentralised framework of the Eurosystem, in the preparation, implementation and explanation of the euro area's monetary policy.

It also participates in banknote production and ensures the quality of banknotes in circulation in France.

Like all central banks, the Banque de France is also charged with safeguarding financial stability. The latter depends on the resilience of the financial sector and the smooth functioning of market infrastructures. The Banque de France identifies the financial system's vulnerabilities and helps to alleviate them. In this context, the Bank has closely followed the development of the financial crisis that began in the summer of 2007 and has taken the action demanded by the situation. This objective of financial stability, which benefits very effectively from the backing of banking supervision by the Banque de France, underpins several of the Bank's tasks at the national level, notably the authorisation and supervision of credit institutions and investment firms, the oversight of means of payment and payment systems, and the assessment of the financial position of companies.

Lastly, within the framework of a public service contract, the State has entrusted the Banque de France with various specific tasks on behalf of private individuals, regional and local authorities, enterprises and banks.



The Banque de France's 2007 *Annual Report* comprises four chapters:

- In the first chapter, which is devoted to *Corporate social responsibility*, the Banque de France highlights its commitment to integrate into its management methods the economic, social and environmental components of sustainable development. The first of these approaches relates to the Bank's operating principles: transparency, collegial decision-making, anticipation and risk prevention. The second deals with issues related to human resource management and the third concerns environmental measures that have been or will be taken.
- The second chapter, which is devoted to *The environment and implementation of monetary policy* presents the main economic developments during the year under review, at a global level, in the euro area and in France, in order to put the monetary policy decisions and their implementation in context.
- The third, *The Banque de France, a key player in the economy*, describes the tasks the Bank carries out at the international, European and national levels. The main responsibilities are illustrated in the light of the main events of 2007 and with the aid of key data. A box summarises the main points concerning the financial crisis in 2007 and the action taken.
- The last chapter presents *The accounts of the Banque de France* for the year under review.





**Sorting machine operators**

Within the European System of Central Banks (ESCB), the Banque de France is the national central bank (NCB) with the broadest range of responsibilities, stemming from both the European framework and national legal and regulatory provisions.

This diversity of tasks requires it to have in place decision-making structures and operating modes that encompass the concept of corporate social responsibility in its three dimensions: the economic dimension, which manifests itself through corporate governance, social relations and environmental concerns.

As regards corporate governance, the Banque de France clearly defines the responsibilities of each of its management bodies (see Section 1) and promotes a collegial operating mode at all levels of the institution. This approach to corporate governance is reflected in the Bank's annual strategic planning, which results in the definition of costed and prioritised objectives for the next financial year and over the medium term (see Section 2).

With the same objective of responsible governance, the Banque de France has set up a risk prevention and internal audit framework aimed at securing transactions while ensuring the effectiveness of the processes in place (see Section 3).

The Banque de France, which is an institution of the French Republic, conducts its activities in a fully transparent manner: the Governor of the Bank appears regularly before Parliament and the Government to report on the tasks that the Bank carries out in the framework of the Treaty on European Union, and those entrusted to it by French law, under the Public Service Contract and the various agreements signed with the State.

Beyond these operating rules, the Banque de France intends to manage its human resources in accordance with the highest social standards (see Section 5), take account of environmental aspects in its operating modes (see Section 6) and incorporate society's sustainable development concerns into its tasks (see Section 7).

## I | Management bodies

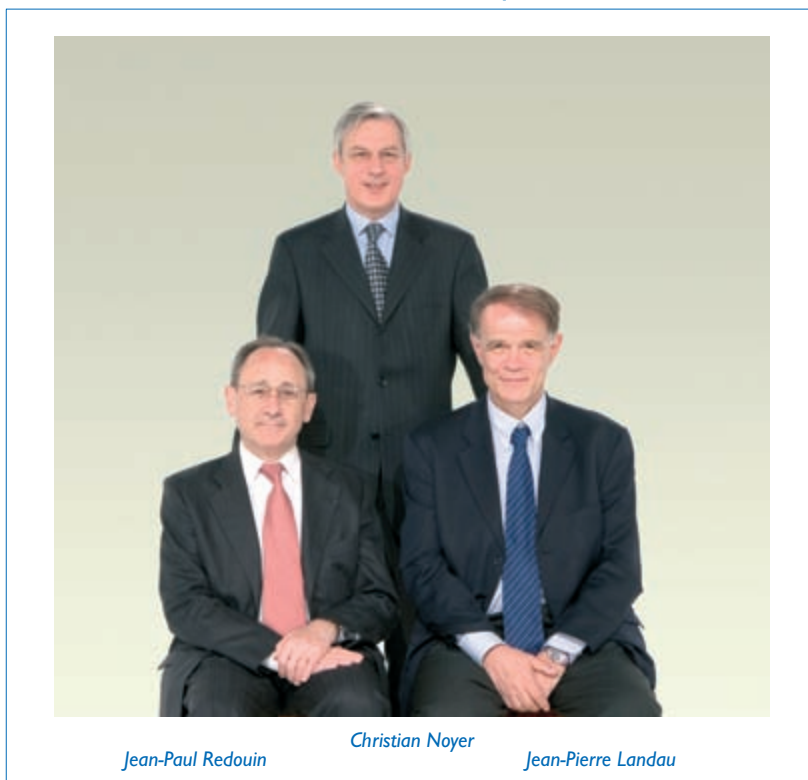
### I | I The Governor and Deputy Governors

The Governor, Christian Noyer, assisted by two Deputy Governors, is responsible for managing the Banque de France. He chairs the General Council, and prepares and implements its decisions. The Governor and Deputy Governors are appointed by decree by the Council of Ministers for a six-year term, which may be renewed once.

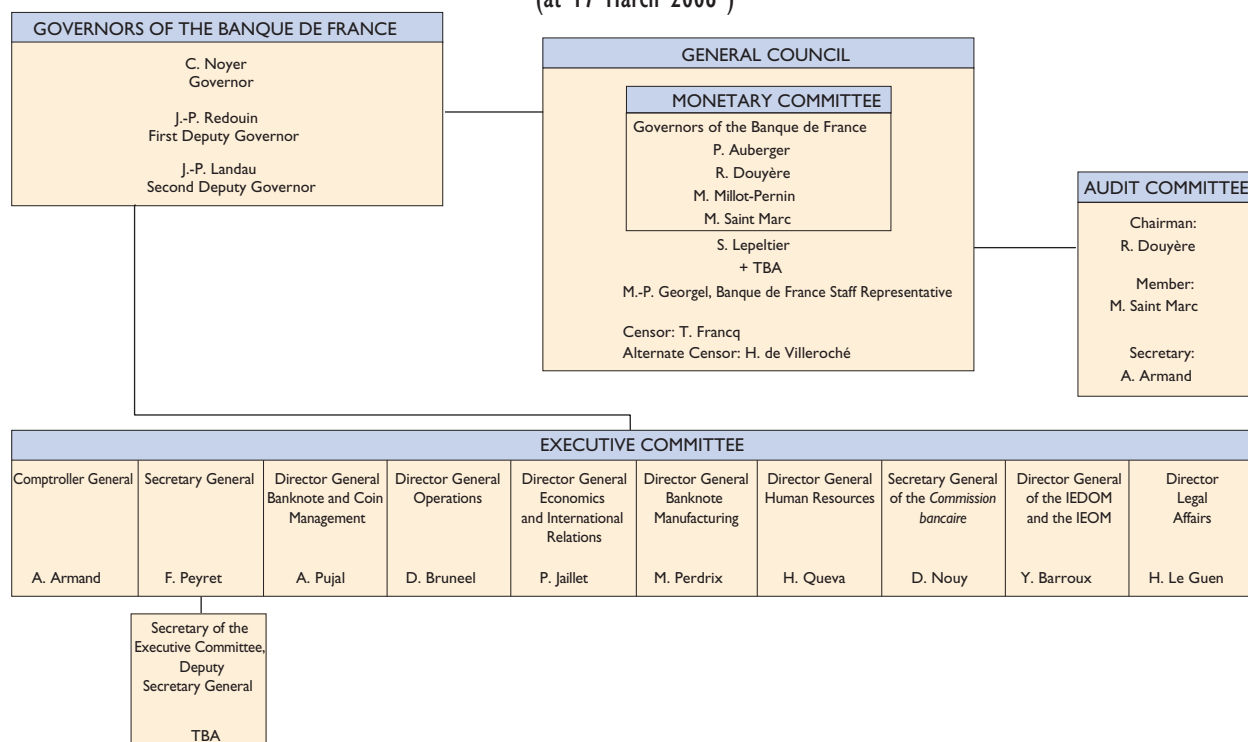
The Governor is in charge of the executive management of the Banque de France. He chairs the Executive Committee, which comprises all of the business area managers, as well as the Careers Committee, which gives its opinion on the appointment of the Bank's senior executives.

The Governor also chairs the *Commission bancaire*, the *Comité des établissements de crédit et entreprises d'investissement* (CECEI – Credit Institutions and Investment Firms Committee), the Banking Mediation Committee and the *Observatoire des cartes de paiement* (Payment Card Observatory). He is a member of the Governing Council of the European Central Bank (ECB).

## The Governors of the Banque de France



## The management bodies of the Banque de France (at 17 March 2008\*)



\* Until 16 March 2008, Yves Barroux and Marc-Olivier Strauss-Kahn were Secretary General and Director General Economics and International Relations respectively.



## I | 2 The General Council

Pursuant to Act 2007-212 of 20 February 2007, the General Council comprises the Governor and the two Deputy Governors, two members appointed by the President of the Senate, two members appointed by the President of the National Assembly, and two members appointed in the Council of Ministers on the proposal of the Minister of the Economy and Finance and a Banque de France Staff Representative. A Censor, or his/her alternate, appointed by the Minister of the Economy and Finance, represents the French State. The Censor attends the Council's meetings in possession of all the necessary information and may submit proposals to the Council and veto any of its decisions.

The General Council acts as an Executive Board. It examines issues relating to the terms of employment of the Bank's staff, which are submitted for approval

to the relevant Ministers, and determines the rules applicable to the Bank's staff in areas where the provisions of the French Labour Code are incompatible with the statutes or public service tasks incumbent on it. The General Council decides on the use of the Bank's own funds. It draws up the Bank's expenditure estimates and annual accounts and makes proposals for the allocation of profits.

In accordance with the above-mentioned principles, the General Council is, in particular, responsible for discussing the Banque de France's short and medium-term strategy. Each year, it therefore examines the business plan for the following year and reviews the progress of the projects underway. It also scrutinises the draft report on the implementation of the Public Service Contract.

The Monetary Committee of the General Council, created by the Act of 20 February 2007, comprises

### The General Council



Marie-Paule Georgel  
Michèle Saint Marc

Serge Lepeltier  
Jean-Paul Redouin

Raymond Douyère  
Christian Noyer

Philippe Auberger  
Jean-Pierre Landau

Thierry Francq  
Monique Millot-Pernin

the Governor, the two Deputy Governors and the members of the General Council appointed by the Presidents of the Senate and the National Assembly. It analyses monetary developments and the implications of the monetary policy conducted within the framework of the ESCB. It formulates the specific measures necessary to transpose into the national body of regulations the decisions adopted by the ECB Governing Council regarding monetary policy operations (see Committee Decision No. 2007-03 of 3 October 2007 concerning the transposition of the new regulations on monetary statistics) and to implement the Eurosystem's collateral and risk control framework (see Committee Decision No. 2007-05 of 7 December 2007 concerning the transposition of the ECB Guideline on monetary policy instruments and procedures).

In accordance with the provisions of Article L. 142-6 of the Monetary and Financial Code, the Head of the Treasury and Economic Policy or his/her representative may participate in meetings of the Committee and may submit any proposals for consideration by the latter, but may not vote.

### **I | 3 Independence of the Governor and the Banque de France's governing authorities**

The independence of the Banque de France, as a member of the ESCB, implies the independence of the Governor and Deputy Governors, and of the General Council, particularly the members of its Monetary Committee.

In accordance with Article L. 141-1 of the Monetary and Financial Code, the Banque de France, represented by its Governor, Deputy Governors or any other member of the Monetary Committee of the General Council, shall neither seek nor accept instructions from the Government nor any other body in the performance of the tasks arising from its participation in the ESCB. Furthermore, in accordance with Article L. 142-6 of the said Code, the Monetary Committee of the General Council shall act with due regard to the principle of independence of its chairman, who is a member of the European Central Bank's Governing Council, and abide by the ECB's confidentiality rules.

Lastly, Articles L. 142-3 and L. 142-7 stipulate that the Monetary Committee of the General Council shall ensure that the professional activities performed by their members comply with the principle of independence of the Banque de France.

### **I | 4 The Audit Committee**

Under the decision of 22 October 2004, the General Council set up an Audit Committee, made up of four non-executive members of the General Council. Its chairman is appointed by the General Council, on the proposal of the Governor, and the Comptroller General of the Banque de France provides its secretariat. The responsibilities and operating rules of the Audit Committee are specified in a charter annexed to the General Council Decision.<sup>1</sup> Its remit covers financial information, external and internal audit, internal control and risk control; in all these fields, the Audit Committee hears the auditors as well as any Banque de France executive, as necessary. It reports to the General Council.

In 2007, the tasks of the Audit Committee were to approve the annual accounts, examine the main conclusions of the internal audit missions, follow up the recommendations issued by these missions, and map out and control the operational risks encountered by all departments. It also examined the draft text on the restructuring of the appendix to the annual accounts. Lastly, the Committee took part in the drawing-up of the internal audit programme for 2008.

The existence of the Audit Committee strengthens the governance structure of the Banque de France by enhancing the already comprehensive internal control and risk management system, which is considered by the Bank's auditors to be "in line with best practices".

### **I | 5 The Executive Committee**

Both in its plenary and reduced form, the Executive Committee is at the heart of the operational functioning of the Banque de France. It constitutes the forum in which the Bank's managers exchange their viewpoints

<sup>1</sup> Cf. Bulletin officiel de la Banque de France, No. 74, February 2005.

on a range of subjects of common interest in order to facilitate the collegial decision-making process.

The Executive Committee, which is chaired by the Governor, comprises the Deputy Governors, the Directors General, the Deputy Secretary General for Strategy and Planning and the Legal Affairs Director. With a view to greater integration with the Bank, the Director General of the IEDOM and the IEOM is also a member of the Committee. The Committee examines issues relating to the Bank's strategy and internal management. The meetings of the Executive Committee may be prepared, if necessary, by smaller committees involving the managerial staff of the Bank directly concerned. The Executive Committee may also act as a Careers Committee charged with formulating an opinion on the appointment of the Bank's senior executives.

In addition to discussing issues relating to the Bank's strategy, the Executive Committee examined the new pay scheme for managerial staff (introduction of performance-based bonuses linked to the attainment of a set of objectives), the gathering of statistical data from credit institutions, and the implementation of the Public Service Contract signed with the State.

## I | 6 The College of Regional Managers and the Banque de France branch network

The Banque de France's branch network (see map) is now made up of 96 departmental branches (22 of which are regional head offices), 21 economic centres and 7 household debt centres.

### The Executive Committee



*Christian Noyer*  
Governor



*Jean-Paul Redouin*  
First Deputy Governor



*Jean-Pierre Landau*  
Second Deputy Governor



*Alain Armand*  
Comptroller  
General



*Frédéric Peyret*  
Secretary  
General



*Armand Pujal*  
Director General  
Banknote  
and Coin  
Management



*Danièle Nouy*  
Secretary  
General of the  
Commission  
bancaire



*Hervé Queva*  
Director  
General  
Human  
Resources



*Hervé Le Guen*  
Director  
Legal Affairs



*Didier Bruneel*  
Director  
General  
Operations



*Michel Perdrix*  
Director General  
Banknote  
Manufacturing



*Pierre Jaillet*  
Director General  
Economics and  
International  
Relations



*Yves Barroux*  
Director General  
of the IEDOM  
and the IEOM

Cash operations are carried out in 72 of these branches and in 4 specialised centres.

In order to maintain the services provided to its users (household debt services, access to payment incident databases and basic banking services) and according to the Public Service Contract signed with the State, the Banque de France has opened 85 customer service and information offices in each town where it did not set up an economic centre or a household debt centre to replace a branch closed during the 2004-2006 period. These temporary offices are on the premises of other public organisations (town halls, etc).

The Bank's network now operates at two levels:

- the region, i.e. the management level; the regional manager (the manager of the branch in the region's capital) co-ordinates and supervises the activity of the various branches throughout the region, and ensures the consistency and quality of the work carried out;
- the *département*, i.e. the operational level; it includes the departmental branch and, possibly, other associated specialised units in charge of implementing the objectives assigned to the branch network in close contact with the Banque de France's usual partners (banks, companies, private individuals, local authorities and administrative bodies).

Regional managers are responsible for fostering initiatives and promoting good practices in all operational fields, allocating budget resources, using financial control instruments, and carrying out activities relating to risk control, etc. They are assisted by units of experts and a specific structure charged with supervising operations and procedures – the regional risk control unit – whose responsibilities should shortly be extended.

In view of their responsibilities, the regional managers are the prime contacts for the Banque de France's Governors and Head Office managers for any questions relating to the branch network. The College of Regional Managers is chaired by the Secretary General and the Branch Network Manager; it also includes the five regional inspectors. Meetings are held once every two months.

## 2| Strategic planning and operational management

### 2|I Strategic plans

Every year, operational managers and support function managers are called upon to propose, in keeping with the general guidelines laid down by the Governor, a series of strategic plans to provide the basis for their activity during the following year, within a medium-term perspective. These proposals, together with their implications in terms of financial and human resources, are examined during a special Executive Committee meeting. Following this meeting, the priorities of the Banque de France are subsequently decided on, prioritised and costed.

A progress report on the implementation of the initiatives laid down in this strategic plan is then presented to the Executive Committee during the year.

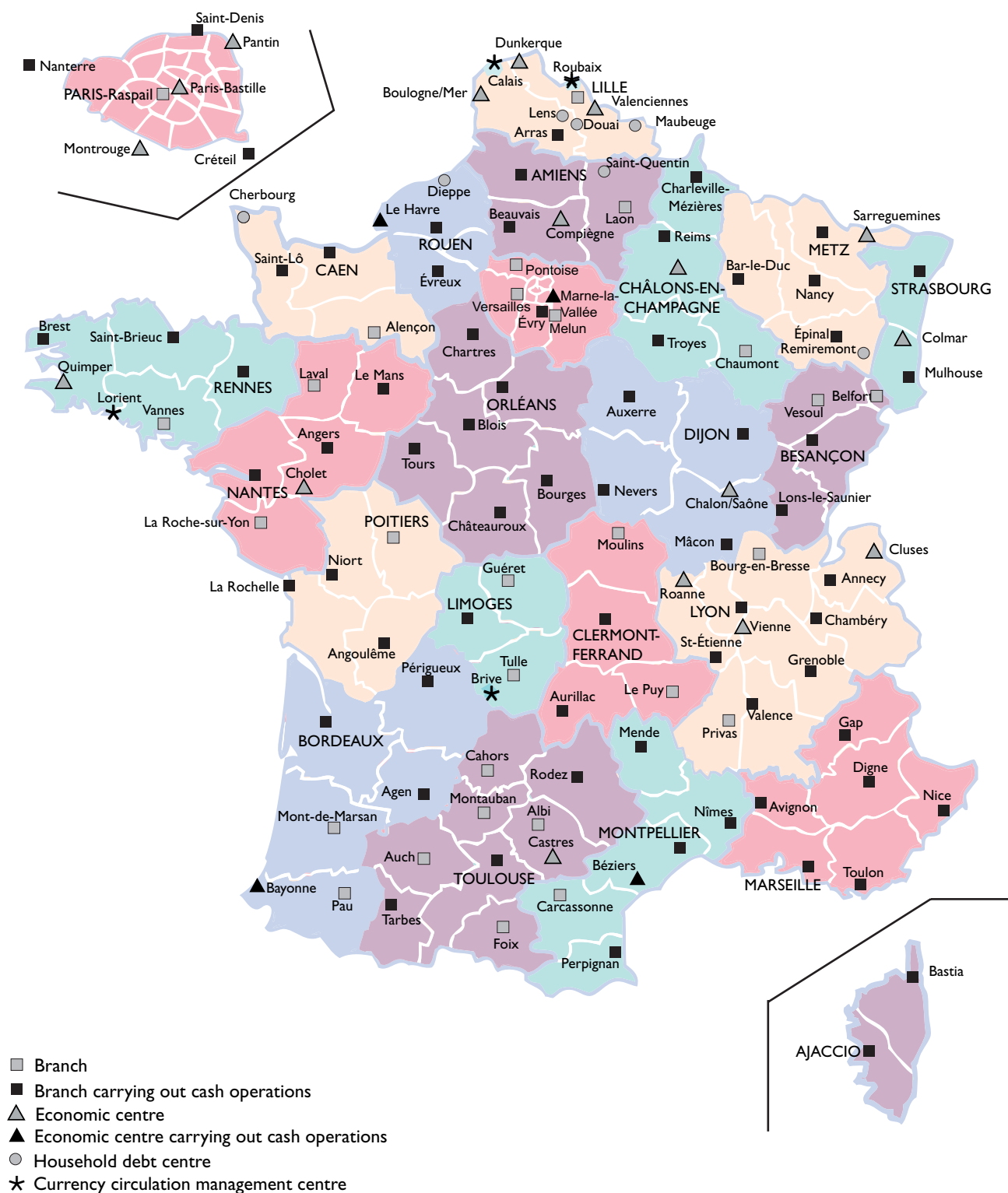
The 2007 business plan comprises three main orientations:

- developing the Bank's range of services offered within the Eurosystem, at a time when the environment is undergoing rapid change and competition is becoming stronger, particularly in the fields of operations, studies and research, banking supervision, cash management and IT;
- consolidating the benefits derived from the reorganisation of the branch network;
- continuing to improve the Bank's management, in order to provide the best service at the lowest cost.

These orientations require active management of human resources, particularly as regards recruitment and training, in order to enable the Bank to adapt as best as possible to a decline in its workforce (a large number of employees are expected to retire between 2012 and 2017).



## The Banque de France branch network at end-2007



## **2 | 2 Operational management**

Two bodies play a crucial role in the conduct of investment policies and market operations: the “Assets-Liabilities” Committee and the Risk Committee.

The Assets-Liabilities Committee, chaired by the Governor, advises him on the Bank’s portfolio investment strategy (both for euro and foreign currency denominated portfolios). It issues opinions, in particular, on the volume of investment, its allocation by type of asset and its duration.

The Risk Committee, chaired by a Deputy Governor, lays down the conditions under which market operations should be conducted for the Bank’s portfolios as a whole. In this regard, it draws up the list of authorised issuers, countries and instruments, validates the methodologies for measuring risk and the performance of market activities, sets the risk limits for these operations and examines the audit, control and activity reports relevant to its field of competence.

The Bank’s support functions also operate on a collegial basis, through two committees placed under the authority of the Secretary General. The IT Strategy Group is responsible for defining the Bank’s short- and medium-term policy with respect to IT investment, while the Real Estate Investment Committee is in charge of managing the Bank’s real estate assets.

The transposition of the Bank’s strategic orientations into concrete actions and the follow-up of their application are evidenced by the quality approaches pursued by the Bank for the past few years. These approaches, which are generally conducted at a decentralised level, are often accompanied by certification; they concern both operational fields (banknote manufacturing, cash management, banking services, etc.) and support functions (IT, audit, real estate, etc.). In 2007, the Banque de France started to examine the lessons to be learned from these approaches and build on the experience acquired.

## **3 | Risk control**

### **3 | 1 Internal audit**

The internal audit covers all of the Bank’s units, processes and activities. It is conducted at the Head Office, the regional administrative centres and in the branch network; its organisation is structured accordingly. The internal audit, whose work programme centres on a risk-based approach, aims to ensure the quality of the management, risk control and internal audit processes. By helping the Bank to attain its objectives, the internal audit contributes to improving corporate governance. The international standards for the professional practice of internal auditing as defined by the Institute of Internal Auditors serve as a reference both with regard to the organisation and the conduct of audit missions; an external assessment aiming to ensure that the organisation and practices of the internal audit comply with these standards will be carried out by the end of 2008.

The work of the internal audit is clearly in line with the framework of the ESCB. The Comptroller General and the head of the Head Office Audit are permanent members of the ESCB Internal Auditors Committee that meets several times a year at the ECB. Together with their NCB and ECB counterparts, they are in charge of defining the ESCB’s audit programme and overseeing the conduct of audit missions. The Committee then submits its conclusions to the Governing Council.

Representatives of the internal audit function take part in the methodological work conducted in the framework of the G10 conferences and working groups set up by the Bank for International Settlements. They also participate in benchmarking exercises aimed at identifying best professional practices. Lastly, a large number of delegations of internal auditors from central banks in developing countries attend training courses in Paris, while Banque de France inspectors conduct on-site technical assistance missions abroad.

## 3|2 Risk prevention

The Banque de France has adopted a risk management approach (the AMARIS method) in order to:

- strengthen the internal control function thanks to a common framework for operational risk control;
- promote the adoption of the best practices recommended by the Basel Committee in this area.

The following organisation was put in place:

- In each Directorate General, risk managers are in charge of mapping operational risks and assisting in the implementation of risk-reduction action plans; in addition, in each regional branch, a risk control unit is responsible for ensuring that the control mechanisms are properly implemented.
- Within the Risk Prevention Directorate, attached to the Comptroller General, a special unit is in charge of providing assessments, co-ordinating work and reporting to the Bank's governing authorities, while another unit is responsible for information security.<sup>2</sup>
- The Internal Control Co-ordination Committee (3CI), which comprises the Directors General and risk managers and is chaired by the Comptroller General, meets twice a year. It is charged with supervising the progress made towards tighter risk control in all of the Banque de France's fields of activity.
- The Executive Committee, to which a report on risk analysis and the implementation of action plans based on an updated overall risk map is presented each year.

## 4| Transparency and responsibility

### 4|1 External controls

#### 4|1|1 Auditors

Like all companies, the Banque de France is subject to the permanent scrutiny of auditors. The two auditing firms that carry out this task are chosen according to strict rules. After the Audit Committee has checked

the legality of the selection procedure, the Governor of the Banque de France proposes the appointment of two auditing firms to the General Council. Once it has been approved, this proposal is then put to the Governing Council of the ECB, which decides (or not) to submit it for approval to the Council of the European Union.

The appointment of the auditing firms only comes into effect after the Banque de France has received the agreement of the Council of the European Union.

#### 4|1|2 Court of Auditors

The Bank's internal management is also regularly audited by the Court of Auditors, which examines the manner in which the Bank performs its tasks and activities, in particular in terms of their financial implications. As is the case for the other public bodies subject to supervision by the Court of Auditors, the results of these investigations are published in a widely available report. The last public report was published in March 2005, with follow-up reports in January 2007 and February 2008.

### 4|2 The application of the Act on data processing, computer records and civil liberties

The Governor decided, in accordance with the provisions of the amended Act 78-17, to appoint a correspondent for the protection of personal data. The latter is charged with ensuring, in an independent manner, compliance with the obligations of the aforementioned Act for all the Banque de France's automated data processing functions. To this end, the correspondent may make any recommendation that he/she considers appropriate to the data processing managers. The correspondent shall be consulted, prior to their implementation, regarding new processes or changes to existing applications. Where necessary, he/she assists and advises the administrative units on their duties vis-à-vis the French Data Protection Authority (CNIL).

The correspondent shall not be given instructions as to the exercise of his/her functions. He/she may consult the Bank's governing authorities, who are responsible for all processing functions, regarding

<sup>2</sup> Regarding information security, in 2007 data classification was the subject of an awareness-raising campaign aimed at Banque de France staff.



**Banknotes entering the sorting machine**



any difficulties encountered in the conduct of his/her duties that cannot be resolved following discussions with the managers in question.

The correspondent shall also carry out the tasks previously entrusted to the data protection officer, a post that was created in 2003 following the publication of the CNIL report on "cybersurveillance in the workplace". In this capacity, he/she is charged in particular with enforcing and updating the provisions of the "Charter for the use of information and communication technologies" and with ensuring the protection of personal data regarding Banque de France staff.

#### **4 | 3 Specific rules applicable to Banque de France staff – Code of Financial Ethics**

Banque de France employees are bound by the confidentiality obligations laid down in Article L. 142-9 of the French Monetary and Financial Code. They may not take or accept any holding or interest in, or remuneration from another company, unless a derogation is granted by the Governor.

These provisions do not apply to scientific, literary or artistic work.

Requests for derogation are examined by a committee, chaired by the Professional Ethics Officer, which issues a reasoned opinion; they are then transferred to the Governor for a decision.

Banque de France employees are also subject to a Code of Financial Ethics. Compliance with this Code is ensured by the Professional Ethics Officer. The Code's provisions aim to prevent any behaviour that might be detrimental to the Bank or situations of conflicts of interest. The strictest provisions apply to employees whose duties in any way involve the negotiation of procurement contracts on the Bank's behalf or employees liable to hold non-public information.

## **5 | Assessment of social responsibility and human resource management**

### **5 | 1 Assessment of social responsibility**

The Banque de France has entrusted an independent external body with the task of assessing the Bank's social responsibility. This assessment covered employment conditions (transparency of the pay system, social protection, etc.), working conditions (health and safety, organisation of and compliance with working hours, etc.), careers and skills management, social relations, non-discrimination and respect for fundamental human rights (equal opportunities, combating harassment, protection of personal data, etc.).

According to the assessor, social responsibility is one of the Banque de France's values. The Bank seeks to establish, as far as possible, a high-quality social dialogue. It is strongly committed to promoting equality between men and women. The republican values of equal opportunities and non-discrimination are widely complied with. The Banque de France is actively rising to the new challenges (harassment, integration of disabled workers, etc.).

The assessment report notes that working conditions at the Banque de France are such that employees are able to reconcile their professional life with their personal life, thanks to flexitime. The Banque de France provides a good level of social protection, and by carrying through the talks on the pension scheme reform, it has met its social responsibility commitments vis-à-vis its staff and French society. The Banque de France has managed the various reorganisations well (banknote manufacturing, bank network reform). Lastly, it is committed to developing skills and employability.

The assessment body has pointed out a number of avenues for improvement in some areas of human resource management, in particular the clarification of the new

pay system and the measures applicable to contract staff as regards career prospects and skills development, and the coordination of the different players involved in the prevention of health risks at work.

## 5|2 Human resource management

### 5|2|1 Staff

On 31 December 2007, the Banque de France counted 12,828 full-time equivalent staff, down by 1.3% on the previous year. Between 1993 and 2007, total staff numbers fell by 28.5%.

The male-female breakdown of statutory staff is roughly equal. However, the high proportion of men among contract staff can be attributed to the large number of men among the security staff.

Statutory employees are mainly in the 30-49 age bracket, with the average age standing at 46 in 2007.

Some 43% of staff members work at the Head Office, 50% in the branch network and 7% in banknote manufacturing.

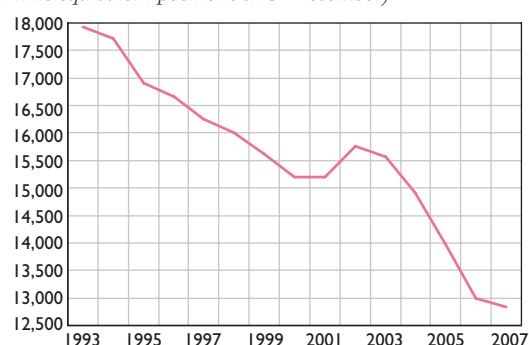
### 5|2|2 Secondments and temporary outplacement of Banque de France staff to external organisations

In 2007, the Banque de France pursued its policy of seconding and outplacing staff to external organisations. At end-2007, staff secondments and outplacements were as follows:

- 56 members of the Bank's staff to various French organisations, including the *Autorité des marchés financiers* (AMF – Financial Markets Authority), the *Autorité de contrôle des assurances et des mutuelles* (ACAM – Insurance Supervisory Authority) and a number of ministries;
- 85 members of staff to European institutions, international organisations and embassies, and in particular to the European Central Bank (36 staff members), the International Monetary Fund and the Bank for International Settlements.

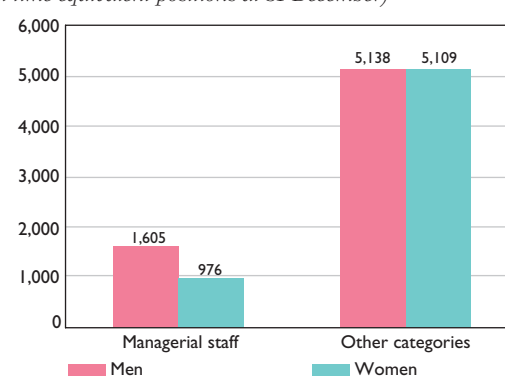
**Chart 1 Staff numbers**

(full-time equivalent positions at 31 December)



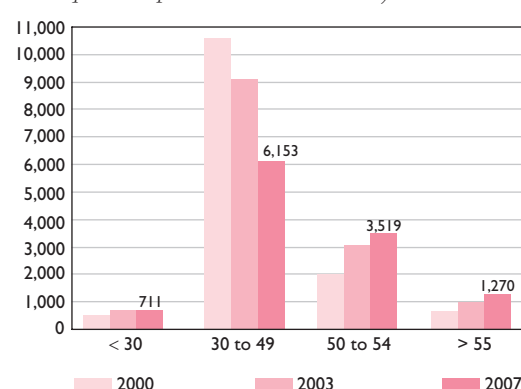
**Chart 2 Male/female breakdown of total staff**

(full-time equivalent positions at 31 December)



**Chart 3 Breakdown of statutory staff by age bracket**

(full-time equivalent positions at 31 December)



**Table I Staff levels**

(full-time equivalent positions at 31 December)

	2006	2007
<b>STATUTORY STAFF</b>	<b>11,829</b>	<b>11,653</b>
Male	6,001	5,862
Female	5,828	5,791
<b>Head office</b>	<b>5,295</b>	<b>5,243</b>
Management	1,487	1,510
Other categories	3,808	3,733
<b>Branch network</b>	<b>5,745</b>	<b>5,636</b>
Management	847	812
Other categories	4,898	4,824
<b>Banknote manufacturing</b>	<b>789</b>	<b>774</b>
Management	9	9
Other categories	780	765
<b>CONTRACT STAFF</b>	<b>1,169</b>	<b>1,175</b>
<b>Specialty-recruited staff</b>	<b>374</b>	<b>406</b>
Head office	231	237
Banknote manufacturing	143	169
<b>Other staff</b> (excluding occasional workers)	<b>795</b>	<b>769</b>
Security staff	601	583
Cleaning and other staff	194	186
<b>TOTAL</b>	<b>12,998</b>	<b>12,828</b>
Men	6,876	6,743
Women	6,122	6,085

## 6| Environmental policy

The industrial activities of the Banque de France have benefited from quality and environmental certifications for several years. The Banknote Manufacturing Directorate has implemented a series of procedures for sorting waste and reducing water and energy consumption, and has committed itself to using "green" electricity, i.e. produced from renewable energy sources (wind and hydroelectric power) for 25% of its needs. The Banque de France has also set up an eco-friendly system (shredder) for destroying used banknotes, to replace the previous incinerator.

It is only more recently that service sector activities have become more environmentally aware. In this respect, the Banque de France has taken a number of awareness-raising measures aimed at its staff and carried out several short- and medium-term initiatives.

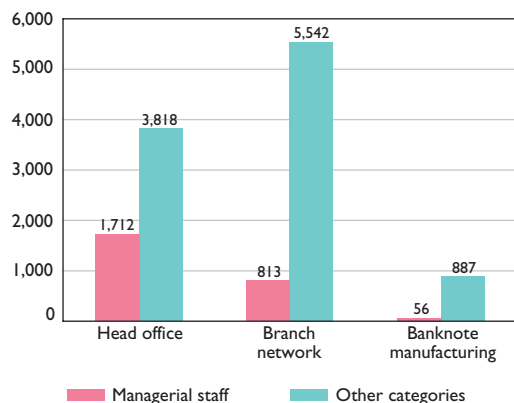
### 6| I Raising staff awareness

In 2007, the Banque de France carried out its first large-scale awareness-raising campaign with the setting of a three-year profit-sharing target of a 30% reduction in paper consumption across all Bank departments. This initiative also included information on good practices essential for reaching the objective, the opening of an Intranet site on sustainable development and the creation of dedicated electronic mailbox for questions relating to the environment. This collective endeavour was a first step towards a more committed formulation of a concerted environmental policy. This policy, which is expected to have an effect as early as 2008, will include the development of a Company Transport Plan for three of the Bank's largest sites and the launch of a carbon footprint methodology, which will be fleshed out over time.

At the same time, the Bank set up a structure for ensuring the smooth co-ordination of initiatives so that the issues relating to sustainable development can be taken into account in administrative processes: a national steering committee serving as a permanent support structure, a sustainable development steering committee for the real estate sector and a sustainable purchasing committee, which now includes an

**Chart 4 Location of staff**

(full-time equivalent positions at 31 December)



eco-responsible component in the selection of the Bank's suppliers.

## **6|2 Real estate strategy**

In 2007, the Banque de France, which manages real estate stock of roughly 1 million square metres, set out to develop and structure its eco-responsible initiatives in this area. Its work mainly focused on the following points:

- Integration of HQE® (*Haute Qualité Environnementale*) targets in new building sites or major redevelopment sites: the new building for the future Avignon branch was constructed according to "very high" energy management standards; the new project of a conference/meeting room at the Head Office also includes HQE® targets.

- A global environmental approach for major renovations, the maintenance and adaptation of the Bank's buildings in accordance with the changes in the Bank's activities. With the support of a specialised firm of architects, the Bank launched two studies on the renovation of the buildings of the La Rochelle and Strasbourg branches, in order to get an overview of the work to be carried out, from an energy-saving perspective.

- As regards efficient energy services, particular attention is paid to the steering of consumption using a centralised technical management system at the Head Office, the Bank's administrative centres and several large units in the network and a computerised maintenance management system (CMMS) at the Head Office and the two administrative centres.

- Regarding heating, lighting and air-conditioning, in addition to improving the insulation of its buildings, the Banque de France has put the following measures in place:

- for heating, the use, wherever possible, of urban heating in the network buildings, like in the case of the Head Office, and the systematic implementation of comparative studies on the choice of energy sources when boilers have to be changed;

- the installation of photovoltaic cells in some Bank branches (Avignon, Ajaccio);

- the increasingly systematic use of energy-saving lamps;

- for air-conditioning, the implementation of energy-saving solutions and, in some cases, the insulation of window and door frames.

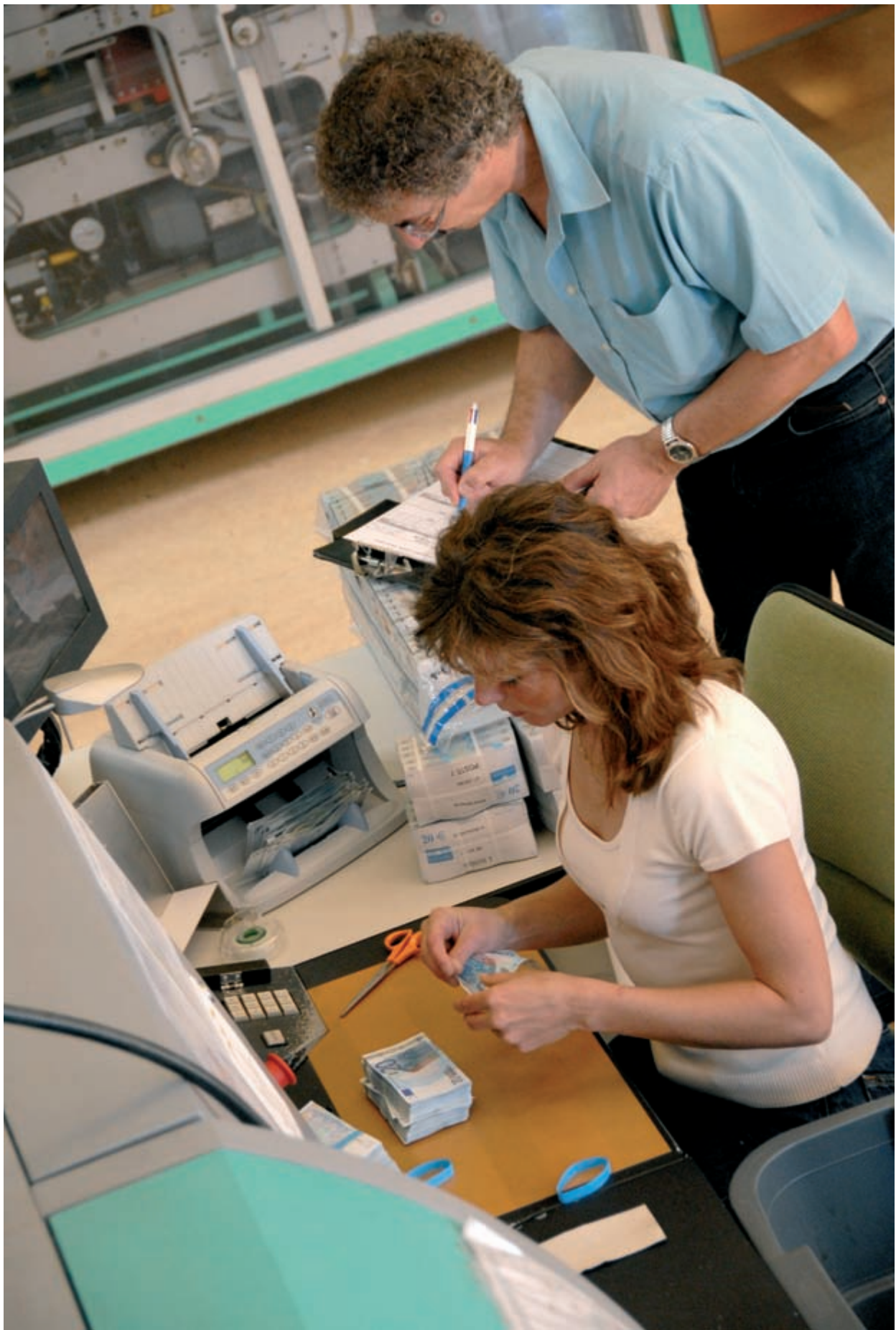
## **7| Sustainable development and the Bank's tasks**

By incorporating sustainable development concerns into its operating modes and staff management, the Banque de France has taken a major step towards taking on board the principles of corporate social responsibility. A second step will be taken with the definition of an action plan to integrate these concerns into the actual framework of the Bank's tasks, by formalising the links between social responsibility and its activities.

Given the Bank's public service missions, this link is already very strong in some areas, in particular with regard to dealing with situations of overindebtedness or ensuring the quality of the circulation of banknotes and coins. In other areas, such as economic research and the assessment of the soundness of companies, taking account of the constraints imposed by the new environmental regulations opens up new possibilities for action. In 2008, the Banque de France will draw up a list of possible actions and rank priorities in order to focus on a few major issues.







**Sorting machine operators**

# THE ENVIRONMENT AND IMPLEMENTATION OF MONETARY POLICY

In 2007, the economic activity of the euro area's main trading partners moderated relative to the past three years. The spillover from the US economic slowdown has nevertheless been mitigated by the continued strength of the emerging economies (see 1|).

Given the soundness of the euro area's economic fundamentals and the rapid growth in money and credit aggregates, the Governing Council of the European Central Bank (ECB) pursued a less accommodative monetary policy stance, raising the key interest rate in March and June from 3.5% to 4%. As of August 2007, in the wake of the subprime crisis, the Governing Council adopted a wait-and-see position, pending additional information on the impact of this crisis before taking further interest rate decisions (see 2|).

The implementation of monetary policy in the euro area was marked by strong liquidity constraints as of August 2007 (see 3|).

## I| The international environment

### I|| Economic growth in countries outside the euro area

#### I||| The United States

US GDP growth slowed in 2007 to reach 2.2% as an annual average, compared with 2.9% in 2006. In particular, the housing market corrected more significantly (see Box 1 "Adjustment in the US housing market"), resulting in a 17% decline in residential investment over the year, which knocked almost one percentage point off US GDP growth. Following a first quarter of lacklustre growth, GDP accelerated sharply in the middle of the year, and then slowed down significantly in the fourth quarter, which can partly be explained by the financial turmoil from the subprime crisis. US household consumption remained relatively robust thanks to the sound labour market, which only started to show signs of weakness towards the end of

the year, with the unemployment rate rising from 4.6% in June to 5.0% in December. Corporate investment also rose sharply (4.8%), in particular in the middle of the year, despite the bleaker prospects for demand and a relative expansion in production capacity. It was underpinned by domestic corporate profitability, which remained above its long-term average. For the first time since 1995, net exports made a positive contribution to annual growth thanks to the sustained strengthening of export markets, the depreciation of the dollar and the slowdown in domestic demand. The improvement in the US trade balance is also reflected in the reduction in the current account deficit, which narrowed from 6.2 percentage points of GDP in 2006 to 5.6 percentage points in 2007.

Inflation, measured by the year-on-year change in the consumer price index, eased from 3.2% in 2006 to 2.9% in 2007. However, the rise in energy prices caused inflation to pick up at the end of the year. Underlying inflation (excluding energy and food) fell in 2007 (2.3 % on average, against 2.5% in 2006). After moderating at the start of the year, which may be attributable to the decline in unit labour costs in the second and third quarters, underlying inflation showed fresh signs of accelerating in September 2007, despite the slowdown in domestic demand and an easing of pressures on production capacity. This acceleration can be ascribed to the price rises in the health, education and transport (excluding fuel) sectors. The housing component<sup>1</sup> showed a clear downward trend in 2007 but still made a significant contribution to inflation.

In response to the slowdown in activity and in order to counter the recessionary impact of the financial turmoil, the Federal Reserve System adopted a more accommodative monetary policy. It embarked on a cycle of interest rate cuts, lowering its target for the federal funds rate, in the second half of the year, from 5.25% to 4.25%. Furthermore, the Fed intervened to stabilise the beleaguered money markets. Measures included injecting liquidity, reducing the spread between the discount rate and the federal funds rate and, at the end of the year, introducing a new refinancing facility, the Term Auction Facility, enabling depository institutions to borrow at longer

NB : Unless otherwise stated, the statistics presented in this chapter were updated on 31 March 2008.

1 Unlike the Harmonised Index of Consumer Prices (HICP) for the euro area, the US consumer price index includes owner-occupied housing costs, as well as rents paid by tenants. These costs are calculated using the owners' equivalent rent method.

**Box I**

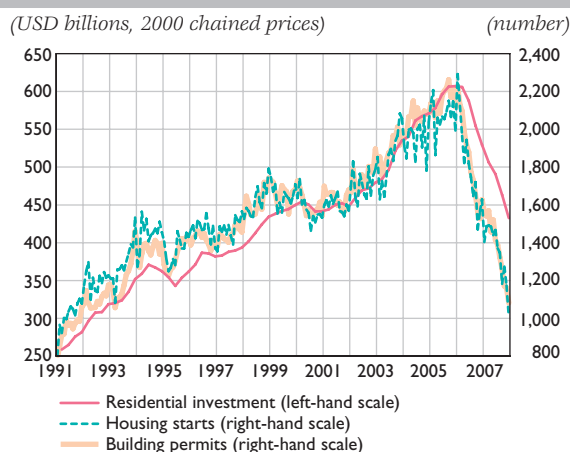
### **The adjustment in the US housing market**

After several years of sharp growth, the US housing market started to show signs of a slowdown in the second half of 2005. This deceleration was due to falling demand on the back of interest rate hikes, the perception that property was overvalued and expectations of a turnaround in the market. With the solvency problems of certain households, which triggered the subprime crisis, and the tightening of lending conditions, the decline in demand accelerated in 2007: home sales contracted substantially, in the case of both new dwellings (-26%, compared with -18% in 2006) and existing dwellings (-13%, compared with -8 % in 2006).

Until then, the market had mainly adjusted through a decrease in housing supply. The number of building permits and housing starts both fell by 26% in 2007. In the fourth quarter, residential investment contracted by almost 30% relative to its high at end-2005. Nevertheless, there still appears to be excess housing supply. The unsold housing stock, in terms of months of sales, reached historical highs: the number of dwellings not finding buyers would cover 10 months of sales at the end of 2007. This stock is also swelling due to the repossession of homes by mortgage lenders whose clients can no longer meet their payments. According to a report by the Mortgage Bankers Association, over 2% of mortgage loans were subject to foreclosure proceedings in Q4 2007, compared with only 1.0% at the start of 2006. This increase largely reflects home repossessions in the subprime segment (8.7%, compared with 3.5% at the start of 2006) as well as the rise among more conventional borrowers (1%, against 0.5%).

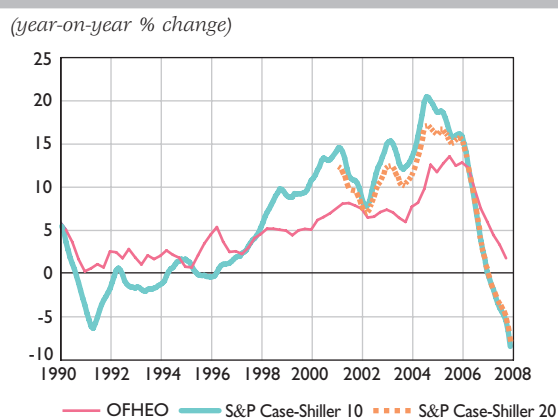
The second adjustment was through house prices. In December 2007, prices, measured by the Case-Shiller index, fell by 9.1% year-on-year in the 20 largest US metropolitan areas. In some cities of Florida and California, this fall exceeded 10% over the same period (-17.5% in Miami, -13.7% in Los Angeles). Moreover, markets are pricing in further declines, whose impact could extend beyond the housing market. In particular, they could further affect household consumption, via negative wealth effects and mortgage equity withdrawals.

**Chart 5 Residential investment in volume and number of houses built**



Sources: Bureau of Economic Analysis, Census Bureau.

**Chart 6 House prices**



Sources: Office of Federal Housing Enterprise Oversight, Macromarkets.



maturities and use a wider range of collateral than in traditional open market operations. As regards fiscal policy, the federal government deficit declined (to stand at 1.2 percentage point of GDP for the 2007 fiscal year, after 1.9 in 2006), due to the sharp rise in income tax receipts and the reduction in spending excluding health and defence. Nevertheless, the consolidated general government deficit increased, mainly as a result of higher welfare spending by local governments.

### 1|1|2 Japan and emerging Asia

GDP growth in Japan eased in 2007, to 2.1%, after 2.4% in 2006. However, it still remains slightly above potential output (estimated at between 1.5% and 2.0%), underpinned by domestic demand and net exports.

Employment conditions improved significantly in 2007, but as of August, the unemployment rate stabilised at around 3.8% and the vacancies-to-unemployment ratio fell substantially, from 1.06 to 0.98 in December, its lowest level since 2005. Despite the 0.7% decline in nominal compensation per employee in 2007, household consumption grew by 1.5%, making a 0.8 percentage point contribution to annual GDP growth.

Corporate investment remained stable at 2.5% in 2007, offsetting the sharp fall in residential investment (11.4% year-on-year in Q3 and 21.4% in Q4). This downturn is due to delays in issuing building permits, following the introduction of the new anti-earthquake measures that bolster existing rules.

Japan's current account surplus grew slightly in 2007. In particular, exports to Asia remained buoyant, offsetting at the end of the year the fall in US demand.

Following further year-on-year declines in the overall consumer price index over much of the year, inflation returned to positive territory in October, due to the rise in energy goods prices. However, annual inflation excluding energy and food remained negative (-0.3%, compared with 0.1% for the overall CPI). The Bank of Japan continued its very gradual normalisation of monetary policy underway since 2006, raising interest rates by 25 basis points in February 2007, to 0.5%.

The strong growth observed in emerging Asian economies as a whole was particularly sustained in China (11.4% in 2007, after 10.7% in 2006) and India (8.9% in 2007, after 9.7% in 2006). Inflationary pressures, partly associated with the surge in food prices, heightened in China in the second half of the year, stressing the need for measures to stop the economy from overheating.

In 2007, the strength of Asian economies raised hopes of at least a partial "decoupling" in the event of a sharp slowdown of the US economy. However, at the end of the year, this remained an open question for 2008 (see Box 2 "US economic slowdown and decoupling").

### 1|1|3 The euro area's partners inside the European Union

Despite the moderation in the housing market and worsening in the trade balance, growth in the United Kingdom came out at 3.1% in 2007, compared with 2.9% in 2006, thanks to robust household consumption, which was underpinned by a solid labour market. Against this backdrop, inflation, measured by the Harmonised Index of Consumer Prices, remained at its 2006 level, i.e. 2.3%, in spite of the rise in energy and food prices. In March, however, it reached a peak of 3.1% year-on-year, prompting the Governor of the Bank of England to write an open letter to the Chancellor of the Exchequer.

**Table 2 Main economic indicators  
for the United States and Japan**

	United States		Japan	
	2006	2007	2006	2007
Gross domestic product (a)	2.9	2.2	2.4	2.1
Industrial production (a)	4.0	1.9	4.8	2.8
Consumer prices (a)	3.2	2.9	0.2	0.1
Unemployment rate (b)	4.6	4.6	4.1	3.9
General government deficit (c)	-2.6	-2.8	-2.9	-3.4
General government debt (c)	61.9	62.2	179.7	180.3
Current account balance (c)	-6.2	-5.6	3.9	4.9

(a) Annual average change.

(b) In level form.

(c) As a % of GDP.

Sources: National and OECD data.

**Box 2**

**US economic slowdown and decoupling**

The recent sharp slowdown in the US economy raises the question as to what impact this may have on other economies. It may be moderate for emerging countries, which still grew strongly in 2007, but more significant for European countries, whose growth was weaker.

Generally, two main transmission channels for shocks between countries are identified: the trade channel and the financial channel. In the former, a decline in US imports, following a slowdown in consumption as well as investment in the United States results in a decrease in demand vis-à-vis exporting countries, and therefore a possible slowdown in their growth. The magnitude of the impact of a decline in US imports on the exports of other countries depends not only on bilateral trade flows with the United States, but also on intermediate goods exports to third countries that transform them in order to export them in turn to the United States. This indirect impact may be especially significant for emerging Asian countries. The transmission of shocks by the trade channel also depends, in times of dollar weakness, on exchange rate developments.

The transmission of shocks via the financial channel is less direct and usually occurs through the wealth effects associated with changes in the value of economic agents' portfolios. Banks, for instance, may have to tighten their credit standards in response to losses on their foreign assets, with adverse consequences for companies and individuals that require financing.

An analysis of the correlations between the growth rate of real GDP in the United States and in other countries over the past decade shows a significantly positive correlation between US growth and European growth. Moreover, this correlation, which has been stable since the 1970s, tends to increase when the United States is in recession. This re-coupling process was particularly evident during the last US recession of 2001. This increase in correlations during recessions has also been observed between the United States and emerging Asian countries, but the average level of the correlations is historically low.

Decomposing the variance of domestic growth rates highlights the important role played by shocks common to different countries (such as oil shocks) in cyclical fluctuations, even though the exact nature of this role varies according to the model used. For instance, the possibility of a decoupling of European countries, i.e. their growth rates relative to those of the United States, also depends on the nature of the shock currently affecting the United States. Yet, while the subprime crisis was, at the outset, a purely American shock, the resulting financial market turmoil took on a global dimension. Nevertheless, we must not overlook the importance of specific factors in cyclical GDP that mitigate the correlation between developments across countries. In this respect, Europe did not experience in 2007 a real estate crisis comparable to that of the United States.

GDP growth in the New Member States (NMSs) of the European Union declined from 6.4% in 2006 to 5.9% in 2007. This slowdown reflects contrasting developments across countries: GDP growth increased in Slovakia and Poland, while it was stable in the Czech Republic and fell in Romania. In Hungary, it remained sluggish due to the implementation of its fiscal consolidation plan. Inflation picked up in almost all NMSs on the back of the rise in food prices, energy prices and indirect taxes associated with European tax harmonisation: the Harmonised Index of Consumer Prices rose by 4.1% in 2007, compared with 3.3% in 2006. The general government deficit narrowed to 2.1% of GDP in 2007, from 2.6% in 2006. However, this average masks significant differences, with a government deficit in Hungary of 6.1% of GDP in 2007, compared with 9.2%

in 2006, and a rise in the deficit in Romania from 1.9% in 2006 to 2.7% of GDP in 2007.

## **I | 2 Financial and commodities markets**

### **I | 2 | 1 Financial markets**

In 2007, there were substantial changes in risk appetite: while the first part of the year was characterised by a sharp decline in implied volatility on the different market segments, risk aversion returned in summer accompanied by heightened volatility.

In 2007, expectations that European growth would weather the increasingly likely US economic slowdown caused the euro to appreciate against the main currencies. The euro's nominal effective exchange rate against the area's main trading partners gained 6.3% in 2007, compared with 4.4% in 2006. The euro appreciated by 9.3% against the pound sterling between end-December 2006 and end-December 2007 and by 3.1% against the yen. The fact that the euro appreciated less against the yen can be explained by the increased volatility of the yen against the main currencies, in particular due to the building-up and unwinding of carry trades. The latter consist in borrowing at low Japanese interest rates to invest in higher-yield currencies. Conversely, the nominal effective exchange rate of the US dollar depreciated sharply by 7.4% in 2007. This decline was particularly marked against commodity-linked currencies, such as the Canadian dollar (-15.8%), the Australian dollar (-11%), as well as the euro (-11.5%) and the yuan (-6.6%).

Furthermore, the dimmer US economic growth outlook led market participants to revise down their expectations of the future federal funds rate, corroborated by two rate cuts between September 2007 and the end of the year, bringing the federal funds rate down from 5.25% to 4.25%. However, confidence in the strength of euro area growth, on the back of the statement that the ECB would show strong vigilance against inflation, led market participants to expect no further rate changes following the last hike in the main refinancing minimum bid rate in June 2007 to 4.00%.

Movements in bond yields were broadly similar on both sides of the Atlantic (see Table 3). Rising until end-May, sovereign bond yields then fell sharply on downward revisions regarding US growth prospects and then further in August due to a flight to quality, as investors moved out of private bonds. Overall, the yield curve steepened on both sides of the Atlantic. This movement can mainly be attributed to expectations of looser monetary policy.

In particular as of summer 2007, the credit risk premium increased due to growing uncertainty over US growth prospects, the surge in subprime defaults, and concerns about the quality of securities backed by such collateral. This rise in risk aversion was first observed on the mortgage loan securitisation

market before spreading to private debt as a whole. The money market then came under pressure, with banks becoming reluctant to lend to one another and dispose of the liquidity made available by central banks. The significant widening of the spread between notably the three-month money market rate and OIS (overnight interest swaps) rates of the same maturity reflects the risk premium on the interbank market in particular. Consequently, central banks had to inject large amounts of liquidity to ease these substantial pressures.

Lastly, the main stock markets ended the year in positive territory despite the sharp corrections seen in the second half of the year. For example, the CAC 40 put on 1.3% to stand at 5,614, while the Dow Jones rose by 6.43% to 13,264. Conversely, the Nikkei lost 11.13%, finishing the year at 15,308.

Trends observed in the second half of 2007 continued into early 2008. Interest rate cuts by the Fed in January 2008, slashing the fed funds rate from 4.25% to 3.00%, caused money market rates to ease further and bond yield curves to steepen sharply, with sovereign bond yields falling most significantly on the short end of the curve. Risk aversion continued to increase and credit premia rose especially for private issuers and more specifically for credit institutions. At end-February 2008, stock markets plummeted (around 14% in continental Europe and around 8% in the United States), wiping out the gains made in 2007.

**Table 3 Government bond yields**

(by maturity, change in basis points, level as a %)

	Change 2007		Level end-2007	
	2-year	10-year	2-year	10-year
France	19	44	4.10	4.42
United States	-180	-69	3.08	4.07
Japan	-10	-18	0.73	1.51

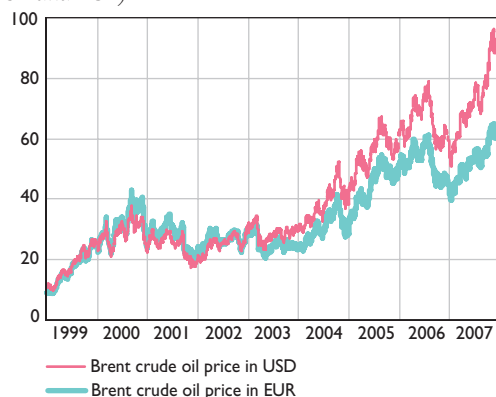
Source: Bloomberg.

## 1|2|2 Rising oil and commodity prices

Oil prices rose further in 2007, Brent crude increasing by 10.7% in dollar terms relative to the previous year (as an annual average). In particular, the acceleration in demand from emerging countries (especially China and India) resulted in structural strains on the market, while past under-investment continued to affect

**Chart 7 Brent crude oil prices**

(in USD and EUR)



Source: Bloomberg.

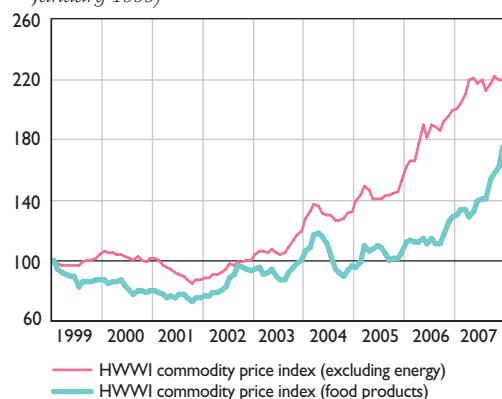
supply capacities. The rise in oil prices accelerated at the end of the year (Chart 7).

Non-energy commodity prices also rose (Chart 8) and in particular those of food in 2007. The structural rise in demand from emerging countries and climatic events affecting harvests considerably increased pressures on these markets.

As regards France, following a sharp rise in 2006 (up by 22.7%), the price of imported commodities<sup>2</sup> fell slightly by 1.9% as an annual average in 2007. The appreciation of the euro in particular against the dollar

**Chart 8 Commodity price index excluding energy**

(100 = January 1999)



Source: OECD.

more than offset the increase in the commodity price index, which rose by 5% in dollar terms, and thus made it possible to partly contain inflationary pressures.

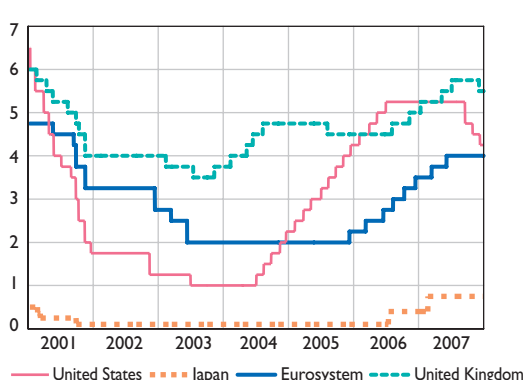
## 2| Eurosystem monetary policy decisions and their economic and financial environment

### 2|1 Two key interest rate hikes in 2007

The ECB Governing Council raised its key interest rate by 25 basis points (bp) both in March and June 2007, continuing its progressive withdrawal of monetary accommodation underway since December 2005, following a two-and-a-half year period where the repo rate was at the historically low level of 2%. These two hikes brought the minimum bid rate applied to the Eurosystem's main refinancing operations to 4% in June 2007. These decisions reflect the Council's determination to withdraw the accommodative monetary policy stance and to take account of the risks to price stability identified by the economic analysis and confirmed by cross-checking its findings with the monetary analysis (see Box 3 on the monetary policy strategy of the Eurosystem). In August 2007,

**Chart 9 Key interest rates of the ECB, the United States, Japan and the United Kingdom**

(%)



Sources: ECB, national central banks.

<sup>2</sup> According to the Banque de France index, which reflects changes in the price of commodities imported by France (energy, agricultural products for food, agricultural products for industrial use and mineral products) by weighting the change in each commodity by its weight in total commodity imports.

Box 3

### The monetary policy strategy of the Eurosystem

*In accordance with the 1993 Treaty on European Union, the primary objective of the Eurosystem's monetary policy is to ensure price stability. The Eurosystem's monetary policy can best contribute to sustainable and balanced growth in the euro area by anchoring inflation expectations at a low and stable level. In order to achieve maximum transparency, which is a prerequisite for aligning private agents' inflation expectations with its objective, the Eurosystem has implemented, from the outset, an explicit monetary policy strategy. This strategy offers a consistent framework for communicating and explaining to the public the Eurosystem's key interest rate decisions and their rationale.*

*The Eurosystem's strategy is based on a quantitative definition of price stability, i.e. an annual increase in the Harmonised Index of Consumer Prices (HICP) below, but close to, 2% in the euro area over the medium term. The Eurosystem's strategy also calls for an assessment of risks to price stability based on a broad analysis of available economic information organised around two "pillars", corresponding to two complementary approaches to inflation and its causes. The first pillar consists of the analysis of a wide range of economic and financial indicators likely to provide information about inflationary pressures in the short and medium term, such as data on real growth, prices and costs, the labour market, foreign exchange rates and fiscal policies. The second pillar is the "monetary" analysis, which focuses more on the outlook for the longer term, cross-checking the findings of the economic analysis against developments in money supply and credit aggregates.*

given the high degree of uncertainty, the Governing Council considered it preferable to collect additional information on the impact of the financial turmoil associated with the subprime crisis before drawing conclusions for monetary policy.

In 2007, economic activity expanded at a brisk pace in the euro area and annual HICP inflation largely exceeded 2% during the last months of 2007, mainly reflecting the rise in oil and food prices. Given the sound economic fundamentals and the strong money and credit growth in the euro area, risks to the outlook for price developments remained on the upside. However, the reassessment of risks and volatility on capital markets was accompanied by a high degree of uncertainty as to their potential impact on the real economy.

In the rest of this section, the salient developments in 2007, presented first from an economic analysis perspective and then from a monetary analysis angle, are considered in greater depth.

## 2|2 Economic analysis

### 2|2|1 Economic activity<sup>3</sup>

In 2007, economic activity in the euro area slowed down on the previous year: GDP rose by 2.6% as an

annual average (quarterly accounts at chain-linked prices, adjusted for seasonal and working-day variations), after 2.9% in 2006. The GDP growth of most euro area countries was lower in 2007 than in 2006. This was particularly the case for France, Germany, Italy and Spain. Furthermore, in 2007 Slovenia entered the euro area, with a GDP of around 0.4% of that of the area as a whole.

The slowdown in euro area GDP can be attributed to the lower contributions of domestic demand excluding inventories (2.2 percentage points, after 2.6 percentage points in 2006) and inventory changes (0.0 percentage point, after 0.1 percentage point in 2006). Conversely, the contribution of foreign trade increased (0.4 percentage point, after 0.2 percentage point). Among the domestic expenditure components of GDP, private consumption and investment both contracted, falling from 1.8% in 2006 to 1.5% in 2007 and from 5.3% to 4.2% respectively. Only government consumption growth firmed in 2007 relative to 2006 (2.2%, after 2.0 %).

However, in 2007, household income was underpinned by the strength of the labour market. Moreover, on average, inflation was lower than in 2006 (2.1%, after 2.2%). Nevertheless, consumer prices accelerated at the end of the year (3.1% year-on-year in December), reflecting the rise in food and energy prices. This rise in inflation weighed on household spending.

3 On the basis of statistics available at 15 May 2008.





**Banknotes rejected by the sorting machine**

Furthermore, the slowdown in household consumption in the euro area in 2007 can be partly explained by its contraction in Germany (see below).

The deceleration in investment is, for its part, largely attributable to the turnaround in the housing market in a number of euro area countries, which also resulted in a decline in construction output of 4.0% year-on-year in December 2007, compared

with a rise of 8.8% in December 2006. Despite tighter financing conditions, resulting mainly from higher interest rates, non-construction investment continued to rise at a sustained pace in 2007, as in the previous year, in a context of increased pressure on productive capacity. The capacity utilisation rate stood at 84.2% as an annual average in 2007 in the manufacturing sector, compared with 83.2% in 2006.

#### Box 4

### France's trade balance in 2007

In 2007, France's goods trade balance (fob-fob) deteriorated by EUR 11.1 billion relative to the previous year, to stand at EUR 39.6 billion (see Table 4).

This decline cannot be attributed to energy products, whose balance improved by EUR 1.4 billion, to EUR -45.1 billion, thanks to the slight fall in average crude oil prices in euro and the reduction in the quantities of oil products imported. However, the sharp rises in commodity prices weighed heavily on the balance on intermediate goods, which declined by EUR 4.4 billion. Similarly, the balance on automotive products dropped significantly by EUR 4.7 billion. This was due to the sharp contraction in the balance on motor vehicles, which recorded a deficit of EUR -0.6 billion, after posting a surplus of EUR 3.7 billion in 2006. Imports of motor vehicles have risen rapidly since 2005, unlike exports (see Chart 10). Excluding energy products, only the agri-food sector registered an improvement in its position, with a balance of EUR 9.1 billion.

Much of the deterioration in France's trade balance can be ascribed to the widening of the intra-EU trade deficit, which exceeded EUR 6 billion; this was particularly marked in the case of Germany (EUR 4.1 billion). Against the backdrop of the stronger euro, the deficit with Asian countries increased by EUR 2 billion, to EUR 25.5 billion, due to the EUR 3.2 billion rise in the deficit with China (Hong Kong included). Lastly, trade with the United States was greatly affected by the current slowdown in the US economy; the bilateral trade balance stood at EUR -1.1 billion, compared with EUR 0.8 billion in 2006, i.e. a deterioration of EUR 1.9 billion.

**Table 4 France's goods trade balance**

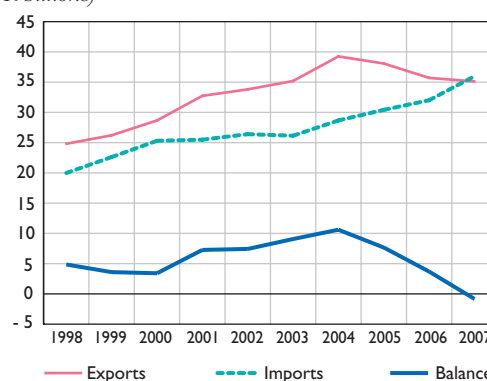
(EUR billions, in unadjusted terms)

	2005	2006	2007	2007/2006
<b>Total balance</b>	<b>-23.0</b>	<b>-28.4</b>	<b>-39.6</b>	<b>-11.1</b>
<i>o/w:</i>				
Agri-food	7.6	8.7	9.1	0.4
Consumer goods	-8.5	-8.2	-9.5	-1.3
Automotive products	8.8	5.7	1.0	-4.7
Capital goods	2.0	5.7	3.5	-2.2
Intermediate goods	-7.9	-7.4	-11.8	-4.4
Energy products	-38.3	-46.5	-45.1	1.4

NB: The balance is expressed in fob-fob data, i.e. without transport and insurance costs for imports. The sectoral balances are expressed in cif-fob terms (transport and insurance costs included).  
Source: Customs and Excise Department (DGDDI).

**Chart 10 External trade in motor vehicles**

(EUR billions)



Source: Ministry of the Economy, Industry and Employment, DGDDI.

Box 5

### Current account transactions in France's balance of payments

France's current account recorded a deficit for the third consecutive year; it stood at EUR 24.4 billion in 2007, compared with EUR 22.5 billion in 2006.<sup>1</sup> This deterioration was largely due to the EUR 8 billion increase in the goods deficit. The current account deficit was stable at 1.3% of GDP, like in 2006.

The services surplus also declined (by EUR 1 billion): the transport deficit narrowed by a little over EUR 1.5 billion, while the travel surplus stabilised and the deficit of services excluding travel and transport worsened by almost EUR 3 billion. International merchanting and miscellaneous business services (including research and development spending) were the main contributors to this deterioration. Over the 2003-2007 period, these two items were accountable for most of the reduction in the surplus of the services sector as a whole. Within miscellaneous business services, the items studies, research and management fees recorded the sharpest falls.

Conversely, the income account surplus improved very significantly, by almost EUR 7.5 billion. The increase in the direct investment income surplus and the decline in the portfolio investment income deficit more than offset the decrease in other investment income (bank interest on loans and borrowings).

The deficit in current transfers remained broadly stable at EUR -22.0 billion.

Table 5 International trade in services balance

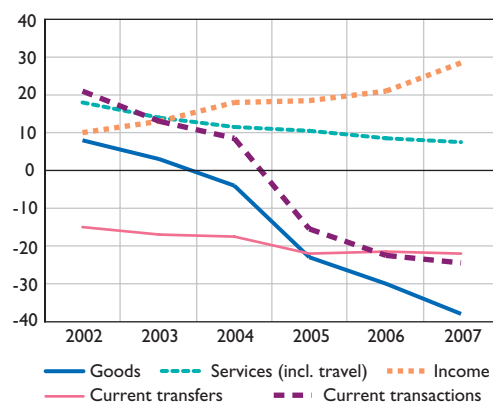
(EUR billions)

	2003	2004	2005	2006	2007
<b>Total services</b>	<b>14.0</b>	<b>11.7</b>	<b>10.6</b>	<b>8.3</b>	<b>7.3</b>
o/w:					
Transport	0.2	-3.0	-3.4	-2.6	-0.9
Travel	11.6	13.2	10.8	12.1	12.0
Communication services	0.4	0.9	1.1	1.3	1.0
Construction services	1.3	1.2	1.6	1.9	2.4
Insurance services	-0.2	-0.4	-0.9	-1.2	-0.8
Financial services	-0.8	-0.8	-0.8	-1.9	-1.4
Royalties and licence fees	1.4	1.7	2.5	2.3	3.1
Merchanting	2.6	1.8	3.2	2.6	0.3
Rentals	-0.2	-0.2	-0.2	-0.7	-1.1
Miscellaneous business services	0.8	0.4	-0.5	-2.1	-3.4

Source: Banque de France – Balance of Payments Directorate.

Chart 11 Current account

(unadjusted data, EUR billions)



Source: Banque de France – Balance of Payments Directorate.

<sup>1</sup> Unlike the statistics published by the DGDDI, where the trade surplus for 2006 was revised, data on foreign trade in goods are based, for 2006, on customs data incorporated in the balance of payments statistics at the time of publication, in July 2007, of the 2006 Annual Report on France's balance of payments. They will be revised, as well as those of all the items of the balance of payments (for 2005 to 2007), in June 2008 when the 2007 Annual Report on France's Balance of Payments is published.

In this less favourable international environment, export growth slowed from 8.1% to 6.0%, but at the same time, the contraction in domestic demand resulted in lower import growth (5.2%, compared with 7.8%), with a overall increase (from 0.2 to 0.4 percentage point) in the contribution of foreign trade to euro area GDP between 2006 and 2007. Like the previous year, this contribution was positive

thanks to the performance of Germany's external sector: net export growth in Germany accounted for more than half of the country's GDP growth in 2007, with a 1.6 percentage point contribution for a growth rate of 2.6%. Despite the ongoing rise in commodity prices in 2007, the euro area posted a foreign trade surplus of EUR 28.5 billion, compared with a deficit of EUR 8.4 billion

**Table 6 Growth in France and the euro area**  
Contributions to GDP growth

(%)

Annual average unless specified otherwise	Euro area			France		
	2005	2006	2007	2005	2006	2007
GDP						
Average annual growth rate	1.7	2.9	2.6	1.9	2.4	2.1
Year-on-year Q4/Q4	2.0	3.2	2.2	1.7	2.2	2.2
Net exports	-0.3	0.2	0.4	-0.6	-0.3	-0.8
Changes in inventories	0.1	0.1	0.0	0.0	-0.1	0.2
Domestic demand, excl. inventories	1.9	2.6	2.2	2.6	2.8	2.7
o/w : private consumption	0.9	1.1	0.8	1.4	1.4	1.4
public consumption	0.3	0.4	0.4	0.3	0.3	0.3
real gross fixed investment	0.7	1.1	0.9	0.9	1.0	1.0

Sources: Eurostat, INSEE.

in 2006. Excluding energy, the trade surplus reached EUR 258.2 billion in 2007, compared with EUR 236.0 billion in 2006.

While the GDP of the four largest euro area economies slowed down in 2007, there were specific reasons for each country that at least partly explain this common movement.

France posted GDP growth of 2.1% in 2007, after 2.4% in 2006. This slowdown is attributable to the lower the contribution of trade to GDP (-0.8 percentage point, compared with -0.3% in 2006), which was only partially offset by the higher contribution of inventory changes (0.2 percentage point, compared with -0.1 percentage point). Household consumption remained a key driver for growth. In 2007, it grew at the same pace as in the previous year (2.5%), as did government consumption (1.4%). Investment edged down from 5.0% to 4.9%. This almost stable figure nevertheless conceals divergent developments, i.e. a sharp decline in household investment (from 7.1% to 3.0%), and very strong corporate investment (7.3%, compared with 5.4% in 2006).

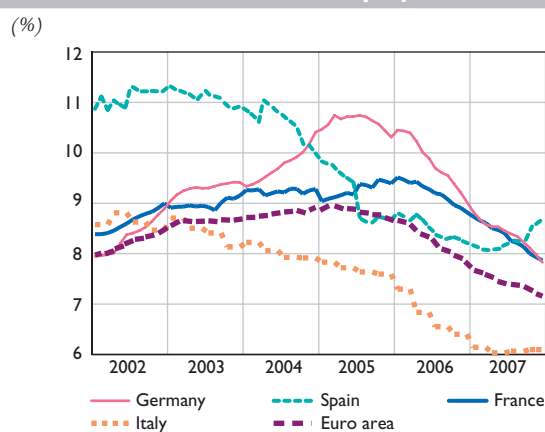
Furthermore, most of the growth differential between France and the euro area (-0.5 percentage point in 2007, like in 2006) can still be explained by the contribution of trade, which is negative for France and positive for the euro area.

Since the start of 2007, the performance of the French economy has nevertheless moved closer to those of other euro area countries. Indeed, it was mainly in the second half of 2006 that the French economy slowed

down relative to that of the other countries in the area: at the end of 2006, growth carried over for 2007 was only 0.6% in France, compared with 1.1% for the euro area as a whole. In 2007 alone, i.e. comparing GDP data adjusted for seasonal and working-day variations in Q4 2007 to those of Q4 2006, growth stood at 2.2% in France, like in the euro area as a whole, compared with 1.8% in Germany.

In Germany, GDP growth contracted from 3.1% in 2006 to 2.6% in 2007. As the three percentage point increase in the value-added tax in January 2007 was announced several months before its implementation, German households made, before the end of 2006, some of the purchases that they would have made in 2007. Furthermore, like in previous years, wage moderation dampened private consumption. Lastly, renewed inflation curtailed

**Chart 12 Harmonised unemployment rate**



Source: Eurostat.



household spending at the end of the year. All in all, household consumption declined by 0.5% in 2007, after a 1.2% increase in 2006. However, wage moderation also contained the cost of producing German products and therefore enhanced their competitiveness, thus contributing to the strong export performance. Overall, German economic growth was affected in 2006 by investments that were brought forward and would otherwise have been made the following year, due to the rescission in early 2007 of government measures to encourage construction investment.

In Italy, GDP growth slowed from 1.8% in 2006 to 1.5% in 2007 (unadjusted data). Household consumption strengthened by 1.4%, compared with 1.0% in 2006, and general government spending increased by 1.2%, against 0.8% the previous year. Between 2006 and 2007, investment nevertheless declined (1.2%, after 2.5%) as did exports (5.0%, after 6.2%) and imports (4.4%, after 5.9%). Besides these developments, the recent performance of Italy's economy gives cause for concern: GDP growth has stood at around 0.2% quarter-on-quarter since the start of 2007, which is far behind that of the euro area as a whole (0.5% on average over the four quarters of the year).

Lastly, in Spain, GDP growth eased very slightly (from 3.9% in 2006 to 3.8% in 2007), with the slowdown in domestic demand growth being almost offset by the stronger contribution of foreign trade, which nonetheless remained negative (-0.7 percentage point in 2007, after -1.2 percentage points in 2006). Economic activity therefore continued to be very buoyant in Spain in 2007, but the fall in construction investment in the second half of the year raises doubts as to the sustainability of this situation, since this sector has been one of the main drivers of growth in recent years.

In the euro area as a whole, the positive impact of the ongoing relatively sustained growth in 2007 translated into a further decline in the Eurostat harmonised unemployment rate. The latter stood at 7.2% of the labour force in December 2007, compared with 7.8% in December 2006 (in seasonally adjusted terms). In all euro area countries except Ireland and Spain the unemployment rate fell. Between December 2006 and December 2007, it declined from 8.8% to 7.9% in France and from 9.0% to 7.8% in Germany.

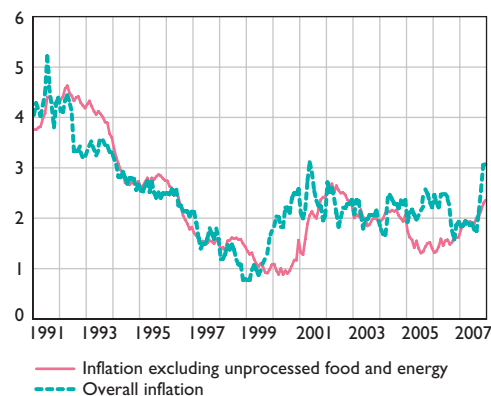
## 2|2|2 Inflation

Since 2000, annual average inflation in the euro area, as measured by the Harmonised Index of Consumer Prices (HICP), has fluctuated between 2.1% and 2.3%. In 2007, it remained within this range: the annual average increase in the HICP stood at 2.1%, a fall of 0.1 percentage point compared with 2006. However, this average is the result of very contrasting developments: although the increase in VAT in Germany that came into effect on 1 January 2007 had an impact estimated at 0.3 percentage point on overall inflation in the euro area, the latter remained stable and below 2% until August 2007. It subsequently posted a significant rise, climbing to 3.1% in December 2007. Underlying inflation (excluding energy and unprocessed food) and non-energy inflation displayed the same pattern with, however, a more moderate increase from August 2007 onwards: both rose from 2% in August 2007 to 2.4% in December 2007. Nonetheless, unlike overall inflation, the annual averages of non-energy and core inflation in 2007 – at 2.1% and 2% respectively – were well above the 2006 rates of 1.6% and 1.5%.

Energy and processed food prices made the greatest contributions to developments in overall inflation, with the increase in the other indices remaining relatively stable over the year as a whole. Thus, while the year-on-year increase in energy prices amounted

**Chart 13 Measures of euro area inflation**

(year-on-year % increase)



Source: Eurostat.



Box 6

**Resurgence of inflationary pressures in France and the euro area**

Since September 2007, France and the euro area have seen a sustained increase in overall inflation. It rose from 1.3% in August 2007 to 2.8% in December 2007 in France, and by 1.7% in August 2007 to 3.1% in December 2007 in the euro area. Three factors help us to understand this higher inflation.

First, the rise in commodity and Brent crude prices has affected food and energy prices. Admittedly, this increase is partly due to temporary factors such as climatic and geopolitical shocks, but it is also attributable to more structural developments. While the expansion in trade with low-cost countries from the mid-1980s onwards fostered disinflation in industrialised countries, the surge in the former's demand for commodities, by weighing strongly on global commodity prices, has slowed, if not halted, this process.

Second, indicators of pressure on the goods market, both in France and the euro area, have risen and are now close to levels seen during the last growth peak. The situation regarding the labour market is more mixed: pressures have increased in the euro area but remain moderate in France, in spite of a falling unemployment rate. These tighter labour market conditions highlight the presence of a risk of wage inflation.

Third, it appears that there is a waning of domestic factors that hitherto made it possible to absorb shocks. In Germany, wages have climbed at a very moderate pace and unit labour costs have hardly risen during the last ten years. We are, however, currently seeing a trend towards faster increases in wages and unit labour costs. Moreover, thanks to a highly competitive environment, the retail sector kept prices very low; however, given that profit margins have been very small, they have not been able to absorb the food commodities price shock.

In France, from 2004 the reform of the Galland Act helped to exert downward pressure on processed food prices. However, their recent increase suggests that the reform is no longer encouraging retailers to reduce their trade margins. It therefore appears necessary to put a new regulatory environment in place that effectively encourages competition. The first step has been taken with the adoption of the Chatel Act in early 2008 but further measures are needed. As regards wages, their dynamic growth in the past did not allow industrial firms to increase their margins. This is currently making it difficult for them to absorb import prices, as is shown by the recent rise in prices of industrial goods.

These prospects point to the resurgence of inflationary pressures and call for vigilance on the part of central banks.

NB: Based on the editorial in the Bulletin de la Banque de France of October 2007.

to 0.8% on average during the first three quarters of 2007, it then rose to 8.1% in the fourth quarter. This development, which reflected movements in the euro-denominated price of oil, was due to the combination of two effects. First, the price of Brent in euro rose significantly in the winter of 2007. Second, the previous profile of oil prices, which included hikes up to July 2006 followed by a fall until November 2007, produced a base effect that first limited the year-on-year increase and then amplified its magnitude. As regards processed food prices, the rise in world food prices was primarily observed from the third quarter of 2007 onwards: the year-on-year increase in processed food prices thus reached 4.5% in the fourth quarter

of 2007, a level comparable to that seen in 1992. The year-on-year increase in unprocessed food prices was also indirectly affected by this global food price shock via the price of meat, which is sensitive to cereal and soya prices. In addition, adverse weather conditions had an upward effect on unprocessed food prices throughout the year, so that their annual average growth stood at 3%.

The inflation rates of industrial goods and services appeared relatively contained against a backdrop of rises in indicators of inflationary pressures. Annual average growth in industrial goods prices thus stood at 1% in spite of the increase in producer prices, fuelled

by industrial commodity and energy prices. Services price inflation was higher, amounting to an annual average of 2.5%

The increase in pressures on the labour market occurred in a context of moderate labour costs. The unemployment rate continued to fall from its previous peak in March 2005, dropping from 9.0% to 7.8% in December 2006, then to 7.1% in December 2007. However, growth in unit labour costs remained moderate (stable at around 1.1% year-on-year in the first three quarters of 2007) as the slight acceleration in per capita wages (around 2% year-on-year in the first three quarters) was partly offset by that in productivity (0.9% on average in the first three quarters of 2007). On the goods and services markets, at year-end the capacity utilisation rate reached a level close to that recorded during the previous business cycle peak in 2000 but growth in profit margins slackened.

The euro's appreciation helped to cushion the impact of the commodity price shocks but did not absorb them completely.

## 2|2|3 Public finances<sup>4</sup>

According to the data reported by the different countries to Eurostat, in 2007 the general government deficit of the euro area narrowed for the fourth consecutive year, to 0.6% of GDP, after 1.3% in 2006; this was its lowest level since 2000. This overall improvement masks divergent developments across countries. Deficits were reduced sharply in Germany, which returned to a balanced fiscal position, and in Italy and Portugal, which came back below the reference value of 3% of GDP; this should allow the excessive deficit procedure for these two countries to be abrogated. By contrast, several member countries recorded merely the stabilisation of their deficit or a reduction in their surplus.

The fiscal improvement recorded in the euro area as a whole was primarily due to the fall in the public expenditure-to-GDP ratio to 46.2% from 46.8% in 2006, as a result of lower unemployment spending and wage moderation in the public sector.

### Box 7

#### **The state of public finances in France in 2007**

*In spite of economic growth close to potential, the reported general government deficit widened in 2007 for the first time since 2003, reaching 2.7% of GDP, after 2.4% in 2006. There was a decline in tax and social security contributions due to cuts in direct taxes paid by households (reform of income tax in the Budget Act for 2006 in particular). These tax cuts were only partly offset by exceptional revenue stemming from strong company profits in 2006. Tax and social security contributions thus amounted to 43.3% of GDP, after 43.9% in 2006. The public expenditure-to-GDP ratio ebbed by 0.3% compared to 2006, to 52.4%. This fall was mainly due to continued rigour in government policy regarding the Budget. By contrast, social benefits and investment expenditure by local government remained very high and interest payments increased as a result of a sharp rise in the average interest rate applied to government debt. Overall, structural efforts to consolidate public finances were limited last year. With the general government balance moving away from the position required to stabilise public debt, the public debt-to-GDP ratio rose to 63.9% in 2007, after 63.6% in 2006.*

*The 2007 fiscal year was marked by the adoption on 22 August of the TEPA Act ("Travail, Emploi et Pouvoir d'Achat") concerning work, employment and purchasing power, which includes several measures aimed at cutting tax and social security contributions, primarily for the benefit of households:*

- exemption of all social security contributions and income tax on overtime;
- tax credit on interest on loans for purchase of one's principal residence;
- reductions in inheritance tax.

*According to official sources, all of these measures will cost around EUR 9 billion in 2008 and EUR 13 billion when they come into full effect. The TEPA Act is expected to lead to a slight drop in tax and social security contributions in 2008.*

<sup>4</sup> On the basis of statistics available at 15 May 2008.

On the revenue side, discretionary cuts in income tax and social security contributions were offset by very strong receipts from corporate income tax and tax levied on financial assets and real estate, which contributed to the stabilising of the revenue-to-GDP ratio at 45.6%.

The euro area's public debt profile is directly determined by that of government deficits.<sup>5</sup> The public debt-to-GDP ratio declined by 2.2 percentage points in 2007 to reach 66.3%, the lowest level since the start of EMU. All countries reduced their debt ratio, even if eight countries continued to have debt ratios above 60% of GDP in 2007 (Belgium, Cyprus, France, Germany, Greece, Italy, Malta and Portugal).

Of all the member countries, only Finland and Spain recorded both an increase in their fiscal surplus and a debt-to-GDP ratio of below 60%.

## 2|3 Monetary analysis

In the euro area, the annual growth rate of M3 increased again in 2007, reaching a historic high since the creation of the euro of 12.3% at end-November before falling back to 11.5% at end-December. Mainly fuelled by growth in loans to the private sector, this acceleration of the broad monetary aggregate was fostered by the gradual flattening of the yield curve as well as by the context of tensions on financial markets that prevailed in the second half of the year and strengthened the attractiveness of liquid investments:

- Within the components of M3, growth in the narrow aggregate M1 continued to slow as a result of higher short-term interest rates and the consequent increase in the opportunity cost of money holdings paying little or no interest.

**Table 7 Monetary developments in the euro area and France**

(outstanding amounts in EUR billions, year-on-year % changes)

	Euro area monetary aggregates (a)				Main monetary assets in France (b)			
	Amount outstanding at 31 Dec. 2007	Growth rate (c)			Amount outstanding at 31 Dec. 2007	Growth rate (c)		
		2005	2006	2007		2005	2006	2007
Currency in circulation	627.0	13.8	11.0	8.2				
+ Overnight deposits	3,199.5	10.9	6.8	3.2	494.8	10.9	5.7	4.8
<b>= M1</b>	<b>3,826.5</b>	<b>11.3</b>	<b>7.5</b>	<b>4.0</b>				
+ Other monetary deposits	3,505.3	5.4	11.7	17.7	565.5	5.3	8.0	17.7
o/w: Deposits redeemable at notice up to 3 months	1,534.5	4.4	0.6	- 3.6	437.8	4.0	6.2	5.1
Deposits with agreed maturity up to 2 years	1,970.8	6.5	27.2	41.4	127.8	16.1	21.3	100.2
<b>= M2</b>	<b>7,331.8</b>	<b>8.5</b>	<b>9.3</b>	<b>10.1</b>				
+ Marketable instruments	1,310.4	0.9	13.2	20.0	508.5	6.8	10.7	16.2
o/w: Money market fund shares/units	680.4	- 0.3	4.7	9.2	325.3	6.4	5.8	1.3
Debt securities up to 2 years	317.3	15.7	54.5	60.2	143.1	28.7	41.8	75.2
<b>= M3</b>	<b>8,642.2</b>	<b>7.3</b>	<b>9.9</b>	<b>11.5</b>				
France's contribution to M3					1,652.9	8.2	10.6	15.9
<b>Loans to the private sector (unadjusted data)</b>	<b>10,145.7</b>	<b>9.2</b>	<b>10.8</b>	<b>11.1</b>	<b>1,812.0</b>	<b>9.3</b>	<b>12.7</b>	<b>14.7</b>
o/w: Loans to NFCs	4,383.2	8.3	13.1	14.4	763.8	8.0	10.9	14.7
Consumer loans	617.6	7.9	7.7	5.3	156.3	5.8	4.8	5.1
Housing loans to households	3,436.7	11.5	9.6	7.1	642.2	14.4	15.2	12.8

(a) Transactions of euro area monetary financial institutions (MFIs) with other euro area residents.

(b) Transactions of French MFIs with other French residents.

(c) Data adjusted for reclassifications and valuation effects.

Sources: ECB, Banque de France.

<sup>5</sup> In principle, stock-flow adjustments can also affect public debt. These adjustments correspond to the difference between the change in public debt and the general government deficit/surplus during a given year. In 2007, at the level of the euro area, stock-flow adjustments played a marginal role in the change in debt.



**Feeding banknotes into the sorting machine**



Box 8

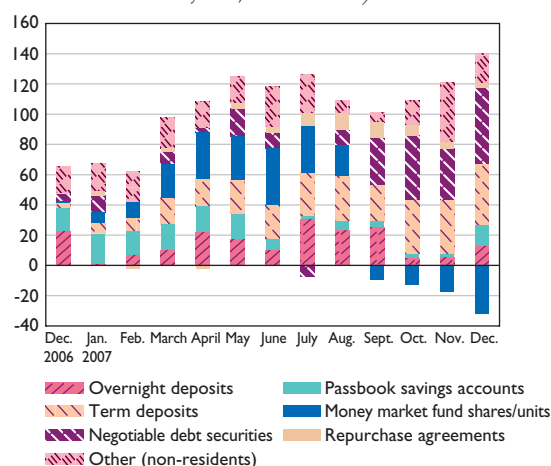
### Impact of the financial crisis on monetary developments in France

Although the financial tensions that emerged in the summer did not significantly affect the overall dynamics of France's contribution to M3 in 2007, they had a strong impact on developments in investment in money market fund shares/units by the money-holding sector in the euro area, especially in France.

Against the backdrop of the aforementioned flattening of the yield curve, growth in investment in money market fund shares/units strengthened markedly in the first half of 2007 to reach an annual rate of 11.8% at end-June 2007. By contrast, in the second half of the year it slowed significantly to the extent that the annual growth rate at year-end stood at 1.3%. In response to the rise in tensions on financial markets, from the middle of the summer resident agents shifted their investments away from money market fund shares/units and into deposits with agreed maturity up to two years and certificates of deposit, the remuneration on which increased significantly in line with interbank rates. Non-financial corporations and insurance companies were primarily involved in this shift, while households hardly participated in it. Motivated to a certain extent by arbitrage considerations, it was also fuelled by uncertainties surrounding the valuation of money market fund portfolios and their degree of exposure to securitisation instruments and other structured products that suddenly became illiquid in the wake of the US subprime crisis. Holdings of money market fund shares/units struggled to recover: after a modest upturn in net subscriptions in October and November, substantial outflows were recorded again in December, in proportions that were well in excess of the usual year-end movement.

Chart 14 Components of France's contribution to M3

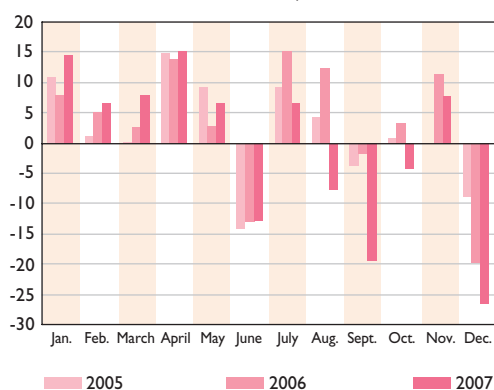
(six-month cumulated flows, EUR billions)



Source: Banque de France – Monetary Analysis and Statistics Directorate.

Chart 15 Holdings of money market fund shares/units

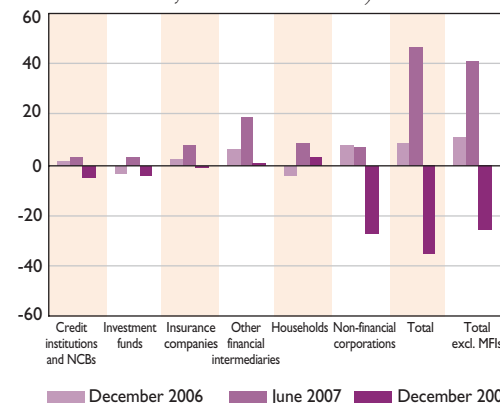
(gross monthly flows, in EUR billions)



Source: Banque de France – Monetary Analysis and Statistics Directorate.

Chart 16 Holdings of money market fund shares/units by sector

(six-month cumulated flows in EUR billions)



Source: Banque de France – Monetary Analysis and Statistics Directorate.

- At the same time, there was a strong surge in other short-term deposits (M2-M1) and marketable instruments (M3-M2) in response to the flattening of the yield curve: economic agents have made portfolio shifts to monetary assets, which are more liquid and less risky than non-monetary assets and provide practically equivalent returns.

- Lastly, the financial market turmoil in the second half of 2007 also prompted some money-holding sectors to make substitutions between different categories of monetary investments (see Box 8 “Impact of the financial crisis on monetary developments in France”). Among the marketable instruments that make up M3-M2, money market fund shares/units, which recorded large-scale outflows, lost ground to negotiable debt securities issued by credit institutions and short-term deposits with agreed maturity of up to two years, two types of investment whose growth, already sustained at the start of the year, went on to become even stronger.

Turning to the counterparts of M3, growth in loans to the resident private sector in the euro area was slightly up from one year-end to the next as a result of the faster growth in loans to non-financial corporations that was observed from the second quarter of 2007. By contrast, continuing the trend under way since the start of 2006, there was a further gradual slowdown in loans to households.

In 2007, the impact of the external counterpart on monetary developments was both significant and variable. Up strongly from end-2006, the contribution of banks' net external assets to annual growth in the broad monetary aggregate reached 4.7 percentage points at end-March 2007, an unprecedented level since the creation of the euro. However, from the second quarter, this contribution declined steadily to become almost zero at the end of the year. These developments were primarily attributable to non-residents' portfolio investment in securities issued in the euro area: having expanded strongly between mid-2006 and the first quarter of 2007, this type of investment has since registered a steady decline.<sup>6</sup>

## **2 | 4 Financing conditions in France and the euro area**

### **2 | 4 | 1 Market rates**

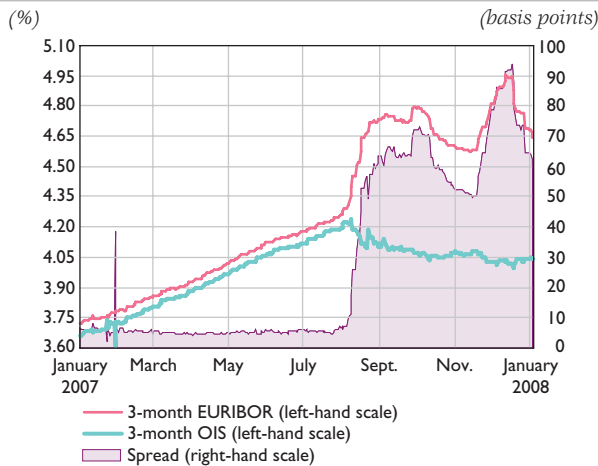
There was growing pressure on money market spot rates in 2007. They rose up to the summer as a result of the tightening of monetary policy by the ECB: two successive increases in the minimum bid rate applied to the ECB's main refinancing operations brought it to 4.00% in early June. From the summer onwards, the drying-up of the interbank market, particularly as a consequence of growing wariness between credit institutions, fuelled the rise in uncollateralised money market rates up to the end of the period under review. As a result, the three-month EURIBOR increased throughout the year, rising by 96 basis points to stand at 4.68% at year-end, compared with 3.72% at the start of the year and 4.26% on 1 August 2007.

By contrast, there were uneven developments in money market rates derived from swaps. They increased in the first part of the year as a result of the monetary policy tightening by the ECB and expectations of further interest rate hikes. From early August, owing to fears about the stability of the financial system, EONIA swap rates fell slightly. The spread between the three-month spot rate and the EONIA swap rate with the same maturity – an indicator of the credit risk premium – rose from 5 basis points prior to August 2007 to a high of 93 basis points in December 2007.

In 2007, non-financial corporations' access to financing on the short-term market was to some extent affected by the crisis. In France, the negotiable debt securities market provides around 80 large companies with short-term financing. In 2007, there was a significant fall in commercial paper outstandings. Although they had risen from EUR 56 billion at the start of the year to EUR 66 billion at mid-June, there was a marked decline in outstandings during the summer,

6 See “L'influence des non-résidents sur la création monétaire dans la zone euro” (in French only), Bulletin de la Banque de France, No. 168, December 2007.

**Chart 17 Spread between the 3-month EURIBOR and the 3-month OIS**



Source: Banque de France – Market Operations Directorate.

which fell to EUR 49.8 billion in early September. They subsequently remained within a range of EUR 50-53 billion. In parallel, an increase in rates was observed from June onwards. Whereas the 1-month rate stood at around 4% at the start of the year, it gradually rose to 4.3% in June and new levels were reached in mid-August (4.57%) and December (4.79%) in particular. The rise in the 1-month rate was accompanied by the widening of its spread with the EONIA: having fluctuated between 0 basis point and 9 basis points before August, the spread then moved between 10 basis points and 33 basis points, before climbing to 64 basis points in December.

Yields on bond markets also posted divergent developments. They rose until July only to shed a large part of their gains subsequently. Nonetheless, over the year as a whole, yields were up, with the yield on 10-year French government bonds increasing by 44 basis points to 4.42% and the 2-year yield rising by 19bp to 4.10%. This steepening of the bond yield curve in the euro area may be accounted for by the relative optimism up to the end of the period under review of market participants regarding the outlook for growth in the euro area. This is demonstrated by the increase in yields on index-linked bonds with the same maturity.

## 2/4/2 Bank lending rates

In 2007, lending rates in France and the euro area continued to rise, an uptrend that had started at the

end of 2005 for all types of lending, although rates on short term and/or floating rate loans (with an initial rate fixation period of up to one year) tended to stabilise in the last quarter. The rates on loans granted by French credit institutions to resident households and non-financial corporations nevertheless remained lower than the average corresponding rates in the euro area as a whole.

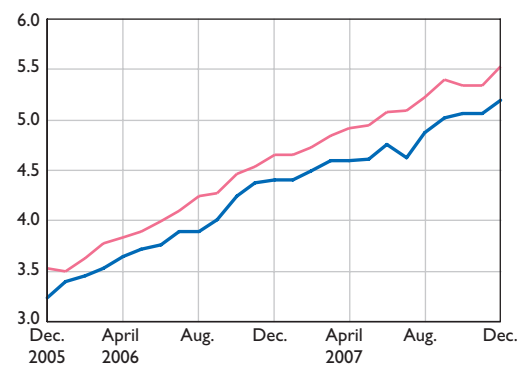
Rates on new loans to non-financial corporations posted the greatest increases, rising by just over 75 basis points in France for loans of up to EUR 1 million and for loans above that amount. These hikes were however smaller than in the euro area, where they totalled 95 basis points and 86 basis points respectively.

Lending rates on new loans to households also increased significantly: in France, they rose by

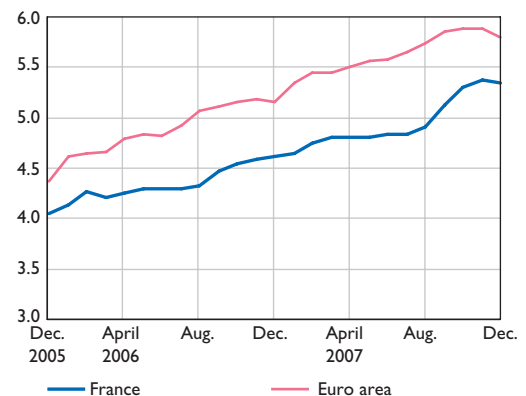
**Charts 18a and 18b New loans (excluding overdrafts) – euro area and France**

(average rate as a %)

### To non-financial corporations



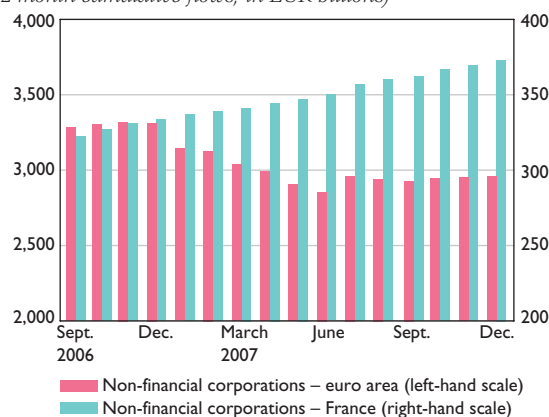
### To households



Sources: ECB, Banque de France.

**Chart 19 New loans to non-financial corporations – euro area and France**

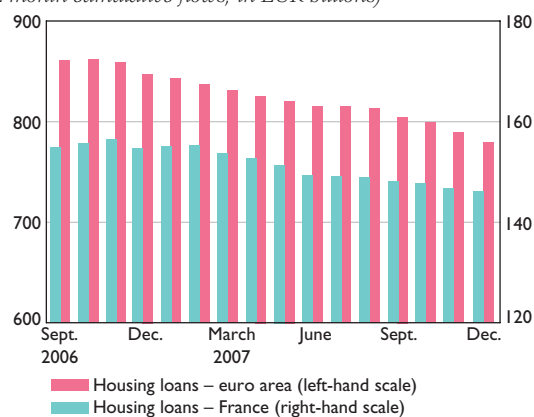
(12-month cumulative flows, in EUR billions)



Sources: ECB, Banque de France.

**Chart 21 New housing loans**

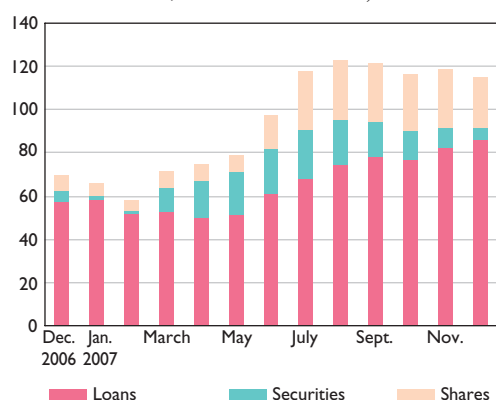
(12-month cumulative flows, in EUR billions)



Sources: ECB, Banque de France.

**Chart 20 Financing of non-financial corporations – France**

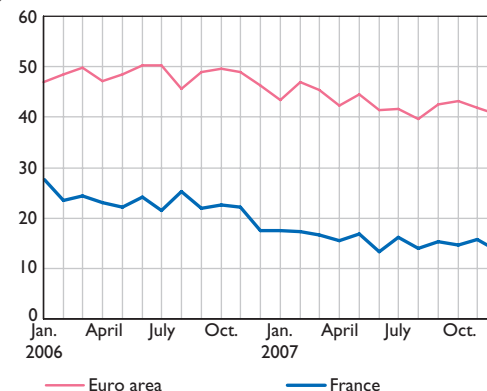
(12-month cumulative flows, in EUR billions)



Source: Banque de France.

**Chart 22 Share of floating rate loans in monthly flows of new housing loans**

(%)



Sources: ECB, Banque de France.

around 65 basis points in the case of consumer loans, 70 basis points for fixed-rate housing loans (initial rate fixation period of over 10 years) and 83 basis points for floating rate loans (initial rate fixation period of up to one year). These increases were slightly greater than those recorded in the euro area as a whole for housing loans (66 basis points and 75 basis points for fixed-rate and floating rate loans respectively).

While loans to non-financial corporations in the euro area were not dampened by the further rises in lending rates and were even up slightly in the second half of the year, more mixed developments were recorded in France. Demand for loans from resident non-financial corporations gradually waned in the first half of the year, mainly on account of

the tendency of large companies to favour market financing as long as the environment was conducive to it. Subsequently, against the backdrop of persistent tensions on financial markets, demand for loans steadily increased as a result of the progressive re-intermediation of financing that until year-end went hand in hand with a sharp slowdown in the issuance of debt securities by non-financial corporations.

Loans to resident households posted a significant fall in 2007. The resulting slower growth in loan outstandings was less marked with respect to consumer credit, which remained fairly buoyant, than to housing loans, the slowdown in which continued throughout the year, mainly as a result of the tightening of credit standards (see Box 9 "Banks' responses to the financial

**Box 9**

### **Banks' responses to the financial crisis according to the Bank Lending Survey**

The financial crisis that emerged from summer 2007 onwards spilled over into credit and financial markets, leading to a revaluation of credit risk, difficulties for banks in accessing liquidity and a virtual halt in loan securitisation transactions.

The Bank Lending Survey provides qualitative data that make it possible to gauge more accurately the impact of the crisis on credit institutions' lending policies. As part of this qualitative survey conducted on a quarterly basis by each of the national central banks of the Eurosystem, the Banque de France questions a representative sample of resident credit institutions. The questionnaire mainly concerns past and expected developments in the supply of and demand for loans with respect to enterprises and households. From the second half of 2007 onwards, specific questions were added relating to the impact of the financial crisis on banks and their lending policies.

#### **The tightening of credit standards for loans to enterprises in the second half of 2007 did not lead to a reduction in the volume of lending extended**

Against the backdrop of further growth in demand for loans from enterprises, the tightening of bank lending conditions led above all to an increase in the cost of credit for both risky and average loans.

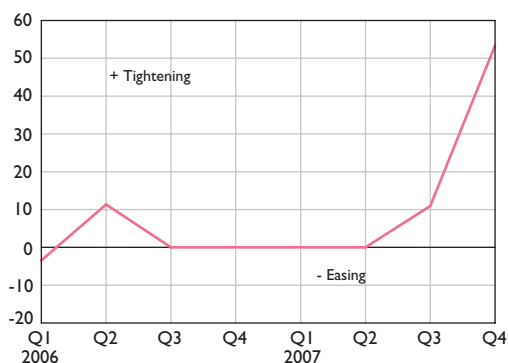
According to the banks surveyed, the increase in their refinancing costs brought about by the crisis also accentuated the trend towards the tightening of credit standards for loans<sup>1</sup> (see Charts 23a and 23b).

This tightening particularly concerned large enterprises, as illustrated by the relatively high proportion of banks reporting the restrictive effects of the crisis on the financing of M&A activity and corporate restructuring. On the other hand, the financing of inventories and working capital was less affected, while the financing of investments did not appear to have been impacted. Overall, SMEs, which had not benefited from as favourable conditions as large enterprises, were hardly affected (cf. Charts 24a and 24b).

**Charts 23a and 23b**

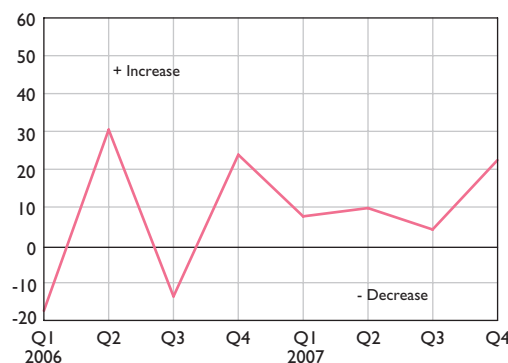
#### **Change in credit standards for loans to non-financial corporations**

(weighted balance of replies as a %)



#### **Change in demand for loans from non-financial corporations**

(weighted balance of replies as a %)



Source: Banque de France – Monetary Analysis and Statistics Directorate (Bank Lending Survey for France).

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<sup>1</sup> The credit standards for loans about which banks are questioned in the Survey are the internal guidelines or criteria that govern a bank's lending decisions.



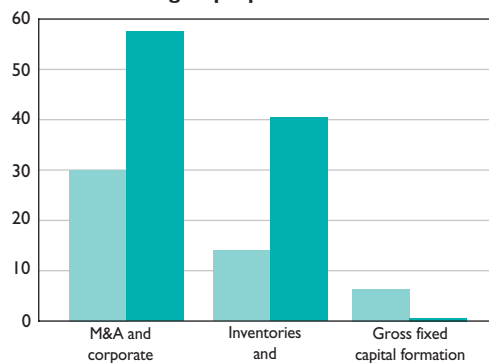
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### Charts 24a and 24b

#### Proportion of banks reporting a dampening impact of the financial crisis on their supply of loans to enterprises

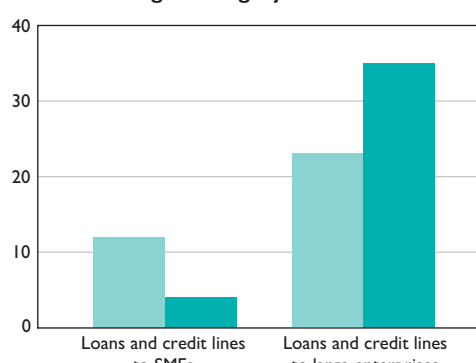
(weighted % of replies)

##### Breakdown according to purpose of loan



Survey conducted in the third quarter of 2007

##### Breakdown according to category of borrower



Survey conducted in the fourth quarter of 2007

Source: Banque de France – Monetary Analysis and Statistics Directorate (Bank Lending Survey for France).

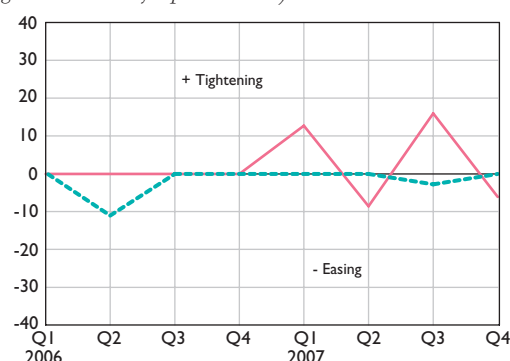
### Up to end-2007, the financial crisis did not appear to have a significant impact on the supply of loans to households

Regarding housing loans, against the backdrop of a fall in demand from the second half of 2006 onwards, credit standards were slightly tightened following the onset of the crisis but have scarcely been changed since (see Charts 25a and 25b). The proportion of banks reporting a dampening impact of the crisis on their supply of loans remained relatively small (see Chart 26). At the end of the year, lending conditions for new housing loans were however tightened, with banks aiming to rebuild their margins.

### Charts 25a and 25b

#### Change in credit standards for loans to households

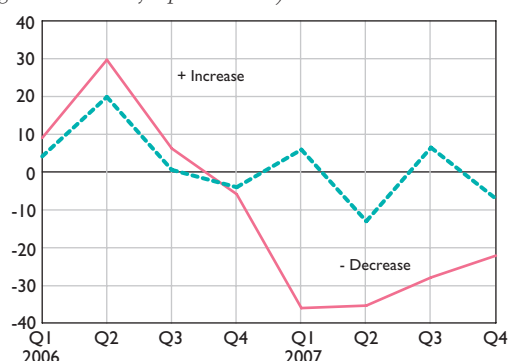
(weighted balance of replies as a %)



Housing loans

#### Change in demand for loans from households

(weighted balance of replies as a %)



Consumer credit

Source: Banque de France – Monetary Analysis and Statistics Directorate (Bank Lending Survey for France).

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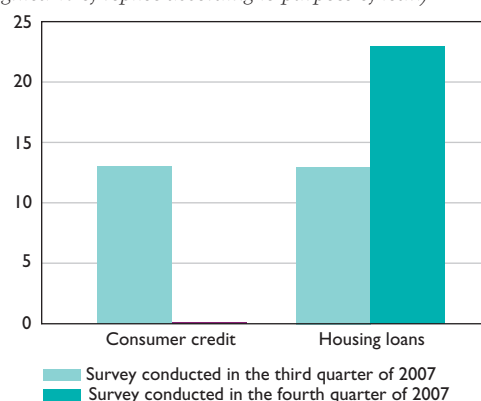
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As regards consumer credit, banks did not alter their lending policies amid relatively stable demand, with most banks considering that the crisis had had no effect on this type of lending.

NB: In the euro area, the other financial intermediaries sector is very heterogeneous. It is made up of four main sub-sectors: non-money market mutual funds, securitisation structures, securities and derivatives market participants and leasing and factoring companies.

**Chart 26 Proportion of banks reporting a dampening impact of the financial crisis on the supply of loans to households**

(weighted % of replies according to purpose of loan)



Source: Banque de France – Monetary Analysis and Statistics Directorate (Bank Lending Survey for France).

crisis according to the Bank Lending Survey"). Against this backdrop, the share of floating rate housing loans continued to wane, falling to around 13% in December, compared with 30% at end-2005. This development was also observed in the euro area as a whole, with this share dropping to just over 40% at the end of the year, compared with nearly 50% two years previously.

Following the introduction of the single list of collateral, French banks' participation in refinancing operations increased significantly, mainly with respect to three-month refinancing operations (accounting for 11.40% of the total allocation of this type of refinancing in 2007, compared with 1.39% in 2006). Overall, the average share of French banks in total euro area refinancing in 2007 came out at 6.7%, compared with 4.3% in 2006.

### 3| Implementation of monetary policy by the Banque de France

#### 3| I Refinancing of the banking system

##### 3| I | Trends from 2006 continuing into early 2007

Liquidity requirements continued to expand, mainly due to growth in currency in circulation (up by 7.6% on 2006). The first half of the year was also marked by the decision to increase the share of longer-term refinancing operations, the amount of which was raised to EUR 50 billion, and which thus represented 34% of total refinancing at 30 June 2007, compared with 25% one year earlier.

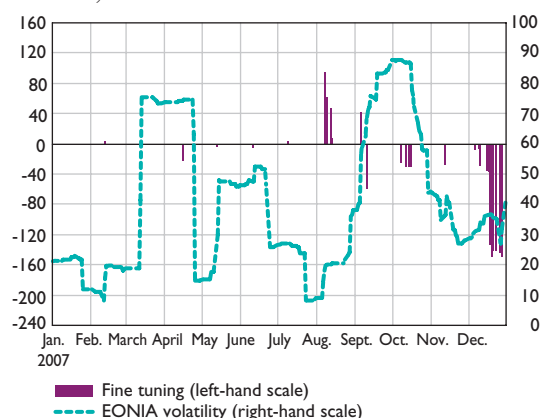
##### 3| I | 2 The second half of the year was marked by exceptional financing in response to the financial crisis

Strong tensions appeared on the markets from August onwards as a result of the US subprime crisis. A large number of exceptional refinancing operations were carried out within the framework of the Eurosystem. In this situation, the Banque de France showed that it could respond quickly and with great determination, particularly through its active participation in the decisions of the Eurosystem.

These numerous operations aimed to meet the banking system's requirements resulting from the low levels of liquidity on interbank transactions with agreed maturity (maturity greater than one month), strong tensions on money markets around the year-end and difficulties in obtaining refinancing denominated in US dollars.

**Chart 27 Fine-tuning operations**

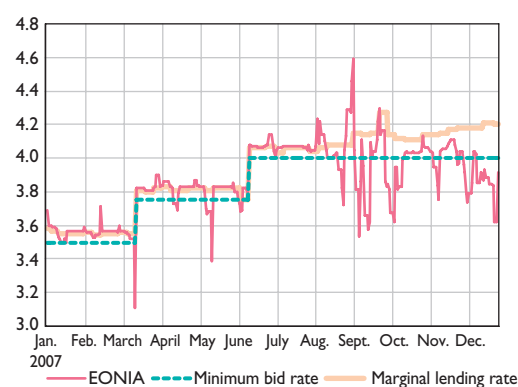
(EUR billions)



Source: ECB data.

**Chart 28 EONIA volatility, widening spread between marginal lending rate and minimum bid rate**

(%)



Source: ECB data.

They consisted of:

- a liquidity injection at a fixed rate;
- a large number of fine-tuning operations (24 compared with 11 in 2006) aimed at providing or removing extra liquidity when this proved necessary;
- expansive main refinancing operations, i.e. allotting more liquidity than was actually needed;
- supplementary three-month refinancing operations;

- an unprecedented refinancing operation in US dollars (USD 20 billion was provided in two operations) against collateral denominated in euro; this operation was carried out jointly with the Federal Reserve Bank of New York and the Swiss National Bank;
- an extension of the maturity (from one to two weeks) of the last main refinancing operation of the year.

The strong tensions observed from August 2007 onwards were reflected in increased volatility in the EONIA and the widening spread between the marginal

### Box 10

#### The adjustment of refinancing operations

From August onwards, due to the upward pressures on overnight interbank interest rates, the Eurosystem deemed it necessary to inject extra liquidity in order to steer market rates close to its key interest rate. This was done first of all via fixed-rate and variable rate fine-tuning operations, thus supplying additional liquidity for the day. The Eurosystem then rapidly implemented an ongoing increase in the amount of liquidity provided in its regular refinancing operations.

The combination of these actions enabled the Eurosystem to steer the overnight bank rate (EONIA) close to the policy rate set by the Governing Council. The excess liquidity created by these operations was adjusted over time in order to avoid a fall in money market rates below targeted levels.

In a second phase, in order to reduce the upward pressures that had appeared on the longer-term segments of the money market (interbank transactions with maturity over one month), the Eurosystem decided to increase the amount of its longer-term refinancing operations (LTROs) through two supplementary three-month LTROs.

The outstandings of LTROs therefore gradually increased, from one-third of total refinancing in March 2007 to 60% at year-end. This longer-term liquidity injection led to an automatic reduction in the amount of the Eurosystem's one-week MROs; this was to avoid excess market liquidity that would have led to a fall in interest rates below targeted levels.

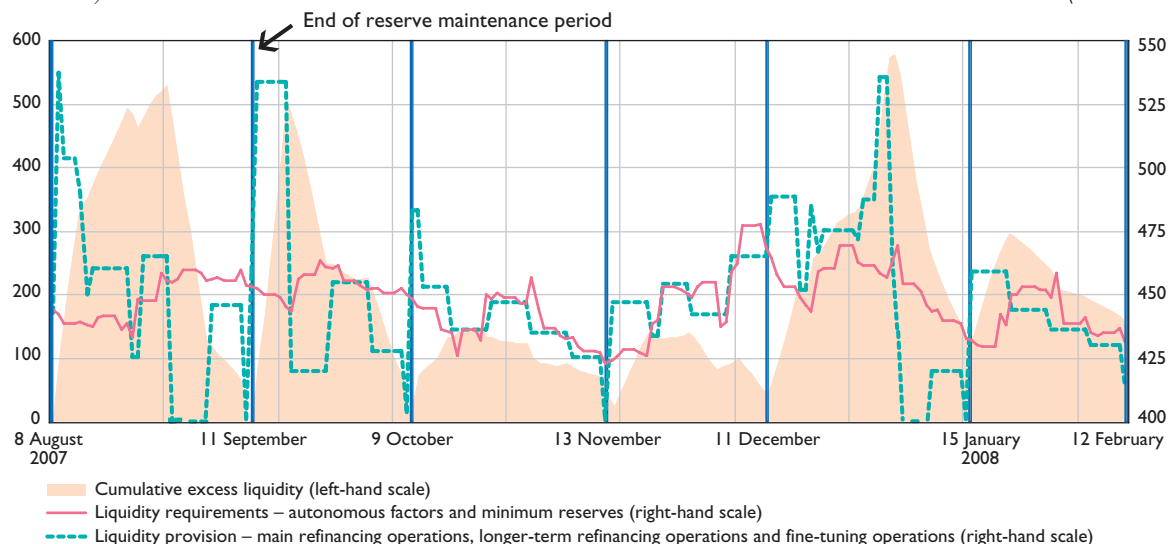
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Chart 29 Excess bank liquidity

(EUR billions)

(EUR billions)



Source: ECB data.

Lastly, to address the difficulties encountered by European banks in borrowing US dollar-denominated funds, the Eurosystem, in conjunction with the Federal Reserve Bank of New York, decided to provide its counterparties with US dollar funding with a maturity of one month.

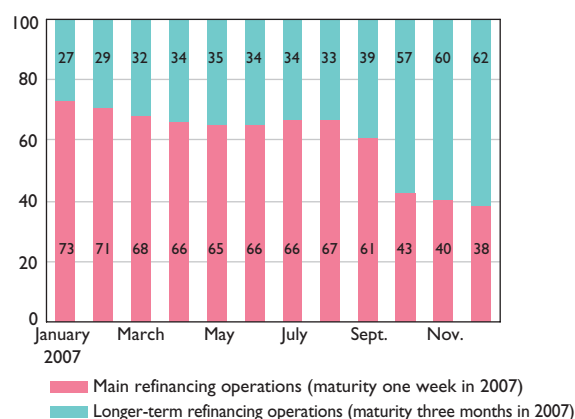
The difficulties encountered by euro area banks in borrowing US dollar funds are mainly attributable to:

- the crisis of confidence on the US interbank market caused by the subprime crisis, which made it increasingly difficult for European banks, which have a structural US dollar borrowing position, to find US counterparties willing to lend to them;
- the limited access of European banks to refinancing from the US central bank, which generally only deals with a small circle of counterparties (primary dealers), American for the most part, and the stigma attached to using its discount window.

The operations in connection with the US dollar Term Auction Facility were conducted in parallel with the refinancing operations in euro, but had no impact on the amounts involved in the latter.

Chart 30 Type of refinancing

(by reserve maintenance period, as a %)



Source: Banque de France – Market Operations Directorate.



lending rate and the minimum bid rate for refinancing operations.

### **3|1|3 Collateral used for central bank refinancing operations**

The amount of collateral used in France rose strongly (up by 69%), as a result of the increase in refinancing operations. Similarly, for intra-day operations, the outstandings of the collateral used grew by 23%. Overall, the amount of collateral put forward for monetary policy operations rose by 36.7% to EUR 79.5 billion on average, to reach EUR 125 billion at year-end.

The assets used as collateral in 2007 included in particular government bonds (24%), credit claims (50%) and asset-backed securities (7.8%).

Compared with 2006, the share of government bonds declined (by 28%) in favour of credit claims (up by 166%) and asset-backed securities (67%). Foreign securities (consisting primarily of government securities from other countries) accounted for 30% of the assets pledged by French banks, a sharp drop compared to 2006 (when they constituted 60% of the total) due to the growing use of credit claims.

The modified inclusion of credit claims as collateral for refinancing operations thus contributed significantly during the financial crisis to the provision of the liquidity required for the smooth functioning of the banking system and therefore, indirectly, to the financing of the economy.

## **3|2 Reserve requirements**

The number of credit institutions in France subject to minimum reserves fell by 2%, from 837 in December 2006 to 820 in December 2007, as a result of consolidation in the banking sector.

The average amount of required reserves to be held by French banks rose from EUR 31 billion in 2006 to EUR 35 billion in 2007 (daily average over the year); this represented an increase of 13%, compared with 14.8% in the euro area. In 2007, their average amount stood at EUR 186 billion, compared with EUR 162 billion in 2006. The share of French banks in total reserve requirements remained stable at 18.8%, after 19.2% in 2006.

The number of breaches remained very small: fourteen breaches were observed, triggering penalties of around EUR 85,000 (the same figure as in 2006).





**Inspection of mutilated banknotes**

# THE BANQUE DE FRANCE, A KEY PLAYER IN THE ECONOMY

The two major aspects of the Banque de France's role testify to its position in the financial and economic landscape:

- an active contribution to the decisions taken within the framework of numerous European and international bodies;
- a concrete contribution to the national economy via its core tasks: monetary stability, financial stability and other general interest tasks.

## I | An active contribution within the framework of European and international bodies

### I | I Relations with the Eurosystem and the ESCB

The Governor of the Banque de France is a member of the ECB's Governing Council, which is the Eurosystem's decision-making body, notably as regards defining monetary policy in the euro area. The Governing Council comprises the governors of the national central banks of countries that adopted the euro (15 since the entry of Malta and Cyprus on 1 January 2008), and the six members of the ECB Executive Board. In 2007, the Governing Council was notably consulted on the enlargement of the euro area, by adopting a convergence report on the States that do not belong to the Monetary Union.

The Banque de France helps to prepare the Eurosystem's monetary policy decisions by compiling data on the French economy and by carrying out economic analysis and research (see 2|1|1 "Statistics and research"). The Bank also contributes towards the preparation of the Governing Council's decisions in its various fields of competence by participating in the work of the ESCB committees: over 120 of the Bank's representatives sit on the committees and working groups on a regular basis together with the

representatives of the other central banks and of the ECB.

In February 2007, the Banque de France, in conjunction with the ECB, organised a seminar bringing together central bankers of the Eurosystem and western and central African countries. This meeting fostered a multilateral dialogue between governors concerning regional economic integration, the impact of changes in commodity prices on monetary and fiscal policies and central bank governance.

### I | 2 International and bilateral relations

The Banque de France is an active member of the major international fora (see Chart below). In this capacity, in 2007, the Bank took part in the major international discussions on economic and financial issues.

Together with the Ministry of the Economy, Finance and Employment, the Bank participated in preparing the International Monetary Fund (IMF) governance reform. Within the framework of the IMF's International Monetary and Financial Committee (IMFC) and Annual Meeting, the work of the Group of Seven (G7) and the Group of Twenty (G 20), the Banque de France presented their analysis on the reform of quotas and voting rights within the IMF, in order to improve the balance of the institution's governance in favour of the most dynamic emerging market economies, as well as the IMF's financing in a context marked by a significant reduction in revenues.

As regards developments in the IMF's activities, the Banque de France contributed actively to the group debate on the multilateral, regional and bilateral surveillance carried out by the IMF in economic policy and the strengthening of the IMF's role in the monitoring of developments in the financial markets.

The Banque de France is a member of the Board of Directors of the Bank for International Settlements and is one of the Group of Ten (G10) central banks.

## THE BANQUE DE FRANCE, A KEY PLAYER IN THE ECONOMY

*An active contribution within the framework of European and international bodies*

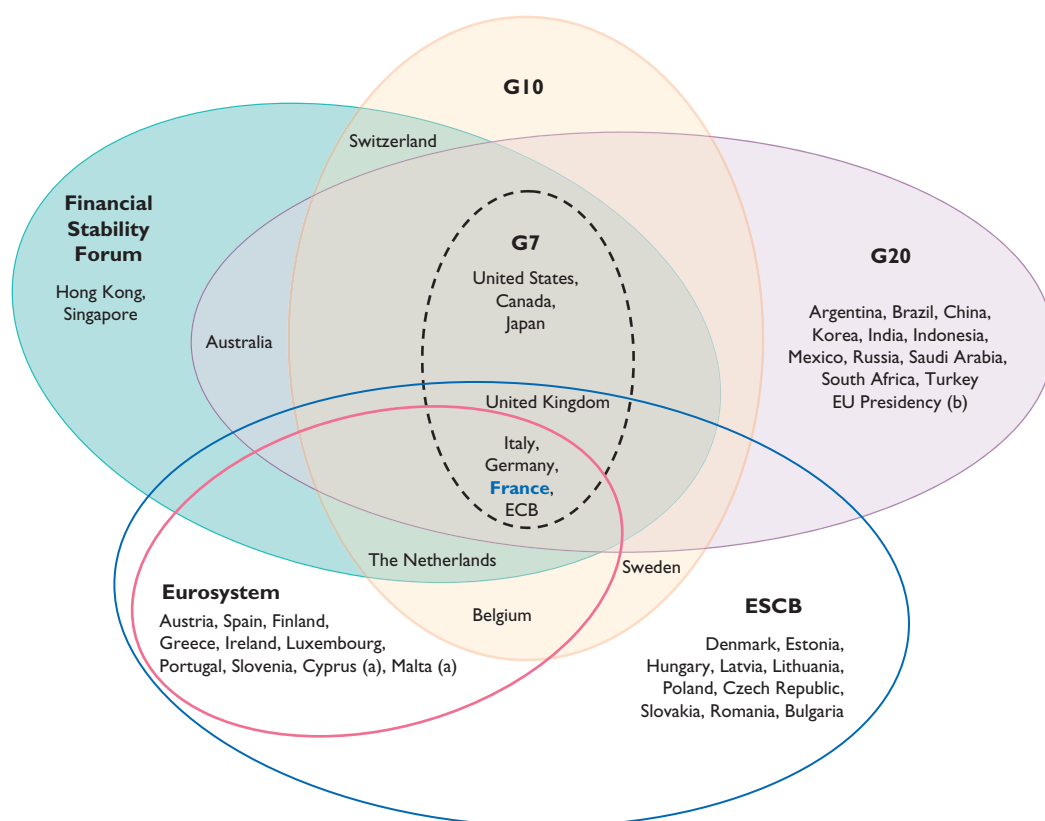
In this capacity, it played an active role in the co-operation between the central banks following the triggering of financial turmoil during the summer of 2007, in the wake of the US subprime mortgage crisis. The Bank's analysis also contributed to the work of the Financial Stability Forum (see Box 13 "The Banque de France and the financial crisis").

The Governor of the Banque de France participated in the meetings of Franc Zone ministers of finance and central bank governors that are organised twice yearly, once in Paris and once in Africa. The Banque de France is in charge of the secretariat and contributes to the preparation of these meetings. The meeting in October 2007 notably provided an opportunity to analyse the conditions to be respected by countries that have benefited from the cancellation of their debt in order for them to borrow in a sustainable manner.

### Key data for 2007

- 22 meetings of the ECB Governing Council
- Some 15 other high-level European meetings (Economic and Financial Committee, Informal ECOFIN, and the French-German Economic and Financial Council)
- Some 30 meetings of international (IMF, BIS, G7, G10, G20, OECD, FSF) and regional (e.g. the Franc Zone) organisations or bodies
- 9 bilateral debt agreements signed
- 94 short-term assignments and 7 long-term secondments in the framework of technical co-operation
- 50 training seminars and 30 study visits arranged for over 1,820 trainees from foreign central banks

### The Banque de France's participation in European and international groupings



NB: Basel Committee = G10 + Spain.

(a) Since January 2008.

(b) The European Union presidency participates in the G7 when it is held by a country that does not belong to the G7.



As regards technical cooperation with European countries, the Banque de France has led a second twinning project with the Bulgarian National Bank, in partnership with the Banca d'Italia and the Nederlandsche Bank. The Bank's experts were also involved in the framework of technical assistance projects led by the ECB in Bosnia, Egypt and Russia. The Bank also participated in a large number of IMF and World Bank assignments.

On a bilateral basis, the Banque de France co-operates closely with the Bank-Al Maghrib (the central bank of Morocco) in the framework of an agreement signed between the governors and provides technical assistance to the central banks of French-speaking countries in Africa, the Middle East and Asia.

## 2| The tasks and activities of the Banque de France

The Banque de France's tasks are directly linked to the functioning of the Eurosystem, while also relating to specific responsibilities that in most cases have been entrusted to it by law. They contribute to three major objectives that underpin the legitimacy of its actions:

- monetary stability;
- financial stability both in respect of its participation in the Eurosystem and its responsibility as a national central bank;
- the provision of specific services to public administrations, enterprises, private individuals and the banking and financial sector.

### 2| I The Banque de France and monetary stability

The Banque de France's duties in the area of monetary stability include the preparation and implementation of monetary policy, the management of foreign currency reserves and the monitoring of the production and quality of banknotes and coins.

#### Tasks conducted within the framework of monetary policy

*The Banque de France performs its central bank tasks within the framework of the Eurosystem, which is made up of the European Central Bank (ECB) and the euro area national central banks. The primary objective of monetary policy – as laid down in the Maastricht Treaty – is to ensure price stability.*

*The Banque de France provides the Eurosystem with an array of business analyses, statistics and studies on the French economy, which are used to define monetary policy. It makes an assessment of the economic situation across the euro area for the Governor of the Banque de France, who participates in the meetings of the ECB Governing Council, which is responsible for interest rate policy.*

*The Banque de France, which is charged with the implementation of the single monetary policy in France, refines credit institutions established in France by supplying them with the liquidity they need.*

#### 2| I I Statistics and research

The Banque de France's participation in the preparation of the Eurosystem's monetary policy and the explanation of this policy are inconceivable without the basis provided by in-depth research and the compilation and analysis of economic, monetary and financial statistics.

##### Active participation in tasks relating to official French and European statistics

For the compiling of monetary, financial and bank interest rate statistics, the Banque de France implements ECB regulations on the reporting requirements of monetary financial institutions (MFIs). The adaptation of the French framework for monitoring monetary statistics continued in 2007: a public consultation was carried out by the Bank to evaluate the costs and advantages of the modification of the reporting framework envisaged by the ECB; in parallel, the simplification and reconciliation of reporting from banks was continued. Lastly, the regulatory framework for monetary statistics was revised following a decision by the Monetary Committee of the General Council of the Banque de France.<sup>1</sup>

<sup>1</sup> Decision 2007-03 of the Monetary Committee of the General Council of 3 October 2007 available in French on the Bank's website ([http://www.banque-france.fr/fr/stat\\_conjoncture/regle/regle\\_stat/dispos5.htm](http://www.banque-france.fr/fr/stat_conjoncture/regle/regle_stat/dispos5.htm)).

### Tasks carried out in the area of statistics and research

In this area, the Banque de France:

- draws up, within the framework of its basic tasks, France's balance of payments and international investment position as well as the country's contribution to the balance of payments and international investment position of the euro area;
- draws up the French components of the monetary and financial statistics that the ECB then aggregates for the whole of the euro area;
- produces a large body of financial statistics pertaining to national accounting;
- conducts a "monthly business survey";
- analyses France's international economic environment and prepares growth and inflation projections within the framework of the Eurosystem;
- produces a large range of publications, including the Bulletin de la Banque de France and the Financial Stability Review;
- contributes to economic and financial research through its own studies, retranscribed and published, notably in the Working Paper Series, and through the work of the Fondation Banque de France and the organisation of or participation in symposia.

The French balance of payments statistics, both for France and for the euro area, were drawn up in the new framework governed by the law of 20 February 2007 (Article L.141-6 of the Monetary and Financial Code) which states the responsibility of the Banque de France in this field. The Annual Report on France's Balance of Payments in 2006 was published in June 2007.

As regards the quarterly financial accounts for the euro area, within the framework of guidelines issued by the ESCB, the Banque de France has undertaken the task of reducing the time taken to publish the accounts under its responsibility to around 90 days. It has also launched an initiative aiming to increase

### Key data for 2007

24,500 statistical series released on the French version of the Bank's website and 3,000 on the English version

3,100 statistical series relating to the euro area and Member States were posted online as part of the Banque de France's contribution to the ESCB's joint publication system

14,000 companies surveyed to produce the monthly business survey

1,550 companies reporting monthly and 18.9 million items of information processed to compile the balance of payments

30 working papers, 52 articles in the Bulletin de la Banque de France and 17 articles in the Financial Stability Review

18 publications in scientific journals with selection panels

the quality of the information gathered on the insurance sector, while making sure that the reporting agents' burden is not increased.

Work continued on modernising the processing and dissemination of business surveys.

The Advisory Council<sup>2</sup> provided the Banque de France's governing authorities with information and advice regarding the state and outlook of the various sectors of the economy.

Lastly, the Banque de France published a charter on the dissemination of its statistical data.<sup>3</sup> The documents concerned, which range from periodical press releases of a few pages to official annual reports, are available free of charge on the Bank's website. Hard copies may also be produced, primarily in the case of official reports. Time series, listing aggregated data compiled by the Banque de France or disseminated by the Eurosystem, can be downloaded free of charge from the Bank's website. Individual data can be made available, as long as the rules of statistical confidentiality are strictly complied with, in accordance with predefined and published procedures.

<sup>2</sup> Its members, appointed for three years by the General Council on the proposal of the Governor, are selected from among leading figures from different sectors of the economy. As at 31 December 2007, they numbered 25 (the composition of the Advisory Council is annexed to this Annual Report). The Advisory Council met 10 times in 2007.

<sup>3</sup> Available in French on the Bank's website ([http://www.banque-france.fr/fr/stat\\_conjoncture/deontologie/deontologie.htm](http://www.banque-france.fr/fr/stat_conjoncture/deontologie/deontologie.htm)).

## Refining analyses and developing studies and research

In 2005, the Banque de France set itself the primary objective of strengthening its position in the domain of research in France and abroad. The Bank's teams of economists, whose numbers are gradually being stepped up, produced around thirty original research papers in 2007,<sup>4</sup> most of which were ultimately destined for publication in international scientific journals. This work draws in particular on quantitative models of structural macroeconometrics, microeconometrics and applied finance. A number of the non-technical articles aimed at a wider public have also been published in the *Bulletin de la Banque de France* and *Financial Stability Review*.

The Banque de France has co-organised a number of international symposia and seminars,<sup>5</sup> that brought together renowned researchers from central banks and French and foreign universities, notably a conference on changes in the dynamics of inflation and the consequences for monetary policy (September 2007, Paris) in co-operation with the ECB, the Euro area Business Cycle Network and the Centre for Economic Policy Research (CEPR). Furthermore, in April 2007, the Banque de France co-organised the Bundesbank's traditional spring conference in Eltville, close to Frankfurt, on the topic of the use of microeconomic data for macroeconomic analysis.

The *Fondation de la Banque de France pour la Recherche en économie monétaire, financière et bancaire* (Banque de France Foundation for Monetary, Financial and Banking Economic Research) put out its twelfth request for proposals for research projects that it selects and finances via grants. As part of the framework of its Visiting Scholars programme, it received academics from France and other countries wishing to co-operate on studies with Banque de France teams and organised ten research seminars, including its sixth "Journées" on 29 and 30 November 2007.<sup>6</sup> The Scientific Council for the Foundation, made up of representatives from French and international academia, is a forum for the exchange of views and discussion of the Foundation's strategic orientations. Its members have been increased in number from 14 to 20.

## 2|1|2 The operational framework of monetary policy

The monetary turmoil which began in August had a significant impact on the second half of 2007. In conjunction with the other central banks, and with the Paris financial centre, the Banque de France endeavoured to identify the stress points and participate in drawing up appropriate measures to face the situation.

In the framework of this general task of defining and implementing monetary policy, major progress was made in 2007. On 1 January 2007, a single list of assets eligible for monetary policy and intraday credit operations came into effect, including a new framework for the assessment of the credit quality of issuers/debtors. The reform has enabled a harmonisation of eligibility criteria in all Eurosystem countries and an increase in the volume of eligible underlying assets (mainly with the extension of the acceptance of credit claims), favouring the financing of the economy. The quality of the rating system implemented by the Banque de France, which has obtained the status of an External Credit Assessment Institution (ECAI), has led all French banks to select, amongst the various possibilities offered to them in order to comply with the "Basel II" provisions (see 2|2|1 "Banking supervision and co-operation with the market authorities"), the Banque de France rating as a credit quality assessment source.

At the same time, the Banque de France has developed a new framework for collateral management in order to improve the efficiency of monetary policy operations. Implemented on 18 February 2008, in parallel with migration to TARGET2 (see 2|2|3 "The Banque de France and the security of means of payment and exchange systems"), the new system helps to increase the flexibility of cash management by credit institutions (see Box 11 "Overall collateral management").

A decision<sup>7</sup> by the Monetary Committee of the General Council has transposed into French law the provisions of the European Central Bank guideline on the

<sup>4</sup> Working Paper Series, available on the Bank's website (<http://www.banque-france.fr/gb/publications/ner/ner.htm>).

<sup>5</sup> Conference on wage bargaining, employment and economic and monetary policies (October 2007, Paris), in collaboration with the Research, Survey and Statistics Directorate (DARES) of the French Ministry of Employment and Ministry of Economy and Finance; conference on the predictability of macroeconomic or financial models and the related risks (November 2007), in collaboration with INSEE's Centre for Research in Economics and Statistics (CREST).

<sup>6</sup> In co-operation with the CEPR, on the topic of "Banking and Asset Markets: Risks and Policy Issues" (available on the Bank's website: <http://www.banque-france.fr/gb/fondatio/calendar/index.htm>).

<sup>7</sup> Available in French on the Bank's website ([http://www.banque-france.fr/fr/poli\\_monel/regle\\_poli/decis07-5.htm](http://www.banque-france.fr/fr/poli_monel/regle_poli/decis07-5.htm)).

### Box 11

#### Overall collateral management

*The technique of collateralisation of securities with the Banque de France was based until recently on repurchase agreements ("repo"), a technique that does not enable credit institutions to optimise their management of assets used as collateral in monetary policy operations. Legal developments and requests from the Paris financial centre led to the launch of a project for overall collateral management. The central idea is to create a fungible stock of assets whose overall amount must remain above the refinancing amount obtained, while making it easier to substitute assets for other assets of the same or a different nature (a government bond for a private debt security for example). The project was implemented on 18 February 2008.*

monetary policy instruments and procedures of the Eurosystem. This text, which governs monetary policy operations, has taken into account France's migration to TARGET2 and the concomitant reform of legal and operational procedures of the earmarking of eligible assets used as collateral for the overall management of collateral needed for monetary policy operations carried out by the Banque de France.

### 2|1|3 The management of foreign exchange reserves

#### Tasks carried out in the management of foreign exchange reserves

*The Banque de France holds and manages the country's gold and foreign exchange reserves; it also manages part of the ECB's foreign exchange reserves.*

*Within the framework of the decisions taken by the ECB Governing Council, the Bank may be required to intervene on foreign exchange markets.*

#### Key data at end-2007

- EUR 80.3 billion in foreign exchange reserves
- 2,594 tonnes of gold, worth EUR 47.4 billion
- EUR 32.9 billion in foreign currency holdings

#### Foreign exchange assets diversified and actively managed

In 2007, the diversification of the foreign exchange investment strategy continued, with a view to optimising the risk/return profile of these assets.

Foreign exchange assets are managed in the trading book, which does not rule out holding a proportion of them to maturity.

#### The management of ECB foreign reserve assets

In the framework of the decentralised management of the ECB's foreign reserve assets, the Banque de France manages dollar and yen reserves proportionate to its share in the subscribed capital of the ECB. In the same way as national foreign exchange reserves, these portfolios are actively managed, in accordance with investment benchmarks defined by the ECB.

Since 1 January 2005, the Banque de France has contributed to the provision of services offered by the Eurosystem for the management of foreign exchange reserves in euro of non-euro area central banks and international organisations. This activity grew considerably during 2007 via the strengthening of ties with existing clients and the development of new contacts. Assets held enjoy legal immunity. The Banque de France is one of the main players providing these services in the Eurosystem.

#### Further gold sales in the framework of the central bank agreement

In 2007, the Banque de France sold 125 tonnes of gold. These sales reflect market transactions within the framework of the agreement reached between 15 European central banks to limit overall gold sales to a maximum of 500 tonnes per year over a five-year period commencing on 27 September 2004.

## **2|1|4 Production and management of banknotes and coins**

### **Developing and modernising banknote production**

The good results for banknote production recorded in 2006 were consolidated in 2007. Following

the historic turning point in 2006, marked by operating profit and the distribution of over two billion banknotes in euro and for export, financial performances improved in 2007, thanks to the renovation of the production facilities, the significant increase in productivity and efficient quality control.

### **Tasks carried out in the production and management of banknotes and coins**

The Banque de France's tasks in the area of banknotes and coins consist in:

- *banknote printing.* It operates a paper-mill at Vic-le-Comte and printing works at Chamalières, both in the Auvergne. Both industrial sites have received a quality and environment certification. While it focuses on the production of euro banknotes, the Banque de France also supplies banknotes to foreign central banks in the framework of institutional partnerships and the provision of specialised engineering services;
- *putting into circulation euro banknotes and coins.* Through its branch network throughout France, it supplies cash to credit institutions, which then distribute it to the public;
- *maintenance of banknotes and coins.* The Bank is charged with ensuring the quality of all banknotes in circulation in France and sorts the notes in order to identify and remove from circulation all counterfeit, worn, torn and stained bills;
- *supervision of the cash industry.*

#### **Processing of coins**

Credit institutions that process and package coins for delivery to the Banque de France must sign an agreement with the Bank regarding the processing of coins for delivery to the Banque de France or use the services of an operator that has concluded such an agreement.

These agreements specify the measures to be implemented by operators (equipment, procedures, etc.) and provide for on-site and documentary inspections by the central bank.

#### **Delivery of banknotes to public automated teller machines (ATMs)**

Operators that replenish self-service ATMs with banknotes that are not directly drawn from a Eurosystem central bank must conclude an agreement with the Banque de France or use the services of an operator that has concluded such an agreement.

These agreements, approved by the Ministerial Order of 20 June 2005, stipulate the resources to be put in place by operators, particularly in terms of equipment. They provide for on-site and documentary inspections by the central bank. They require operators to draw up written operating and control procedures and to provide specific information to the Banque de France.

### **Key data for 2007**

- 2 billion banknotes delivered by the banknote production facilities, including 1.4 billion in euro
- 7.4 billion banknotes sorted annually
- 7.6 billion banknotes distributed by the Banque de France
- 7.4 billion banknotes received at the Banque de France
- 0.9 billion coins put into circulation





**Checking the new banknotes on a sample basis**

**Table 8 Banknote manufacturing**  
Deliveries and staffing levels in 2006 and 2007

(annual volumes in billion banknotes, staffing levels in full-time equivalent terms)

	Annual volumes manufactured and delivered	Headcount
2006	2.1	949
2007	2.0	944

In terms of volumes produced and delivered, the 2007 level is virtually identical to the previous year. Banknote production continues to benefit from the combined effect of a high quota of euro banknotes (1,249 million notes) assigned to the Banque de France as part of the pooling system<sup>8</sup> and a sustained export market amounting to an average 600 million banknotes annually. Furthermore, at the end of 2007 the facilities were able to produce and distribute ahead of the 2008 euro order, thus smoothing the following year's production of euro and export, total volumes of which exceed 2.3 billion banknotes. Indeed, the production schedule for the next few years will continue to expand, due to the continued increase in euro banknotes in circulation and the preparation of the future "euro 2" series, guaranteeing an annual delivery of between 2 and 2.5 billion banknotes, which should consolidate the profitability of the banknote production facilities.

As regards manufacturing, the two production sites (the paper mill at Vic-le-Comte and the printing works at Chamalières) have reached "cruising speed", notably with the successful launch in the first half of the second sheet-fed printing line equipped with state-of-the-art machines.

From the European standpoint, the Banque de France contributed in 2007 to the preparation of the second series of euro banknotes as leader of the public group including France, Italy, Belgium, Spain and Austria. The ECB has entrusted this group with the origination and production of a pilot series of EUR 50 banknotes that will be the first denomination to be issued in January 2011. The Banque de France

will be highly involved in the mass production of these banknotes, printing a billion of them by end-2010. This responsibility imposes an obligation on the Bank to achieve a result vis-à-vis the Eurosystem and a sustained effort of technical preparation and co-ordination.

In the medium term, the operational priorities for banknote production are focused on the consolidation of the financial break-even reached in 2006 and 2007 and the capacity to create sufficient leeway to be able to participate in the Eurosystem's centralised system of tenders to be implemented in 2012 for the supplying of euro banknotes. To this end, three priorities have been set:

- Completing the renovation of the production facilities via the necessary investments and redeployment of machinery to a state-of-the-art technical level and with the capacity to meet the future deadlines for the second series of euro banknotes.
- Continuing the systematic improvement of productivity by reducing the error rate, optimising the performance of the machines and adapting the working structure to the workload schedule of the coming years.
- Endeavouring to reduce all costs, notably optimising supplies through systematic competitive tendering between suppliers and cutting back on operating costs.

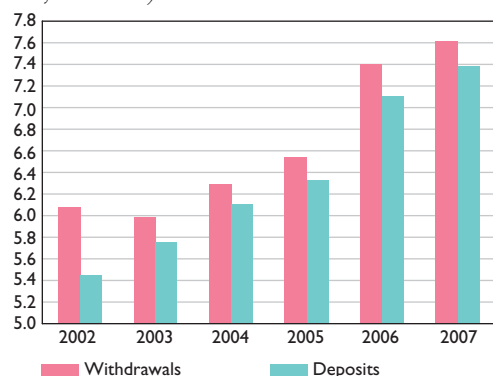
### Ensuring the quality of banknotes in circulation

Following a very sharp increase in the volume of banknotes handled by the Banque de France in 2006 as a result of the implementation of the Decree on the recycling of euro banknotes and coins (see Box 12 "Monitoring the recycling of euro banknotes and coins in 2007"), volumes increased more moderately in 2007. This trend was accentuated in certain regions following the gradual development of banknote recycling by private companies.

<sup>8</sup> Since 2002, a pooling system has operated between national central banks for the production of euro banknotes in the Eurosystem: each NCB specialises in the production of a number of denominations, which are then partly exchanged with the other members of the Eurosystem. In 2007, the Banque de France produced EUR 5, EUR 10 and EUR 20 banknotes.

**Chart 31 Volumes of euro banknotes handled by the Banque de France**

(billions of banknotes)



Source: Banque de France.

In 2007, deposits (7.4 billion banknotes amounting to EUR 174 billion) and withdrawals (7.6 billion banknotes amounting to EUR 178.8 billion) grew in volume terms by 4.0% and 2.9% respectively, after rises of 12.3% and 13.1% in 2006.

In this context, the banknote sorting activity remained particularly sustained: 503.0 million more banknotes were sorted than in 2006, increasing volumes of banknotes processed to 7.4 billion.

The net issuance of euro banknotes<sup>9</sup> in France stood at EUR 62.1 billion at end-December 2007, up by 8.1% compared to end-2006. France remained in fourth position in the Eurosystem,<sup>10</sup> behind Germany (EUR 283.3 billion), Italy (EUR 128.5 billion) and Spain (EUR 85.5 billion).

Compared to other euro area countries, France continues to stand out in using a greater number of medium-value denominations. The growth in

net issuance in France is mainly thanks to that of denominations used in everyday transactions (EUR 5, 10, 20 and 50), which increased by 10.7% in nominal terms, compared with 6.6% in the Eurosystem. Conversely, net issuance in France of large-value denominations (EUR 100, 200 and 500) posted a lower increase than the euro area average (4.6% in France compared with 7.7% for the Eurosystem).

At end-2007, banknote circulation in the Eurosystem amounted to EUR 676.6 billion, of which EUR 128.8 billion (19%) was recorded on the balance sheet of the Banque de France.<sup>11</sup>

French franc banknotes continued to be returned to the Banque de France in 2007, with an upturn in activity at the beginning of the year due to the end of the exchange period for the Pascal 500 franc note on 28 February 2007. Throughout the year, exchanges of French franc notes came to a total volume of 2.3 million banknotes for a value of FRF 542.4 million, i.e. EUR 82.7 million.

Developments in the volume of coins handled by the Banque de France during 2007 were more striking than for banknotes: withdrawals diminished sharply by 8.7%, i.e. by 199.2 million coins; likewise, deposits decreased by 5.6%, i.e. by 70.3 million coins. This significant drop in activity resulted from delays in the delivery of new coins during the first half of 2007. In this context, the growth in net issuance of euro coins in France declined slightly to 5.7% at end-2007 from 5.9% at end-2006. For net issuance in volume terms, growth dropped to 9.1% in 2007 from 11.5% in 2006. In 2007, 76.4% of total net currency outflows consisted of copper coins (1 cent, 2 cents and 5 cents), due to the continuing very low rate of return of these denominations.

<sup>9</sup> Since 1 January 2002, "banknotes in circulation" designates all euro banknotes issued in the Eurosystem. National Statistics now use the concept "net currency in circulation", defined as the difference between withdrawals and deposits at the counters of the national central bank since the first issue of each banknote.

<sup>10</sup> Outstandings, excluding national currencies.

<sup>11</sup> Pursuant to the ECB's Decision of 6 December 2001 on the issue of euro banknotes, 8% of the total value of euro banknotes is allocated to the ECB, while the remainder is allotted to the NCBS in proportion to their paid-up shares in the ECB's capital.

**Box 12**

**Monitoring the recycling of euro banknotes and coins in 2007**

**Agreements regarding the processing of coins; inspections carried out by the Banque de France**

The system of inspection was fully put in place during 2006; it has thus been totally operational for a year and a half.

At end-2007, 43 processing agreements were in force, concluded between the Banque de France and credit institutions, cash-in-transit and cash-processing companies and companies operating vending machines. In total, there were 178 sites in France handling coins for delivery to the Banque de France at 31 December 2007.

In 2007, 117 sites were the subject of on-site inspections by Banque de France teams. The inspections carried out by the Bank identified a number of malfunctions (inadequacy of equipment, operating and internal control procedures, etc.) that were gradually rectified by the operators concerned. It nonetheless proved necessary to carry out three follow-up inspections at sites where serious shortcomings were identified.

**Agreements regarding the automatic distribution of banknotes not drawn from a central bank; inspections carried out by the Banque de France**

In 2006, the Decree's entry into force led many banks to review their practices concerning the replenishment of their ATMs. Those that did not meet the requirements stipulated by the Decree and the Conventions stopped recycling banknotes; others took advantage of the transitional period provided for in the standard agreements.

In 2007, most credit institutions gradually started to work on the possibility of recycling banknotes in-house compliant with the target system laid down by the standard agreements. A number of trials were thus carried out in order to comprehend the different configurations offered according to the equipment proposed by the distributors: either recycling with back office equipment or recycling via equipment integrated into the ATM. Strategic choices are beginning to be made.

At end-2007, 38 agreements concerning "the distribution by ATMs of banknotes not directly drawn from a Eurosystem central bank" had been signed. The Banque de France carried out 34 on-site inspections in signatory institutions during the year.

**Training bank employees in the authentication of banknotes**

In accordance with the provisions of Article R122-6 of the Monetary and Financial Code, the Bank continued to give support to banks that requested it in training staff charged with the manual distribution of banknotes in bank branches.

Accordingly, 920 credit institution staff members were trained along these lines by the Banque de France in 2007.

**Implementation of the Decree in overseas departments**

The Banque de France has charged the French overseas departments note-issuing bank (IEDOM) with the administration of the system with regard to credit institutions whose headquarters are located in the overseas departments and in Mayotte.

Eight agreements covering the automatic processing of euro coins were signed in respect of eleven production sites. The IEDOM conducted 6 on-site inspections.

At end-December 2007, two agreements concerning the delivery by ATMs of recycled banknotes were concluded with a credit institution and one on-site inspection was conducted.

The IEDOM participated in the training of bank employees in banknote authentication.

NB : Report produced pursuant to Articles R121-3 to R123-2 and R162-5 of the Monetary and Financial Code implementing Article 6 of the Council Regulation (EC) 1338/2001 of 28 June 2001 (entered into force on 17 January 2006).



## 2|2 The Banque de France and financial stability

One of the Banque de France's main tasks is to ensure the security and smooth operation of the financial system. In this capacity, the Bank must detect and mitigate threats to financial stability.

The Banque de France's assessment capacity and responsiveness in this domain are partly linked to the central bank being entrusted with banking supervision functions and partly to the Bank's operating capacity based on the market knowledge obtained from its own operations, its collateral management and statistical system.

### 2|2|1 Banking supervision and co-operation with the market authorities

#### A key role of banking supervision

The *Commission bancaire*'s main task is to ensure the safety of public deposits and, more generally speaking, to safeguard banks' soundness. In order to ensure the latter, it is fundamental that the French banking and financial system be managed prudently. The *Commission bancaire* is also responsible for making sure that the institutions subject to supervision comply with regulations concerning the fight against money laundering and the financing of terrorism.

As regards the regulatory framework of supervision, of particular note is the entry into force in 2007 of the capital requirements directive (CRD), which transposes the Basel II agreement into European law. This system provides significant progress for banking supervision:

- greater scope of risks covered (including credit risk, operational risk, market risk);
- incentive for banks to adopt more sophisticated methods of risk measurement;
- various additional measures beyond the minimum capital requirements (which constitute pillar 1), structured dialogue between banks and supervisors concerning risk analysis (pillar 2) and market discipline and transparency (pillar 3).

#### Tasks carried out with regard to banking supervision and financial regulation

The Banque de France, either directly or via its administration of the general secretariats of the Comité des établissements de crédit et des entreprises d'investissement (CECEI – Credit Institutions and Investment Firms Committee), the Comité consultatif sur la législation et la réglementation financières (CCLRF – Advisory Committee on Financial Legislation and Regulation, which also works in the field of insurance) and the Commission bancaire, contributes to the smooth functioning of the banking sector and the financial system.

Within this framework, it carries out or participates in the following tasks:

- delivering the authorisations and licences required for credit institutions and investment firms to carry out the various stages of creation, development and restructuring related to their activity;
- ensuring these institutions' compliance with the banking and financial regulations in force through permanent off-site monitoring (solvency, liquidity, internal control, the fight against money laundering and the financing of terrorism, etc.) and on-site inspections;
- drafting and implementing the legal texts governing the banking and financial sector in the context of the harmonisation of European and international rules.

The Banque de France is a member of the other French financial market authorities, which comprise the Autorité de contrôle des assurances et des mutuelles (ACAM – Insurance Supervisory Authority), the Autorité des marchés financiers (AMF – Financial Markets Authority) and the Conseil consultatif de la législation et de la réglementation financières (CCLRF – Advisory Committee on Financial Legislation and Regulation).

The Banque de France's regional managers are the AMF's representatives in the regions.

The Banque de France provides the secretariat for the CECEI, the General Secretariat of the Commission bancaire and the CCLRF.

Since most of the large institutions opted for the use of more sophisticated internal ratings-based approaches as of 1 January 2008, the General Secretariat of the



*Commission bancaire* worked intensively in 2007 towards the authorisation of internal risk assessment models developed by the main banking groups.

The fact that the Banque de France is in charge of banking supervision, via the tasks performed by the *Commission bancaire*, constituted a major advantage in the close monitoring of impact of the subprime crisis on French banks. In order to obtain a detailed assessment of the latter's situation, the *Commission bancaire* has decided to carry out ad hoc on-site inspections, notably focusing on the suitability of market risk models (Value at Risk), the assessment of risks taken on monoline insurers and the valuation of depreciated assets following the crisis.

Pan-European supervisory co-operation has been strengthened via the Committee of European Banking Supervisors (CEBS), chaired until January 2008 by the Secretary General of the *Commission bancaire*. The aim of this committee is to establish and foster steps towards an effective coherence of national practices in matters of banking supervision. In this regard, the supervision of major cross-border European banking groups has been increased within the operational networks aimed at sharing information and monitoring common operational issues, that bring together host-country and home-country supervisors in the framework of the CEBS.

In order to favour a common reporting framework within European banking groups, and pending the complete harmonisation of European reporting requirements, the principle of which was adopted in 2006, the *Commission bancaire* has accepted that the participating banks that are subsidiaries of foreign groups may address their COREP data (prudential statements) in the format defined by the supervisor of their parent company, instead of adhering to the French regulatory framework. As regards the latter, the first submissions under FINREP (consolidated financial reporting framework based on the IFRS) took place for the period ending 30 June 2007.

At the international level, the General Secretariat of the *Commission bancaire* (SGCB) continued to contribute to work by various international co-operation bodies, such as the Basel Committee and the Joint Forum.

Within the Basel Committee, the SGCB has notably worked on four main projects whose importance was reiterated following the financial turmoil of the summer of 2007:

- the implementation of Basel II, which should help to strengthen the quality of risk measurement and management;
- the analysis of bank practices in the measurement of liquidity risk management, notably in situations of stress, as well as the authorities' supervisory methods;
- the improvement of valuation methods adopted by the financial institutions;
- enhancing transparency and market discipline concerning complex and illiquid financial instruments.

The SCGB has also directly contributed to work carried out by the Joint Forum in the three sectors (banking, insurance, markets) concerning the marketing of financial products, the concentration and transfer of credit risk, and the evaluation of the implementation of principles related to the supervision of financial conglomerates.

### Close co-operation between the financial market authorities

Within the framework of the provisions laid down by the law, the Banque de France and the *Commission bancaire* co-operate closely with the other financial market authorities. The first Deputy Governor of the Banque de France, who generally chairs the *Commission bancaire* on behalf of the Governor, sits on the Board of the *Autorité des marchés financiers* (AMF – Financial Markets Authority) as well as its Audit Committee and one of the specialised commissions that decide on the referral of individual cases to the disciplinary commission. The staff of the two institutions also collaborate: the Banque de France's Regional Managers represent the AMF in the regions; at the AMF's request, the Banque de France's Inspectorate carries out inspections in credit institutions and investment firms; and the secretariats of the two institutions exchange views in the course of regular meetings

on numerous regulatory issues and individual cases. They also participate in working groups on subjects of common interest (such as alternative multi-management) with a view to addressing financial stability issues. Exchanges of staff between the general secretariats of the AMF and the *Commission bancaire* take place on a regular basis and the on-site inspection programmes of the two boards are harmonised where necessary.

There is also close co-operation between the *Commission bancaire* and the *Autorité de contrôle des assurances et des mutuelles* (ACAM – the Insurance Supervisory Authority). The first Deputy Governor is a member of this body and a charter sets out the terms of the co-operation between the two authorities and their general secretariats: joint meetings, joint on-site inspections of financial groups that engage in both banking and insurance activities and exchanges of staff. The Governor of the Banque de France and the Chairman of the ACAM take turns in chairing the joint ACAM-*Commission bancaire* sessions, during which subjects of common interest that come within the competence of the two bodies are discussed.

The Governor of the Banque de France, as Chairman of the *Commission bancaire*, also sits on the *Collège des autorités de contrôle des entreprises du secteur financier* (CACES – Board of supervisory authorities for companies in the financial sector), in which cross-sector issues concerning all three supervisory authorities are addressed, chaired by the Minister in charge of economic affairs or his/her representative.

### Key data for 2007

- Number of institutions subject to supervision: 925, of which 775 credit institutions and 150 investment firms

#### Commission bancaire

- 113 on-site inspections: 8 individual letters requesting improvements or letters of injunction and 6 proceedings leading to penalties

#### CECEI

- 307 individual cases examined, of which 17 authorisations and 109 revocations of authorisation

## 2|2|2 Financial stability

The importance of financial stability issues has led the Banque de France to create a Financial Stability Directorate, whose tasks include the following:

- identifying the developments and changes in the financial system;
- contributing to adapting regulations;
- analysing the impact of these regulations on the system;
- defining the scope of intervention in order to regulate the system in the event of a crisis;
- actively contributing to the robustness of the Paris financial centre.

### Activities relating to financial stability at the centre of current events

The Financial Stability Committee, an internal body chaired by the Governor, has examined the issues related to changes in regulations and banking and financial supervision in Europe, including in their approach to handling financial crises, the regulation of hedge funds and the first lessons to be learned from the subprime crisis in the different fields (liquidity, valuation, rating agencies, Basel II and securitisation, etc.).

A special issue of the *Financial Stability Review* published in April 2007 focused on hedge funds which, due to their role in financial markets, are receiving increasing attention, notably within international fora such as the G7. In order to gain further insight into the major topics related to financial stability and regulation, the *Review* gathered different viewpoints from prominent professionals and economists, representing financial institutions, universities, central banks and supervisory authorities. On the occasion of the *Review*'s launch, a conference was held in Washington alongside the spring meetings of the International Monetary Fund. Chaired by the Governor, with a panel of speakers including central bank governors, economists and professionals, the conference attracted a wide audience. A seminar on

the *Review* was held a few days later at New York University, directed at the academic community and the financial community.

In a context marked by the financial turmoil following the crisis during the summer (see Box 13 “The Banque de France and the financial crisis”), the Banque de France (which ensures the supervision of the French negotiable debt securities (TCN) market) closely monitored the sharp increase as of August 2007 in the outstandings of certificates of deposit issued by credit institutions. The size of the TCN market, which also comprises commercial paper issued by non-financial corporations and negotiable medium-term notes, and which plays a crucial role in the financing of banks and businesses, has increased significantly. Total outstandings increased from almost EUR 450 billion at end-2006 to just over EUR 550 billion at end-2007. Implementation of a new IT application, NORIA, used for the collection and compilation of data on negotiable debt securities, helped to improve the supervision and transparency of this market.

Furthermore, the Banque de France plays a key role in the promotion of the Short Term European Paper (STEP) label, intended to foster the integration, recognition and quality of European short-term securities markets. This label, launched in 2006, was highly successful during 2007. Following a decision by the ECB’s Governing Council, non-bank securities with this label have been eligible for the refinancing of the Eurosystem since 2 April 2007 – provided that the other criteria are complied with. Their outstandings have increased considerably, from over EUR 120 billion at end-2006 to EUR 320 billion at end-2007. The Banque de France continues to provide considerable support in the labelling process, while the ECB is in charge of publishing statistics on yields and outstanding amounts on its website.

The French TCN market, which is continental Europe’s leading short-term securities market and the third largest in the world after its US and UK equivalents,

### **Key data for 2007**

#### **Financial Stability**

- 4 meetings of the Banque de France’s internal Financial Stability Committee and 3 meetings of the working group on resilience made up of representatives from the financial sector
- 17 articles published in the Financial Stability Review (FSR)

#### **Supervision and development of the negotiable debt securities market**

- 357 financial memoranda analysed and posted on the Banque de France’s website as at 31 December 2007

accounts for 75% of outstanding amounts of STEP securities.

### **Operational continuity objective**

The Banque de France also chairs a working group made up of representatives from the financial sector whose aim is to improve the resilience of the financial system against operational shocks. This group on resilience, comprising representatives from the main credit institutions, payment systems and regulatory and supervisory authorities has concluded its work. In March 2007, the group set out a dozen concrete recommendations to strengthen the operational continuity of the French financial centre. These recommendations have been presented to professionals. Their implementation notably led to the creation of an emergency committee whose purpose is to share information on any serious event that could potentially have an impact on the financial centre, to facilitate an analysis of the situation and to follow its development. The group has also undertaken a gradual approach of tests aimed to improve the financial centre’s overall resilience.

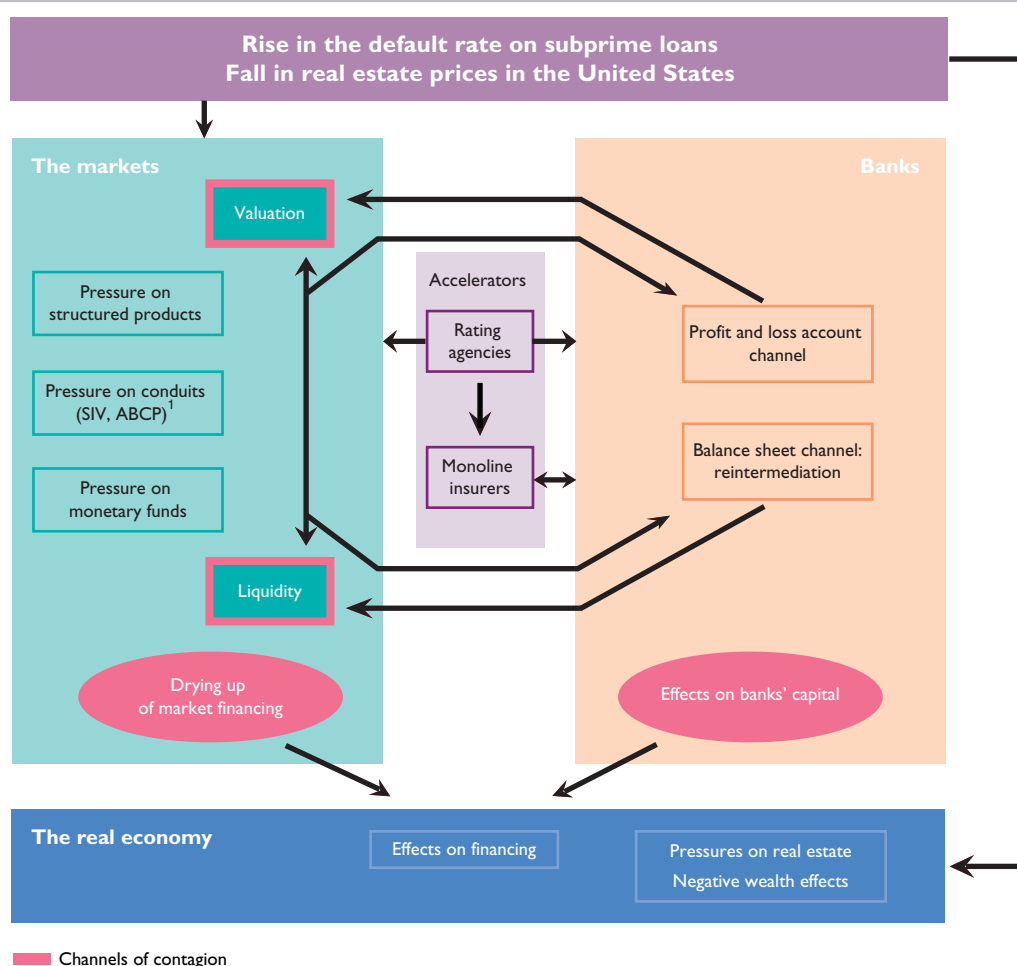
The Banque de France has also actively participated in work undertaken at the Eurosystem level as far as business continuity is concerned.

## Box 13

### The Banque de France and the financial crisis

After several years of considerable financial innovation, very high profits and low volatility in the financial markets, 2007 was marked by a large-scale financial shock, triggered by the subprime mortgage crisis in the United States. In certain segments of the credit market, notably the mortgage-lending market, risk premiums have increased with unprecedented speed and volatility. The interbank markets of the main industrialised countries have been seriously disrupted by more intensive and longer lasting turmoil than in the wake of the September 11 attacks in 2001. The leading banks have had to face a shift back to credit intermediation and the drying up of financing on the interbank market, which has led them to manage their liquidity in a conservative manner and seek a greater amount of financing from central banks. The hedging of direct or indirect risks on the subprime market also led to a sharp drop in profits in the second half of the year. Above all, the crisis has shown the intensity of cross-border ties and interconnections between the markets and financial institutions, as the shock wave from the United States has spread to the financial markets of all developed countries.

#### A crisis in three stages: the financial markets, banks and the real economy



<sup>1</sup> SIV: structured investment vehicles; ABCP: asset-backed commercial paper.

Source: Banque de France – Financial Stability Directorate.

.../...

Central banks, and particularly the Banque de France, have been in the front line in the management of the financial crisis that began in the summer of 2007. The priority was to provide the necessary liquidity for the smooth functioning of the money market. At the same time, analysis of the causes of this turmoil was crucial, while continuing to closely monitor the markets and the financial sector.

### **Mobilisation to ensure liquidity and the successful execution of operations**

In the framework of the refinancing of banks carried out by the Eurosystem, the Banque de France has endeavoured to restore market liquidity conditions by playing the role of co-ordinator between the various market players and relaying information from the financial centre to the Eurosystem. In contact with the liquidity managers of banks and asset management firms, the Bank has assessed the day-to-day movements in interest rates, liquidity needs and the adequacy of available collateral, in an environment marked by increased uncertainty. Thanks to a rapid circulation of information and the efficiency of projects developed, the Bank provided assistance to market initiatives to enable institutions to better utilise the assets they had in order to obtain refinancing from the Eurosystem. The liquidity required to end the fiscal year without major tensions was provided. This was essential to avoid a potential breach or delay in payment being interpreted as an institution's solvency default.

### **Analysis to understand developments in the crisis**

Over the months, the nature of the financial crisis has changed as it has spread from the financial markets to banks and financial institutions in general, while the markets anticipated that it could eventually impact the real economy. At the different stages, the Banque de France has carried out in-depth analysis on the mechanisms of the crisis, the triggers and the propagation channels.

In relation to market players and other central banks, numerous in-depth studies have been carried out on problems that affect the functioning of the financial markets related to liquidity, the valuation of complex structured products, rating agencies and factors of vulnerability (SIVs, monoline insurers, etc.). These studies were able to draw on the extensive statistical information held by the Banque de France on the segments directly affected by the crisis, such as the asset-backed securitisation market, money market funds and the availability of credit to the private sector. They enabled the policy-makers to make a precise real-time diagnosis of developments and to envisage measures to respond to the crisis.

The diagnosis was also based on an overview of French banks' exposures and their systemic situation in terms of liquidity and solvency, obtained from prudential data provided in the framework of the control and supervision of credit institutions. Lastly, an evaluation of the potential impact of the crisis on the real economy was initiated at the beginning of the crisis and has been regularly updated, in order to formulate a monetary policy assessment.

### **Co-operation at all levels with the other authorities**

During the crisis, the Banque de France co-operated closely with the other national authorities, the Ministry of the Economy, Industry and Employment, the Autorité des marchés financiers (AMF – financial market authorities) and the Autorité de contrôle des assurances et des mutuelles (ACAM – the Insurance Supervisory Authority). At the international level, the Eurosystem conducted joint actions with the US and UK central banks, notably in order to alleviate the strong pressure observed in the short-term funding markets, particularly at the turn of the year. The ECB organised daily teleconferences on market operations between the central bank governors and the various levels of Eurosystem experts. Lastly, the Banque de France, alongside the other financial authorities, firmly committed to working towards recommendations to improve market practices and to adjust the regulation framework to structurally strengthen the resilience of the financial system, notably in the framework of the Financial Stability Forum and Committees that contribute to it (such as the Basel Committee).





**Workshop for processing stained banknotes**

## 2|2|3 The Banque de France and the security of means of payment and exchange systems

### **Tasks carried out in respect of means of payment and exchange systems**

*Within the framework of the Eurosystem, the Banque de France performs a two-fold duty.*

*The Banque de France keeps the accounts of credit institutions and participates in the management of the European TARGET system, which ensures the secure settlement of large-value payments and thereby the smooth functioning of the euro area interbank market.*

*The Banque de France is responsible for ensuring the security of means of payment and the relevance of applicable standards in this area. The Bank is also charged with monitoring systems of payment and market infrastructures, ensuring that their organisational structure and operating rules prevent them from playing a part in triggering or spreading systemic risk. Lastly, the Bank ensures the efficiency of these systems, which is critical for the smooth operation of capital markets and of the economy as a whole.*

*The Banque de France participates in European working groups and reforms regarding means of payment and payment systems.*

### **Key data for 2007**

- 690 accounts of credit institutions and investment firms (of which roughly 100 accounts in the TBF system, France's real-time gross settlement system)
- EUR 570 billion worth of payments processed daily in TBF
- 24% of TARGET traffic transits via TBF

## Implementation of major projects

The Banque de France is directly involved in the development and operational management of exchange systems and also ensures the smooth running of the migration of the Paris financial centre to these new systems.

### **TARGET2**

In 2007, as part of its role in managing interbank systems, the Banque de France, together with the Deutsche Bundesbank and the Banca d'Italia, in accordance with the announced schedule, set up the Single Shared Platform that constitutes the core of the TARGET2 settlement system. Following several months of tests with the different European banking communities, the new system was implemented on 19 November 2007 for eight countries, the migration being conducted for the different banking communities in three successive stages (November 2007, February and May 2008).

The start-up of TARGET2 constitutes a great success for the Eurosystem and for the three central banks, including the Banque de France, which developed and currently manage the Single Shared Platform of TARGET2. It also constitutes a success for the different European banking communities, including the French banking community, which contributed substantially to the development of the system's functions and prepared themselves for the migration towards the new system.

The Banque de France ensured the supervision of the entire project as well as the functional co-ordination (the design of all of the system's functionalities). Furthermore, the Bank has set up a computerised decision-support system to ensure the management of records of all transactions in the system and to provide the different categories of users (credit institutions, central bankers, payment system overseers, etc.) with the information they need in order to perform their tasks.

In the framework of the preparation of France's migration to TARGET2, planned for 18 February 2008, a committee bringing together credit institutions and securities settlement systems in the Paris financial centre was created, under the responsibility of the Banque de France. The French banking community's information on issues relating to TARGET2 is ensured via various channels (topic-specific workshops, information bulletins and a dedicated interactive section on the Banque de France's website<sup>12</sup> and a TARGET2 mailbox for credit institutions and securities settlement systems).

### TARGET2 Securities

The TARGET2 Securities (T2S) project provides for the setting up of a single application platform for the settlement of securities transactions, both for national and cross-border transactions, in central bank money. However, all custody functions will be excluded from the scope of T2S. By centralising the operations currently processed on several different platforms, the T2S project aims to significantly reduce the cost of delivery-versus-payment transactions.

The Banque de France actively participated in the user requirements survey, organised by Eurosystem during the second half of 2007. On the basis of the results of a public consultation launched on 18 December 2007, the Governing Council will decide whether or not to engage in the following phase of the project. Pending this decision, the Banque de France has undertaken preparatory work in close co-operation with the Deutsche Bundesbank, Banca d'Italia and Banco de España in order to develop the T2S platform as soon as the decision is taken.

### SEPA (Single Euro Payments Area)

The SEPA project aims to create a Europe-wide area for payments. It envisages the introduction of pan-European payment instruments (bankcards, credit transfers, direct debits) in Europe, which will gradually replace the equivalent domestic payment instruments. The use of these new instruments will be facilitated by the implementation of a harmonised European legal framework, thanks to the Directive on Payment Services. The Banque de France actively participates in work on transposing the Directive, which should be achieved by 1 November 2009, and

in steering France's migration to SEPA, within the national SEPA implementation committee, chaired jointly by the Banque de France and the *Fédération bancaire française* (French Banking Federation) and which brings together all of the stakeholders. The implementation committee's work led in October 2007 to the adoption of a second version of France's national migration plan<sup>13</sup> and the creation of a website ([www.sepafrance.fr](http://www.sepafrance.fr)).

### Oversight of means of payment security

The Banque de France assesses the level of compliance of payment instrument issuers and operators with the security objectives that the Bank has defined. To achieve this, the Bank uses the quantitative and qualitative data that the institutions communicate to the Banque de France annually, notably information relating to the security of cheques – since 2005 – and of the prepaid *chèque emploi service universel* (CESU – all-purpose employment service cheque) – since 2007. A survey was also conducted in 2007 on the security of the main online banking websites, in order to assess the level of implementation of the Bank's recommendations concerning the strengthening of authentication measures.

The Banque de France also contributes within the framework of the Eurosystem to the task of defining the minimum security objectives for payment instruments<sup>14</sup> that may be used cross-border (payment cards, new European credit transfer and direct debit schemes – SEPA).

In 2007, the Bank carried out work with the banking community<sup>15</sup> in order to strengthen security for cheques (using watermarks on bank cheques and monitoring transactions received to detect duplication) and direct debit (reminder of commitments, extension of possibilities for debtor to dispute a transaction).

### Oversight of exchange systems and market infrastructures

In the domain of systems oversight, in 2007, the Banque de France carried out the evaluation and pre-evaluation of new exchange systems that are set to replace the current settlement systems. These new systems are based on cross-border exchange platforms or are open to other banking communities.

<sup>12</sup> Document available on the Bank's website: [http://www.banque-france.fr/gb/sys\\_mone\\_fin/target2/target2.htm](http://www.banque-france.fr/gb/sys_mone_fin/target2/target2.htm).

<sup>13</sup> Available in French on the Bank's website ([http://www.banque-france.fr/fr/sys\\_mone\\_fin/telechar/rapports/sepa\\_27102006.pdf](http://www.banque-france.fr/fr/sys_mone_fin/telechar/rapports/sepa_27102006.pdf)) and on the National SEPA implementation committee's website ([http://www.sepafrance.fr/files/SEPA\\_v2\\_11102007.pdf](http://www.sepafrance.fr/files/SEPA_v2_11102007.pdf)).

<sup>14</sup> The Observatory for Card Payment Security annual reports are available on the Observatory's website at: <http://www.observatoire-cartes.fr>.

<sup>15</sup> Available in French on the Bank's website ([http://www.banque-france.fr/fr/sys\\_mone\\_fin/telechar/rapports/ob\\_secu\\_cheq.pdf](http://www.banque-france.fr/fr/sys_mone_fin/telechar/rapports/ob_secu_cheq.pdf)).

TARGET2 has to comply with international security and efficiency standards applicable to systemically important payment systems. The Banque de France has made a significant contribution to the complete assessment of TARGET2, carried out in 2007 under the co-ordination of the European Central Bank. On the basis of this assessment, TARGET2 exhibits a high degree of compliance with the applicable standards.

The delivery-versus-payment system for financial instruments ESES-France, managed by the group Euroclear, replaced RGV2 on 26 November 2007. ESES-France is based on a common platform whose purpose is to ensure the delivery-versus-payment system for financial instruments in Belgium, France and the Netherlands, in a context of very broad harmonisation of practices in these three financial centres. In close co-operation with the Belgian and Dutch authorities, the Banque de France made sure there were no major problems before starting up ESES-France. The complete evaluation will be carried out following migration of the Belgium and Dutch systems to ESES.

Lastly, the current SIT clearing system for retail payments is in the process of being replaced by a new system, developed by the company STET. The latter will take up the clearing and settlement of payment instruments processed until now by SIT as well as the new payment instruments compliant with SEPA standards. The Banque de France has started a preliminary evaluation of this new system. The complete evaluation will take place following the effective migration of all of the exchanges processed by SIT to the system managed by STET.

## **2|3 The other tasks specific to the Banque de France**

### **2|3|1 Services to public administrations**

A second Public Service Contract<sup>16</sup> between the Bank and the State was signed on 8 October 2007 by Jean-Louis Borloo, Minister of Ecology, Energy, Sustainable Development and Territorial Development, Christine Lagarde, Minister of the Economy, Finance and Employment, and the Governor of the Banque de France, Christian Noyer.

The contract took effect on 1 January 2007 and is valid from 2007 to 2009.

### **2|3|2 Data on non-financial corporations**

In 2007, there were three significant events in the area that illustrate the Banque de France's commitment to the service of monitoring companies: recognition

#### **Tasks carried out in the context of relations with public administrations**

*The Public Service Contract signed between the Bank and the State covers a large part of the tasks carried out by the Bank that are not related to European System of Central Banks (ESCB) tasks, in particular:*

- *services to individuals: management of the secretariats of the household debt commissions, management of payment incidents databases, processing of requests to allow individuals to exercise their right of access to banking services;*
- *monitoring of economic developments and labour pools in the regions;*
- *services to regional and local authorities, public economic bodies and administrations.*

#### **Key data for 2007**

- *45,000 technical opinions delivered by commissions for monitoring and granting assistance to companies*
- *around a hundred studies were carried out in the framework of conventions signed with the Délégation interministérielle à l'aménagement et à la compétitivité des territoires (DIACT – Interministerial Task Force for Regional Planning and Competitiveness) or the French Government's agency for industrial innovation "OSEO"*
- *50 agreements were signed with regional and local authorities in order to facilitate the marketing of economic and financial assessments of companies (GEODE) and 285 assessments were carried out within this framework*
- *30 ACSEL (Localised Cyclical and Structural Economic Analysis) analyses were conducted.*

<sup>16</sup> Available in French on the Bank's website ([http://www.banque-france.fr/fr/instit/telechar/histoire/contrat\\_sp.pdf](http://www.banque-france.fr/fr/instit/telechar/histoire/contrat_sp.pdf)).



### Tasks carried out in respect of company data

The Banque de France has managed the FIBEN company database since 1982 to cater for its own needs, those of the Commission bancaire and the banking industry, and to provide company managers with an external assessment of their company's financial position relative to that of other firms.

### Key data for 2007

- Over 5 million entities listed in FIBEN
- 230,000 companies rated on the basis of tax or consolidated statements (4,000 groups)
- Almost 45,000 meetings with company managers

as an external credit assessment institution (ECAI), the marking of FIBEN's 25<sup>th</sup> anniversary and the publication of a special issue of the Bank's monthly bulletin on small and medium enterprises that symbolise the development of studies based on the use of individual company data. These three events form part of the strategy aimed at constantly improving the quality of analysis of the "enterprise" sector.

### The status of external credit assessment institution (ECAI)

Following a decision by the *Commission bancaire* on 19 June 2007, the Banque de France was recognised as an External Credit Assessment Institution. This decision enables credit institutions to use the Banque de France ratings to assess the capital requirements necessary to cover corporate credit risk, using the standardised approach, under the new regulatory framework commonly referred to as "Basel II". This recognition means that the Banque de France rating meets all the international criteria of an effective credit risk assessment framework: objectivity of the method and results, independence of the credit rating body, regular review of ratings, transparency and disclosure, acceptance by the market.

Banque de France credit ratings are a reference tool for company analysis, forming part of a set of information services that the Bank makes available to the banking profession in real time, through FIBEN. Accessible via an effective credit risk assessment system, the

ratings can be easily used by credit institutions both for risk analysis prior to client development or decision-making on individual dossiers and for the monitoring of existing risks or the selection of debt instruments that may ensure monetary refinancing and payment systems. The ratings may now also contribute towards determining regulatory capital requirements.

By attributing a rating to almost all enterprises in the "corporate" category (loans of over EUR 1 million) as well as to a large number in the "retail" portfolio, the Banque de France provides banks that consult the database with the framework necessary for analysing credit risk, as required by regulation.

### The 25<sup>th</sup> anniversary of the FIBEN banking database on companies

The 25<sup>th</sup> anniversary of FIBEN provided the opportunity to recall the many achievements since 1982 in terms of the consultation of the database that vouch for the product's credibility in the eyes of the banking community. FIBEN is a frame of reference, considered as a "market tool", pooling information for the banking community. New information is constantly added to the database, as demonstrated in the field of credit risk data collection; following the lowering of the reporting threshold for corporate bank loans there was an increase in the number of loans compiled in the credit register: 1,930,000 beneficiaries and EUR 1,735 billion in bank loans compared with 1,835,000 beneficiaries and EUR 1,512 billion at end-2006. FIBEN provides value-added services, notably a wide range of information accessible on line to calibrate or contribute to the smooth functioning of banks' internal rating systems.

The very deep and original pool of individual company data that FIBEN constitutes is increasingly used for studies conducted by the Banque de France itself, as well as in co-operation with other central banks such as the ECB in 2007, for example.

### Publication of studies on companies

In 2007, the Banque de France published articles in its Monthly Bulletin recounting the studies conducted on companies, notably the customary analysis on the industrial sector and a study on the impact of IFRS.



The publication in October of a Monthly Bulletin special issue on SMEs was considered to be both an innovation and a notable event. The document, to which several external authors contributed, provides insight into a sector that is arousing considerable expectations due to the potential that SMEs represent in terms of contributing to economic growth, creating jobs and improving external trade balances.

### Reactivation of the Trade Credit Observatory

Since 2006, the Banque de France has been charged with the secretariat of the Trade Credit Observatory, a body that was reactivated by an Order published in the *Journal officiel* of 29 June 2006. Set up in September 2006, the new Observatory's task is to draw up a detailed assessment of the situation regarding payment periods and to analyse the economic impact of the developments observed. Chaired by Jean-Paul Betbèze (director of the Economic Research department at Crédit Agricole and member of the French Council of Economic Analysis), the Trade Credit Observatory brings together players from the economic sphere, administrations with competence in economic and statistical areas and prominent experts. The Observatory's second report was submitted to the French Secretary of State for Foreign Trade on 18 December 2007. Following the proposal that will be made to Parliament in the first half of 2008 to reduce the trade accounts receivable and payable to 60 days, this report will be used as a reference to facilitate the setting up of future sectoral negotiations. In parallel, an impact study on the consequences of such a reduction in trade accounts receivable and payable will be conducted.

### The European dimension

Lastly, the European dimension of this activity takes the form of the Banque de France's role as chair of the BACH group (Bank for Accounts of Companies Harmonized) and its active participation in the European Committee of

Central Balance Sheet Data Offices (ECCB). In the same vein, the Central Credit Register helped to develop data exchange with five other European central credit registers (Belgium, Germany, Italy, Portugal and Spain).

### 2|3|3 The management of the Treasury's account and of payment means on behalf of the Treasury

The main functionalities of the new application for the management of client accounts (EVCLI) have been in the production phase since 3 December 2007. The client internet interface, originally only made available to the *Agence France Trésor*, will gradually be extended to other clients in 2008.

#### **Tasks carried out in the management of the Treasury's account**

*In accordance with the agreement of April 2002 between the State and the Banque de France, the latter:*

- manages the Treasury's central account;
- implements the national and international settlement and collection circuits in euro and foreign currency that make it possible to carry out flow transactions on behalf of Treasury accountants;
- manages all these services, while complying with the quality and risk control indicators laid down in the agreement.

#### **Key data for 2007**

*Transactions performed on behalf of the State:*

- 175 million cheques collected
- 301 million direct debits presented
- 250 million credit transfers initiated

### 2|3|4 Services provided in the area of relations between private agents and the financial sphere

#### National payment incident databases

The management and promotion of the FNCI, which were outsourced to an external company following a European tender procedure, have been under the new designation Vérifiance-FNCI-Banque de France (to replace Resist) since 1 January 2007.

#### Overindebtedness

In 2007, the number of applications to the household debt commissions fell slightly (by 1%) while remaining at a high level. The average debt per application was EUR 32,900 at end-December 2007, bearing in mind that

#### Tasks carried out in database management

The Banque de France manages the household payment incident databases:

- the Fichier national des incidents de remboursement des crédits aux particuliers (FICP – National Register of Household Credit Repayment Incidents), which records clear-cut payment incidents related to credit granted to natural persons as well as measures for handling cases of household overindebtedness;
- the Fichier central des chèques (FCC – Central Cheque Register) records clear-cut payment incidents related to the use of cheques, with the aim of improving the security of payment instruments; within the framework of an agreement with the bank card consortium, the Banque de France also manages the database of bank card incidents;
- the Fichier national des chèques irréguliers (FNCI – National Register of Irregular Cheques), which compiles and disseminates data, particularly on stolen or lost cheques, to merchants and service providers seeking to verify the validity of cheques.

#### Key data for 2007

- 65 million consultations of the FCC
- 2.35 million individuals registered in the FICP
- 167 million consultations of the FNCI

#### Other tasks carried out in respect of relations with private individuals

The Banque de France carries out a number of tasks that are entrusted to it for the most part by law:

- since 1990, it has provided the secretariat for the household debt commissions. The commissions, of which at least one was set up in each of France's départements, are charged with finding solutions to the problems encountered by private individuals who have incurred excessive debts or who experience a drop in income as a result of unforeseeable events;
- it processes requests to allow individuals to exercise their right of access to banking services, which entitles all persons domiciled in France without a deposit account to open such an account;
- it provides the secretariat for the Banking Mediation Committee, which is chaired by the Governor and is responsible for supervising the mechanism set up in 2003 and drafting an annual report on mediation;
- it performs administrative duties for the Comité consultatif du secteur financier (CCSF – Advisory Committee on the Financial Sector) which is charged with studying issues associated with relations between credit institutions, insurance companies and investment firms and their respective clients, and with proposing appropriate measures in this area in the form of either opinions or general recommendations;
- it helps to inform private individuals about banking regulations and practices via its "Infobanque" service;
- it manages the database on banking and financial sales activities on behalf of the Autorité des marchés financiers (AMF – Financial Markets Authority), the Comité des établissements de crédit et des entreprises d'investissement (CECEI – Credit Institutions and Investment Firms Committee) and the Autorité de contrôle des assurances et des mutuelles (ACAM – Insurance Supervisory Authority).
- it monitors the microcredit activity of businesses and individuals for the Observatory for Micro-Finance, created in September 2006, and contributes to the analysis and development of its practices.

#### Key data for 2007

- 183,000 cases submitted to the household debt commissions
- 30,500 applications for access to banking services

housing loans are included in 7% of the applications, loans with short-term maturities (personal loans, loans extended for the financing of a specific item) are in 42% of them and loans without maturities (overdrafts, revolving loans) are in 86%.

In 2007, the Banque de France continued to publish the overindebtedness barometer, thus fulfilling a commitment made as part of the Public Service Contract concluded with the State. This barometer, developed within the framework of a consultation process conducted in collaboration with the *Comité consultatif du secteur financier* (CCSF – Advisory Committee on the Financial Sector), consists of a set of representative indicators enabling developments with regard to overindebtedness to be measured.

Moreover, the average processing time of the out-of-court settlement phase by the household debt commissions' administration stood at 3.5 months at end-2007, which is less than the maximum specified in the public service contract (4 months). Lastly, a new application for processing cases of overindebtedness was implemented throughout the Banque de France's branch network during 2007, thus providing the commission secretariats with a more ergonomic and high-performance tool with which to process cases.

### **Access to banking services**

Since April 2006 and notably following on from the work carried out under the aegis of the CCSF, private individuals may now authorise the credit institution that has turned down their application to communicate to the Banque de France their request for access to banking services. This enhanced access to the procedure goes hand in hand with the commitment

made by the Banque de France to designate – within the space of a working day – the credit institution that should open the account.

### **Informing private individuals and banking mediation**

An information helpline, reached on 0811 901 801, was set up in January 2007; it enables individuals to obtain information concerning banking and credit regulations, overindebtedness and access to payment incident databases.

As part of the supervision of the banking mediation framework, the Banque de France pursued its action in favour of extending the mediators' field of competence; this resulted in the adoption by parliament of a relevant article included in Act 2208-3 of 3 January 2008 on the development of competition for the benefit of consumers. Under the terms of this text, bank mediators now have the jurisdiction, not only in disputes related to the management of deposit accounts, grouped sales or sales with premiums, but also in all disputes relative to services provided and the execution of contracts signed for credit transactions, savings and financial investment products, on the condition that these disputes are in connection with credits granted to individuals for non-professional purposes.

The *Bilan de la médiation bancaire* (report on banking mediation) as well as a directory of contact addresses for mediators, which is regularly updated, can be consulted on the French language version of the Banque de France's website ([www.banque-france.fr](http://www.banque-france.fr), under the headings *organisation et activités/services rendus/protection du consommateur/médiation bancaire/Répertoire des adresses de saisine des médiateurs*).



**Storage of banknotes in the vault**



# THE ACCOUNTS OF THE BANQUE DE FRANCE

## I | Report on assets, liabilities and results

The accounts for the year ended 31 December 2007 were approved by the General Council at its meeting of 21 April 2008. With net profit of EUR 2,317 million, representing an increase of 86%, the Bank's net income reached an exceptional level. This improvement resulted, on the one hand, from efforts to control operating costs, and on the other, from the sharp rise in monetary income in euro.

*In the interests of clarity, this section discusses aggregated balance sheet and profit and loss items extracted from the published accounts, which are presented in accordance with the Order of the Minister of Economy, Finance and Industry of 7 February 2000 (see below). Details of the accounting principles applied by the Banque de France are provided in the Notes to the annual accounts.*

## I | I Assets and liabilities

In 2007, the financial position of the Banque de France improved further, mainly thanks to the increase in net sources of funds from banknote operations, which were up by EUR 8.7 billion from one year-end to the next.

### Financial position

No sign: net source of funds (liability); minus sign: net asset position.  
(EUR millions)

	Outstanding amounts at 31/12		Change 2007/2006
	2007	2006	
Net sources of funds from banknote operations	127,167	118,431	8,736
Gold and net foreign exchange position	-33,124	-29,384	-3,740
Net position with credit institutions, the ESCB and the ECB	-65,088	-72,029	6,941
Euro-denominated portfolios	-44,405	-29,491	-14,914
Net position with customers	9,397	7,304	2,092
Other transactions	6,052	5,169	884
<b>Total</b>	<b>0</b>	<b>0</b>	<b>0</b>

These additional sources of funds contributed to a significant increase in the amount of euro-denominated assets, which advanced by EUR 14.6 billion from one year-end to the next.

Gold and foreign exchange assets (net of revaluation accounts) also grew, but to a lesser extent, with purchases of foreign currency during the year more than offsetting the further sales of gold.

## I | I | Net sources of funds from banknote operations

### Net sources of funds from banknote operations

(Year-end amounts, EUR millions)

	2007	2006	Change 2007/2006
Banknotes put into circulation by the Banque de France	62,142	57,182	4,960
Adjustment to the allocation mechanism based on the ECB's capital key	77,914	73,502	4,412
Allocation of 8% of banknotes to the ECB	-11,204	-10,455	-749
Banknotes in circulation allocated to the Banque de France (balance sheet item PI)	128,852	120,229	8,623
Advance to the IEDOM	-2,680	-3,066	386
<b>Net sources of funds from banknote operations (euro banknotes)</b>	<b>126,172</b>	<b>117,163</b>	<b>9,009</b>
<b>French franc banknotes</b>	<b>995</b>	<b>1,267</b>	<b>-272</b>

### Euro banknotes

Since the introduction of euro banknotes at the start of 2002, 92% of the total amount of euro banknotes in circulation has been allocated at each month-end between each of the national central banks (NCBs) in the Eurosystem in proportion to its subscription to the capital of the European Central Bank (ECB).

Having rapidly returned to the levels seen prior to the introduction of euro banknotes, the amount issued by the Eurosystem has grown at a pace which is gradually declining but is nonetheless still firm (annual average of 8.9% in 2007, compared with 11.2% in 2006).



Under the formula for allocating banknotes between euro area NCBs, this growth was reflected in a year-on-year increase of EUR 8.6 billion in net sources of funds from euro banknote operations in the accounts of the Banque de France.

The share of euro banknotes allocated to the Banque de France is substantially higher than net issues of euro banknotes carried out by the Bank. The difference constitutes a claim on the ESCB (balance sheet item A8.3), which bears interest at the marginal rate applied to main refinancing operations. The size of this adjustment reflects a number of factors, including the inflow of banknotes into France as a result of tourism and the fact that demand from outside the euro area is to a fairly large extent met by other NCBs in the Eurosystem.

The IEDOM is the Banque de France's correspondent responsible for managing banknote circulation in the overseas departments and in the departmental unit of Mayotte and the territorial unit of St Pierre and Miquelon. It receives a non interest-bearing advance in return for the notes it distributes in the name of and on behalf of the Banque de France. The amount of this advance, which was previously set at 3% of France's euro banknote allocation, has since 1 July 2007 been calculated according to the allocation mechanism in force within the Eurosystem, which resulted in a EUR 386 million fall in this amount from one year-end to the next. This advance is eliminated in the Banque de France/IEDOM combined accounts.

### French franc banknotes

French franc banknotes not yet handed in to the Banque de France constitute a purely domestic source of funds, classified as a miscellaneous liability (balance sheet item P11). At end-December, French franc banknotes represented a liability of EUR 995 million, a fall of EUR 272 million compared with end-2006 owing to notes handed in to the Banque de France, and in particular to the repayment to the State of the balance of FRF 500 banknotes that had not been returned to the Bank by the end of legal tender for these banknotes (February 2007).

## 11|2 Gold and foreign exchange transactions

The balance sheet items used to record gold and foreign exchange transactions were affected by the

large fluctuations in exchange rates from one year-end to the next.

### Gold and foreign exchange transactions

Gold and foreign exchange transactions			
(Year-end amounts, EUR millions)			
	2007	2006	Change 2007/2006
<b>Assets</b>	<b>94,539</b>	<b>82,404</b>	<b>12,134</b>
Gold	47,558	42,210	5,348
Foreign exchange assets and investments	45,533	38,391	7,142
Relations with the IMF	1,448	1,804	-356
<b>Liabilities</b>	<b>61,415</b>	<b>53,021</b>	<b>8,394</b>
<b>External liabilities</b>			
Foreign exchange liabilities	11,874	7,580	4,294
Counterpart to SDR allocations	1,167	1,241	-74
<b>Revaluation reserves</b>			
Revaluation accounts (gold, foreign exchange assets and securities denominated in foreign currencies)	26,971	21,117	5,854
Revaluation reserve of State gold reserves	18,499	20,034	-1,535
Revaluation reserve of State foreign exchange reserves	2,904	3,049	-145
<b>Total gold and foreign exchange</b>	<b>-33,124</b>	<b>-29,384</b>	<b>-3,740</b>

Year-end revaluation rates			
	Gold (per kg)	US dollar (EUR/USD)	Special Drawing Rights (EUR/SDR)
End December 2006	15,518.8	1.3170	0.8760
End December 2007	18,269.2	1.4721	0.9311

### Gold reserves

Against a backdrop of high gold prices, the Banque de France's gold reserves decreased by 125 tonnes, and at year-end stood at 2,594 tonnes. This reduction reflects the sales carried out in accordance with the agreement reached between 15 European central banks to limit overall gold sales to a maximum of 500 tonnes per year over a five-year period commencing on 27 September 2004. Despite these sales, the sharp rise in gold prices increased the value of

Banque de France gold reserves by EUR 5.3 billion from one year-end to the next.

Following the entry into force of the second rider to the agreement between the State and the Bank, the “revaluation reserve of State gold reserves” is no longer supplemented at each year-end by realised gains on gold sales. The amount of EUR 1,535 million was levied from this reserve in respect of profit realised from sales of gold during the 2004-2006 period, and realised gains totalling EUR 1,078 million on sales of gold in 2007 were assigned to the “revaluation reserve of State foreign exchange reserves”. The gold revaluation account opened on 1 January 1999, which tracks unrealised capital gains from that date, stood at EUR 26.8 billion at year-end.

### Foreign exchange assets and operations with the International Monetary Fund

Net foreign exchange assets increased by EUR 2.8 billion from one year-end to the next owing to the further purchase of foreign exchange assets; this was in spite of the depreciation of the US dollar against the euro.

The claim on the IMF fell to EUR 1.4 billion as a result of reimbursements of financing provided by the IMF on the one hand, and the 6% decline in the exchange rate of Special Drawing Rights (SDRs) against the euro, on the other.

Inter-currency arbitrage and reimbursements of SDRs generated EUR 12 million of net foreign exchange gains, taken to the revaluation reserve of State foreign exchange reserves. Unrealised losses mainly on the US dollar (EUR 2,769 million) were taken to the profit and loss account and covered by drawing on the revaluation reserve of State foreign exchange reserves.

## 1|1|3 Net position with euro area credit institutions and with the ESCB

### Net position with credit institutions

In year-on-year terms, the refinancing secured by credit institutions surged by EUR 57 billion following the exceptional liquidity injections by the ECB in response to pressures on the money market observed since the start of the financial crisis.

### Net position with euro area credit institutions and with the ESCB

(Year-end amounts, EUR millions)

	2007	2006	Change 2007/2006
<b>Assets</b>	<b>74,980</b>	<b>26,497</b>	<b>48,483</b>
Loans granted in the framework of monetary policy operations	71,055	13,695	57,360
Other euro-denominated loans to euro area credit institutions	3,925	2,149	1,776
Intra-ESCB TARGET accounts	0	10,653	-10,653
<b>Liabilities</b>	<b>85,773</b>	<b>26,396</b>	<b>59,377</b>
Current accounts of banks	73,698	26,378	47,320
Other deposits from euro area credit institutions	40	18	22
Intra-ESCB TARGET accounts	12,035	0	12,035
<b>Net position with credit institutions</b>	<b>10,793</b>	<b>-101</b>	<b>10,894</b>
Claim on the Eurosystem for banknotes in circulation	67,312	63,452	3,860
Claim on the ECB for foreign exchange assets transferred	8,569	8,476	93
Other net positions with the ESCB	-75,881	-71,928	-3,953
<b>Net position</b>	<b>-65,088</b>	<b>-72,029</b>	<b>6,941</b>

In this environment, the current accounts of credit institutions posted a sharp rise at year-end. French banks also became net lenders towards the rest of the euro area to the tune of EUR 12 billion, as reflected in intra-ESCB accounts used to record transactions processed through TARGET. The Bank's previous net lending position with credit institutions switched to a net borrowing position amounting to EUR 10.8 billion.

### Other net positions with the Eurosystem

This comprises (i) the claim arising on the ESCB for the difference between banknotes put into circulation by the Banque de France and the banknotes allocated to the Banque de France under the allocation mechanism defined within the Eurosystem (see “Net sources of funds from banknote operations”) and (ii) the claim arising from foreign exchange assets transferred to the ECB, which is denominated in euro and of which 85% bears interest (to take account of the non-interest bearing 15% corresponding to a gold transfer). Both claims are remunerated at the marginal rate applied to Eurosystem main refinancing operations.

## 1|1|4 The Banque de France's euro-denominated portfolios

Euro-denominated portfolios			
(Year-end amounts, EUR millions)			
	2007	2006	Change 2007/2006
<b>Euro-denominated monetary portfolios</b>	<b>40,365</b>	<b>25,773</b>	<b>14,592</b>
Available-for-sale	14,504	8,222	6,282
Held-to-maturity	25,861	17,552	8,309
<b>Own funds investment portfolio</b>	<b>4,040</b>	<b>3,717</b>	<b>323</b>
Available-for-sale	1,741	1,644	97
Held-to-maturity	1,058	832	225
Participating interest in the ECB	836	835	1
Other participating interests	405	405	0
<b>Euro-denominated securities</b>	<b>44,405</b>	<b>29,491</b>	<b>14,914</b>

### Euro-denominated monetary portfolios<sup>1</sup>

The increase of EUR 14.6 billion in 2007 reflects the management framework adopted by the Eurosystem in 2003, which allows NCBs to build up their portfolios within annually-reviewed limits.

### Own funds investment portfolios

These portfolios, which stood at EUR 4 billion at end-December showed an increase on account of the expansion of own funds resulting from decisions regarding the appropriation of 2006 profits.

following a reimbursement by the Treasury. However, the balance on the Treasury's account rose to EUR 310 million at end-December.

### Other operations with institutional customers

Operations with institutional customers, primarily central banks from outside the euro area who use the Banque de France to invest some of their foreign exchange reserves, posted a very sharp increase, notably due to the impact of the financial crisis on the markets. Institutional customers' deposits and the investments they are used to back are recorded in dedicated accounts.<sup>2</sup>

Operations with institutional customers			
(Year-end amounts, EUR millions)			
	2007	2006	Change 2007/2006
<b>Assets</b>	<b>62,330</b>	<b>13,746</b>	<b>48,584</b>
Advance in respect of coins	42	82	-40
Other advances to the French Treasury	0	0	0
Euro-denominated claims on non-euro area residents	2,257	2,303	-46
Other banking operations	60,031	11,361	48,670
<b>Liabilities</b>	<b>71,726</b>	<b>21,050</b>	<b>50,676</b>
French Treasury current account	310	235	74
Euro-denominated deposits from euro area residents (other than the French Treasury)	10,737	8,175	2,562
Euro-denominated deposits from non-euro area residents	3,981	4,263	-282
Other banking operations	56,699	8,377	48,322
<b>Net position with customers</b>	<b>9,397</b>	<b>7,304</b>	<b>2,092</b>

## 1|1|5 Operations with institutional customers

### Operations with the French Treasury

The advance in respect of coins diminished by EUR 40 million from one year-end to the next

## 1|1|6 Other transactions

The net balance on other transactions at 31 December 2007 was EUR 6,053 million. The year-on-year increase of EUR 884 million can largely be attributed to the EUR 1,072 million rise in net profit.

<sup>1</sup> From an accounting standpoint, this aggregate item comprises balance sheet item A7 "Euro-denominated fixed-income securities" which consists of the Bank's available-for-sale portfolios and the portion of A11 "Other euro and foreign currency denominated financial assets" consisting of the euro-denominated held-to-maturity portfolio. Available-for-sale portfolios are stated net of revaluation accounts, which are shown on the liabilities side of the balance sheet in item P13.2.

<sup>2</sup> See note 28 of the Notes to the annual accounts.

## Other transactions

(Year-end amounts, EUR millions)

	2007	2006	Change 2007/2006
<b>Assets</b>	<b>5,307</b>	<b>4,512</b>	<b>796</b>
Other claims on the Eurosystem	49	31	19
Miscellaneous assets	4,362	3,618	744
Fixed assets	896	863	33
<b>Liabilities</b>	<b>11,359</b>	<b>9,682</b>	<b>1,677</b>
Items in course of settlement	574	364	210
Miscellaneous liabilities	3,693	3,698	-5
Other provisions for liabilities and charges	675	577	98
Accelerated tax depreciation on fixed assets	63	48	15
Fund for general risks	670	550	120
Capital, reserves and retained earnings	3,367	3,198	169
Net profit for the year	2,317	1,246	1,071
<b>Net balance of other transactions</b>	<b>6,052</b>	<b>5,169</b>	<b>883</b>

## Net income on activities

(EUR millions)

	2007	2006	Change 2007/2006
<b>Net income on activities of the Banque de France</b>	<b>5,644</b>	<b>3,937</b>	<b>1,707</b>
Euro monetary income	3,264	2,021	1,243
Income from refinancing of the banking system	1,187	814	374
Pooling of monetary income	2,272	1,335	937
Income from available-for-sale and held-to-maturity portfolios	1,096	685	412
Interest on claims arising on transfer of reserve assets to the ECB	281	201	80
Interest paid on minimum reserves	-1,414	-904	-511
Other interest-bearing accounts	-159	-109	-49
Foreign currency monetary income	1,714	1,339	375
ECB and IEDOM dividends	50	28	22
Net profit from non-monetary activities	616	548	68

## I | 2 Results

Net profit for the year ended 31 December 2007, which posted a strong increase compared to 2006, was EUR 2,317 million, its highest level since the early 1980s.

### I | 2 | 1 Net income on activities

Monetary income on euro and foreign exchange transactions accounts for nearly 90% of net income on activities of the Banque de France, which amounted to a total of EUR 5,644 million in 2007. Overall, it rose by EUR 1,618 million to reach EUR 4,978 million. Non-monetary income increased by EUR 68 million to EUR 616 million.

### I | 2 | 2 Euro monetary income

Monetary income from euro transactions is the biggest component of income for the Banque de France. It represents the excess of income derived from euro monetary assets (refinancing of the banking system, securities portfolios, pooling of Eurosystem monetary income) over the interest paid on deposits from credit institutions, mainly comprising minimum reserves. Net monetary income rose by EUR 1,243 million to EUR 3,264 million.

This marked increase was due to a rise in income from the allocation of monetary income by the Eurosystem (interest on intra-ESCB balances corresponding to adjustments to banknotes in circulation – see above – and net result of pooling of monetary income<sup>3</sup>),

<sup>3</sup> The net result of the pooling of monetary income is the final component of the mechanism for the monthly adjustment of the claim arising on the Eurosystem for banknotes issued; it takes account of intra-month trends in banknote circulation, deposits made by credit institutions, and income actually derived from monetary policy operations. In the case of the Banque de France, the pooling of monetary income generated additional income of EUR 49 million, an increase of EUR 18 million relative to 2006.

to bank refinancing and to extra income generated by the available-for-sale and held-to-maturity portfolios. This performance reflects a combination of larger volumes of interest-bearing investments and higher euro area short-term interest rates; over 2007 as a whole, the average interest rate on main refinancing operations was 3.94%, compared with 2.82% in 2006.

### Foreign currency monetary income

Foreign currency monetary portfolios generated income of EUR 1,714 million, an increase of EUR 375 million over the 2006 figure.

This increase was attributable partly to the expansion of the Bank's portfolios, but also to a better rate of return on these assets, with short-term dollar-denominated investments benefiting from the fact that the high level of interest rates reached in 2006 continued during the first three quarters of 2007.

### ECB and IEDOM dividends

The ECB used the total profit generated in 2006 and 2007 to consolidate its provision for currency and interest rate risks. Consequently, no dividend was paid in 2007 and no interim dividend in respect of ECB seigniorage income was paid to the Banque de France.

The dividend paid by the IEDOM in 2007 in respect of the year ended 31 December 2006 rose to EUR 50 million, an increase of EUR 22 million.

### Net profit from non-monetary activities

Non-monetary activities recorded a net profit of EUR 616 million, an increase of EUR 68 million compared to the previous year.

The increase was mainly due to other income from services (which was up by EUR 57 million), including the sale of goods to other central banks (exports of banknotes other than euro banknotes), financial intermediation services for international institutions, and provision of services to commercial banks (including management of payment media and databases). This rise was partly offset by the fall in income from the provision of services to the State, which declined by EUR 9 million.

Income from the portfolios in which the Bank's own funds and the Employee Reserve Fund are invested

totalled EUR 225 million, an increase of EUR 20 million compared to the previous year.

## 1|2|3 Operating expenses

Operating expenses			
(EUR millions)			
	2007	2006	Change 2007/2006
<b>Operating expenses</b>	<b>-1,850</b>	<b>-1,776</b>	<b>-73</b>
Exceptional expenses	-156	-61	-95
Provision for tax adjustment	3	-61	64
New provisions	-159	0	-159
Personnel and related expenses	-1,345	-1,341	-4
Taxes other than income tax	-34	-31	-3
Provisions, depreciation and amortisation	-115	-115	0
Capitalised production	62	50	12
Other operating expenses	-263	-279	17

If the exceptional expenses linked to the creation of new provisions for social purposes and the partial release of the provision for tax exposures made in 2006 are excluded, operating expenses were down by 1.2% on the previous year and stood at EUR 1,694 million.

Overall, personnel expenses are stable. The savings made in personnel expenses relating to the current workforce as a result of the reform of the Banque de France's branch network were offset by a corresponding increase in pension-related expenses.

Depreciation and amortisation expenses were unchanged in 2007, at EUR 115 million.

Capitalised production costs rose by EUR 12 million reflecting the stepping-up of efforts to meet delivery deadlines for several major IT projects.

Other operating expenses were down by EUR 17 million. This fall resulted from progressive releases notably from the provision for the restructuring of the branch network, and was partly offset by the rise in IT expenditure and an increase in purchases of commodities for banknote manufacturing. At a structural level, the reduction in the number of Banque de France branches that occurred in 2004-2006 has significantly contributed to cutting overheads.



## 1|2|4 Profit for the year

Main profit and loss account balances			
(EUR millions)			
	2007	2006	Change 2007/2006
Net income on activities of the Banque de France	5,644	3,937	1,707
Operating expenses	-1,850	-1,776	-73
Profit before tax and exceptional items	3,794	2,160	1,634
Net transfer to fund for general risks and accelerated tax depreciation	-135	-160	25
Exceptional items	54	53	1
Corporate income tax	-1,396	-807	-589
<b>Profit for the year</b>	<b>2,317</b>	<b>1,246</b>	<b>1,072</b>

An exceptional gain of EUR 54 million was recorded in 2007. As in 2005 and 2006, it comprises gains on the disposal of property vacated as a result of the reform of the Bank's branch network.

After an additional contribution of EUR 120 million made to the fund for general risks and an accelerated tax depreciation charge of EUR 15 million, and after a corporate income tax charge of EUR 1,396 million, net profit for the year ended 31 December 2007 amounted to EUR 2,317 million.

After retained earnings of EUR 0.6 million, the profit available for appropriation was EUR 2,318 million.

At its meeting of 21 April 2008, the General Council of the Banque de France examined the accounts for 2007 and decided on the appropriation of profits. One such appropriation is automatic, as it results from the legal requirements applying to the Banque de France: 5% of the net profit for the year, representing an amount of EUR 115.9 million, must be appropriated to the reserve established pursuant to Article 28 of the Decree of 3 December 1993.

In accordance with the methods for financing the pension obligations defined as part of the reform of the Banque de France pension scheme, the General Council decided, on the one hand, to appropriate EUR 126 million to the Employee Reserve Fund in order to cover the pension entitlements acquired by employees over the past year, and, on the other, to allocate EUR 337 million to a special pension reserve.

The dividend paid to the State amounted to EUR 1,739 million.

The remaining EUR 0.1 million was carried forward as retained earnings.



**Delivery of secure bags by security carriers**

## 2| Annual accounts of the Banque de France

### 2| I Balance sheet and profit and loss account

Balance sheet at 31 December 2007				
(EUR millions)				
Notes to annual accounts		ASSETS	2007	2006
1	A1	Gold	47,557	42,210
2	A2	Foreign exchange assets (excl. relations with the IMF)	37,896	36,002
		2.1 Foreign exchange assets held with non-euro area residents	23,856	28,606
		2.2 Foreign exchange assets held with euro area residents	14,040	7,396
3	A3	Relations with the IMF	1,448	1,804
		3.1 Financing provided to the IMF	768	1,080
		3.2 Acquisitions of Special Drawing Rights	680	724
5	A4	Euro-denominated claims on non-euro area residents	2,257	2,303
4	A5	Euro-denominated loans to euro area credit institutions in the framework of monetary policy operations	71,055	13,695
5	A6	Other euro-denominated loans to euro area credit institutions	3,925	2,149
6	A7	Euro-denominated fixed-income securities	14,511	8,222
	A8	Relations within the Eurosystem	76,766	83,447
		8.1 Participating interest in ECB	836	835
7		8.2 Claims arising on the transfer of reserve assets to the ECB	8,569	8,476
8		8.3 Claims on the Eurosystem for euro banknotes in circulation	67,312	63,452
9		8.4 Other claims on the Eurosystem	49	10,684
10	A9	Advance to the IEDOM	2,680	3,066
11	A10	Claims on the French Treasury	42	82
12	A11	Other euro and foreign currency denominated financial assets	97,312	34,541
13	A12	Miscellaneous	3,959	3,373
14	A13	Fixed assets	1,301	1,269
		13.1 Tangible and intangible assets	896	863
		13.2 Participating interests (other than interest in the ECB)	405	405
<b>TOTAL ASSETS</b>			<b>360,707</b>	<b>232,162</b>
Notes to annual accounts		LIABILITIES	2007	2006
15	P1	Banknotes in circulation	128,852	120,229
4	P2	Euro-denominated liabilities to euro area credit institutions in the framework of monetary policy operations	73,698	26,378
		2.1 Current accounts	49,261	26,377
		2.2 Other liabilities	24,437	1
	P3	Other euro-denominated liabilities to euro area credit institutions	40	18
16	P4	Euro-denominated liabilities to non-euro area residents	10,737	8,175
2	P5	Foreign exchange liabilities	11,874	7,580
3	P6	Counterpart to SDR allocations	1,167	1,241
17	P7	Relations within the Eurosystem	12,035	0
18	P8	Euro-denominated liabilities to other euro area residents	4,290	4,498
		8.1 Treasury's account	309	235
		8.2 Other liabilities	3,981	4,263
19	P9	Items in course of settlement	574	364
20	P10	Banking transactions	54,366	8,377
21	P11	Miscellaneous	7,021	4,965
22	P12	Provisions for liabilities and charges	675	577
23	P13	Revaluation accounts	27,558	21,633
	P14	Fund for general risks and accelerated tax depreciation	733	598
24	P15	Revaluation reserve of State gold reserves	18,499	20,034
24	P16	Revaluation reserve of State foreign exchange reserves	2,904	3,049
25	P17	Capital, reserves and retained earnings	3,367	3,198
	P18	Profit for the year	2,317	1,246
<b>TOTAL LIABILITIES</b>			<b>360,707</b>	<b>232,162</b>

## 2007 Profit and loss account

(EUR millions)

Notes to annual accounts			2007	2006
	<b>1.</b>	<b>Net income on activities of the Banque de France</b>	<b>5,644</b>	<b>3,937</b>
30	1.1.	Net interest income	4,973,	3,501
	1.1.1.	Interest and related income	8,464,	5,293
	1.1.2.	Interest and related expenses	-3,491	-1,792,
31	1.2.	Net income/loss on financial transactions	54	-94
	1.2.1.	Net of realised gains/losses and and unrealised losses on foreign exchange	-1,679	899
	1.2.2.	Net of charges to/releases from foreign exchange revaluation reserves	1,679	-899
	1.2.3.	Net of other income and expenses on financial transaction	54	-94
	1.3.	Commission	6	4
	1.3.1.	Commission (income)	54	49
	1.3.2.	Commission (expense)	-48	-45
32	1.4.	Income from equity securities and participating interests	105	69
33	1.5.	Net result of pooling of monetary income	49	31
34	1.6.	Net of other income and expenses	458	425
	<b>2.</b>	<b>Operating expenses</b>	<b>-1,850</b>	<b>-1,776</b>
35	2.1.	Personnel and related expenses	-1,345	-1,341
	2.2.	Taxes other than income tax	-34	-31,
	2.3.	Provisions, depreciation and amortisation	-115	-115
	2.4.	Net of other operating income and expenses	-356	-290
		<b>Profit before tax and exceptional items (1 + 2)</b>	<b>3,794</b>	<b>2,161</b>
	<b>3.</b>	<b>Net charge to the fund for general risks and accelerated tax depreciation</b>	<b>-135</b>	<b>-160</b>
36	<b>4.</b>	<b>Extraordinary items</b>	<b>54</b>	<b>53</b>
	4.1.	Extraordinary income	54	53
	4.2.	Extraordinary charges		
37	<b>5.</b>	<b>Corporate income tax</b>	<b>-1,396</b>	<b>-807</b>
		<b>Profit for the year (1 + 2 + 3 + 4 + 5)</b>	<b>2,317</b>	<b>1,246</b>

## 2|2 Notes to the annual accounts

### 2|2|1 Accounting principles and valuation methods

#### Legal framework

The annual accounts of the Banque de France are presented in accordance with the Order of the Minister of the Economy, Finance and Industry of 7 February 2000. Their structure is designed to reflect the specific nature of the tasks carried out by the Bank within the framework of the ESCB and its diverse range of activities. The accounts are expressed in millions of euro.

The accounting and valuation methods applied by the Banque de France are defined in Article R 144-6 of the Monetary and Financial Code, which specifies that:

- The Banque de France must comply with the accounting and valuation methods laid down by the Governing Council

of the ECB in its 10 November 2006 Guideline for all activities carried out within the framework of the ESCB. This Guideline establishes in particular the accounting rules applicable to refinancing operations for the banking sector, securities, foreign currency transactions carried out in the course of foreign exchange reserve management, and the issue of banknotes.

- The accounting rules established by the *Comité de la réglementation comptable* (CRC – Accounting Regulations Committee) apply to all the other activities of the Bank. However, the Bank's General Council may, after consulting with the Monetary Policy Council (*Conseil de la politique monétaire* – CPM), also decide to apply the accounting and valuation rules recommended by the ECB to its other activities.

With effect from 1 January 2003, the Banque de France has extended the accounting methods laid down by the Governing Council of the ECB in its 5 December 2002 Guideline to cover the securities portfolios recorded in asset item A11 (since replaced by the Guideline of 10 November 2006).

## Valuation methods

### Foreign exchange gains/losses

Spot and forward purchases and sales of foreign currencies are recorded in off-balance sheet accounts at the trade date. They are recognised in the balance sheet at the settlement date.

#### *Foreign exchange gains/losses on State gold and currency reserves*

Realised gains/losses are computed for each currency. Every day, a weighted average price is calculated, firstly on inflows (spot or forward purchases on the trade date and income in foreign currencies, in particular daily accrued interest), and secondly on outflows (spot or forward sales on the trade date and expenses in foreign currencies, in particular accrued interest in foreign currencies). The realised gain/loss is calculated by applying the difference between these average prices to the lower of the day's inflows or outflows.

Where outflows exceed inflows, a second realised gain/loss is calculated, equating to the difference between the net outflows of the day valued at the average outflow price on the one hand, and at the average price of the day's opening position on the other. Where inflows exceed outflows, the net inflow is added to the assets held at the beginning of the day, thus changing the average price of the position.

Gold and foreign exchange positions are valued at year-end on the basis of the rates/prices prevailing on the last business day of the year. Unrealised gains are recorded as liabilities in revaluation accounts (item P14). Unrealised losses are taken to the profit and loss account in item 1.2.1. Unrealised gains and losses are not netted.

#### *Revaluation reserve of State gold reserves and revaluation reserve of State foreign exchange reserves*

In order to neutralise the impact on the Bank's profit and loss account of realised gains and losses and of unrealised losses at year-end, the 31 March 1999 agreement between the State and the Banque de France on management of and accounting for State foreign exchange reserves (as supplemented by the rider dated 26 November 2002) requires the impact to be cancelled out by debiting or crediting the profit and loss account, with the matching entry posted

to the revaluation reserve of State foreign exchange reserves or the revaluation reserve of State gold reserves. However, the amount of net foreign exchange gains taken to the revaluation reserves is limited to the net profit for the year before the transfer to the reserves.

Furthermore, with effect from 31 December 2007, pursuant to the rider of 27 December 2007, net foreign exchange gains realised from sales of gold are allocated to the revaluation reserve of State foreign exchange reserves. This rider also stipulates that foreign exchange gains realised from sales of gold during the 2004-2006 period be transferred from the revaluation reserve of State gold reserves to the revaluation reserve of State foreign exchange reserves.

### Other foreign exchange gains/losses

The Banque de France applies Regulation 89-01 of the *Comité de la réglementation bancaire et financière* (CRBF – Banking and Financial Regulation Committee) to foreign exchange operations that are not connected to its main responsibilities. Foreign currency deposits and investments are marked to market on the last business day of the year. Realised and unrealised foreign exchange gains and losses are posted to the profit and loss account in item 1.2.3 "Net of other income and expenses on financial transactions". Accrued income and expenses are converted into euro at the rate prevailing on the day the transaction is recorded. Forward foreign exchange hedges are valued at the closing date exchange rate.

### Securities portfolio (excluding pension fund)

The Banque de France holds held-to-maturity securities, shown in asset item A11. These are fixed-income securities which the Banque de France has decided to retain to maturity, and which it is able to retain to maturity. Unrealised gains and losses on these securities are therefore not recognised in the accounts.

Other fixed-income securities are shown in either asset item A2 or asset item A7, depending on whether they are (i) securities denominated in foreign currencies held in connection with foreign exchange reserve management, or (ii) euro-denominated securities. The only exception concerns securities linked to the Bank's own funds, included in asset item A11.

Variable-yield securities are recorded in item A11.



Gains and losses on disposals of fixed-income securities not held to maturity, and on variable-yield securities, are calculated on the basis of the weighted average cost of each line of securities. At the end of the year, securities are marked to market line-by-line on the last business day of the year. Unrealised gains are recorded as liabilities in revaluation accounts (item P14). Unrealised losses are booked as expenses on financial transactions (profit and loss account item 1.2.3). Unrealised gains and losses are not netted.

For all fixed-income securities, differences between the acquisition and redemption price are spread over the remaining life of the securities on a discounted basis.

The valuation methods used for securities held in connection with the pension reserve fund of Banque de France employees are described in the section on the pension scheme below.

#### **Forward financial instruments**

Interest rate forward financial instruments traded on organised markets are recorded off-balance sheet at the notional amount, while daily margin calls paid or received are recognised in the profit and loss account.

Interest rate swaps, denominated in foreign currencies and in euro, are revalued at market value at 31 December. Unrealised gains are recorded as liabilities in revaluation accounts and unrealised losses taken to the Bank's profit and loss account amortised over the remaining life of the contract. The interest is recorded in the profit and loss account on an accruals basis.

Currency option premiums are recorded on the asset side of the balance sheet if they relate to currency purchases and on the liabilities side if they relate to currency sales. In the event that the option is exercised, the premium is included in the price of the currency purchased. If the option is not exercised, at its expiry date the premium is recorded in item 1.2.1 of the profit and loss account "Net balance of foreign exchange realised gains and losses and unrealised losses".

Open positions on currency options at the balance sheet date are valued at their market price. Unrealised

gains are recorded as liabilities in revaluation accounts and unrealised losses taken to item 1.2.1 of the profit and loss account "Net balance of foreign exchange realised gains and losses and unrealised losses".

#### **Tangible and intangible fixed assets**

Tangible and intangible fixed assets are accounted for and valued in accordance with CRC regulations.

Land is valued at acquisition cost. Buildings and equipment are carried at historical cost, less depreciation or provisions for impairment set up since they were brought into service. Costs incurred in developing computer applications intended to be used over a number of years are capitalised using the following method: project management and ownership costs are recorded in the profit and loss account as operating expenses; an intangible asset of the same amount is recognised in the balance sheet, but cancelled out by a matching credit recorded under profit and loss item 2.4 "Net of other operating income and expenses".

In accordance with Article 322-1 of the French General Chart of Accounts (*Plan Comptable Général* – PCG), the depreciation period for each asset is determined on the basis of its probable useful life. Components of the Bank's property assets are depreciated over 50, 33, 20 or 10 years, depending on the type of asset. Computer equipment is depreciated over 4, 5 or 10 years, and most other equipment over periods ranging from 2 to 10 years. Purchased software is amortised over 3 or 5 years. All fixed assets are depreciated using the straight line method.

The Banque de France records accelerated tax depreciation for assets that can be depreciated more rapidly for tax purposes than for accounting purposes.

#### **Fund for general risks**

In 1998, the Banque de France set up a fund for general risks to cover any general risks inherent in the activities of a central bank. Charges to and releases from this fund are recorded in the profit and loss account.

#### **Pension scheme**

See note 29.

## Post balance sheet events

### Change in the Banque de France's share in the capital key of the ECB as of 1 January 2008

The entry of Cyprus and Malta on 1 January 2008 into the Eurosystem has once again changed the Banque de France's share of subscribed and paid-up capital of the ECB, which declined from 20.70% to 20.64%.

## 2|2|2 Information on balance sheet, off-balance sheet and profit and loss items

A certain amount of confidential information relating to operations carried out in the exercise of the Banque de France's core tasks is not disclosed, in accordance with decisions taken by the General Council following recommendations by the Monetary Committee of the General Council and pursuant to Article R144-6 of the Monetary and Financial Code.

## Balance sheet

### Note 1: Gold

In 2004, the Eurosystem central banks, the Swiss National Bank and the Sveriges Riksbank renewed the agreement capping their sales of gold. Under the new agreement, entered into for a five-year period commencing on 27 September 2004, annual sales by the 15 central banks may not exceed 500 tonnes.

### Note 2: Foreign exchange assets and liabilities

Foreign exchange reserves are invested in overnight deposits, fixed-term deposits, reverse repo transactions with delivery of securities, and fixed-income securities. The Bank may also borrow foreign currencies in the form of repurchase agreements with delivery of securities, recorded in liability item P5.

The Banque de France also owns fixed-income held-to-maturity securities denominated in foreign currencies. In accordance with standardised Eurosystem accounting rules, these securities are classified in asset item A11.

Claims on euro area residents denominated in foreign currency (item A. 2.2) also comprise dollar-denominated claims, taking the form of securities repurchase agreements, with an amount of EUR 964 million equivalent, vis-à-vis

### Foreign exchange assets and liabilities (excl. relations with the IMF)

Asset item A2 and Liability item P5

(EUR millions)

	2007	2006
<b>ASSETS</b>		
<b>Foreign currency assets</b>		
Overnight deposits	282	28
Fixed-term deposits	6,798	6,374
Securities received under repurchase agreements	14,720	6,416
Fixed-income securities	15,788	22,870
Accrued interest receivable	308	313
<b>Total</b>	<b>37,896</b>	<b>36,002</b>
<b>LIABILITIES</b>		
<b>Foreign exchange liabilities</b>		
Securities delivered under repurchase agreements	11,861	7,565
Accrued interest payable	13	15
<b>Total</b>	<b>11,874</b>	<b>7,580</b>

euro area counterparties in the framework of the dollar-denominated temporary Term Auction Facility. Under this programme, the US Federal Reserve System provided USD 20 billion to the ECB by means of a temporary reciprocal currency arrangement (swap line), with the aim of offering short-term US dollar funding to Eurosystem counterparties. The ECB simultaneously entered into back-to-back swap transactions with NCBs that have adopted the euro, which used the resulting funds to conduct liquidity-providing operations with Eurosystem counterparties. These back-to-back swap transactions resulted in non-remunerated intra-Eurosystem balances between the ECB and the NCBs, reported under liability item P7 "Relations within the Eurosystem".

### Note 3: Relations with the IMF

The amount of financing provided to the IMF is equivalent to the euro value of:

- the portion of France's share in the capital of the IMF settled in gold and other foreign exchange assets, uplifted for net euro usage by the IMF, in particular euro-denominated drawings and repayments by member countries vis-à-vis France;
- drawings made within the framework of the General Arrangements to Borrow and the New Arrangements to Borrow.

#### Relations with the IMF

Asset item A3 and Liability item P6

(EUR millions)

	2007	2006
<b>ASSETS</b>		
Financing provided to the IMF	766	1,075
Acquisitions of Special Drawing Rights	676	719
Accrued interest receivable	6	10
<b>Total</b>	<b>1,448</b>	<b>1,804</b>
<b>LIABILITIES</b>		
Counterpart to SDR allocations	1,160	1,233
Accrued interest payable	7	8
<b>Total</b>	<b>1,167</b>	<b>1,241</b>

The item "Acquisitions of SDRs" (Special Drawing Rights) includes the euro equivalent of the SDRs held by France. The amount shown here should be taken together with that recorded in liability item P6 "Counterpart to SDR allocations" to determine France's net SDR position.

#### Note 4: Monetary policy operations

Asset item A5 and liability item P2.2 show operations carried out by the Banque de France within the framework of the single monetary policy of the Eurosystem.

#### Euro-denominated loans to euro area credit institutions within the framework of monetary policy operations

Asset item A5

(EUR millions)

	2007	2006
Main refinancing operations	24,751	12,037
Longer-term refinancing operations	46,118	1,647
Fine-tuning operations	—	—
Structural operations	—	—
Marginal lending facility	—	—
Margin calls paid	—	—
Accrued interest receivable	186	11
<b>Total</b>	<b>71,055</b>	<b>13,695</b>

Liability item P2.1 comprises the current accounts opened by credit institutions in the books of the Banque de France. These accounts mainly comprise minimum reserves. The minimum reserve build-up period begins on the main refinancing operation settlement date following the Governing Council meeting at which the monthly assessment of monetary policy direction is made (Article 7 of EC Regulation 1745/2003 of the ECB, dated 12 September 2003).

#### Euro-denominated liabilities to euro area credit institutions within the framework of monetary policy operations

Liability item P2

(EUR millions)

	2007	2006
<b>Current accounts</b>	<b>49,170</b>	<b>26,310</b>
<b>Remaining liabilities</b>	<b>24,432</b>	<b>1</b>
Deposit facilities	0	—
Collection of fixed-term deposits	23,000	—
Repurchase agreements	0	—
Margin calls received	1,432	1
<b>Accrued interest payable</b>	<b>96</b>	<b>67</b>
<b>Total</b>	<b>73,698</b>	<b>26,378</b>

Minimum reserves are remunerated at the marginal rate applied to main refinancing operations.

#### Note 5: Items A4 "Euro-denominated claims on non-euro area residents" and A6 "Other euro-denominated loans to euro area credit institutions"

These items include euro-denominated investments linked to euro-denominated deposits recorded in liability item P4 (see note 16). These claims and loans, which do not relate to monetary policy operations, are split between these two asset items according to whether the counterparty is located within or outside the euro area.

#### Note 6: Euro-denominated fixed-income securities

These securities are valued using the weighted average cost method and may be sold prior to maturity. At the end of the year, unrealised losses are written off. Unrealised gains are recorded in the balance sheet, in "Revaluation accounts".

#### Note 7: Claims arising on the transfer of reserve assets to the ECB

This claim held by the Banque de France results from the transfer of foreign exchange reserves to the ECB. The claim is denominated in euro and is equivalent to the euro value of the transferred foreign exchange reserves as at the date of the transfer. It is remunerated at the marginal rate applied to main refinancing operations, adjusted to reflect the fact that the gold component of the transferred reserve assets is not remunerated.

#### Claims arising on the transfer of reserve assets to the ECB

Asset item A8.2

(EUR millions)

	2007	2006
Claims arising on the transfer of reserve assets to the ECB	8,288	8,275
Accrued interest receivable	281	201
<b>Total</b>	<b>8,569</b>	<b>8,476</b>

The enlargement of the EU through the accession of Bulgaria and Romania and the concomitant adjustment of the total limit of NCBs' claims and weightings in the ECB's capital key (see note 14 "Fixed assets"), along with Banka Slovenije's transfer of foreign reserve assets upon Slovenia's adoption of the single currency, account for the variation in claims held by the NCBs against the ECB with respect to the transfer of reserve assets.

#### Note 8: Claim on the Eurosystem for euro banknotes in circulation

The intra-ESCB claim arising from the allocation of euro banknotes within the Eurosystem and the liability to the ECB relating to the 8% share of euro banknotes in circulation are shown as a net amount in item A8.3 "Claim on the Eurosystem for euro banknotes in circulation", along with accrued interest receivable as at 31 December 2006. The remuneration of this net claim, and the related adjustments over the 2002-2007 period are shown in profit and loss item 1.1.1 "Interest and related income" (see note 15 on banknotes in circulation).

#### Note 9: Other claims on the Eurosystem

This item chiefly comprises any income receivable from the ECB in respect of the distribution of the balance of monetary income (see note 33 of the profit and loss account). In 2007, the net balance arising on cross-border transfers via TARGET with other NCBs in the ESCB became positive (see note 17).

#### Other claims on the Eurosystem

Asset item A 8.4

(EUR millions)

	2007	2006
TARGET and <i>lori/nostri</i> claim of Eurosystem NCBs	0	10,604
Accrued interest receivable	0	50
Other claims on the Eurosystem	49	31
<b>Total</b>	<b>49</b>	<b>10,684</b>

#### Note 10: Advance to the IEDOM

The circulation of banknotes in the overseas departments, the territorial unit of Saint Pierre and Miquelon and the departmental unit of Mayotte is managed by the *Institut d'émission des départements d'outre-mer* (IEDOM) – French overseas departments note-issuing bank – in the name of, on behalf of and under the authority of the Banque de France.

To this end, the Banque de France grants the IEDOM a non-interest-bearing advance for an amount corresponding to an estimate of the value of the banknotes in circulation in the territories concerned.

#### Note 11: Claims on the French Treasury in respect of coins

Article L141-3 of the Monetary and Financial Code prohibits the Banque de France from advancing funds to the Treasury or any other public body or State-owned corporation. However, Article 6 of EU Council Regulation 3603/93 authorises national central banks to advance funds to the public sector in respect of coins, provided that the advance represents less than 10% of coins in circulation.

The claim of the Banque de France on the French Treasury in respect of coins is non-interest-bearing.

#### Note 12: Other euro and foreign currency denominated financial assets

##### Other euro and foreign currency denominated financial assets

Asset item A11

(EUR millions)

	2007	2006
Fixed income securities held until maturity (a) (b)	66,110	28,188
Other fixed-income securities and variable-yield securities	2,321	2,978
Other operations	28,012	2,854
Accrued interest receivable	869	521
<b>Total of other euro- and foreign currency-denominated financial assets</b>	<b>97,312</b>	<b>34,541</b>

(a) In 2007, none of these securities were transferred to another portfolio and none of these securities were sold before maturity.

(b) Of which foreign currency denominated securities: EUR 39,706 million, of which EUR 32,173 million in collateralised securities (see Note 28).

## Securities portfolios

Extract from Asset item A11

(EUR millions)

	2007			2006
	Fixed income securities held until maturity	Other securities	Total	Total
<b>Fixed-income securities</b>				
Government securities	56,195	103	56,299	24,344
Securities issued by public bodies	4,927	0	4,927	2,031
Other issuers	4,988		4,988	1,933
Accrued interest receivable	655	0	655	491
<b>Net balance sheet value</b>	<b>66,765</b>	<b>103</b>	<b>66,869</b>	<b>28,800</b>
<b>Equities and other variable-yield securities</b>				
French and foreign mutual funds		994	994	986
Capitalisation mutual funds		1,134	1,134	974
Other variable-yield securities		90	90	80
<b>Net balance sheet value</b>		<b>2,217</b>	<b>2,217</b>	<b>2,040</b>

Fixed-income securities held until maturity included in item A11 are funded by four types of specifically identified resources: capital, provisions, customer deposits and banknotes in circulation.

## Note 13: Miscellaneous

### Miscellaneous

Asset item A12

(EUR millions)

	2007	2006
<b>Deferred income, accrued expenses, etc.</b>	<b>541</b>	<b>356</b>
Accrued income	545	113
Prepaid expenses	14	10
Other items	-18	233
<b>Miscellaneous</b>	<b>3,416</b>	<b>3,016</b>
<b>Total</b>	<b>3 957</b>	<b>3 373</b>

## Note 14: Fixed assets

### Fixed assets

Asset item A8.1 and A13

(EUR millions)

	31 Dec 2007	Increase (a)	Decrease (a)	31 Dec 2006
Participating interest in the ECB (gross value)	831	1		830
FX translation difference on participating interest in the ECB	5			5
<b>Participating interest in ECB (balance sheet value)</b>	<b>836</b>	<b>1</b>		<b>835</b>
<b>Non-ECB participating interest (gross value)</b>	<b>405</b>			<b>405</b>
<i>Intangible fixed assets (gross value)</i>	<i>457</i>	<i>142</i>	<i>67</i>	<i>381</i>
<i>Amortisation</i>	<i>272</i>	<i>28</i>	<i>2</i>	<i>246</i>
Net value of intangible fixed assets	185	114	65	135
<i>Tangible fixed assets (gross value)</i>	<i>2,047</i>	<i>268</i>	<i>308</i>	<i>2 086</i>
<i>Depreciation and provisions</i>	<i>1,336</i>	<i>91</i>	<i>114</i>	<i>1 357</i>
Net value of tangible fixed assets	711	179	197	729
<b>Total tangible and intangible fixed assets (net value)</b>	<b>896</b>	<b>294</b>	<b>262</b>	<b>863</b>

(a) Increases and decreases also include transfers between fixed asset accounts.

### Information relating to subsidiaries and participating interests at 31 December 2007

Asset item A8.1 and A13.2

(EUR millions)

	Asset item	Listed	% share capital held	2007 Shareholders' equity	2007 profit/loss equity	2007 book value
Bank for International Settlements	A13.2	No	9.16	12,914	687	405
European Central Bank	A8.1	No	20.7	12,965	-	830
La Prévoyance immobilière	A13.2	No	98.20	4	0	ns
Banque de France Gestion	A13.2	No	99.99	2	4	ns

ns: not significant



### Participating interest in the ECB

Under article 28 of the ESCB Statute, the capital of the ECB is held solely by the NCBs of the ESCB. The formula for determining the capital subscription of each NCB to the ECB (the "capital key") is defined in article 29.3 of the ESCB Statute and adjusted every five years. The first five-yearly adjustment was made on 1 January 2004. On 1 May 2004, a second adjustment to the key was made as a result of the accession of ten new Member States.

In accordance with Article 49.3 of the Statute of the ESCB, which was added to the Statute by the Treaty of Accession, the ECB's subscribed capital is automatically increased when a new member joins the EU and its NCB joins the ESCB. The increase is determined by multiplying the prevailing amount of the subscribed capital (i.e. EUR 5.565 billion at 31 December 2006) by the ratio, within the expanded capital key, between the weighting of the entering NCB(s) and the weighting of those NCBs that are already members of the ESCB. Therefore, on 1 January 2007, the subscribed capital of the ECB was increased to EUR 5.761 billion.

In accordance with Article 49.1 of the Statute of the ESCB and with a legal act adopted by the Governing Council on 30 December 2006,<sup>1</sup> Banka Slovenije paid EUR 17,096,556 on 1 January 2007, representing the remainder of its contribution to the ECB's capital.

The non-euro area NCBs are required to pay up 7% of their subscribed capital as a contribution to the operational costs of the ECB. Consequently, on 1 January 2007, the Bulgarian National Bank and the National Bank of Romania respectively paid up EUR 3,561,869 and EUR 10,156,952. Including these amounts, this contribution totalled EUR 122,952,830 at end-2007. Non-euro area NCBs are not entitled to receive any share of the distributable profits of the ECB, including income arising from the allocation of euro banknotes within the Eurosystem, nor are they liable to fund any loss incurred by the ECB.

Due to the combined effect of the above three developments, the ECB's paid-up capital increased from EUR 4,089,277,550 at 31 December 2006 to EUR 4,127,136,230 at 1 January 2007 and the share held by the Banque de France in the ECB's

### Interest held by the Banque de France in the capital of the ECB (%)

To December 2003	From 1 January 2004 to 30 April 2004	From 1 May 2004 to 31 December 2006	Since 1 January 2007
16.8337	16.5175	14.8712	14.3875

capital key decreased from 14.8712% at 31 December 2006 to 14.3875% at 1 January 2007.

### Note 15: Banknotes in circulation

The ECB and the 12 euro area NCBs, which together make up the Eurosystem, have issued euro banknotes since 1 January 2002. The total value of euro banknotes in circulation in the Eurosystem is allocated on the last working day of each month in accordance with the banknote allocation key.<sup>2</sup>

The ECB has been allocated an 8% share of the total value of euro banknotes in circulation; the remaining 92% has been allocated to euro area NCBs according to their weightings in the ECB's capital key. The share of banknotes in circulation allocated to each NCB is disclosed in the liability item "Banknotes in circulation".

The difference between the value of euro banknotes allocated to each NCB in accordance with the banknote allocation key and the value of the euro banknotes that it actually puts into circulation also gives rise to remunerated intra-Eurosystem balances (see asset item A8.3).

From 2002 to 2007, the intra-Eurosystem balances arising from euro banknote allocation are being adjusted in order to avoid significant changes in the NCBs' income positions as compared with previous years.<sup>3</sup> The adjustments are effected by taking into account the differences between, on the one hand, the average value of banknotes in circulation of each NCB in the period between July 1999 and June 2001 and, on the other hand, the average value of banknotes that would have been allocated to them during that period under the ECB's banknote allocation key. The adjustments will be reduced in annual stages until 2007, after which income on banknotes will be allocated fully between the NCBs in proportion to their paid-up share in the ECB's capital.

<sup>1</sup> ECB/2006/30 Decision of 30 December 2006 on Banka Slovenije's paying-up of capital, transfer of foreign reserve assets and contribution to the European Central Bank's reserves and provisions, OJ L 24 of 31 January 2007.

<sup>2</sup> ECB decision of 6 December 2001 on the issue of euro banknotes (ECB/2001/15).

<sup>3</sup> ECB decision of 6 December 2001 on the allocation of monetary income from 2002 (ECB/2001/16).



**New banknotes stacked on pallets**

Interest income and expense on these balances are cleared through the accounts of the ECB and included in "Net interest income" in the profit and loss account.

The ECB Governing Council has decided that the ECB's seigniorage income arising from the 8% share of euro banknotes in circulation allocated to it is due to the NCBs in the same year it accrues and distributed to them on the second working day of the following year in the form of an interim distribution of profit.<sup>4</sup> This income is distributed in full unless the ECB's net profit is less than the income earned on euro banknotes in circulation and unless the Governing Council decides to reduce the redistribution by the amount of the costs incurred by the ECB on the issuance and storage of euro banknotes. The Governing Council may also decide to transfer all or part of the ECB's seigniorage income to a provision for foreign exchange rate, interest rate and gold price risks. The amount distributed to NCBs is included in item 1.4 "Income from equity securities and participating interests".

With respect to 2007, the ECB Governing Council decided that the seigniorage income would be retained in full by the ECB.

French franc banknotes, which ceased to be legal tender on 17 February 2002, may still be exchanged until 17 February 2012. Prior to that date, French franc banknotes in circulation but not yet remitted to the Treasury will continue to be recorded as a liability of the Banque de France. This liability has since 1 January 2003 been included in balance sheet item P11 "Miscellaneous" (see note 21).

#### Note 16: Euro-denominated liabilities to non-euro area residents

This item comprises credit balances in euro (excluding TARGET) with central banks, commercial banks and non-financial customers in non-Eurosystem member countries. In most cases, the assets matching these liabilities are included in asset items A4 or A6 (see note 5) or asset item A11 (see note 12), depending

#### Euro-denominated liabilities to non-euro area residents

Liability item P4

(EUR millions)

	2007	2006
Euro-denominated liabilities to non-euro area residents	10,635	8,131
Accrued interest payable	102	44
<b>Total</b>	<b>10,737</b>	<b>8,175</b>

on whether they are invested in the same currency or are covered by cross-currency swaps (see note 28).

#### Note 17: Euro-denominated liabilities to the Eurosystem

Euro-denominated liabilities to the Eurosystem comprise France's net debt arising on cross-border transfers via TARGET with other NCBs in the ESCB. These liabilities also include non-interest bearing debt of EUR 1,042 million vis-à-vis the ECB arising from foreign exchange swaps entered into with the latter in the framework of the dollar-denominated temporary Term Auction Facility (see note 2).

#### Euro-denominated liabilities to the Eurosystem

Liability item P7

(EUR millions)

	2007	2006
Euro-denominated liabilities to the Eurosystem	11,935	–
Accrued interest payable	100	–
<b>Total</b>	<b>12,035</b>	<b>–</b>

#### Note 18: Liabilities to other euro area residents denominated in euro

Liability item P8.1 comprises the Treasury's account, which since 1 May 2002 has been remunerated at the marginal rate applied to main refinancing operations up to EUR 300 million; above this amount, it is remunerated at the deposit facility rate. Interest is credited to the Treasury's account on the last business day of the month.

<sup>4</sup> ECB decision of 17 November 2005 (ECB/2005/11) on the distribution of the income of the ECB on euro banknotes in circulation to the NCBs of participating Member States.



**Euro-denominated liabilities  
to other euro area residents**  
Liability item P8

(EUR millions)

	2007	2006
Treasury's account	308	235
Other liabilities	3,981	4,253
Accrued interest payable	12	10
<b>Total</b>	<b>4,290</b>	<b>4,498</b>

Liability item P8.2 "other liabilities" mainly comprises the current account with the IEDOM, the assets matching this liability being mainly recorded in asset item A9 "Advances to the IEDOM" (see note 10).

**Note 19: Items in course of settlement**

In compliance with banking rules, balance sheet item P9 "Items in course of settlement" includes only items (primarily cheques) debited or credited to a customer's account but not yet credited or debited to a credit institution's account, and vice versa.

**Note 20: Banking transactions**

This item mainly comprises overnight and fixed-term deposits denominated in foreign currencies constituted by French or foreign public bodies. The management of such foreign currency transactions is totally separate from the management of the State's foreign exchange reserves. The assets matching these liabilities, which may be covered by cross-currency swaps, are included either in asset items A11 (see note 12) or in item A4 or A6 (see note 5), depending on whether they are invested in a foreign currency or in euro.

Euro-denominated deposits made by institutional customers (other than monetary financial institutions) and private customers are recorded in liability item P8.2.

**Banking transactions**  
Liability item P10

(EUR millions)

	2007	2006
Overnight deposits	505	550
Other banking transactions	53,205	7,738
Accrued interest payable	657	88
<b>Total</b>	<b>54,366</b>	<b>8,377</b>

**Note 21: Miscellaneous**

**Miscellaneous**  
Liability item P11

(EUR millions)

	2007	2006
Deferred income, accrued expenses, etc.	283	268
Accrued expenses	283	268
Deferred income, etc.	0	0
French franc banknotes in circulation	995	1,267
Miscellaneous	5,743	3,430
<b>Total</b>	<b>7,021</b>	<b>4,965</b>

This item includes in particular the capital of the Banque de France Employee Reserve Fund (see "Pension obligations" below) and French franc banknotes still in circulation (see note 15).

**Note 22: Provisions for liabilities and charges**

Provisions for liabilities and charges mainly comprise:

- provisions for restructuring relating to the "cash activities" and "banknote manufacturing" plans, the plan to adapt the Banque de France's branch network, and the plan to discontinue retail banking activities;
- provisions relating to the early retirement incentive scheme for employees reaching the end of their working life;
- provisions for retirement benefits;
- provisions for various social liabilities (death benefits, long-service medals, extended sick leave, pensions for industrial injuries, and benefits and bonuses paid to retirees for which the Bank remains directly liable);
- provisions for major repairs.

**Provisions for liabilities and charges**  
Liability item P12

(EUR millions)

	2007	Increase	Decrease	2006
Provisions for restructuring	244		71	315
Provisions for changing the age pyramid	24		2	26
Provisions for retirement benefits	102	3		99
Other	305	170	1	136
<b>Total</b>	<b>675</b>	<b>173</b>	<b>74</b>	<b>577</b>

In 2007, the Bank also made a provision to cover various social obligations to retired employees (death benefits, etc.) that are not funded by the pension scheme. These new provisions account for the bulk of the increase in other provisions for liabilities and charges observed between 2006 and 2007.

### Note 23: Revaluation accounts

Gold and foreign exchange assets and liabilities are revalued at the reference prices indicated by the ECB on 31 December 2007. The unrealised gain on gold was calculated using a price of EUR 18,269 per kilogram of fine gold, compared with EUR 15,519 at end-2006.

The revaluation rates used at 31 December 2007 for the main currencies held were the following:

- 1 euro = 1.4721 US dollars (compared with 1.3170 at end-2006)
- 1 euro = 0.9311 SDRs (compared with 0.8760 at end-2006)

Revaluation accounts Liability item P13		
(EUR millions)		
	2007	2006
Revaluation account – gold	26,825	20,646
Revaluation account – foreign exchange	46	464
Revaluation account – securities	685	523
Revaluation account – Forward financial instruments	2	–
<b>Total</b>	<b>27,558</b>	<b>21,633</b>

### Note 24: Revaluation reserve of State gold reserves and revaluation reserve of State foreign exchange reserves

In accordance with the rider of 27 December 2007 to the agreement of 31 March 1999 between the State and the Banque de France on the management of and accounting for State foreign exchange reserves:

- Foreign exchange gains realised from sales of gold during the 2004-2006 period – i.e. EUR 1,535 million – were transferred from the revaluation reserve of State gold reserves to the revaluation reserve of State foreign exchange reserves.

- Net foreign exchange gains realised in 2007 from sales of gold were assigned to the revaluation reserve of State foreign exchange reserves (see note 31).

### Note 25: Capital, reserves and retained earnings

Capital, reserves and retained earnings Liability item P17		
(EUR millions)		
	2007	2006
<b>Capital</b>	<b>457</b>	<b>457</b>
<b>Reserves</b>	<b>2,910</b>	<b>2,738</b>
Statutory reserves	293	230
Long-term capital gains	100	100
Special pension reserve fund (see note 29)	109	0
Other reserves (a)	2,407	2,408
<b>Retained earnings</b>	<b>1</b>	<b>3</b>
<b>Total</b>	<b>3,367</b>	<b>3,198</b>

(a) Under the Decree of 3 December 1993, the Bank must maintain reserves to finance its investments. The Bank is also its own insurer with respect to civil liability risks, claims on property it owns and damages to this property by third parties. The "Other reserves" item chiefly comprises these two types of reserves.

### Off-balance sheet items

### Note 26: Securities commitments

Securities commitments		
(EUR millions)		
	2007	2006
Securities to be received	4,955	513
Securities to be delivered	582	1,419

### Note 27: Forward contract commitments

Notional amount of forward contracts		
(EUR millions)		
	2007	2006
<b>Outright transactions</b>		
<i>Organised markets</i>		
Foreign currency denominated forward contracts		
Purchases	3,241	3,298
Sales	0	642
Euro-denominated forward contracts		
Purchases	4,962	270
Sales	7,015	15,774
<i>Over-the-counter markets</i>		
Foreign currency denominated interest rate swaps	315	–
Euro-denominated interest rate swaps	10	



## Note 28: Forward foreign exchange transactions with customers and the ECB

The Banque de France collects euro-denominated deposits from non-euro area residents, in particular foreign central banks and international bodies; these deposits are recorded in liability item P4. The Banque de France also collects foreign currency denominated deposits, mainly from non-resident institutions; these deposits are recorded in liability item P11.

These euro-denominated or foreign currency denominated deposits are invested either in the same currency or in a different currency (euro-denominated investments are recorded in asset items A4 or A6 depending on the area of residence of the counterparty, while foreign currency investments are recorded in item A11); where necessary, foreign exchange risk is neutralised by cross-currency swaps of the same amount and maturity as the deposit. These foreign-currency deposits and investments, and the related spot and forward foreign exchange transactions, form part of an activity that is totally separate and independent from the management of foreign exchange reserves. Consequently, they are recorded in dedicated accounts separate from those used for the management of foreign exchange reserves, and are valued in accordance with the standards issued by the CRC (see "Other foreign exchange gains/losses" in section 2|2|1 "Accounting principles and valuation methods", and note 20).

The table below shows amounts of foreign currency receivable and deliverable in respect of transactions carried out with customers.

### Amounts of foreign currency receivable and deliverable in respect of transactions carried out with customers

(EUR millions)

	2007	2006
<b>Euro to be received against foreign currency to be delivered</b>		
Euro to be received	4,242	4,504
Foreign currency to be delivered	4,167	4,347
<b>Foreign currency to be received against euro to be delivered</b>		
Foreign currency to be received	62	8
Euro to be delivered	64	8
<b>Foreign currency to be received against foreign currency to be delivered</b>	43,244	6,009
<b>Foreign currency to be delivered against foreign currency to be received</b>	44,321	5,575

In addition, at 31 December 2007, the amount remained of the forward contract commitment to deliver dollars to the ECB with a value equivalent to EUR 964 million, under the temporary dollar-denominated Term Auction Facility introduced by the Federal Reserve System (see notes 2 and 17).

## Note 29: Pension obligations

Banque de France employees benefit from a pension scheme set up by an Imperial Decree of 16 January 1808. This scheme is currently governed by Decree 2007-262 of 27 February 2007, which entered into force on 1 April 2007 and aligned the Banque de France pension scheme with that of the civil service.

### The Employee Reserve Fund (CRE)

The Banque de France has a pension fund known as the *Caisse de réserve des employés de la Banque de France* (CRE – Banque de France Employee Reserve Fund), which is designed to service the pensions of the Bank's statutory employees. The CRE does not have a legal personality distinct from that of the Bank; it constitutes, as the *Conseil d'État* set out in its decisions of 5 November 1965 and 28 April 1975, "a means for the Bank to manage itself assets that are assigned to a special purpose and whose separate financial identity has been recognised with the sole purpose of showing the results of this management in a special account."

As a consequence, the CRE is subject to separate accounting treatment. However, its assets, liabilities, income and expenses are an integral part of the Bank's accounts.

The pensions provided by the CRE to retirees are partly funded by the income on a securities portfolio, which has been set up over time and is specifically devoted to this purpose. The securities acquired by the CRE appear in balance sheet item A12 "Miscellaneous". The CRE's capital is shown in liability item P11 "Miscellaneous".

Securities purchased by the CRE are recorded, in accordance with CRBF Regulation 90-01, as available-for-sale and held-to-maturity securities. Differences between the acquisition and redemption price are spread over the remaining life of the securities according to the internal rate of return method. Unrealised losses on available-for-sale securities are provided for on a line-by-line basis. However, under the CRE's rules, realised gains and losses and unrealised losses recognised in the profit and loss account require a matching charge to or withdrawal from the CRE's capital.

Retirement expenses are included in the profit and loss account item 2.1 "Personnel and related expenses". The proceeds of the CRE's securities portfolios are recorded in profit and loss account item 1.6 "Net of other income and expenses".

#### Other sources of financing for pensions

In order to ensure the progressive financing, by 2014-2016, of the unfunded portion of liabilities in respect of pension rights acquired before the entry into force of Decree 2007-262 of 27 February 2007, in 2007 the General Council set up a special pension reserve, in accordance with the third indent of Article R144-4 of the French Monetary and Financial Code. This reserve will be regularly replenished, within the limits permitted by the gross income of the Banque de France and the payment to the State of the predominant share incumbent on it. The special pension reserve appears in liability item P17 "Capital, reserves and retained earnings".

In addition, as part of the restructuring programmes implemented since 1999 ("cash activities" and "banknote manufacturing" plans, the plan to adapt the Banque de France's branch network and the plan to discontinue retail banking activities), early retirement schemes were set up, with additional seniority granted to retirees. This additional seniority, including that resulting from the neutralisation of the effects of the pension scheme's reform on employees benefiting from the early retirement scheme at the date of the reform's entry into force have been entirely provisioned. The corresponding provisions appear in liability item P12 "Provisions for liabilities and charges".

The resources constituted by this special pension reserve and these provisions have been invested in a securities portfolio that appears in asset item A11. This portfolio is recorded in accordance with the rules set out in the

section on the valuation methods used for securities portfolios. The income from this portfolio is shown, depending on the case, in items 1.1 "Net interest income", 1.2.3 "Net of other income and expenses on financial transactions" or 1.4 "Income from equity securities and participating interests" of the profit and loss account.

#### Actuarial assumptions

The amount of pension liabilities has been calculated in accordance with actuarial standards (using the projected unit credit method), taking into account all current employees, retirees and their dependants. The amount of obligations vis-à-vis current employees was determined using a prospective method with career-end salaries.

Since the reform of the pension system with effect from 1 April 2007, pension entitlements may be accessed between 60 and 65. The increase in the number of quarters required to obtain a full pension will take place gradually at the rate of one quarter per half-year to reach 164 quarters in the second half of 2013 (as against 150 until 2006). The pensionable age is being raised in parallel (from 60 to 65) to allow employees to acquire the requisite number of quarters to obtain a full pension. In addition, a system of supplements/reductions will progressively be put in place from 1 January 2009 and will apply to employees who start drawing their pension with a greater/smaller number of quarters than that required to obtain a full pension.

The level of pensions is adjusted at the beginning of every year with reference to projected developments in the household consumer price index excluding tobacco.

Calculations of pension liabilities and the underlying assumptions used are validated and monitored by the Bank's actuary. In 2007, as in previous years, a discount rate of 4.5% was applied.

#### Pension liabilities and funding

Liabilities			Funding		
	2007	2006		2007	2006
<b>Liabilities in respect of the special retirement scheme</b>	<b>9,099</b>	<b>9,744</b>	<b>Funding</b>	<b>3,253</b>	<b>2,886</b>
o/w to current workforce	4,115	4,684	o/w Employee Reserve Fund	3,144	2,886
o/w to retirees	4,984	5,060	o/w Special pension reserve	109	0
Liabilities in respect of the additional seniority granted as part of restructuring plans	124	97	Provisions	124	97
<b>Total gross liabilities</b>	<b>9,222</b>	<b>9,841</b>	<b>Total funding</b>	<b>3,376</b>	<b>2,983</b>
<b>Net liabilities</b>	<b>5,846</b>	<b>6,858</b>			

## Profit and loss account

### Note 30: Net interest income

<b>Net interest income</b> Profit and loss item 1.1		
(EUR millions)		
	<b>2007</b>	<b>2006</b>
Interest on foreign exchange assets	1,780	1,464
Interest on claims on the IMF	47	57
Interest on euro-denominated claims on non-residents		
Interest on lending to credit institutions	1,285	521
Interest on euro-denominated securities	558	234
Interest on claims arising on transfer of reserve assets to the ECB	281	201
Interest on net claims on the Eurosystem (a)	0	296
Interest on the net euro banknote position	2,223	1,305
Total of other euro- and foreign currency denominated financial assets	2,290	1,215
<i>o/w: Interest on available-for-sale securities</i>	<i>ns</i>	<i>ns</i>
<i>Interest on held-to-maturity securities</i>	<i>991</i>	<i>647</i>
<i>Other interest</i>	<i>1,299</i>	<i>567</i>
<b>Total interest and related income (A)</b>	<b>8,464</b>	<b>5,293</b>
Interest on euro-denominated liabilities to monetary financial institutions in the euro area	-1,592	-1,002
<i>o/w: Interest paid on minimum reserves</i>	<i>-1,414</i>	<i>-904</i>
Interest on euro-denominated liabilities to non-euro area residents	-398	-212
Interest on foreign exchange liabilities	-462	-166
Interest on counterpart to SDR allocations	-49	-46
Interest on net claims on the Eurosystem (a)	-60	0
Interest paid on the Treasury account	-8	-4
Other interest	-922	-362
<b>Total interest and related expenses (B)</b>	<b>-3,491</b>	<b>-1,792</b>
<b>Net interest income (C = A + B)</b>	<b>4,973</b>	<b>3,501</b>

(a) Interest on the Banque de France's net position within the TARGET system (see notes 9 and 17).  
ns: not significant

### Note 31: Net income/loss on financial transactions

In 2007, the net balance of realised gold and foreign exchange gains and losses and unrealised foreign exchange losses was a gain of EUR 1,679 million.

In accordance with the agreement of 31 March 1999 between the State and the Banque de France on management of and accounting for State foreign exchange reserves, supplemented by riders dated 26 November 2002 and 27 December 2007, the realised gains on gold and foreign exchange amounting to EUR 1,679 million were allocated to the *Réserve de réévaluation des réserves en devises de l'État* (RRRDE – revaluation reserve of State foreign exchange reserves), with the matching entry taken to the profit and loss account (item 1.2.2).

### Net of other income and expenses on financial transactions

Extract from profit and loss item P1.2.3

(EUR millions)

	<b>2007</b>	<b>2006</b>
Net gain/loss on foreign currency denominated securities (a) (b) (c)	89	-67
Net gain/loss on euro-denominated securities included in item A7 (b) (c)	-45	-47
Net gain/loss on available-for-sale securities included in item A11	2	8
Net foreign exchange gain/loss (excluding foreign exchange reserve management)	8	11
<b>Total</b>	<b>54</b>	<b>-94</b>

(a) Excluding the impact of foreign exchange fluctuations, shown in profit and loss item 1.2.1.

(b) These items include realised gains and losses, and unrealised losses at year-end.

(c) These items also include margin calls on interest rate futures and forwards.

### Note 32: Income from equity securities and participating interests

In 2007, the ECB did not pay a dividend in respect of the 2006 financial year. In addition, the ECB retained its 2007 seigniorage income in full following the Governing Council's decision based on the ECB's forecast results. Consequently, in 2007 the Banque de France did not receive its share, amounting to EUR 415 million in the form of an interim dividend (see note 15).

### Income from equity securities and participating interests

Profit and loss item 1.4

(EUR millions)

	<b>2007</b>	<b>2006</b>
ECB dividend	–	–
Dividends from other participating interests	69	47
Dividends from available-for-sale securities	34	20
Other income	2	2
<b>Total</b>	<b>105</b>	<b>69</b>

### Note 33: Net result of pooling of monetary income

The monetary income of each NCB is determined by measuring the actual annual income derived from the earmarkable assets held against its liability base.

The liability base is composed of the following items: banknotes in circulation; liabilities to credit institutions in connection with euro-denominated monetary policy operations; intra-Eurosystem liabilities arising from TARGET transactions; and net intra-Eurosystem liabilities arising from the allocation of euro banknotes within the Eurosystem. Any interest accruing on liabilities included in the liability base is deducted from the monetary income to be pooled.

Earmarkable assets consist of the following items: euro-denominated loans to euro area credit institutions in the framework of monetary policy operations; claims arising on the transfer of reserve assets to the ECB; the net intra-Eurosystem claim arising from TARGET transactions; the net intra-Eurosystem claim arising from the allocation of euro banknotes within the Eurosystem; and a limited amount of gold in proportion to each NCB's interest in the ECB's capital under the capital key. Gold is deemed not to generate any income. Where the value of an NCB's earmarkable assets exceeds or falls short of the value of its liability base, the difference is offset by applying to the value of the difference the average rate of return on the earmarkable assets of all the NCBs taken together.

The monetary income pooled by the Eurosystem is allocated between NCBs according to the subscribed capital key. The difference between the monetary income pooled by the Banque de France (EUR 4,745 million) and that reallocated to the Bank (EUR 4,794 thousand) constitutes the net result arising from the calculation of monetary income recorded in profit and loss item 1.5.

### Note 34: Net of other income and expenses

Net of other income and expenses Profit and loss item 1.6		
(EUR millions)		
	2007	2006
Remuneration for services rendered to the State	158	168
Other income (a)	313	264
<b>Total other income (A)</b>	<b>471</b>	<b>432</b>
<b>Total other expenses (B)</b>	<b>-13</b>	<b>-7</b>
<b>Net of other income and expenses (C = A + B)</b>	<b>458</b>	<b>425</b>

(a) This item notably includes fees charged for use of the databases managed by the Banque de France (FNCI, FICP, FCC, FIBEN).

### Note 35: Personnel and related expenses

Personnel and related expenses Profit and loss item 2.1		
(EUR millions)		
	2007	2006
Salaries, wages and related taxes	-738	-753
Social security expenses	-152	-149
Retirement expenses	-420	-404
Profit-sharing and incentive plans	-35	-35
<b>Total personnel expenses</b>	<b>-1,345</b>	<b>-1,341</b>

### Note 36: Extraordinary items

Extraordinary items for the year ended 31 December 2007 comprise net gains arising on the sale of some of the branches closed as part of the reform of the Banque de France regional network.

### Note 37: Corporate income tax

Under Article 8 of Act 2007-212 of 20 February 2007 on various measures concerning the Banque de France, the taxable profit or loss of the Banque de France is calculated using accounting rules defined in accordance with Article L144-4 of the Monetary and Financial Code and the agreement in Article L141-2 of the same Code.

These new provisions have been in force since 1 January 2007.

Corporate income tax Profit and loss item 5		
(EUR millions)		
	2007	2006
Income taxes for the year	1,396	807
on recurring income	1,376	789
on exceptional items	20	18

### Other information

Remuneration of management bodies		
(EUR millions)		
	2007	2006
Total remuneration paid to management bodies	2.9	2.8

The members of the General Council and the Executive Committee constitute the Bank's management bodies. Remuneration comprises gross remuneration plus payment in kind, where relevant. The Staff Representative and the Censor are not remunerated for positions they hold in the General Council.

## 2 | 3 Auditors' report on the annual accounts of the Banque de France

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**Deloitte & associés**  
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### REPORT OF THE AUDITORS ON THE ANNUAL ACCOUNTS Year ended 31 December 2007

In accordance with the assignment entrusted to us by the Banque de France's General Council, we hereby report to you for the year ended 31 December 2007 on:

- the audit of the accompanying annual accounts of the Banque de France;
- the basis for our assessments;
- the specific procedures required by Article R144-8 of the Monetary and Financial Code.

The annual accounts have been approved by the Governor. Our responsibility is to express an opinion on these annual accounts based on our audit.

#### 1 | Opinion on the annual accounts

We conducted our audit in accordance with professional standards applicable in France; these standards require that we plan and perform the audit to obtain reasonable assurance as to whether the annual accounts are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the annual accounts. It also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the annual accounts give a true and fair view of the results of its operations for the year to 31 December 2007, and of the financial position and assets and liabilities of the Banque de France at that date, in compliance with the accounting rules and principles set out by the European System of Central Banks (ESCB) for central banking activities and securities portfolios (other than those of the Banque de France Employee Reserve Fund), and with French accounting rules and principles for other activities.

Without qualifying our opinion, we draw your attention to the following matters:

- The notes to the annual accounts provide a detailed description of the presentation and accounting principles applied by the Bank, a number of which are specific to the ESCB.
- As explained in the Notes to the annual accounts, the General Council, exercising the right provided for in Article R144-6 of the Monetary and Financial Code, assessed the level of detail of the financial information published.
- As explained in the Notes to the annual accounts, with effect from 31 December 2007, pursuant to the rider of 27 December 2007 to the agreement of 31 March 1999 between the State and the Bank, net foreign exchange gains realised from sales of gold are allocated to the revaluation reserve of State foreign exchange reserves. This rider also stipulates that foreign exchange gains realised from sales of gold during the 2004-2006 period be transferred from the revaluation reserve of State gold reserves to the revaluation reserve of State foreign exchange reserves.

.../...



## 2| Basis for our assessments

As required by Article L.823-9 of the Commercial Code relating to the basis for our assessments, we draw your attention to the following:

- The Banque de France books provisions for risks and charges to cover risks such as those detailed in note 22 of the Notes to the annual accounts. Our work consisted in evaluating the data and assumptions on which these estimates are based, checking the Banque de France's calculations, comparing the accounting estimates in previous periods with the corresponding actual figures, and examining the procedures in place for the validation of these estimates by the Bank's management. We used these elements to carry out an assessment of the reasonableness of these estimates.

- Note 29 to the annual accounts sets out the method for assessing pension obligations and other related liabilities. These obligations have been assessed by actuaries. Our work consisted in examining the data used, evaluating the assumptions utilised, checking the calculations and verifying that note 29 provides appropriate information. We carried out an assessment of the reasonableness of these estimates.

Our assessment of these issues was made within the context of our audit approach to the annual accounts taken as a whole, and contributed to our opinion as expressed in the first part of this report.

## 3| Specific procedures and disclosures

We have also performed the other procedures required by the law, in accordance with professional standards applicable in France.

We have no comment to make as to the fair presentation and consistency with the annual accounts of the information given in the Report on the Bank's assets, liabilities and results.

Courbevoie and Neuilly-sur-Seine, 21 April 2008  
The Auditors

**Mazars & Guérard**

Patrick de Cambourg  
Charles de Boisriou

**Deloitte & associés**

Thierry Aubertin

### 3| Combined accounts

#### 3| I Combined balance sheet and profit and loss account

##### Combined balance sheet at 31 December 2007

(EUR millions)

Notes to combined annual accounts		ASSETS	2007	2006
	A1	Gold	47,557	42,210
		Foreign exchange assets (excl. relations with the IMF)	37,896	36,002
	A2	2.1 Foreign exchange assets held with non-euro area residents	23,856	28,606
		2.2 Foreign exchange assets held with euro area residents	14,040	7,396
		Relations with the IMF	1,448	1,804
	A3	3.1 Financing provided to the IMF	768	1,080
		3.2 Acquisitions of Special Drawing Rights	680	724
	A4	Euro-denominated claims on non-euro area residents	2,257	2,303
	A5	Euro-denominated loans to euro area credit institutions in the framework of monetary policy operations	71,055	13,695
	A6	Other euro-denominated loans to euro area credit institutions	3,925	2,149
	A7	Euro-denominated securities	14,511	8,222
	A8	Relations within the Eurosystem	76,766	83,447
		8.1 Participating interest in the ECB	836	835
		8.2 Claims arising on the transfer of reserve assets to the ECB	8,569	8,476
		8.3 Claim on the Eurosystem for euro banknotes in circulation	67,312	63,452
		8.4 Other claims on the Eurosystem	49	10,684
2	A9	Claims on the French Treasury in respect of coins	42	82
	A10	Other euro and foreign currency denominated financial assets	97,315	34,543
I	A11	Miscellaneous	4,242	3,612
	A12	Fixed assets	1,330	1,288
		12.1 Tangible and intangible assets	917	875
		12.2 Participating interests (other than interest in the ECB)	414	414
<b>Total assets</b>			<b>358,344</b>	<b>229,357</b>
		LIABILITIES	2007	2006
	P1	Banknotes in circulation	128,852	120,229
	P2	Euro-denominated liabilities to euro area credit institutions in the framework of monetary policy operations	73,698	26,378
		2.1 Current accounts	49,260	26,377
		2.2 Other liabilities	24,437	1
	P3	Other euro-denominated liabilities to euro area credit institutions	40	18
	P4	Euro-denominated liabilities to non-euro area residents	10,737	8,175
	P5	Foreign exchange liabilities	11,874	7,580
	P6	Counterpart to SDR allocations	1,167	1,241
	P7	Relations within the Eurosystem	12,035	0
	P8	Euro-denominated liabilities to other euro area residents	1,212	1,229
		8.1 Treasury's account	502	433
		8.2 Other liabilities	711	796
2	P9	Items in course of settlement	769	377
	P10	Banking transactions	54,366	8,377
	P11	Miscellaneous	7,033	4,986
	P12	Provisions for liabilities and charges	689	592
	P13	Revaluation accounts	27,558	21,633
	P14	Fund for general risks	670	550
	P15	Revaluation reserve of State gold reserves	18,499	20,034
	P16	Revaluation reserve of State foreign exchange reserves	2,904	3,049
I	P17	Capital, reserves and retained earnings	3,832	3,625
		17.1 IEDOM capital grant, reserves and retained earnings	137	137
		17.2 Banque de France capital, reserves and retained earnings	3,695	3,488
	P18	Profit for the year	2,408	1,284
<b>Total liabilities</b>			<b>358,344</b>	<b>229,357</b>

## 2007 Combined profit and loss account

(EUR millions)

Notes to combined annual accounts			2007	2006
	<b>1.</b>	<b>Net income on the activities of the Banque de France</b>	<b>5,731</b>	<b>4,005</b>
2	1.1.	Net interest income	5,099	3,590
	1.1.1	Interest and related income	8,667	5,294
	1.1.2	Interest and related expenses	-3,568	-1,704
	1.2.	Net income/loss on financial transactions	54	-94
	1.2.1	Net balance of realised gains/losses and unrealised losses on foreign exchange	-1,679	899
	1.2.2	Net of charges to/releases from foreign exchange revaluation reserves	1,679	-899
	1.2.3	Net of other income and expenses on financial transactions	54	-94
	1.3.	Commission	6	4
	1.3.1	Commission (income)	54	49
	1.3.2	Commission (expense)	-48	-45
2	1.4.	Income from equity securities and participating interests	55	41
	1.5.	Net result of pooling of monetary income	49	31
	1.6.	Net of other income and expenses	468	433
	<b>2.</b>	<b>Operating expenses</b>	<b>-1,891</b>	<b>-1,811</b>
	2.1.	Personnel and related expenses	-1,360	-1,355
	2.2.	Taxes other than income tax	-34	-28
	2.3.	Provisions, depreciation and amortisation	-117	-117
	2.4.	Other operating expenses	-380	-311
		<b>Profit before tax and exceptional items (1 + 2)</b>	<b>3,840</b>	<b>2,194</b>
	<b>3.</b>	<b>Net charge to the fund for general risks</b>	<b>-120</b>	<b>-140</b>
	<b>4.</b>	<b>Extraordinary items</b>	<b>54</b>	<b>53</b>
	4.1.	Extraordinary income	54	53
	4.2.	Extraordinary charges	0	0
I	<b>5.</b>	<b>Corporate income tax</b>	<b>-1,366</b>	<b>-824</b>
		<b>Profit for the year (1 + 2 + 3 + 4 + 5)</b>	<b>2,408</b>	<b>1,284</b>

## 3|2 Notes to the combined annual accounts

### 3|2|1 Scope of consolidation

#### Undertakings excluded from the consolidation

At 31 December 2007, the Banque de France held a participating interest in four undertakings (see note 14 to the balance sheet of the Banque de France).

The Banque de France holds an interest of over 20% in three of these undertakings.

The interests in Banque de France Gestion and La Prévoyance Immobilière are excluded from the consolidation on grounds of immateriality.

Under the Statute of the ESCB and ECB, the ECB Governing Council functions in such a way that the Banque de France does not exert control or significant

influence over the ECB. Monetary policy is defined by the Governing Council on the basis of the "one member, one vote" principle, in compliance with Article 10.2 of the Statute.

#### Consolidation of the Institut d'émission des départements d'outre-mer (IEDOM)

In compliance with Order No. 2000-347 of 19 April 2000, amending Order No. 59-74 of 7 January 1959 reforming issuance arrangements in the overseas departments of Guadeloupe, French Guiana, Martinique and Réunion, the French overseas departments note-issuing bank (IEDOM) came under the control of the Banque de France as from 1 July 2000. The Banque de France does not, however, hold an equity interest in the IEDOM.

The IEDOM is a national, financially autonomous, public institution with legal personality. It receives a capital grant from the State.

It is administered by a supervisory board composed of 15 members, seven of whom are appointed by the

Governor of the Banque de France for a four-year term. The Governor, or his representative, chairs the supervisory board.

The Director General of the IEDOM is appointed by the chairman of the supervisory board.

The IEDOM pays the balance of its net profits, after the constitution of reserves, to the Banque de France. Any losses are borne by the Banque de France.

Article 9 of the aforementioned Order states that the accounts of the IEDOM are to be consolidated with those of the Banque de France.

### 3|2|2 Activities of the IEDOM

The IEDOM's catchment area is the four overseas departments of Guadeloupe, French Guiana, Martinique and Réunion, the territorial unit of Saint Pierre and Miquelon and the departmental unit of Mayotte.

Its tasks are:

- tasks carried out within the framework of the ESCB (putting banknotes into circulation, and implementing the minimum reserve system);
- relations with the Treasury (keeping current accounts of paymasters-general and their accredited representatives, and centralising transactions);
- executing transfers of public and private funds between metropolitan France and the territorial units in its catchment area;
- providing services to the banking community and the public (keeping of data files, economic and monetary studies, processing of household debt files) within the framework of legal, regulatory and contractual provisions.

### 3|2|3 Accounting principles and valuation methods used in the combined accounts

The same accounting principles and valuation methods apply to both the combined accounts and the individual annual accounts of the Banque de France, except in the computation of corporate income tax which, in the

combined accounts, takes into account all temporary timing differences arising for tax purposes.

### 3|2|4 Information on individual items in the combined balance sheet and profit and loss account

#### Note 1: Deferred taxes

A net deferred tax asset of EUR 279 million is included in item A11 "Miscellaneous" in the combined balance sheet. It arises solely on temporary timing differences between the recognition of expenses and income for accounting purposes and their recognition for tax purposes. This asset is made up of the items shown in the table below.

Deferred tax assets and liabilities		
(EUR millions)		
	Deferred tax assets	Deferred tax liabilities
Income temporarily exempted from taxation		20
Tax on unrealised gains and losses on mutual funds	88	
Other deferred tax relating to securities	11	
Provisions not deductible for tax purposes	211	
Charges deducted for tax purposes but not yet recognised in the accounts	11	
Other recurring timing differences		22
<b>Total</b>	<b>321</b>	<b>42</b>

The matching entry for this deferred tax asset is split between:

- the tax charge for the year, which is EUR 45 million lower than in the individual annual accounts for fiscal 2007;
- item P17 "Capital, reserves and retained earnings", which includes the balance of EUR 234 million, representing the net deferred tax asset at the start of fiscal 2007.

Apart from the recognition of deferred taxes, the principal consolidation adjustments are (i) the elimination of inter-institutional transactions with the IEDOM and (ii) the elimination of tax-regulated provisions from the balance sheet and of charges to/ releases from the profit and loss account.

## Note 2: Elimination of inter-institutional transactions

Elimination of inter-institutional transactions relate to:

- the advance to the IEDOM (asset item A9 in the individual balance sheet of the Banque de France);
- the IEDOM's current account with the Banque de France (included in liability item P8.2 in the individual balance sheet);

- interest paid on the IEDOM current account (included in item 1.1.2 "Interest and related expenses" in the individual profit and loss account);

- and the dividend paid by the IEDOM (included in item 1.4 "Income from equity securities and participating interests" in the individual profit and loss account).

## 3|3 Auditors' report on the combined annual accounts

**Mazars & Guérard**  
61 rue Henri Regnault  
92075 La Défense Cedex

**Deloitte & associés**  
185 avenue Charles de Gaulle  
92524 Neuilly-sur-Seine Cedex

### REPORT OF THE AUDITORS ON THE COMBINED ANNUAL ACCOUNTS Year ended 31 December 2007

*In accordance with the assignment entrusted to us by the General Council, we have audited the accompanying combined annual accounts of the Banque de France and the Institut d'émission des départements d'outre-mer – IEDOM (French overseas departments note-issuing bank) for the year ended 31 December 2007.*

*The combined annual accounts have been approved by the Governor. Our responsibility is to express an opinion on these annual accounts based on our audit.*

#### 1| Opinion on the combined accounts

*We conducted our audit in accordance with professional standards applicable in France; these standards require that we plan and perform the audit to obtain reasonable assurance as to whether the combined financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the annual accounts. It also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.*

*In our opinion, the combined annual accounts, prepared in accordance with article 9 of Order No. 2000-347 of 19 April 2000, give a true and fair view of the results of the operations of the Banque de France and the IEDOM combined for the year to 31 December 2007, and of their financial position and assets and liabilities at that date, in compliance with the accounting rules and principles set out by the European System of Central Banks (ESCB) for central banking activities and securities portfolios (other than those of the Banque de France Employee Reserve Fund), and with French accounting rules and principles for other activities.*

.../...



Without qualifying our opinion, we draw your attention to the following matters:

a) In establishing the combined annual accounts of the Banque de France and the IEDOM, inter-institutional transactions have been eliminated and deferred taxation has been recognised. These adjustments are described in the summary notes to the combined annual accounts. With the exception of deferred taxes, the impact of which is described in the notes to the combined annual accounts, these adjustments do not materially affect the overall annual accounts.

b) The notes to the annual accounts and to the combined annual accounts provide a detailed description of the presentation and accounting principles applied in the combined annual accounts, a number of which are specific to the ESCB.

c) As explained in the Notes to the annual accounts, the General Council, exercising the right provided for in Article R144-6 of the Monetary and Financial Code, assessed the level of detail of the financial information published.

d) For reasons set out in paragraph a) above, the combined annual accounts are not specifically commented on in the Report on the Bank's assets, liabilities and results.

e) As explained in the Notes to the annual accounts, with effect from 31 December 2007, pursuant to the rider of 27 December 2007 to the agreement of 31 March 1999 between the State and the Bank, net foreign exchange gains realised from sales of gold are allocated to the revaluation reserve of State foreign exchange reserves. This rider also stipulates that foreign exchange gains realised from sales of gold during the 2004-2006 period be transferred from the revaluation reserve of State gold reserves to the revaluation reserve of State foreign exchange reserves.

## 2| Basis for our assessments

As required by Article L.823-9 of the Commercial Code relating to the basis for our assessments, we draw your attention to the following:

- The Banque de France books provisions for risks and charges to cover risks such as those detailed in note 22 of the Notes to the annual accounts. Our work consisted in evaluating the data and assumptions on which these estimates are based, checking the Banque de France's calculations, comparing the accounting estimates in previous periods with the corresponding actual figures, and examining the procedures in place for the validation of these estimates by the Bank's management. We used these elements to carry out an assessment of the reasonableness of these estimates.

- Note 29 to the annual accounts sets out the method for assessing pension obligations and other related liabilities. These obligations have been assessed by actuaries. Our work consisted in examining the data used, evaluating the assumptions utilised, checking the calculations and verifying that note 29 provides appropriate information. We carried out an assessment of the reasonableness of these estimates.

- As indicated in the Notes to the combined accounts, the Banque de France shows a net deferred tax asset of EUR 279 million as at 31 December 2007. The Bank believes that profits earned in future periods will enable this asset to be recovered. As part of our assessment, we reviewed documentation supplied by the Banque de France in support of these positions, and satisfied ourselves as to its reasonableness.

Our assessment of these issues was made within the context of our audit approach to the combined accounts taken as a whole, and contributed to our opinion as expressed in the first part of this report.

Courbevoie and Neuilly-sur-Seine, 21 April 2008  
The Auditors

**Mazars & Guérard**

Patrick de Cambourg  
Charles de Boisriou

**Deloitte & associés**

Thierry Aubertin



**A gold bar weighs roughly 12.5 kg**



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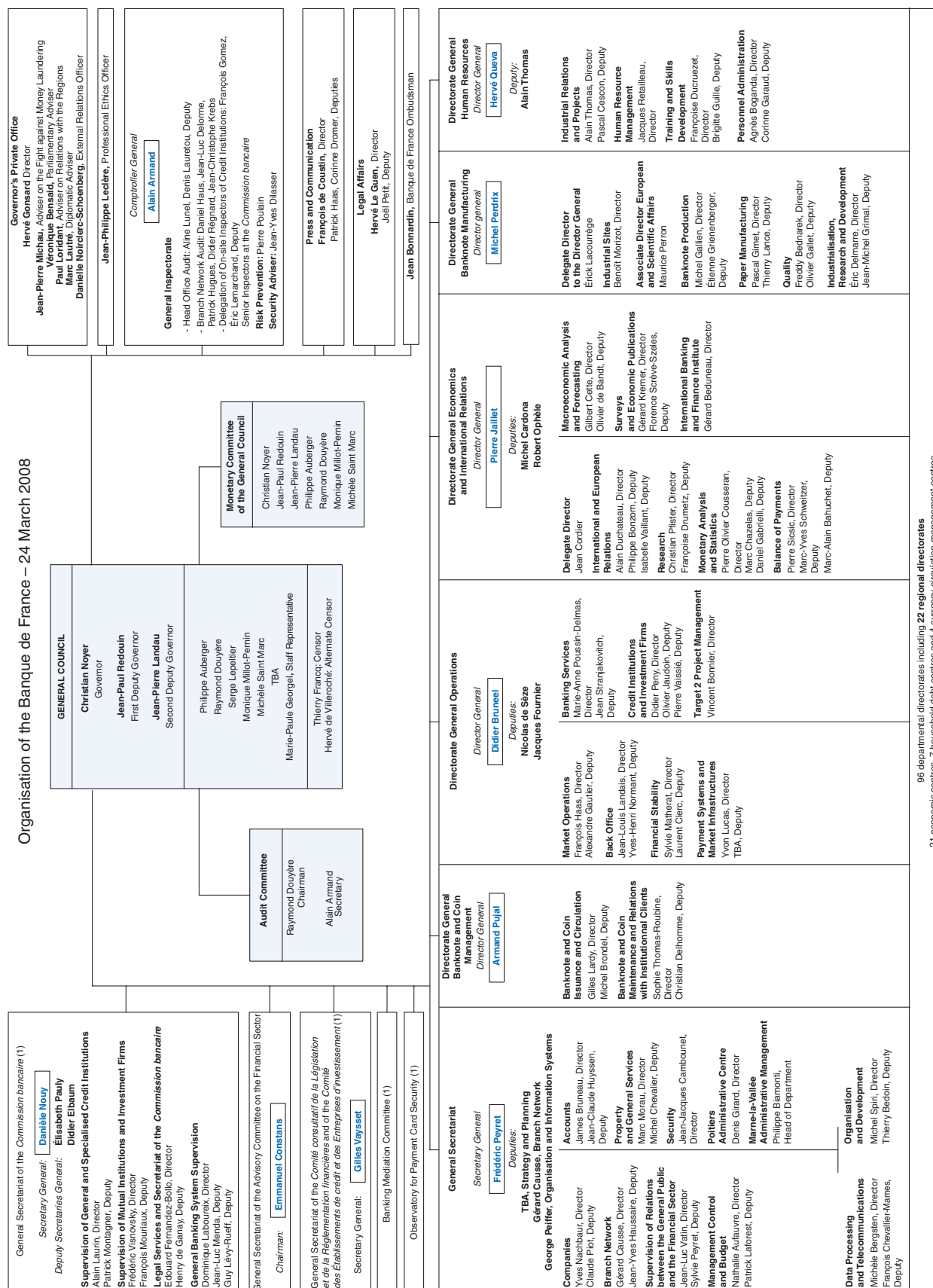


## The Banque de France's Advisory Council at 17 April 2008

Edmond Alphandéry	Chairman of the Supervisory Board of the Caisse nationale de Prévoyance
Jean-Paul Bechat	Former Chairman of the Executive Board of the SAFRAN group
Jean-Louis Beffa	Chairman and CEO of Compagnie de Saint-Gobain
Vincent Bolloré	Chairman of the Board of Bolloré Participations
Martin Bouygues	Chairman and CEO of the Bouygues group
Jacques Calvet	Company Administrator
Martine Clément	Manager of Vaneau Industrielle et commerciale
Bertrand Collomb	Honorary Chairman of Lafarge
Thierry Desmarest	Chairman of the Board of Total
Élisabeth Ducottet	Chairman and CEO of Thuasne
Xavier Fontanet	Chairman and CEO of Essilor International
Pierre Gadonneix	Chairman of the Board of EDF
Brigitte de Gastines	Chairman of SVP International
Jean-Louis Giral	Chairman of the Supervisory Board of Desquenne et Giral
François Grappotte	Honorary Chairman of the Legrand group
Marc Ladreit de Lacharrière	Chairman and CEO of FIMALAC
Bernard Liautaud	Chairman and CEO of Business Objects
Henri Martre	Honorary Chairman of GIFAS
Gérard Mestrallet	Chairman and CEO of Suez
Jean-Charles Naouri	Chairman and CEO of the Casino Euris group
Denis Ranque	Chairman and CEO of Thalès
Louis Schweitzer	Chairman of the Board of Renault
Ernest-Antoine Seillière	Chairman and CEO of Wendel Investissement
Serge Tchuruk	Chairman of the Board of Alcatel-Lucent
Thierry de la Tour d'Artaise	Chairman and CEO of Seb SA



## Organisation of the Banque de France – 24 March 2008



96 departmental directorates including 22 regional directorates  
21 economic centres, 7 household debt centres and 4 currency circulation management centres.

(1) The Governor chairs the *Comité des établissements de crédit et des entreprises d'investissement*, the *Commission bancaire*, the Banking Mediation Committee and the Observatory for Payment Card Security.





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