

2008 | ANNUAL REPORT
BANQUE DE FRANCE

To
The President of the Republic
And Parliament

By Governor Christian Noyer



**The photographs featured in this report
were taken by Pascal Assailly, Jean Derennes and Philippe Jolivel.**

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A WORD FROM THE GOVERNOR

The fundamental task of a central bank is to foster monetary and financial stability. Put simply, its actions are aimed at maintaining *confidence* in the currency and the banking system. The management of the far-reaching financial crisis that we are currently experiencing has highlighted the crucial role played by the Banque de France as a member of the Eurosystem and the institution responsible for banking supervision in France.

This *Annual Report* presents the Banque de France's perspective on the current crisis and its impact on the economy as well as the measures taken to stem it and bolster economic activity, notably via the credit channel.

Regarding the Banque de France's role, I would like to underscore three points:

- Its *responsiveness*, which enabled it from the onset of the crisis in August 2007 to provide the interbank market with funds very rapidly and on a massive scale and to support bank liquidity. The Banque de France subsequently prepared and implemented changes to the Eurosystem's refinancing procedures. These comprised extending the maturity of its refinancing operations, broadening the range of eligible currencies and collateral and conducting fixed-rate tenders with full allotment. The Banque de France's capacity to act quickly and adapt to new circumstances attests to the professionalism of its staff, to whom I would like to pay tribute here for their competence and intense operational efforts.

- Its *expertise*: the Bank's knowledge of the markets and of banks are mutually reinforcing. The supervision of French banks — whose position is relatively healthy compared with that of banks in many countries — has benefited from the close links between the bank supervisory authorities and the Banque de France. These advantages are now clearly visible both in France and at the European level. The Banque de France has thus been able to actively contribute to the discussions aimed at overhauling the governance of the financial system at national, European (within the context of France's presidency of the European Union)



and international (G7, G20, the Financial Stability Forum) levels.

- The *service* it provides to the national community. Two examples illustrate this. The first relates to the Bank's role in designing and managing payment infrastructures. The Banque de France has long been responsible — along with the banking industry — for the management and development of payment and transfer systems. The financial crisis has demonstrated the resilience of these systems. The second concerns the analysis and monitoring of the transmission mechanisms of the crisis to the real economy with respect to the financing of both businesses and households. The Banque de France's competencies prompted the government to give it an enhanced role in this area, to assist the work of the Credit Mediator. The directors of the Banque de France's branches implemented the mediation mechanism in France's *départements* without delay.

Amid the substantial demands being made on it, in 2008, the Banque de France continued its efforts to adapt and modernise the institution's management, thus acting in the best interests of the national community. The *Annual Report* also gives account of these developments.



*Trading room
at the Banque de France*

THE IMPLEMENTATION OF MONETARY POLICY IN THE CONTEXT OF THE FINANCIAL CRISIS

The year 2008 saw very contrasting developments. Until the summer, it appeared that the impact of the financial crisis might remain contained, that developed and emerging economies would merely register a slowdown in growth and that inflation would constitute the main threat to be addressed by monetary policy. However, the failure of Lehman Brothers, the extremely sharp contraction in activity and plummeting commodity prices completely changed the outlook during the last quarter. This calls for a closer analysis of more recent developments, above and beyond average yearly trends.

I | The international environment

I | I | Financial and commodity markets

I | I | I | Financial markets

In 2008, the functioning of financial markets deteriorated with the unfolding of each episode of the financial crisis. The difficulties faced by monoline insurers (Fitch's downgrade of Ambac's credit rating in January), JP Morgan's takeover of Bear Stearns in March, the nationalisations of Fannie Mae and Freddie Mac on 7 September and, more particularly, the failure of Lehman Brothers on 15 September, were the most critical events. Across all market segments, the weakening of the financial system triggered a major liquidity shortfall, causing investors to become extremely risk averse. A large number of leading market participants shunned the markets, notably asset managers faced with actual or potential client withdrawals. The concomitant deterioration in the economic environment – marked by the entry into recession of most developed economies during 2008 and the contagion of the crisis to emerging economies – also contributed to a further decline in financial markets. By contrast, measures adopted by central banks and governments supported financial markets (an outline of the main measures can be found at the end of the present chapter).

The money market sustained the heaviest pressure in 2008, with various investors – interbank or otherwise – reducing their lending to credit institutions across all maturities irrespective of its type (both secured and unsecured loans). This pressure reached its peak in the wake of the Lehman Brothers collapse. Pressures were underscored by a sharp increase in volatility derived from options on money market rates (see Box 1). It was only thanks to the measures implemented by central banks and governments that trading resumed on the money market, although this did not constitute a return to normal activity.

As in the money market, risk aversion in other market segments also acted as the main driver of capital flows.

In the forex markets, 2008 also witnessed a flight to the US dollar as a safe-haven currency. As a result, in 2008, the United States recorded positive net capital inflows for the first time since 1960. Carry trade strategies were also abandoned in 2008 owing to the sharp increase in volatility and falling interest rates. The US dollar therefore appreciated against all other currencies apart from the yen and the dollar's nominal effective exchange rate (as measured against the currencies of the United States' main trading partners) rose by 13% over the year. The rise in the yen's real effective exchange rate (taking into account inflation differentials with partner countries, which is a significant factor for a country with extremely low inflation such as Japan) was particularly pronounced in 2008 (30%). This appreciation can be mainly ascribed to the unwinding of yen carry trades which consisted in buying back yen previously borrowed and sold to finance investments in high-yield currencies. In 2008, the euro and the US dollar therefore depreciated against the yen by 22.1% and 18.6% respectively. As a result of lower volatility on investments, the euro's nominal effective exchange rate against the currencies of 24 leading trading partners rose by only 2.5%. By contrast, sterling depreciated considerably vis-à-vis its main trading partners, with its nominal effective exchange rate dropping by 24.9% over the year. Sterling's strong correlation to financial sector trends, as well as the unwinding of yen-financed sterling-denominated investments, largely accounts

Box 1

A sharp increase in volatility on financial markets in 2008

Volatility measures the magnitude of fluctuations in a financial asset's value.¹ The level of volatility makes it possible to assess the dispersion of market operators' expectations, with high volatility pointing to a high dispersion of expectations. It also reflects investor risk appetite. In this respect, the 2004-2007 period was characterised by low volatility, reflecting marked risk appetite, and as a result low return on risk. 2008 constituted a decisive break with this period.

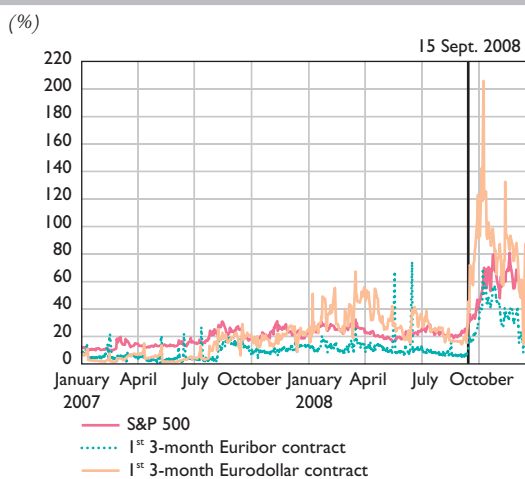
The return of volatility and strong risk aversion occurred in the immediate aftermath of the major episodes of the financial crisis during 2008. The difficulties faced by Bear Stearns at the end of March triggered an initial brief upsurge. The difficulties faced by Freddie Mac and Fannie Mae, the sharp decline in commodity and oil prices, the dollar appreciation and tumbling share prices – in emerging and developed economies alike – drove volatility significantly upwards from 15 July 2008 onwards. Lastly, the failure of Lehman Brothers on 15 September and the ensuing destabilisation of financial markets pushed volatility to unprecedented highs across all market segments. The rise was directly proportional to the withdrawal of investors from all asset types and hence to the reduction in liquidity for each investment segment. In early 2009, volatility eased back from these historic levels, but nonetheless remained high.

The increase in volatility was particularly marked on the money market. The failure of Lehman Brothers on 15 September 2008 was accompanied by a dry-up of liquidity in the interbank market. This triggered a sharp increase in volatility derived from options on money market rates. Implied volatility, which stood at below 10% at the start of 2007, rose briefly above the 100% mark (on options traded on 3-month Eurodollar contracts).

Implied volatility on stock markets, which stood at around 20% at the start of 2008, reached levels close to 80% in October and November, i.e. far higher than the historic peaks observed during previous stock market crises (44% in September 1998 and 43% in September 2001).

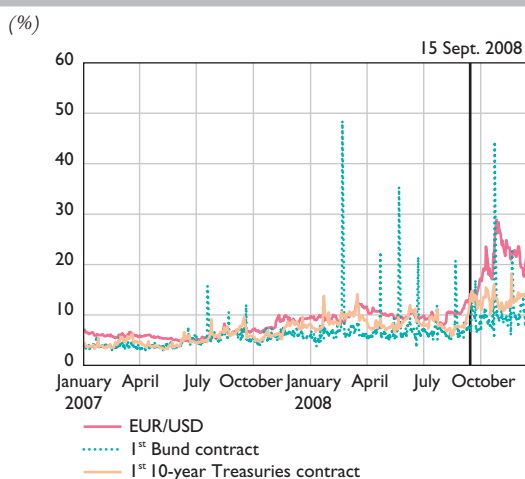
¹ Historical and implied volatility are differentiated. Historical volatility is the standard deviation observed ex post between two periods, while implied volatility is the forward-looking parameter used to calculate the value of buy and sell options traded in markets. Implied and historical volatilities are correlated, notably because the implied volatility that is used to price options depends on the actual volatility observed on the markets.

Chart 1 Implied volatility of options on the stock and money markets



Source : Bloomberg.

Chart 2 Implied volatility of options on the forex and bond markets



Source: Bloomberg.

.../...

On the forex market, the 1-month implied volatility on the EUR/USD exchange rate, which stood at a low of 5% in 2007, increased to 30% in October 2008. The rise in volatility was even more pronounced for the USD/JPY exchange rate, this being a less liquid currency pair that was impacted by massive carry-trade unwinding transactions. On commodity markets, owing notably to lower market liquidity, volatility derived from gold options also increased sharply, reaching almost 60% (1-month).

By contrast, volatility on long-term sovereign bond yields remained more stable. Although it increased significantly over the period – doubling between January and December both in Europe and the United States, and intermittently reaching levels close to 15-18% in October and November – due to the constant flow of investor purchases of these risk-free investments, volatility remained lower than on other market segments.

for the collapse of the UK currency, which primarily occurred from September 2008 onwards. Driven by large-scale capital outflows, emerging currencies also depreciated substantially, with the Brazilian real plunging by 23% against the US dollar, and the Russian rouble by 32%.

Risk premia on private bond issues rose sharply. The different episodes of increasing risk aversion significantly dampened investor appetite for this asset type. Risk premia reached historic peaks in mid-September, in the wake of the Lehman Brothers' failure. The increase impacted issuers with lower ratings in particular. The yield spread between a 5-year bond of a BBB-rated private issuer and a sovereign issue of equivalent maturity reached 814 basis points for dollar-denominated issues at end-December 2008 (i.e. a 573-basis point increase over the year) and 640 basis points for euro-denominated bonds (a 482-basis point rise). Furthermore, issuance volumes for structured credit products declined sharply against a backdrop of general investor wariness about this type of instrument. Financing conditions in emerging countries also deteriorated during the second half of the year. The JP Morgan EMBI Global index, which tracks yield spreads of emerging market bonds relative to their US counterparts, increased from 323 basis points at end-August to 725 basis points by the end of the year.

Global stock markets fell sharply during 2008: by 33.8% on the Dow Jones index, 40.5% on the Nasdaq index, 42.1% on the Nikkei, 42.6% on the CAC 40 and 43.6% on the EuroStoxx 50 index. Stock prices fluctuated with the level of risk aversion (thereby facilitating a temporary rebound from mid-March to mid-May). In sectoral terms, non-cyclical stocks (healthcare and retail) proved more resilient than automobile stocks and, even more so, financial stocks. Although overall emerging stock markets held up well until mid-May, they subsequently fell sharply, with Morgan Stanley's MSCI Emerging Markets Index shedding 55% over the year as a whole.

Investors seeking risk-free investments favoured sovereign debt issued by developed countries. As a result, the main government debt markets appreciated, also benefiting from central bank interest rate cuts and a deflationary environment that became particularly marked during the second half of the year. The yield curves of developed country bond markets steepened significantly, with the exception of Japan's, which remained stable. Accordingly, the short end of the yield curve dropped more markedly (by 202 basis points to 2.08% and by 236 basis points to 0.72% for the French and US 2-year rates respectively) than long-term yields (down by 100 basis points to 3.42% by and by 200 basis points to 2.07% for the French and US 10-year rates respectively).

Hence, the steepening of the yield curve was more significant in the euro area, especially for debt instruments, excluding German government bond issues. Within the euro area, bond yield spreads vis-à-vis Germany widened sharply during the fourth quarter, most notably for Spain, Ireland, Portugal and Italy, reaching extremely high historical levels.

Investor concerns over the extent of certain budgetary commitments, the fragility of the economic growth model (weight of real estate investments in Ireland and Spain) and even the lack of depth of the government bond market (Finland's, for example) drove large amounts of capital towards German government debt, which was perceived as more secure and more liquid.

Box 2

Credit derivatives

Credit derivatives include a wide variety of products (targeting specific debt or indexed to a basket of securities, index-linked products, products backed by securitisation transactions, etc.) and often fall under the generic umbrella of credit default swaps (CDS). These instruments enable operators who trade in them (protection buyers) to transfer to other players (protection sellers) all or part of the credit risk associated with an underlying bond or debt. Outstanding amounts of credit derivatives have ballooned since their creation at the end of the 1990s. With notional market outstandings of USD 62 trillion in June 2008, credit derivatives volumes have comfortably exceeded their equity derivatives equivalent (USD 10 trillion), but still fall well short of interest rate derivatives (USD 458 trillion).

The multiplication of bank failures and, potentially, the number of business failures caused by the financial crisis has made it necessary to rapidly secure the CDS market using adapted market infrastructures. These measures were requested at the G20 meeting of November 2008 and could be rolled out during the course of 2009. These measures have a three-pronged target:

- **Limiting counterparty risk**

The banking crisis triggered widespread doubts as to the soundness of market participants. Yet, this market segment functions only if protection buyers have the guarantee that they will be repaid by their counterparty in the event of a default. A clearing house that acts as a substitute for a defaulting counterparty provides transactions with this crucial safety net.

- **Introducing more transparency**

The Lehman Brothers collapse demonstrated the complexity of unwinding OTC derivatives transactions to which the bank was a party. The total extent of exposure was unknown and this uncertainty weighed heavily on market participants. Several counterparties found themselves unprotected against risks that they had sought to hedge. Others remained unsure of whether they would be able to regain their collateral or investment.

- **Reducing systemic risk (“too interconnected to fail”)**

The failures – or near failures – of leading financial players underscored the potential for systemic contagion following a counterparty's default, notably involving a major market participant at the centre of numerous transactions. Such failures notably result in increasing the fragility of protection buyers who lose their coverage and who, in turn, weaken the position of their own counterparties. Accordingly, in the wake of Lehman Brothers' failure, correlation increased and there was an across-the-board rise in banks' CDS premia. The emergence of this type of systemic risk necessitates the crafting of global solutions to limit contagion effects owing to counterparty default.

Box 3

Contagion mechanisms of the crisis

How did an initially limited and localised event (defaults on the US real estate segment) spill over to other markets, resulting in a global financial crisis of unprecedented proportions?

- **First, product sophistication hampered risk assessment**

The subprime crisis spread throughout the global financial system via the securitisation mechanism, which enabled loan risks to be spread to investor balance sheets worldwide. In practice, this mechanism consists in selling a pool of loans to an independent vehicle known as a “conduit” or “structured investment vehicle,” which secures financing from the markets by issuing asset-backed securities (ABS) and, in this case, residential mortgage-backed securities (RMBS). Certain tranches of these products were subsequently pooled again, this time into collateralised debt obligations (CDO). The last stage consisted of investors buying these structured products without complete knowledge of the underlying risk due to the layer structure.

- **The amplifying role of credit rating agencies and monoline insurers**

The widespread success of structured products can be attributed to the fact that they were highly rated by credit rating agencies, guaranteed by credit enhancers referred to as monoline insurers and offered attractive yields. When initial losses on subprime loans occurred, the extremely sharp rating downgrades on a number of previously highly rated products fuelled investor fears. Monoline insurers, facing capital shortfalls, were soon unable to meet their commitments. They suffered their own rating downgrades, which, in turn, automatically fed through to the ratings of structured products they had insured.

- **Liquidity dry-up and valuation problems**

The reappraisal of risks linked to structured products, combined with unclear and complex financial structures, drove investors away, leading to prolonged illiquidity on these markets. The suspension of trading therefore made it impossible to determine a market price and heightened uncertainty over asset valuations.

- **The re-intermediation process**

A number of securitisation vehicles that were relying on short-term financing but which held assets over the long term could no longer secure financing. Consequently, they drew down their bank credit lines, thereby triggering a liquidity crisis on the interbank lending markets. Furthermore, banks that had retained links with securitisation vehicles were forced to bring back onto their balance sheets the assets they had previously sold.

- **The impact of contagion via liquidity and valuation problems on bank solvency**

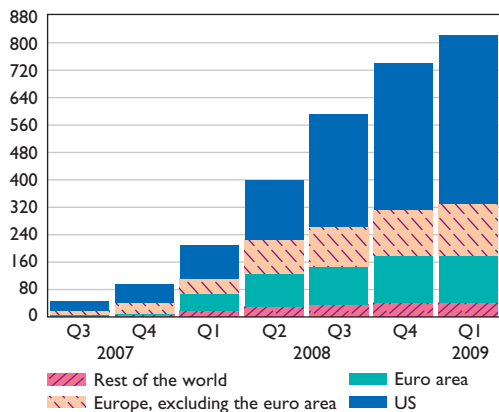
Banks were obliged to book these assets at market value and thus generated large-scale capital losses. To maintain their solvency levels, they not only had to raise capital but were also forced to dispose of assets and gradually reduce the size of their balance sheets (i.e. deleverage), which exacerbated the vicious circle of tumbling securities prices. In total, global bank losses rose from USD 100 billion at end-2007 to over USD 800 billion at end-2008.

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Chart 3 Amount of writedowns* and loan losses

Sample of 80 international banks

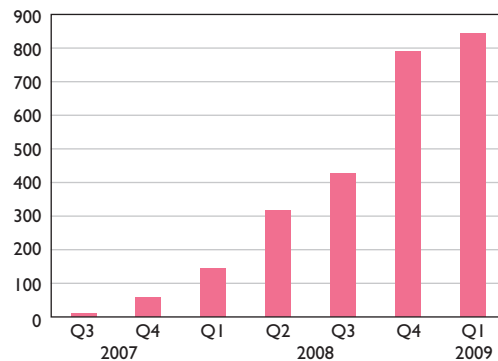
(USD billions)



* Writedown: the downward adjustment of the accounting value of securities and loans.
Source: Bloomberg.

Chart 4 Recapitalisations in the banking sector

(USD billions)



Source: Bloomberg.

The Lehman Brothers collapse in September pushed the uncertainty and instability clouding the entire financial system to peak levels. Indeed, it triggered a profound crisis of confidence in the solvency of financial institutions and sparked fears of a systemic crisis. Risk premia on banking sector default (credit default swaps) reached record highs before easing in the wake of decisive action by central banks and governments. The aim of this raft of measures taken by public authorities was, among other things, to ensure lending to the economy by limiting knock-on effects to the real sector (see Section 3).

1|1|2 Commodity markets

Averaging USD 97.9 per barrel of Brent in 2008, oil prices jumped by around 35% relative to 2007's annual average price (USD 72.6 per barrel). The price of crude oil was nonetheless subject to extreme volatility during that time. The price of Brent in early 2008 stood at around USD 90 per barrel and, extending the uptrend that began in August 2007, reached a record high of USD 145 per barrel in mid-July, before plummeting during the second half of the year, finishing the year at around USD 40 per barrel, i.e. its January 2005 level.

The sharp rise in Brent prices during the first half of 2008 was triggered by the possibility of maintaining growth in Europe and emerging countries despite weaker US economic growth (the decoupling assumption) and, therefore, of sustaining an increase in demand (from China and India, in particular). However, demand

started to fall away in most developed nations as of the summer of 2008, thereby inverting price trends. Commodity prices eased further from September, when the global growth outlook was revised downwards.

Commodity prices excluding energy were also extremely volatile. The acceleration in the rise in food commodity prices, which began in 2007, continued during the first quarter of 2008. Food prices subsequently stabilised until the summer before plunging along with all commodity prices.

A number of observers considered that the sharp increase in agricultural commodity prices was notably caused by the structural rise in demand from new emerging economies. The appearance of these new players on the global economic scene was accompanied by a rise in the per capita income in these countries and by the gradual change in their consumption structures. This structural increase

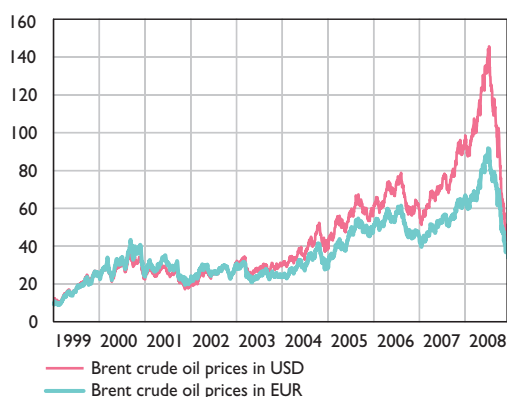
in demand was only partially matched by a shift in supply. Furthermore, a series of extreme climatic events over the past few years has strongly affected farming production, which is highly concentrated. Moreover, rising oil prices have weighed indirectly on food supply. The search for oil substitutes becomes economically viable as of a certain price level, resulting in using more land for ethanol production. This has reduced the amount of land available for producing other cereal crops, whose demand has not decreased, thereby triggering price pressures.

These various phenomena sparked price pressures that were partially contained by a marked drop in the level of global agricultural commodity inventories. Hence, in 2008, wheat, corn and rice inventories fell to 30-year lows, both in terms of days of available consumption and absolute amounts. Declining energy prices and the prospect of improved harvests triggered a significant price decrease in the second half of the year.

After easing slightly in 2007 by 1.9%, the Banque de France index of imported commodity prices rose sharply in 2008 in annual average terms (33.3%). The jump in the index can be largely attributed to spiralling oil prices. However, euro exchange rate developments, notably against the dollar, reduced the volatility of the index.

Chart 5 Brent crude oil prices

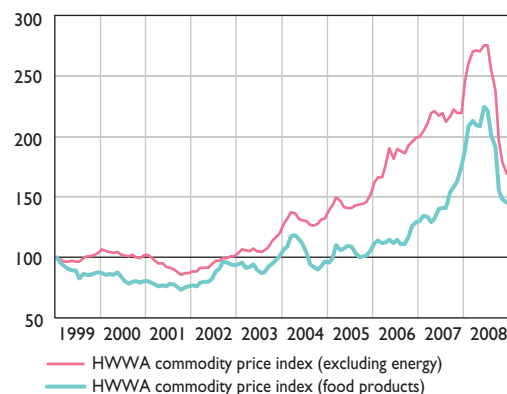
(in USD and EUR)



Source: Datastream.

Chart 6 Commodity price index excluding energy

(100 = January 1999)



Source: Datastream.

Euro appreciation during the first half of the year partially offset increased crude oil prices (which are dollar-denominated), while euro depreciation in the second half, in contrast, cushioned the impact of falling oil prices.

I | 2 Economic growth in non-euro area countries

The growth of the great majority of economies – both developed and emerging – underwent a sharp slowdown in 2008, i.e. generally 2-3% below than that of 2007. By aggregating national data at purchasing power parity, the International Monetary Fund (IMF) estimated that from 2007 to 2008, global economic growth had declined from 5.2% to 3.4% and even to 1.1% in year-on-year terms during the final quarter.

I | 2 | 1 The United States

US gross domestic product growth slackened significantly in 2008, but still stood at 1.1% as an annual average (2.0% in 2007). However, December 2007 was marked as the official start of the recession as job destructions commenced during this month and increased thereafter. In total, almost 3 million jobs were cut during the ensuing year, sending the unemployment rate from 4.9% to 7.2% from one year end to the next.



Growth, which was weak in the first quarter (0.2%), picked up during the second (0.7%) due to the effects of the first stimulus package rolled out in February (the Economic Stimulus Act). However, the situation was reversed in the third quarter and, above all, in the fourth (-0.1% and -1.6%), reflecting the deepening financial turmoil and its spill-over effect to the real economy.

The adjustment in the US housing market continued throughout the year and resulted in sharp price decreases (at the end of 2008, the Case-Shiller home price index of twenty large US cities had dropped by 27% relative to its peak in 2006) and in a further and significant decline in housing investment (almost 20% year-on-year and 40% over three years), shaving almost one percentage point off 2008 growth. Admittedly, household consumption and business investment grew slightly over the year, but they slackened markedly in the second half (by 1.4% and 3.0% respectively) compared with the first half. Foreign trade contributed positively to annual growth and to a larger extent than in 2007 (adding 1.4 percentage points to GDP growth, after 0.6%) thanks to a reduction in imports (down 3.4% in volume terms) linked to waning domestic demand and rising exports (up by 6.2% in volume terms), driven by a weaker dollar. In value terms, the improvement is less marked owing to the hike in oil import prices, but still remains significant. Furthermore, the current account deficit dropped from 5.3 percentage points of GDP in 2007 to 4.7 percentage points of GDP in 2008.

Inflation, measured by the year-on-year change in the consumer price index, reached an average of 3.8% in 2008, after 2.9% in 2007. This rise, which can be attributed to the sharp hike in energy product and commodity prices, was not even: these price increases then reversed in the final quarter of the year and, from September to December, they dropped by

3.3%, with the 12-month price increase standing at only 0.1%. Even underlying inflation (i.e. excluding energy and food) was impacted and registered a 0.1% decrease in the fourth quarter. This was the result of a sharp slowdown in domestic demand and the easing of production capacity pressures. The production capacity utilisation rate, which slid from 78.3% in August to 73.6% in December, fuelled fears of a deflationary spiral.

During 2008, the US Federal Reserve implemented a wide range of measures to combat the sustained weakening of activity, the rapid deterioration of financial markets and the risk of deflation. It implemented conventional measures, i.e. cutting the key Fed funds rate seven times, from 4.25% to a target range of between 0% and 0.25%. It also expanded refinancing operations and rolled out – on an exceptional and temporary basis – credit facilities to inject liquidity while directly supporting a number of financing circuits such as short-term business financing (Commercial Paper Funding Facility), consumer credit securitisation (Term Asset-backed Securities Loan Facility) and mortgage loans (Mortgage-backed Securities Purchase Program). Mr Bernanke described these moves as “credit easing” as opposed to “quantitative easing”, such as that formerly practiced by Japan. In all, the Federal Reserve’s balance sheet more than doubled in 2008.

The federal deficit widened during the 2008 financial year (which ran from 1st October, 2007 to 30 September, 2008) to 3.2% of GDP, versus 1.2% in 2007. The recession affected tax revenues, which suffered from a decline in tax receipts and corporate income tax, while military spending saw its sharpest increase since 2004. February’s stimulus package also contributed to the deterioration in the federal budget. This is, however, only the beginning of the



trend, with the deficit likely to exceed 10% of GDP in 2010 as the different financial assistance to federal agencies (Housing Economic Recovery Act, voted in by Congress in July 2008) and banks (Troubled Assets Relief Program, voted in by Congress in October), as well as the stimulus package of February 2009 (American Recovery and Reinvestment Act), are implemented.

1|2|2 Japan

Japan's GDP contracted by 0.7% in 2008, after rising by 2.4% in 2007. After recording GDP growth of 0.3% in the first quarter, Japan entered into recession with three consecutive quarterly declines in GDP of 1.2%, 0.4% and 3.2%, respectively. This rapid deterioration in activity can be attributed to shrinking export demand and the absence of domestic sources of growth.

Labour market conditions worsened significantly during the year. The vacancies-to-employment ratio dropped sharply to 0.72 in December, i.e. its lowest level since 2003. The decline in the labour force, the result of "discouraged" workers leaving the labour market, held the unemployment rate down in 2008 (4.0% as an annual average). However, a significant acceleration in unemployment occurred in the latter months of the year (4.4% in December). The weakening labour market also fed through to wages. Employees' nominal wages rose by only 0.4% over the year and dragged on household consumer spending, which dropped by 0.5% relative to 2007.

In 2008, the trade surplus declined by 80% compared with 2007, representing 0.3% of GDP, versus 2.1% in 2007. The Japanese trade balance even posted a deficit during the latter months of the year. Exports to the rest of Asia, which account for half of Japan's

revenues, remained stable in the first half of the year, but decreased markedly after July.

Corporate investment decreased sharply against a backdrop of lacklustre domestic consumption and a contraction in foreign demand.

Inflation, measured by the year-on-year change in the consumer price index, rose on average in 2008, but retreated sharply after peaking in July 2008 (at 2.3%), before subsequently moving back to 0.4% in December. The acceleration in inflation during the first half of the year was mainly due to the rapid rise in energy and commodity prices. In the second half of the year, prices fell in an increasing number of sectors, with the year-on-year change in the consumer price index likely to return to negative territory in 2009.

In order to boost its economy and avoid the recession-deflation spiral, the Japanese government announced a raft of measures of a financial nature (facilitating access to credit for small- and

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

	United States		Japan	
	2007	2008	2007	2008
Gross domestic product (a)	2.0	1.1	2.4	-0.7
Industrial production (a)	1.7	-2.6	2.9	-3.3
Consumer prices (a)	2.9	3.8	0.1	1.4
Unemployment rate (b)	4.6	5.7	3.9	4.0
General government deficit (c)	-1.2	-3.2	-2.4	-1.4
General government debt (c)	65.0	70.0	170.1	173.0
Current account balance (c)	-5.3	-4.7	4.8	3.2

a) Annual average change.

b) In level terms.

c) As a % of GDP.

Sources: National and OECD data.

medium-sized businesses with guarantees and support to the banking sector) and a fiscal nature, totalling JPY 75,000 billion (EUR 600 billion or 13% of GDP). In addition, the Bank of Japan eased its monetary policy, lowering the key interest rate to 0.1%. It also extended the range of eligible collateral, increased its monthly treasury securities purchases from JPY 1,200 billion to JPY 1,400 billion and started remunerating its excess reserves (at 0.1%) to provide sufficient liquidity to cover its requirements for the end of both the calendar and fiscal year (30 March).

1|2|3 The euro area's partners inside the European Union (EU)

Economic growth in the United Kingdom slowed sharply to 0.7% in 2008, as against 3.1% in 2007, due to the global financial crisis and the massive adjustment in the UK property market. The United Kingdom officially entered into recession with negative growth in the final two quarters of 2008. At the same time, after accelerating sharply during the first half of the year (peaking at 5.2% year-on-year in September), inflation, measured by the harmonised index of consumer prices (HICP) slowed significantly in the fourth quarter, reaching 3.1% year-on-year in December. This slowdown can be attributed to the shrinking energy component, which still contributed 12.0%, compared with a negative contribution of 3.7% for the euro area, and the temporary reduction in VAT from 17.5% to 15% between 1 December and end-2009. Average yearly inflation stood at 3.6%, after 2.3% in 2007. Accelerating inflation at the start of the year complicated the Bank of England's handling of monetary policy amid a weakened economy, with inflation largely exceeding the Bank's 2% target rate, fuelling concerns of an unmooring of inflation expectations. In the fourth quarter, when it became evident that the economy had entered into recession, the Bank of England nonetheless eased its monetary policy, cutting the key interest rate by 300 basis points between October and December. The general government deficit widened significantly in the context of the financial and economic crisis,

reaching 4.6% of GDP, after 2.7% in 2007, on the back of the Government's moves to shore up the banking sector and stimulate domestic demand.

GDP growth in the EU's New Member States (NMS) fell from 6.1% in 2007 to 4.3% in 2008. The economic slowdown impacted all countries, barring Romania, whose GDP accelerated from 6.2% in 2007 to 7.1% in 2008. Countries with high foreign debt such as the Baltic States and Hungary, which are more vulnerable to the global financial crisis, were particularly affected. Estonia posted negative growth (-3.6%, after +6.3% in 2007), as well as Latvia (-4.3%, after +10.0% in 2007), while Lithuania's economic growth slowed sharply (3.0%, after 8.9% in 2007). Growth in Hungary remained lacklustre at 0.5%, versus 1.1% in 2007. Against this backdrop, Hungary and Latvia requested financial assistance from the EU and the IMF at the end of the year. Growth slowed at a steadier pace in the other countries. Poland posted growth of 4.8%, after 6.6% in 2007, while the Czech Republic recorded 3.1%, versus 6.0% in 2007. Slovakia's growth rate declined from 10.4% to 6.4% between 2007 and 2008, while Bulgaria's was almost stable at 6.0% after 6.2% in 2007.

At the same time, prices accelerated markedly during the first half of the year, in line with rising commodity prices. Average inflation advanced from 4.2% in 2007 to 6.2% in 2008 for all NMS. Inflation accelerated in all countries, except for Hungary, and exceeded 10% in the Baltic States and in Bulgaria. However, year-on-year, the pace of price rises slowed significantly during the final months of the year, along with falling energy prices and the abrupt weakening in activity. General government deficits increased from 2.0% of GDP in 2007 to 2.4% of GDP in 2008 for NMS as a whole. However, this average masked major differences, with a significant deterioration in Romania, where the deficit widened to 5.2% of GDP from 2.5% in 2007, in contrast to Hungary, which pursued its fiscal consolidation, bringing its deficit of 5.5% of GDP in 2007 down to 3.3% of GDP in 2008. Bulgaria's budget surplus stood at 3.2% of GDP in 2008, contracting slightly relative to the 2007 reading of 3.4%.

1|2|4 The principal emerging countries

The crisis hit emerging economies with a lag, raising hopes of a “decoupling” between advanced and emerging economies. However, the crisis caught up with these economies in summer 2008, and became a truly global phenomenon.

Until the end of 2007, emerging economies were generally resilient to the financial turmoil affecting developed economies. They even benefited temporarily from a reallocation of international assets in their favour. At the time, their stock markets outperformed those of advanced countries.

Signs that the crisis had spread to emerging countries multiplied from the start of 2008. The pace of foreign capital inflows and, notably, that of portfolio investment, slowed. Emerging country stock markets posted steep declines, although initially in equivalent proportions to those of industrialised countries. Endogenous factors also existed to explain the contraction, after a period of excessive stock price valuations. In June 2008, the decline in emerging markets accelerated and they started to underperform their advanced counterparts. Emerging market currencies began to depreciate against the US dollar as of the summer of 2008.

The contagion to emerging economies stepped up from September 2008, triggered by the collapse of Lehman Brothers. The slowdown of capital inflows during the previous phase was followed by an outflow. Emerging market investment funds, in particular, recorded USD 30 billion in net outflows at end-October 2008. As a result, US dollar refinancing became more difficult to obtain, leading to steeper stock market losses. In October 2008, the crisis emerged. On 22 October, the EMBI spread (difference between the yield of an emerging market sovereign bond and that of a US Treasury bond) reached 950 basis points in Russia and 850 basis points in Turkey, versus 127 and 263 basis points respectively at the beginning of the previous month, and only 76 and 79 basis points a year earlier. Concomitantly, downward pressures observed since the summer on most emerging currencies mounted. These currencies not only wiped out the appreciation of the initial months of the year, but, above all, depreciated in net terms, retreating to historical lows.

Table 2 Principal economic indicators of the BRIC economies

(GDP and foreign exchange reserves are in billions of dollars. Annual growth rates are expressed as percentages unless otherwise indicated)

	Brazil	Russia	India	China
Nominal GDP	1,573.0*	1,677.0	1,210.0	4,402.0
GDP change	5.1	5.6	7.3	9.0
Inflation trends (CPI)	5.7	14.1	8.3	5.9
Budget balance (% of GDP)	-0.9	3.5	-5.4	-0.3
Current account (% of GDP)	-1.8*	6.1	-2.8	10.0
Foreign exchange reserves	192.9	421.4	271.0	2,134.5
Change in foreign exchange reserves	7.5	-9.7	1.3	39.4

* Estimate.

Source: IMF, *World Economic Outlook*, April 2009.

The crisis then affected the real economy. In September, a halt was observed in the two-year rapid rise in average GDP growth in emerging economies of around 7%, with the latter falling to 5.5% in the last quarter. Decreases in consumption, investment and net exports all contributed to this slowdown.

2| Situation of the euro area and Eurosystem monetary policy

2|1 Economic and financial situation of France and the euro area

2|1|1 Economic analysis

Economic activity

Euro area economic activity slowed significantly in 2008: average yearly GDP growth advanced by only 0.7% (quarterly accounts at chain-linked prices, adjusted for seasonal and working day variations), versus 2.6% in 2007. The year was marked by the area falling into technical recession (two consecutive quarters of contraction in activity).

As was the case in Germany, after rising sharply in the first quarter, euro area GDP contracted during the second quarter, and further declined in the third quarter. The decline intensified in the fourth quarter against the backdrop of the major financial crisis and the sharp slowdown in global demand. While GDP growth remained positive on average in 2008, plunging activity levels at the end of the year weighed on the following year's GDP, with a carry-over of -1.4% for 2009 at end-2008.

The euro area's economic slowdown can be mainly attributed to a steep deceleration in domestic demand (excluding inventories), with the latter contributing 0.8 point to GDP growth, after 2.3 points in 2007. To a lesser extent, it was also due to the shrinking contribution of foreign trade (zero, after 0.3 point in 2007) and inventory changes (-0.1 point, after zero in 2007). Private consumption and investment, two components making up domestic demand, slowed sharply from 1.6% to 0.5%, and from 4.3% to 0.6% respectively between 2007 and 2008.

Approximately one-third of the decline in euro area activity was due to lower household spending in 2008. This was notably caused by the erosion of purchasing power linked to the sharp acceleration –until mid-year– of food and energy prices, which drove inflation to an average 3.3% in 2008, after 2.1% in 2007, despite a year-end decrease due to easing commodity prices. Furthermore, the turnaround in the labour market weighed on household income and spending trends. Employment growth gradually lost steam, becoming negative during the third quarter of 2008.

The fall-off in investment was already significant in 2007 owing to a dimmer demand outlook and a downturn in the real estate market in several euro area countries (particularly Spain and Ireland). This development continued into 2008 and accelerated at the end of the year due to the financial crisis. The crisis led to tighter lending conditions and a negative wealth effect due to plunging share prices. These developments resulted notably in a slowdown in construction, which shrank by 8.2% year-on-year in the fourth quarter

of 2008, compared with a year-on-year decline of 2.4% in the fourth quarter of 2007. They also weighed on productive investment, which slowed markedly in 2008 after two years of strong growth.

The deceleration of exports that began in 2007 continued in 2008, with volume growth of only 1.6% over the year as a whole, compared with 5.9% in 2007 and 8.5% in 2006. At the same time, euro area imports also slowed due to slackening domestic demand, which posted a rise of only 1.7% in 2008, after 5.3% in 2007 and 8.3% in 2006. In spite of starting to fall in the middle of the year, commodity prices increased sharply on average in 2008 (by 26.0%), leading to a worsening of the euro area's trade balance. The latter posted a deficit of EUR 32.1 billion, as against a EUR 15.8 billion surplus in 2007. The area's trade balance excluding energy posted a surplus of EUR 250.9 billion in 2008, compared with EUR 228.2 billion in 2007.

In 2008, the economic growth of the four largest euro area economies recorded a much sharper slowdown than in 2007. The commodity price shock, slowing global demand and the financial crisis were common factors that, to a large extent, account for the similarities observed in these countries, albeit to varying degrees.

France posted GDP growth of only 0.3% in 2008, as against 2.3% in 2007. This constituted the country's weakest performance since 1993. As in the euro area as a whole, household consumption slowed significantly (growth of 0.9% in 2008, after 2.4% in 2007), as did investment (up by 0.4% in 2008, after 6.5% in 2007). As in previous years, the contribution of France's foreign trade to GDP growth was negative (-0.3 percentage point) and trailed the rest of the euro area, which has been the case since 2002. Nonetheless, the overall performance of the French economy almost matched that of the euro area in 2008 and, even if the first-quarter reading lagged the region as a whole (up by 0.4% for France, compared with 0.7% for the euro area), activity in France in the second half of the year performed slightly better than in the euro area as a whole, whose GDP contracted more rapidly than France's in the last two quarters.

Box 4

Current account transactions in France's balance of payments

France posted a current account deficit for the fourth consecutive year. In 2008, it stood at EUR 44 billion, compared with EUR 18.9 billion in 2007 (balance of payments data). This fresh deterioration can be predominantly attributed to the goods deficit, which increased by EUR 15.1 billion (based on customs data) due to the sharp rise in oil prices during 2008.

Goods trade

Against the backdrop of the sharp slowdown in world trade, French goods exports increased in value terms (based on customs data) by only 2.2% in 2008, after a 3.2% rise in 2007. Fob imports also slowed – albeit more modestly – posting a 5.4% rise in 2008, compared with 5.8% in 2007 (see Table 3). This annual increase was achieved in the first half of 2008, with imports declining during the second half-year. As a result, the worsening of France's goods trade balance continued in 2008. The fob-fob trade deficit¹ reached EUR 55.6 billion, after EUR 40.5 billion in 2007, i.e. almost 3% of GDP.

Table 3 Annual developments in France's goods trade balance

(EUR billions, % change)

	2006	2007	2008
Fob exports	388.9	401.4	410.3
Year-on-year change	9.0	3.2	2.1
Fob imports	417.8	442.0	465.9
Year-on-year change	9.9	5.8	5.3
Fob-fob balance	-29.0	-40.5	-55.6
Year-on-year change	-5.7	-11.6	-15.1

Source: Ministry of the Economy, Industry and Employment – Customs and Excise Department (estimated unadjusted data).

In contrast to 2007, the deterioration in 2008's total trade balance can be ascribed to the rising oil bill, which increased from EUR 45.8 billion to EUR 58.7 billion. The cause is three-fold: a sharp hike in oil prices during the first half of 2008, a rise in natural gas prices, which lag oil price hikes and stable import volumes.

The stability in the goods trade balance excluding energy stemmed from favourable performances in the following segments:

- capital goods (due to aerospace exports);
- consumer goods (thanks to pharmaceutical goods exports);
- agricultural products (owing to extremely high average agricultural commodity prices in 2008).

These solid performances offset the decline in the external trade balance for the automotive industry, agri-food industry products (despite substantial sales increases) and intermediate goods (see Table 4).

The deterioration in the automotive industry continued in 2008, with the sector trade balance turning negative (with a deficit of EUR 3.4 billion) owing to a particularly sharp drop in exports towards the end of the year. Year-on-year, the decline reached 10.6% and 12.6% for motor vehicles alone. The industry's exports have declined by almost 15% since 2004 (see Chart 7). The fall in French automotive exports was very marked in its main market, namely Europe (down by 12.3% year-on-year), even though the European market share of French carmakers stopped shrinking in 2008 (see Chart 8). Indeed, in terms of car sales in Europe, US and Asian carmakers were more severely impacted than their European competitors.

¹ i.e. excluding transport and insurance costs on imports.

.../...

Table 4 Sector trends

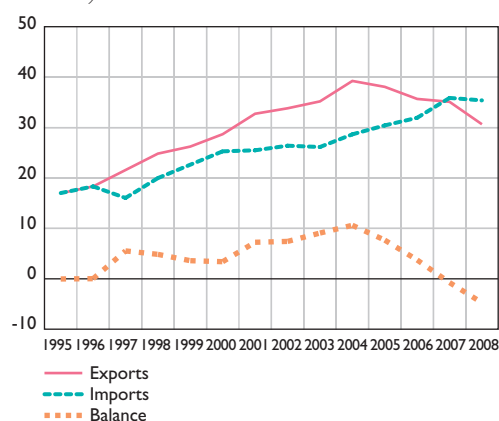
(EUR billions, % change)

	Exports		Imports		Balance	
	2008	2008/2007 change	2008	2008/2007 change	2008	2008/2007 change
Goods trade balance (fob-fob)	409.6	2.1	465.3	5.3	-55.7	-15.1
<i>o/w:</i>						
Agricultural products	13.7	15.9	10.3	4.6	3.5	1.4
Agri-food	36.3	4.4	30.5	9.6	5.8	-1.1
Consumer goods	62.1	3.0	71.4	1.2	-9.3	1.0
Automotive products	45.7	-10.6	49.0	-2.3	-3.4	-4.3
Capital goods	97.2	3.6	90.5	-0.2	6.7	3.5
Semi-processed goods	123.3	-1.8	136.5	-1.2	-13.1	-0.7
Energy products	23.1	37.9	81.8	30.8	-58.7	-12.9

Source: Ministry of the Economy, Industry and Employment – Customs and Excise Department (estimated unadjusted data for the total and unadjusted data for sector revenues).

Chart 7 External trade in motor vehicles

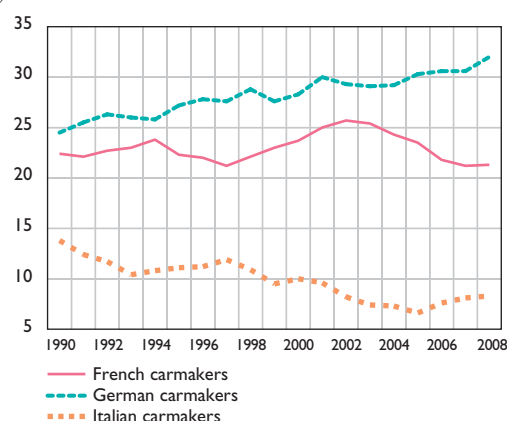
(EUR billions)



Source: Ministry of the Economy, Industry and Employment – Customs and Excise Department (DGDDI).

Chart 8 Market share in Europe

(%)



Note: Automobile constructors' share of new registrations for private vehicles in EU-15 plus EFTA countries.
Source: ACEA, Banque de France calculations.

From a geographical standpoint (see Table 5), much of the deterioration in France's overall trade balance in 2008 can be ascribed to trade with:

- oil-producing countries. Imports climbed by 30.7% in 2008, while exports, up by 14.2%, benefited considerably, but only partially, during the year from recycled oil and gas revenues;
- Western European countries, with Spain foremost among them, whose economic slowdown dented French exports;
- China. Chinese imports continued to expand rapidly in 2008 (up by 6.4%), while exports stagnated;
- the United States. French exports to the United States contracted markedly (down by 4.9%) due to the unfavourable economic situation in that country.

.../...

Trade in services

France's services sector surplus remained relatively stable at EUR 14.5 billion, after EUR 15 billion in 2007. However, a closer analysis of each component reveals contrasting developments. The global economic downturn weighed on tourism spending, causing France's travel surplus to narrow by EUR 4.3 billion to EUR 8.5 billion in 2008. In contrast, merchanting recorded an improvement of almost EUR 2.6 billion year-on-year to reach EUR 8.2 billion in 2008.

Income and current accounts

The income account surplus grew by almost EUR 4 billion to EUR 24.8 billion in 2008, and was driven by rising portfolio investment income and direct investment income. The current transfer deficit increased slightly to EUR 24.2 billion.

Table 5 International trade in services balance

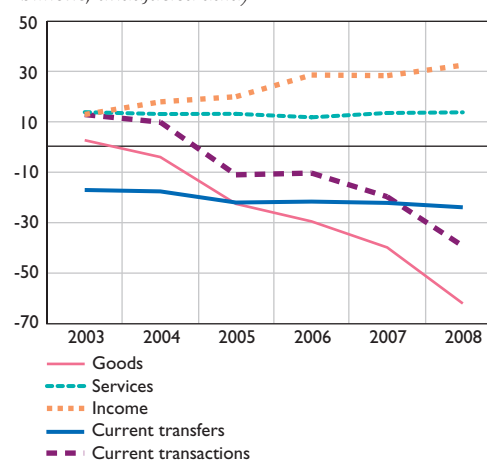
(EUR billions)

	2004	2005	2006	2007	2008
Total services	13.3	13.3	13.4	15.0	14.5
o/w:					
Transport	-3.0	-3.4	-1.9	-0.3	-0.9
Travel	13.2	10.8	12.1	12.8	8.5
Communication services	0.9	1.1	1.3	1.2	1.0
Construction services	1.2	1.6	1.9	2.3	2.8
Insurance services	-0.4	-0.9	-1.2	-0.8	-0.8
Financial services	-0.8	-0.8	-0.6	-0.1	0.0
Royalties and licence fees	1.7	2.5	2.3	3.0	3.7
Merchanting	3.3	5.9	6.2	5.6	8.2
Rentals	-0.2	-0.2	-1.2	-1.3	-1.1
Miscellaneous business services	0.4	-0.5	-2.2	-3.6	-3.1

Source: Banque de France.

Chart 9 Current account

(EUR billions, unadjusted data)



Source: Banque de France.

In Germany, GDP growth totalled 1.0% in 2008, after 2.6 % in 2007. This slowdown can be almost entirely attributed to the declining contribution of foreign trade to the country's GDP growth (-0.4 percentage point in 2008, after +1.5 percentage points in 2007) owing to a sharper deceleration in exports (up by 2.3% in 2008, after 7.7% in 2007) than in imports (up by 3.6%, after 5.2%). Despite a further fall in unemployment, household consumption stagnated (after a 0.3% decrease in 2007), having been dampened by price increases in the first half of the year.

In Italy, the deceleration in GDP growth was even more marked. After posting only a 1.4% rise in 2007, Italy's economic activity contracted by 1.0% in 2008. Household spending notably fell by an

annual average of 0.9%, having increased by 1.5% in 2007. Investment also shrank significantly (-3.0%, after +0.8% in 2007). The pronounced contraction in domestic demand triggered an even sharper decline in imports (down by 4.5%) than in exports (down by 3.7 %). These developments underscore a more marked deterioration in the situation in Italy, which was the only economy of the four leading euro area countries to have posted negative growth in 2008.

Lastly, Spain's GDP growth slowed considerably in 2008 albeit remaining in positive territory (up by 1.2% in 2008, compared with 3.7% in 2007). High household debt levels and a downturn in the property market rendered the economy particularly vulnerable to the financial turmoil. The steep decline in the growth of



Trading room at the Banque de France

domestic demand excluding inventories (which made a 0.2-percentage-point contribution to GDP growth, compared with a 4.6-point contribution in 2007) was only partially offset by the upturn in the contribution made by external trade, which became positive again (+1.2 percentage points in 2008, after -1.0 percentage point in 2007). Investment in construction, which has been the country's main engine for growth in recent years, dragged significantly on growth in 2008.

The average annual unemployment rate in the euro area was virtually unchanged in 2008 at 7.5%, after 7.4% in 2007. However, while unemployment had decreased almost continuously since 2005, it surged during 2008, mainly in the second half of the year, reaching 8.2% in December, compared with 7.2% a year earlier. While unemployment continued to fall in Germany (7.2% at end-2008, compared with 7.9% at end-2007), it rose in France (8.3% in December 2008, compared with 7.7% in December 2007), in Italy (6.9% in the fourth quarter of 2008, versus 6.4% in the fourth quarter of 2007) and especially in Spain (14.7% in December, compared with only 8.8% in December 2007), where falling construction sector activity impacted significantly on employment developments.

Inflation

From 2000 to 2007, annual average inflation in the euro area, as measured by the harmonised index of consumer prices (HICP), fluctuated within the range of 2.1%-2.3%. In 2008, it moved out of this range: the annual average increase in the HICP reached 3.3%, i.e. a rise of 1.2 percentage points relative to 2007. This level of inflation had not been observed in the euro area since 1993. In fact, this average spans two very contrasting periods. Euro area inflation, which started to climb as of the autumn of 2007, stood at 3.1% in December 2007 and continued to rise, peaking at 4.0% in July 2008 before falling to 1.6% in December 2008. Core inflation (excluding energy and unprocessed food) remained considerably more stable, edging up from 2.4% in December 2007 to 2.5% in July 2008, before easing to 2.1% in December. As with overall inflation, average annual core inflation exceeded the 2007 level, i.e. 2.4% in 2008, compared with 2.0% in 2007, although this level had already been reached in 2002.

As in 2007, energy and food prices were the main drivers of overall inflation developments. Accordingly, the year-on-year change in energy



prices jumped from 9.1% in December 2007 to 17.0% in July, before plunging to -3.6% in December 2008. This development is linked to euro-denominated oil prices, which doubled between January 2007 and June 2008, rising from EUR 42 to EUR 85 per barrel of Brent, before easing to EUR 32 per barrel in December. The rise in global food prices was gradually passed through to consumer prices between the third quarter of 2007 and the third quarter of 2008. The year-on-year change in processed food prices climbed from 2.0% in July 2007 to 7.2% in July 2008, before falling to 3.6% in December 2008. The year-on-year increase in unprocessed food prices was also indirectly impacted by the global food price shock via the price of meat, which is sensitive to cereal and soya bean prices. This resulted in an annual average increase of 3.5% in unprocessed food prices.

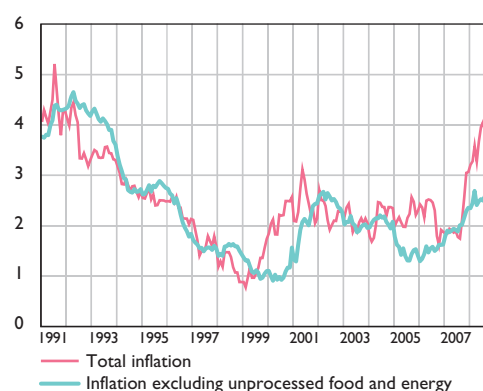
Price developments in industrial goods and services remained contained despite the fact that production capacity utilisation rates were close to historic highs at the start of the year. The average annual inflation rate for these products was 0.8%. Rises in producer prices, driven by industrial commodity and energy prices, remained confined to oil products and intermediate goods. Producer prices of final goods continued to climb at a moderate pace. Inflation in services prices, which is closely linked to wage

developments, remained stable at a high level (2.6% in annual average terms).

Easing inflation and the deterioration in the labour market during the second half of the year did not yet impact labour costs. Compensation per employee was driven upwards, particularly in the public sector as a result of new wage settlements. Against this backdrop, the pace of the increase in unit labour costs accelerated sharply (from 2.4% year-on-year in the first quarter to 4.5% in the fourth quarter of 2008).

Chart 10 Measures of euro area inflation

(year-on-year % increase)



Source: Eurostat.

Box 5**Narrowing of the inflation differential between the euro area and France**

In 2008, inflation in France, measured by the harmonised index of consumer prices (HICP), reached an annual average of 3.2%, i.e. a level very close to that recorded in the euro area (3.3%). The near-match in inflation rates is exceptional and due to temporary factors.

From the start of the 1990s, inflation in France was almost systematically lower than that in the euro area, with an average differential of 0.5 percentage point between the two. It only exceeded the euro area rate on three occasions and then only for short durations: from March to July 1996, from July 2003 to August 2004, and from April to June 2008. The first period was due to the sharp increase in processed food prices in the wake of the implementation of the Galland and Raffarin Laws governing the retail sector, an increase that was associated with a steeper rise in energy prices in France than for the rest of the euro area. The second episode was triggered by an extremely sharp hike in tobacco prices in France.

In 2008, the narrowing and very brief reversal of the inflation rate differential was primarily caused by a temporary discrepancy in price developments between France and the euro area, which accentuated price rises in 2008 relative to 2007 and 2006. Euro-denominated oil price developments feed through to energy consumer prices faster in France than in the rest of the euro area. The reverse is true concerning the feed-through of agricultural commodity prices to food prices, notably owing to the price-setting arrangements of farmers with the rest of the agri-food industry via quarterly contracts. The former factor had the greatest impact in 2008, which explains why France's HICP exceeded that of the euro area when oil prices peaked.

Moreover, consumer prices for industrial goods rose more quickly in France than in the rest of the euro area due to the cut in reimbursement rates on a number of medicines (the HICP includes healthcare expenses covered by households, unlike the national CPI, which includes all healthcare goods and services. Cuts in reimbursements therefore impact the HICP, but not the NCPI).

In more structural terms, cost increases nonetheless remained lower in France than in the euro area in 2008. Compensation per employee slowed in France from end-2006. First, the end of the minimum wage convergence provided for by the Fillon Act stopped pushing wages upwards at the lower end of the wage scale. Second, a more flexible labour market has eased pressures in this market at a given unemployment rate. Productivity gains, which were sharply reduced due to declining activity and the lagged adjustment of employment, were comparable in France and the rest of the euro area.

Public finances

According to data reported to Eurostat, the general government deficit in the euro area widened sharply in 2008, reaching 1.9% of GDP, after 0.6% in 2007, thereby cutting short the fiscal consolidation trend initiated in 2004. The deterioration in public accounts was particularly marked in Ireland and Spain, where the fiscal position switched from a surplus to a large government deficit. This development was largely due to the financial crisis and its effects on the real economy. Following the recommendations of the European Commission on 26 November 2008, a large number

of European countries launched stimulus packages to boost their economies amounting to more than one percentage point of GDP, with the fiscal effects focused on 2009. The impact of these measures on growth is unlikely to truly emerge until the second half of 2009. In 2008, five euro area countries (France, Spain, Ireland, Malta and Greece) posted deficits exceeding 3% of GDP, which should lead to the Commission recommending that excessive deficit procedures against these countries be initiated. Indeed, the current worsening of economic conditions is only partially responsible for these excessive deficits, which primarily reflects structural imbalances requiring consolidation efforts.

Box 6

The state of public finances in France in 2008

The general government deficit widened by 0.7 percentage points of GDP in 2008 amid very adverse macroeconomic conditions and reached 3.4% of GDP. The return to a situation of excessive deficit for the first time since 2004 cannot be ascribed exclusively to cyclical effects. Statutory contributions decreased due to the cuts in the fiscal burden brought in by the TEPA Act of 2007 (Travail, Emploi et Pouvoir d'Achat) concerning work, employment and purchasing power. In addition, government income suffered from lower corporate tax revenues resulting from weak company earnings in 2008. The ratio of the fiscal burden to GDP thus stood at 42.8% in 2008, after 43.2% in 2007. By contrast, the public expenditure-to-GDP ratio rose by 0.3 points relative to 2007 to reach 52.7% of GDP. This development was primarily due to the growing debt burden, which, in total, increased by 4.3% to 68.1% of GDP.

The 2008 fiscal year was marked by the adoption of two revised budget acts:

- the revised budget act (Loi de finances rectificative) in October concerning the financing of the economy, which is analysed in detail in Section 3.3;
- the revised budget act (Loi de finances rectificative) in December concerning the stimulus package totalling EUR 26 billion (i.e. 1.3% of GDP), which relates almost exclusively to 2009. It principally aims to boost companies' cash flow and encourage investment to support growth and employment in the short and medium term.

The fiscal deterioration throughout the euro area stemmed from a decline in the public revenue-to-GDP ratio to 44.8%, compared with 45.4% in 2007, and an increase in the expenditure-to-GDP ratio to 46.7% of GDP, compared with 46.1% in 2007. On the revenue side, the impact of discretionary cuts in income tax and social security contributions was amplified by lower tax receipts from corporate taxes and taxes levied on financial assets and real estate. Increased government expenditure can notably be attributed to the operation of automatic stabilisers (rising unemployment spending) and to fiscal stimulus in the form of public investment and support for targeted sectors.

The general government debt ratio increased sharply by 3.4% in 2008 to stand at 69.4% of GDP. The euro area's public debt profile was not only directly shaped by the government deficits of its member states, but also by the impact of financial system rescue measures adopted as of autumn 2008.¹

Against this unfavourable backdrop, the only euro area countries to maintain both a fiscal surplus and a debt-to-GDP ratio of below 60% in 2008 were Cyprus, Luxembourg, Finland and the Netherlands.

2|1|2 Monetary analysis and financing conditions in France and the euro area

Monetary developments in France and the euro area

After several years of sustained growth, the annual growth rate of M3 in the euro area moderated from the end of 2007 onwards. It decreased from 11.5% at end-2007 to 7.5% at end-2008, thereby recording its lowest level since May 2005. This gradual normalisation of M3 growth mainly resulted from the slowdown in loans to the private sector.

This occurred against the backdrop of an inverted yield curve up until October and persistent pressures in financial markets that encouraged shifts into liquid investments.

¹ The impact of bank recapitalisations by governments is mirrored in stock-flow adjustments. These adjustments correspond to the difference between the change in public debt and the general government deficit/surplus during a given year. In 2008, stock-flow adjustments stood at 3% of GDP for the euro area.

• The prolonged inversion of the yield curve during the first three quarters triggered asset reallocations within the broad M3 aggregate. Growth in the marketable instruments included in M3-M2 therefore also fell off sharply, with investors opting for more liquid and higher-yielding monetary assets, notably short-term deposits and savings accounts, included in M2-M1. The latter development was particularly marked in France, where banks paid attractive interest on the "A" passbook savings account. The narrow M1 aggregate, which largely consists of transaction holdings, continued to lose pace owing to weakening economic activity.

• As of October 2008, the drop in short-term market rates in the wake of ECB key rate cuts contributed to a change in the behaviour of non-financial agents in the euro area. M1 rebounded sharply despite the recession that was taking hold, and cash holdings appeared less risky at a time when the solvency of the banking system was in question (with a sharp rise recorded in October) and, more typically, the fall in interest rates resulted in a decrease in the opportunity cost of money holdings bearing little or

no interest. As a result, term deposits and negotiable debt securities lost ground, whereas the large-scale outflows on money market fund/shares seemed to have come to an end, with their annual growth rate ceasing to decline as of July.

Turning to the counterparts of M3, growth in loans to the private sector gradually slowed throughout 2008 within the euro area, due notably to the continued tightening of credit standards and, more generally, to the worsening economic outlook, which weighed heavily on demand for financing from companies and households. The slowdown commenced at end-2006 for household loans, while loans to non-financial corporations started to recede in May 2008.

The external counterpart had a restrictive impact on monetary developments during virtually the whole of 2008. As a result, the contribution of resident banks' net external assets to M3 growth was increasingly negative as of February 2008, and in July reached its lowest level since 2001 (-3.6%). However, it gradually became less negative during the second half of the year (-1.4% in December).

Table 6 Monetary developments in the euro area and France
(amounts outstanding in EUR billions, growth rate expressed as a %)

	Euro area (a)				France			
	Amount outstanding at end-Dec. 2008	Growth rate (b)			Amount outstanding at end-Dec. 2008	Growth rate (b)		
		2006	2007	2008		2006	2007	2008
Monetary aggregates (seasonally adjusted data) (c)								
Currency in circulation	710.7	11.0	8.1	13.4				
+ Overnight deposits	3,267.6	7.0	3.2	1.4	482.3	5.7	6.0	-3.6
= M1	3,978.3	7.6	3.9	3.3				
+ Other monetary deposits	4,027.7	11.7	17.7	13.6	670.0	8.0	17.7	18.5
o/w: Deposits redeemable at notice up to 3 months	1,557.1	0.6	-3.6	1.0	485.9	6.2	5.0	11.0
Deposits with agreed maturity up to 2 years	2,470.6	27.2	41.4	23.3	184.0	21.3	100.4	44.0
= M2	8,006.0	9.4	10.1	8.2				
+ Marketable instruments	1,379.7	13.3	20.0	3.7	541.8	10.7	16.5	6.1
o/w: Money market fund shares/units	752.9	4.9	9.2	4.8	368.0	5.8	1.5	11.1
Debt securities up to 2 years	271.2	54.4	59.6	-10.9	125.2	41.8	74.0	-8.3
= M3	9,385.7	10.0	11.5	7.5				
France's contribution to M3					1 749.5	10.7	16.3	5.0
Loans to the private sector (unadjusted data)	10,779.0	10.8	11.2	5.7	1,942.9	12.7	14.9	6.9
o/w: Loans to NFCs	4,828.8	13.1	14.4	9.5	845.0	10.9	14.8	10.5
Consumer loans	632.0	7.7	5.3	1.7	156.2	4.8	5.1	-0.2
Housing loans to households	3,492.3	9.6	7.1	1.5	690.5	15.2	13.0	7.3

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

b) Data adjusted for reclassifications and valuation effects.

c) Transactions of French MFIs with other French residents.

Source: Banque de France.

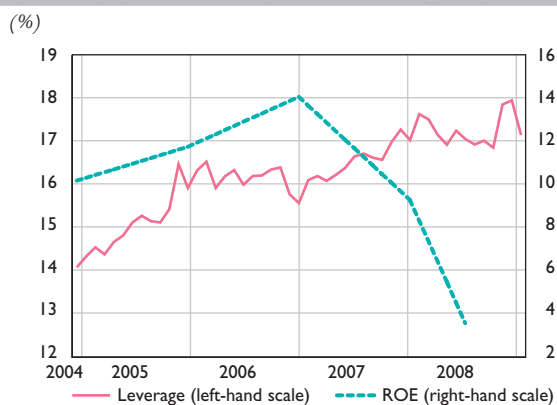
Box 7

Bank lending, balance sheets and leverage

After expanding significantly over the past few years, French banks' leverage, as measured by the equity-to-total assets ratio, reached historic highs (see Chart 11).

During the second half of 2007, this leverage indicator rose markedly, at a time when credit institutions were finding it difficult to raise capital amid persistent financial turbulence. This growth in leverage mechanically increased banks' exposure to liquidity and counterparty risk at the same time as the first signs of an economic downturn began to emerge. As a result, credit institutions clearly sought to stabilise or even reduce their leverage in 2008: banks' total asset growth rate consequently shrank significantly, returning to 2005 levels (see Chart 12).

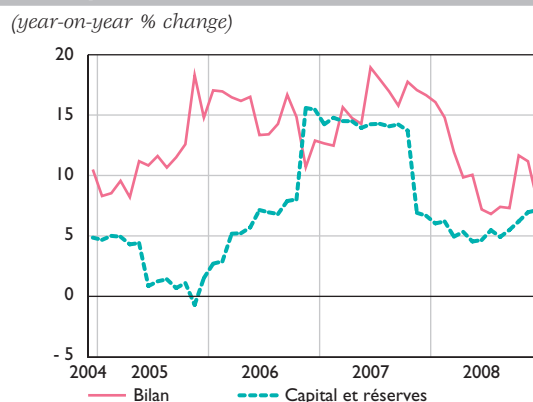
Chart 11 Equity-to-total assets ratio (leverage) and ROE (Return on Equity)



Note: Calculated using data from the company accounts of credit institutions in mainland France and French overseas departments.

Source: Banque de France – General Secretariat of the Commission bancaire.

Chart 12 Growth rate of MFIs' total assets and equity



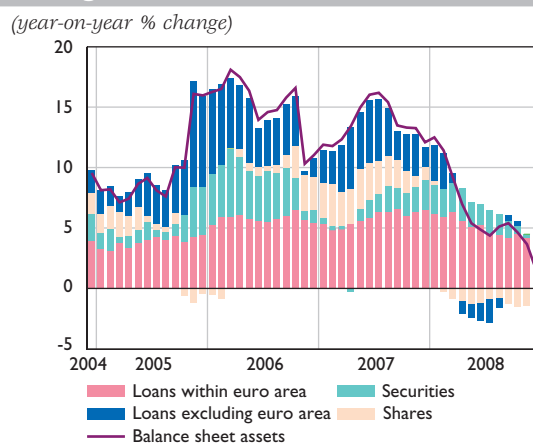
Note: Calculated using data from the company accounts of credit institutions in mainland France and French overseas departments.

Source: Banque de France – General Secretariat of the Commission bancaire.

Interbank and miscellaneous transactions aside – items that are intrinsically highly volatile and difficult to interpret – the decrease in total bank assets principally concerned certain asset items such as securities portfolios, as well as outstanding non-resident financing transactions.

Banks appear to have adjusted their balance sheets by first paring down the items most readily reduced and the least profitable ones in their portfolios, while witnessing sizeable depreciations on marketable instruments (see Chart 13).

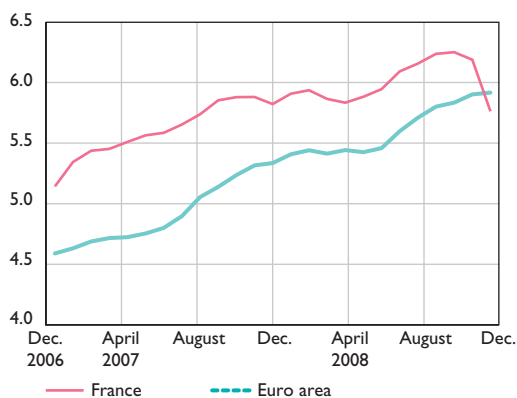
Chart 13 Contribution to balance sheet asset growth



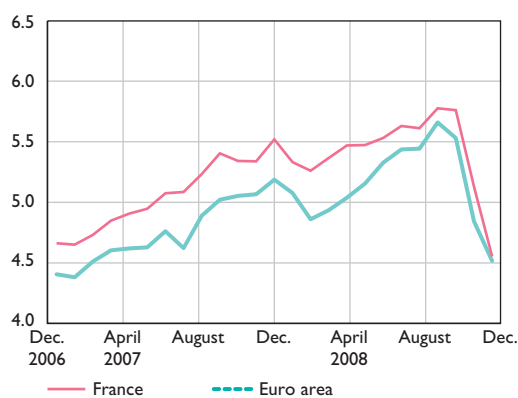
Charts 14 and 15 New loans (excluding overdrafts) – Euro area and France

(average rate as a %)

To households



To non-financial corporations



Sources: ECB, Banque de France.

Financing conditions in France and the euro area

Bank lending rates

In 2008, the rates on new loans to non-financial corporations (NFCs) continued the uptrend initiated in 2007 until October 2008 when they fell sharply on the back of the key rate cuts implemented by the European Central Bank (ECB). At end-December, the decline was slightly less marked in France than in the rest of the euro area and the differential between lending rates in the euro area and France, which is traditionally in French NFCs' favour, narrowed significantly as a result.

Due to the lag in the feeding through of market rate developments to rates on loans to households, the latter had hardly begun to fall at the end of 2008. Consequently, at end-2008, rates in most segments still exceeded their corresponding end-2007 levels. In France, the increase in lending rates on new loans to households continued in 2008 and stood at around 50 basis points between January and December. The rise was less marked for consumer credit, excluding overdrafts (25 basis points) than for housing loans (48 basis points). In the euro area, the increase in average rates on new loans was not as significant, with the fall in market rates from October onwards, impacting bank lending conditions a little faster than in France, notably owing to the larger share of floating-rate housing loans. As a result, the advance in

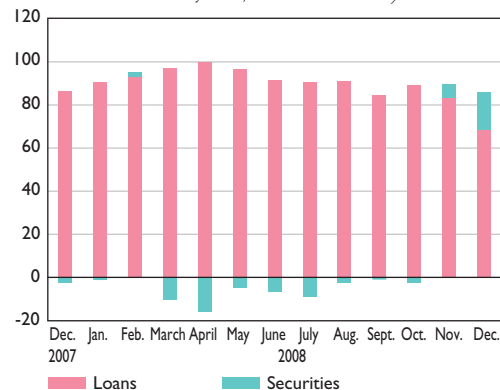
lending rates observed during the first three quarters of the year (up by 42 basis points for consumer credit and by 32 basis points for housing loans) was almost completely reversed during the final quarter.

Financing flows

In 2008, loans to non-financial corporations (NFCs) continued to grow in the euro area, despite the further rise in lending rates in the first three quarters. Developments were more mixed in France, notably towards the end of the year, when new loans posted a sizeable decrease in annual terms. Total resident

Chart 16 Financing of non-financial corporations France

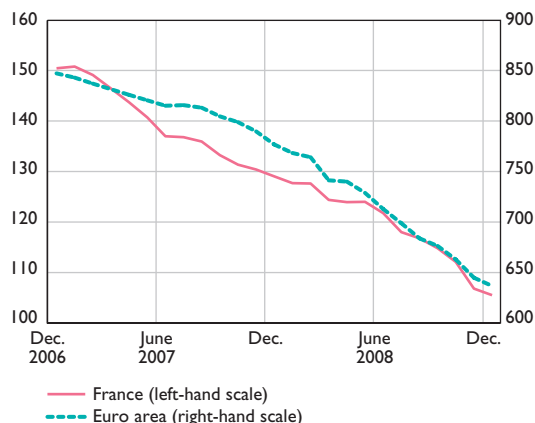
(12-month net cumulative flows, in EUR billions)



Source: Banque de France.

Chart 17 New housing loans

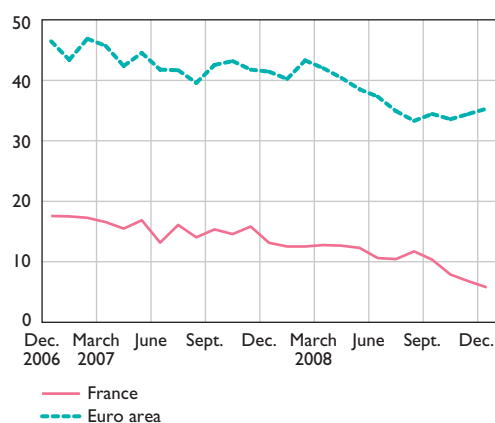
(12-month net cumulative flows, in EUR billions)



Sources ECB, Banque de France.

Chart 18 Share of floating rate loans in monthly flows of new housing loans

(%)



Sources: ECB, Banque de France.

NFC loans nonetheless held up during the year as dwindling new loans were offset by NFCs tapping the markets at year-end to secure financing, notably by issuing negotiable debt securities.

The trend that emerged at end-2006 extended into 2008, with new resident household loans declining significantly during the year. The decline can be mainly attributed to the housing loan segment, which

was impacted by tighter credit standards and weaker demand in the context of falling property prices. The proportion of floating rate loans continued to decline in France, dropping from 13% of total new loans in January to 7% at end-2008, i.e. its lowest level since the creation of the euro. A similar trend emerged for the euro area average, with the share of fixed rate housing loans retreating to 36% in December 2008, from 40% in January.

Box 8

Loan supply and demand developments in 2008 based on the findings of the Bank Lending Survey for France

The quarterly Bank Lending Survey conducted by each of the Eurosystem's national central banks provides qualitative data to gauge more accurately past and expected developments in the supply of and demand for loans with respect to corporate and household customers. As a part of the survey, the Banque de France questions a representative sample of resident credit institutions.

Corporate lending: much tighter loan conditions and a continued sharp contraction in demand

Banks questioned in the survey reported that the increase in the cost of lending due to the financial crisis and the deterioration in the general economic outlook prompted them to tighten credit standards for loans to enterprises¹ throughout the year (see Chart 19). This tightening primarily concerned small- and medium-sized enterprises as of the second half of the year.

¹ This refers to credit standards about which banks were surveyed and which are covered in internal guidelines and criteria that govern banks' lending decisions.

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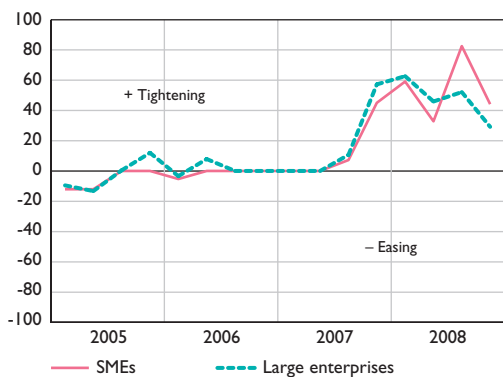
Teleconference to launch the credit mediation mechanism on 10 November 2008

In this environment, which also saw higher lending rates until the start of the fourth quarter and waning investment and merger and acquisition transactions, demand for loans from enterprises also declined significantly (see Chart 20).

Tighter bank credit standards on new loans and credit lines led, in particular, to higher margins and, to a lesser extent, thinner financing volumes and shorter lending periods.

Chart 19 Change in credit standards for loans to enterprises

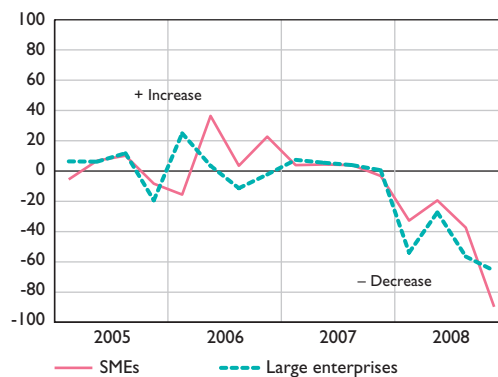
(weighted balance of replies as a %)²



Source: Banque de France, Bank Lending Survey for France.

Chart 20 Change in demand for loans from enterprises

(weighted balance of replies as a %)²



Source: Banque de France, Bank Lending Survey for France.

² The balance was calculated from survey responses and is equal to the difference between the percentage of sample banks that reported an increase in loan demand and the percentage of those that reported a decrease.

.../...

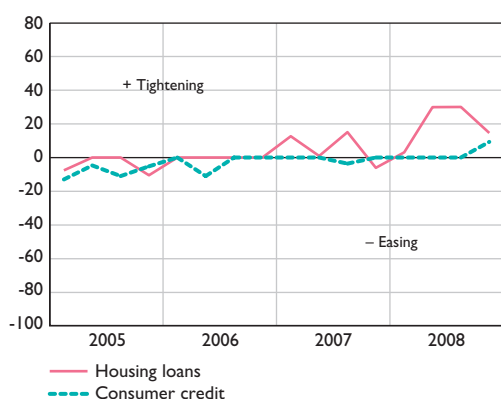
Household lending: moderate tightening of credit standards against the backdrop of a sharper slowdown in loan demand

As part of the continuing trend that commenced at the end of 2006, banks reported a more pronounced slowdown in demand for housing loans at the start of 2008. Although this development was largely linked to the continued rise in lending rates until December, it was also due to the steady deterioration of the outlook for the residential housing market. In this context, credit standards for housing loans were slightly tightened during the year (see Charts 21 and 22).

As regards consumer credit, banks hardly altered their lending standards in the face of demand that also slackened considerably as of the third quarter. The banks surveyed mainly ascribed the downtrend to the gloomier macroeconomic outlook, weaker household confidence and lower consumer spending.

Chart 21 Change in credit standards for loans to households

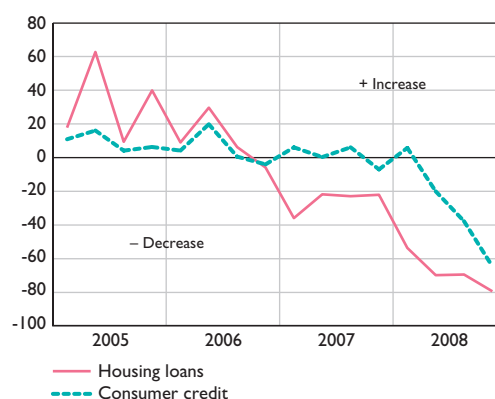
(weighted balance of replies as a %)



Source: Banque de France, Bank Lending Survey for France.

Chart 22 Change in demand for loans from households

(weighted balance of replies as a %)



Source: Banque de France, Bank Lending Survey for France.

2 | 2 Eurosystem monetary policy decisions

The first half of 2008 was marked by exceptionally deep uncertainty about the outlook for economic activity and the consequences of the persistent financial turmoil. Concomitantly, inflationary risks in the euro area intensified, linked to the rapid increase in commodity prices, particularly energy and food prices. As a result, annual euro area inflation, as measured by the HICP, rose from 3.2% in January to 4% in June and July. At the same time, the money supply continued to expand at a very fast pace and added weight to indications of medium-term upside risks to inflation derived from available measures of economic

agents' inflation expectations. Throughout the first half of 2008, the Governing Council of the ECB therefore decided to leave the Eurosystem's key interest rate unchanged pending clearer visibility on the financial markets. In early July, the Council decided to raise its key interest rate by 25 basis points to 4.25% to underscore its resolve to maintain price stability and curb the risk of an upward drift of inflation expectations.

Between July and September, the great uncertainty about economic activity and extreme commodity price volatility, combined with uncertainty about the extent and consequences of the financial crisis, prompted the Governing Council to keep interest rates on hold pending additional data.

The financial crisis worsened dramatically in mid-September, triggering a sharp deterioration in the overall economic outlook. The financial turmoil was accompanied by a sharp increase in market volatility, a more generalised drying-up of liquidity and unprecedented economic policy measures in the majority of countries. At the same time, investors' flight to quality led to much costlier corporate financing conditions, which amplified the effects of falling demand on the real economy. The weakening growth outlook significantly dampened the inflationary risks perceived earlier in the year, while, to a large extent, sharply falling commodity prices drove inflation down. Inflation decreased from 3.6% in September to 1.6% in December and, at year-end, stood at a level consistent with the Eurosystem's definition of price stability.

The ECB's Governing Council, faced with a darker economic outlook and a deepening financial crisis, and taking into account lower risks to price stability, decided, in co-ordination with five other central banks (the Bank of Canada, the Bank of England, the US Federal Reserve System, the Bank of Sweden and the Swiss National Bank), to lower the key interest rate by 50 basis points on 8 October 2008. Two further rate cuts were implemented during the fourth quarter of 2008, namely a 50-basis-point cut in November and a 75-basis-point cut in December. Thus, between the start of October and the end of December, the ECB's key interest rate dropped from 4.25% to 2.5%, constituting an unprecedented move in the history of the Eurosystem both in terms of the size and speed of the rate cuts.

2 | 3 The implementation of Eurosystem monetary policy decisions by the Banque de France and action regarding liquidity

The turmoil on money markets from August 2007 and, more particularly, from September 2008, underscored a high degree of uncertainty surrounding losses generated by asset writedowns sparked by the subprime crisis. This uncertainty caused liquidity and

transactions on the interbank market to dry up and triggered a sharp rise in interest rates, particularly for long maturities.

To contain upside interest rate pressures, the Banque de France took a pro-active stance throughout 2008 by providing liquidity to credit institutions within the framework set by the Eurosystem.

At first, France's central bank extended the measure put in place in 2007 through:

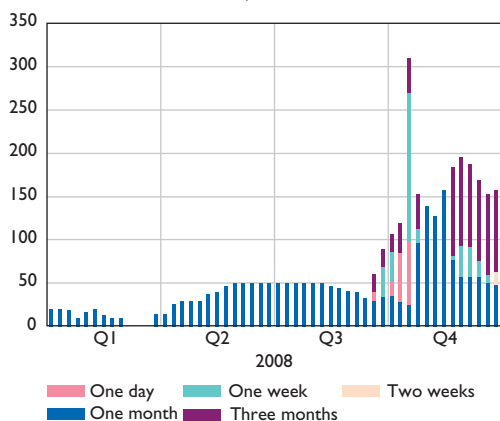
- extensive liquidity allocations to the main refinancing operations in euro, thereby providing banks with about EUR 20 billion in excess of their expected liquidity needs (as against EUR 1 billion generally before the crisis) with a view to steering the overnight interbank lending rate as close as possible to the key rate set by the Governing Council;
- the implementation of supplementary longer-term refinancing operations in euro (six-month operations as of 3 April 2008) and the increase in the amounts allocated to standard longer-term operations (three months), taking the share of longer-term refinancing allocations – LTROs – to 58% at end-June 2008, compared with 33% at end-June 2007;
- stepped-up dollar-denominated refinancing operations, with the latter reaching USD 50 billion at end-June 2008, compared with USD 20 billion at end-December 2007.

From September 2008, the liquidity-providing measures took on a new dimension. This large-scale action encompassed foreign currency denominated refinancing, tender procedures and the type of collateral accepted.

- One-day, one-week and three-month dollar facilities and, later, currency swaps (provision of dollars in exchange for euro) were added to the existing arrangements (one-month facilities). These measures, made possible thanks to the agreement reached between the ECB and the Federal Reserve System, enable banks to secure dollar-denominated funding at a time when off-shore dollar and foreign exchange

Chart 23 US dollar refinancing outstandings by maturity
 Euro area

(weekly average, in USD billions)



Sources: ECB, Banque de France.

swaps markets are no longer functioning correctly. In a similar vein, under the agreement struck between the ECB and the Swiss National Bank (SNB), the Eurosystem and the SNB conducted Swiss franc liquidity-providing swap operations against euro for European banks from October 2008 – at an initial one-week maturity and subsequently at a three-month maturity.

Pressures in the refinancing market also quickly spread to the euro market.

- The ECB therefore decided in early October that refinancing operations would henceforth be conducted as fixed rate tender procedures with full allotment. This move guaranteed that banks would be sure of securing the refinancing needed and could control refinancing costs. The Eurosystem subsequently extended the measure to include all euro-denominated refinancing (notably three-month and six-month maturities) and foreign currency denominated transactions.

- This adjustment to tender procedures was accompanied by a narrowing of the corridor of standing facilities. The deposit facility and lending facility rates were set at 50 basis points below and above the interest rate on the main refinancing operations respectively, as opposed to 100 basis points previously. As a result, banks were able to reduce the cost of a one-off overnight refinancing request from the central bank (and, at the same time, all things being equal, increase the yield on an overnight deposit). The Eurosystem's commitment to provide unlimited liquidity (in euro and other currencies) rapidly led to excess liquidity in the banking system.

Box 9

Refinancing of European banks in US dollars

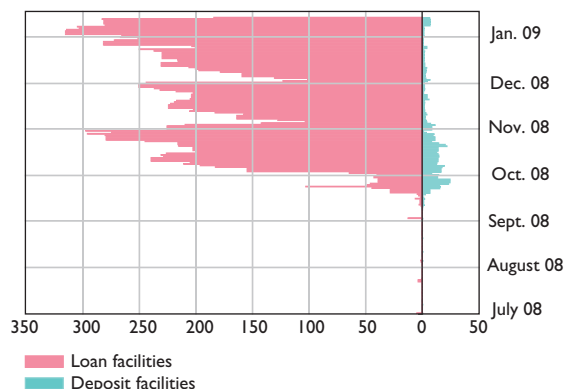
The Eurosystem, in order to provide foreign currency liquidity (US dollars and Swiss francs) to European banks, concluded a swap agreement with the US Federal Reserve System, in particular with the Federal Reserve of New York (NY Fed). The latter made dollars available to Eurosystem central banks, initially for limited and subsequently for unlimited amounts. In exchange, the NY Fed benefited from a supply of euro that was credited to its account with the European Central Bank.

Dollar-denominated loans are granted to European banks via a tender procedure whose characteristics are overall identical to standard euro tenders, namely, that these transactions must be effected using appropriate collateral. The Eurosystem accepts two types of collateral as dollars are lent through Term-Auction Facilities (TAF) and currency swaps. In the first case, eligible assets are exactly the same as those that are used as collateral for refinancing in euro. That said, haircut add-ons are nonetheless applied to cater for the forex risk the Eurosystem is exposed to as the assets used are denominated in euro. In the second case, dollar-denominated loans are granted against a deposit of an equivalent amount (excluding haircuts) in euro (swap or foreign exchange swap).

Disruptions in the interbank lending market, illustrated by a spectacular rise in the implied refinancing premium, necessitated increased transaction volumes. As a result, the Eurosystem lent a maximum of USD 300 billion to European banks in mid-October 2008.

Chart 24 Use of permanent facilities by euro area banks

(EUR billions)



Source: Banque de France.

Overall financing for banks exceeded their actual requirements. The surplus, instead of being lent to banks with intermittent borrowing needs, was then re-deposited at the central bank via deposit facilities, as illustrated by Chart 24.

- However, this additional refinancing demanded larger quantities of collateral as all Eurosystem lending is systematically guaranteed by adequate collateral. Consequently, on 15 October 2008, the Eurosystem decided to expand its range of eligible collateral, i.e. collateral accepted by the central bank. The credit threshold was lowered from A- to BBB- and a number of assets, notably those issued in other currencies, were henceforth accepted. This extension was naturally accompanied by a number of complementary measures regarding haircut add-ons to protect the Eurosystem against the risk of counterparty default. Although the range of eligible collateral was extended, the Eurosystem, in its annual risk evaluation review of September 2008, nevertheless concomitantly modified certain eligibility criteria for collateral, notably for asset-backed securities (ABS). The adopted measures (haircut add-ons, structure, financing and rating of conduits) corresponded to developments in the securitisation market.

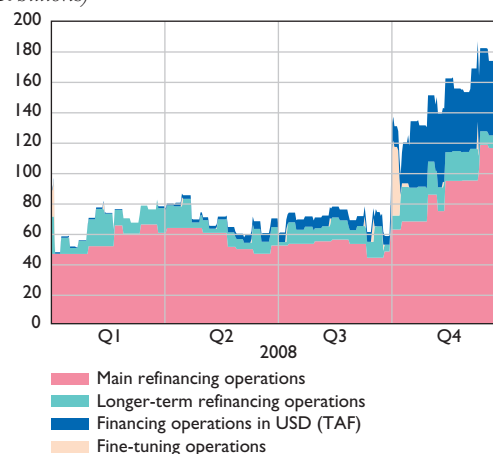
At end-2008, the refinancing provided by the Eurosystem amounted to more than EUR 900 billion (plus over USD 200 billion), compared with EUR 450 billion in July 2008. The Eurosystem's consolidated balance sheet virtually doubled, thereby reinforcing the intermediation role of the central bank.

French banks' share of total refinancing, which stood at 5.5% during the previous three years, rose to an average of 14% in 2008.

In February, the Banque de France also introduced a new collateral management system (known as "3G") which allows banks to manage in a unified and comprehensive way all the collateral used in their refinancing operations with the Bank whether in their participation in the Eurosystem's monetary policy operations or in the securing of intra-day borrowing. This constituted a major change in the procedures used by French banks to obtain refinancing from the Banque de France. It promoted the Paris financial centre to among the highest of European standards and occurred in the context of a future common platform for all Eurosystem central banks for the operational management of collateral used in refinancing operations (known as "CCBM2").

Chart 25 Refinancing of French banks

(EUR billions)



Sources: ECB, Banque de France.

Box 10

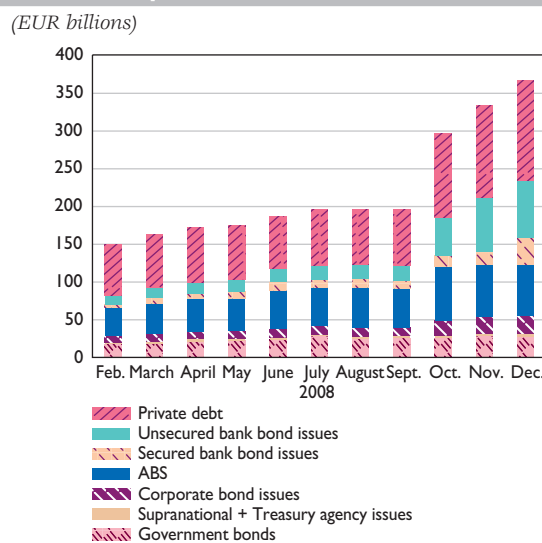
Extension of eligible collateral for Eurosystem lending transactions

All assets accepted by the Eurosystem as collateral for lending operations are referred to as eligible assets. Due to the high demand for refinancing from the central bank and price volatility on these assets, on 15 October the Eurosystem decided to temporarily lower the credit threshold of eligible assets to BBB- rated assets and accept formerly ineligible assets.

This decision broadened the range of potentially eligible collateral to an estimated EUR 1,500 billion (compared with an estimated total of EUR 10,000 billion at end-2008, but only part of this amount was recorded on banks' balance sheets and liable to be used as collateral) and thereby ensured that banks were in a position to deliver sufficient collateral to be eligible for Eurosystem refinancing. These newly eligible assets notably comprised debt securities issued by credit institutions and traded on non-regulated markets but accepted by the Eurosystem, subordinated debt instruments protected by an acceptable guarantee (such as sovereign-guaranteed debt), as well as marketable debt instruments issued in the euro area but denominated in dollars, yen and pound sterling.

French bank deposits therefore totalled EUR 350 billion at end-2008, versus less than EUR 150 billion at the start of the year. The increase was largely due to bank issues of newly eligible debt securities and ABS issues.

Chart 26 Collateral deposited by banks at the Banque de France



Source: Banque de France.

3| Action taken by public authorities to manage the crisis

3|I Management of the financial crisis

3|I|I The concerted action of European governments

The handling of the financial crisis took on a marked international dimension on 10 October when the group of seven industrialised nations (G7) established five guiding principles for government action:

- ensuring the viability of the financial system and avoiding the failure of systemically important financial institutions;
- guaranteeing access to liquidity;

- recapitalising public and private financial institutions where required;
- restoring depositor confidence by issuing government guarantees for deposits;
- shoring up the mortgage loan market and beginning work on improving valuation methods, the transparency of credit pools and accounting rules.

The next day, at the instigation of the French presidency, European governments organised a sound and consistent plan of action at European Union level. First, the authorities decided to guarantee short- and long-term bank financing so that banks could in turn properly finance the economy. Second, governments confirmed their support for the recapitalisation of banks. Moreover, wide-reaching reforms to accounting rules were introduced. As was already the case in the United States, they allow banks to transfer securities hitherto booked at market value to portfolios where

Box 11

**Government support for the banking sector in Europe:
intervention methods and amounts involved**

Governments intervened on a massive scale to support their countries' banking systems, at times with targeted bail-outs to avert the bankruptcy of financial institutions (e.g. Northern Rock, Bradford and Bingley and Royal Bank of Scotland in the United Kingdom, IKB and Hypo Real Estate in Germany, Fortis in Belgium and the Netherlands, Dexia in Belgium, France and Luxembourg), and, at others, within the framework of more extensive plans designed to ensure that adequate financing continued to be provided to the economy.

Government support for the banking sector was based on three principal actions:

- capital injections to assist troubled institutions or bolster the capital of solvent banks;
- financing assistance via government guarantees on bank liabilities (general or more specific guarantees, e.g. for bond issues) or direct government loans;
- buybacks or asset guarantees by governments to clean up bank balance sheets.

Table 7 Type and amount of government interventions in the European Union's leading countries and the European Union as a whole

(estimate of effective interventions from October 2008 to end-March 2009)

	Capital injections		Support for liabilities		Support for assets		Total	
	EUR billions	as a % of GDP	EUR billions	as a % of GDP	EUR billions	as a % of GDP	EUR billions	as a % of GDP
Austria	2	0.7	24	8.2			26	8.9
Belgium	15	4.1	91	25.4	21	5.8	126	35.3
France	11	0.5	96	4.9	4	0.2	111	5.6
Germany	38	1.5	124	4.8			162	6.3
Ireland			376	202.0			376	202.0
Netherlands	14	2.3	18	2.9	29	4.7	60	9.9
Spain			32	2.8			32	2.8
United Kingdom	60	3.2	308	16.3	530	28.1	898	47.6
Total EU *	147	1.1	1,106	8.6	585	4.5	1,837	14.2

* Totals include amounts for the entire European Union (EU) and are not limited to countries listed in the table.

A total of over EUR 1,800 billion was mobilised by the Member States of the European Union to shore up their banking institutions, i.e. 14% of EU GDP. Government guarantees of bank debt and direct financing were the most common means of support (60% of the total amount extended by European Union countries), followed by asset buybacks and guarantees (32%). That said, the United Kingdom made considerable use of the asset protection mechanism (to support RBS's and Lloyds TSB Group's assets). Capital injections accounted for a total of 8% of public spending carried out.

The extent of the interventions varied greatly from one country to the next. The United Kingdom's share alone accounted for almost half of the funds mobilised in the EU. France was at the lower end of the range, with aid currently representing less than 6% of national GDP, of which only 0.5% took the form of capital injections. Most countries still have significant leeway, both in terms of share of GDP and relative to the initial amounts earmarked.

they are valued using methods better suited to the absence of market prices. The aim was to curb the illiquidity-devaluation spiral that was forcing banks to book heavy writedowns. Furthermore, at European level, legislation to enhance protection for savers was introduced via an increase in the deposit guarantee threshold.²

Lastly, the G20 summit held on 15 November 2008, which gathered together a larger-than-usual number of countries, including the leading emerging economies, established a global plan of action. The plan set out a list of reforms designed to strengthen financial markets and step up financial regulation to avoid fresh crises. A number of these reforms called for immediate action by end-March 2009, while others will be carried out over the medium term. The Financial Stability Forum, in which the Banque de France takes part, will be – on the basis of a wider, yet-to-be-defined membership – closely associated with the G20's reform agenda.

3|1|2 Action taken by the French Government

The French Government took a two-pronged approach to managing the crisis, namely refinancing assistance for banks and capital injections to reinforce bank capital ratios.

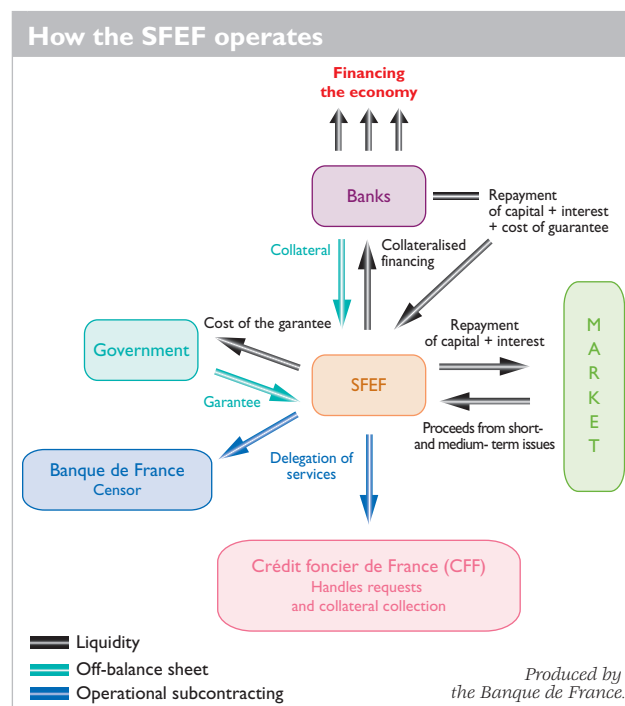
Refinancing assistance for banks

In October 2008, the French Government created the *Société de financement de l'économie française* (SFEF) to enable French banks to secure medium- and long-term financing in a context where this type of financing had become extremely difficult on financial markets. This financing vehicle, majority owned by France's leading banks, raises funds on the financial markets via AAA-rated bond issues maturing in five years or under, which are guaranteed by the French Government (the threshold for guaranteed issues stands at EUR 265 billion, with the Government extending EUR 55 billion to Dexia). The SFEF then lends to banks in exchange for collateral at a rate that prices in the SFEF's issuance rate, to which is added the median of the CDS premium relating to the

borrower bank, plus an additional premium of 20 basis points. In this way, the Government is remunerated for the guarantee it extends to banks. By early 2009, EUR 39 billion of refinancing had been granted via eight SFEF issues (between 13 November 2008 and 3 March 2009).

Reinforcing banks' capital

The Government, in addition to supporting bank financing, assisted banks in shoring up their capital to facilitate the future financing of the economy via the *Société de prise de participation de l'État* (SPPE), which has funds of EUR 21 billion³ to be used in two tranches. The mechanism consists in the Government subscribing to subordinated bonds or preference shares issued by banks. In return, the banks pledged to increase the outstanding amounts of their loans to the economy and to adhere to a number of ethical rules, notably regarding governance and compensation. As a result, in early 2009, the top managers of the country's leading banks unanimously waived their bonuses for 2008.



2 Increase of the minimum threshold contained in the European Directive from EUR 20,000 to EUR 50,000 per depositor. The French deposit guarantee fund already afforded one of the highest guarantees, i.e. EUR 70,000. At 31 December 2010 at the latest, the level of guarantee for all of the savings deposited by the same depositor will be set at EUR 100,000.
 3 The amount of EUR 40 billion initially earmarked by the French State was revised downwards to EUR 21 billion when the European Commission adopted the French plan on 8 December 2008.



Press conference given on 20 October 2008 at the Banque de France by Christine Lagarde, Minister of Economy, Industry and Employment with Christian Noyer and Michel Camdessus to announce the establishment of the SFEF

Furthermore, the measure provides that the Government can take capital stakes in a bank facing difficulties. Dexia benefited from this measure, with the Government taking a EUR 1 billion stake in the bank. Dexia also received a EUR 3 billion capital injection from its Belgian shareholders and the Belgian Government, one of EUR 376 million from the Luxembourg Government and a further EUR 2 billion from the *Caisse des Dépôts et Consignations*.

3 | 2 Support for the financing of the economy

A series of initiatives was taken by the public authorities to facilitate the financing of the economy and to avoid banks cutting down too sharply on their lending:

General measures

- To secure refinancing from the SFEF (see above), banks must formally pledge to sustain lending to households, the corporate sector and regional and

local authorities (the loan growth target in 2009 is 3-4% relative to the 2008 figure).

- To co-ordinate efforts to provide financing to businesses, a credit mediation mechanism was set up in October 2008 that closely involved the Banque de France. The credit mediation committee receives and processes applications from enterprises facing serious cash-flow problems. Also present at departmental level, the credit mediation mechanism can be accessed by any enterprise, which can apply to the credit mediator, either directly or through the departmental paymaster-general. The Banque de France plays an active role in this mechanism via the departmental branch network as Banque de France directors have the role of departmental mediators.

- The Strategic Investment Fund (SIF), created in October 2008, will take long-term capital stakeholdings to enhance business development, notably for small- and medium-sized enterprises. The SIF is owned by the *Caisse des Dépôts et Consignations* (51% of the capital) and the Government (49%). In 2009, the SIF is expected to have stakeholdings and funds to invest amounting to EUR 20 billion.

Sectoral measures

- At European level, the European Investment Bank (EIB) is to set aside EUR 30 billion for banks to finance SMEs in Europe over the 2008-2011 period.
- In addition, from October 2008 the French Government made available EUR 26 billion in loans to ensure the proper financing of SMEs, which form the backbone of employment and growth in France. This amount includes:
 - EUR 17 billion in regulated savings surpluses transferred to banks, which have pledged to use them to assist SMEs and intermediate-sized businesses and to provide the Government with monthly reports as to the use of these funds;
 - EUR 5 billion in OSEO financing (government aid organisation for SMEs) for lending to SMEs, mainly via guarantee mechanisms. OSEO's remit is to support SME innovation and growth and to facilitate short-term cash-flow financing and business investment projects by sharing the risk with banks;
 - an extra EUR 4 billion as part of the stimulus package through OSEO to satisfy the continuing high demand for financing from SMEs.
- The financing subsidiaries of carmakers also have access to EUR 2 billion in refinancing to boost loans for motor vehicle purchases. This measure is part of a wider plan to support the automotive sector (EUR 6.5 billion in loans over five years to finance clean vehicles, and guarantee funds for equipment-makers and subcontractors, amongst others).
- In January 2009, concomitantly with the second wave of capital injections financed by the SPPE (see above), French banks pledged to finance export contracts to the tune of EUR 7 billion, of which EUR 5 billion has been dedicated to the aerospace sector and will be refinanced through the SFEF.

3 | 3 Fiscal stimulus packages

The deepening crisis prompted all governments to take large-scale fiscal action. In Europe, until September 2008, government measures were confined to a small number of countries (notably Spain and Italy). From September onwards, there was a generalisation of stimulus packages devised to deal with the spread of the financial (and real estate) crisis to the real economy. Against this backdrop, on 26 November, the European Commission unveiled an Economic Recovery Plan amounting to EUR 200 billion, i.e. 1.5% of the European Union's GDP. Each Member State was asked to contribute 1.2% of its national GDP, with the remaining 0.3% provided by European budgets. The European Investment Bank (EIB) therefore decided to step up its interventions in the European Union by EUR 15 billion per annum in 2009 and 2010, notably by boosting finance to SMEs, energy efficiency and new Member States. The Commission indicated that flexibility margins under the Stability and Growth Pact during crisis periods could be used via sensible application of the Pact.

The amounts involved are generally close to 1.2% of GDP, with the effects focused on 2008 and 2009, barring Germany and Spain, which are exceptions at European level, with a fiscal stimulus of 3.3% (the total for both packages) and 3.7% of GDP respectively.

The recovery plan announced by the European Commission and approved by the European Council in December recommended several general principles (namely calling for timely, temporary, targeted and, if possible, co-ordinated fiscal stimulus measures), without, however, suggesting precise measures. A wide variety of instruments were utilised, either in the form of additional spending or lower taxes. A number of packages focus on stimulating demand (the United Kingdom and, to a lesser degree, Spain, Italy and Germany's second plan), while others are supply-oriented (France's package and Germany's first package).

THE IMPLEMENTATION OF MONETARY POLICY IN THE CONTEXT OF THE FINANCIAL CRISIS

Action taken by public authorities to manage the crisis

These differences are largely due to specific domestic factors, both in terms of the nature of the effects of the crisis and the fiscal leeway available. Thus:

- The United Kingdom and Spain were hit the earliest and the hardest by weakening demand and rising unemployment, which explains these countries' recourse to massive aid to support household incomes and consumer demand. Germany followed suit in its second stimulus package, whereas the first package mainly targeted aid to businesses.

- The French economy is less dependent on exports than Germany. Furthermore, household spending is stronger in France than in its European counterparts. This explains France's relatively lesser use of measures to bolster consumption compared with more targeted support for public and private investment. Moreover, the country's delicate fiscal position led to the package mainly consisting of future spending being brought forward.

Table 8 Principal measures to support the real economy in Germany, France and the United Kingdom

Country	Date of announcement	Measures announced	Amounts unlocked/ comments
Germany	5 November 2008	<ul style="list-style-type: none"> • Tax credits for ecological car purchases • Loans to SMEs guaranteed by the Kreditanstalt für Wiederaufbau (KfW) • Diminishing balance amortisation for productive investment set at 30% • Aid to households for home renovation • Infrastructure investments • 6-month extension to seasonal unemployment benefits 	EUR 32 billion over 2 years (1.3% of GDP), including EUR 12 billion in new aid
	13 January 2009	<ul style="list-style-type: none"> • Infrastructure investments • Reduction in social security contributions for healthcare insurance (employers and employees) • Income tax reductions • One-off payment of EUR 100 per child • Revaluation of aid to the unemployed and higher benefits for layoffs • Scrap bonus of EUR 2,500 per vehicle • EUR 100 billion guarantee fund to finance businesses 	EUR 50 billion over 2009-2010, i.e. 2% of GDP Debt repayment plan included in the stimulus package
	Total		EUR 82 billion over 2009-2010 i.e. 3.3% of GDP

.../...

Table 8 (continued) Principal measures to support the real economy in Germany, France and the United Kingdom

France	4 December 2008	<ul style="list-style-type: none"> Stimulus via large-scale projects (bringing forward projects already approved) implemented by the Government, regional and local authorities and state-owned enterprises (EUR 10.5 billion) Support for productive investment (guarantees, accelerated amortisation) Support for cash-flow of businesses, particularly SMEs (> EUR 10 billion) EUR 200 for households claiming the new minimum guaranteed income benefit (EUR 760 million) Support for very small enterprises via the total exoneration of employers' contributions on recruitments in 2009 (EUR 700 million) Employment policy (state-assisted contracts, professional training) (EUR 500 million) Support for the automotive industry, including subcontractors (EUR 2 billion) Scrap bonus of EUR 1,000 per vehicle (EUR 220 million) Support for the building/residential housing industry (construction, doubling of zero-interest rate loans, etc.) (> EUR 2 billion) 	<p>EUR 26 billion (1.3% of GDP)</p> <p>The public deficit is expected to largely overshoot the 3% threshold and public debt is likely to exceed 70% of GDP in 2009 and 2010.</p> <p>In addition, on 20 November 2008, a Strategic Investment Fund (SIF) was created to boost and stabilise the capital of French companies</p>
	18 February 2009	<p>Support package for low-income households</p> <ul style="list-style-type: none"> Improvement in the amount of partial unemployment benefits and an extra payment for the newly unemployed Elimination of the last two-thirds of tax for taxpayers falling within the first tax bracket One-off payment for low-income families with children, and vouchers for personal services Creation of a social investment fund 	EUR 2.6 billion
	Total		EUR 28.6 billion i.e. 1.5% of GDP
United Kingdom	September 2008	<ul style="list-style-type: none"> Urgent housing market support package Aid to families affected by rising energy prices 	GBP 910 million
	25 November 2008	<ul style="list-style-type: none"> Cut in the standard VAT rate from 17.5% to 15% from 1 December 2008 to 1 January 2010 (GBP 12.5 billion, including GBP 3.8 billion before April 2009) Aid to the poorest households (benefit increases brought forward, savings incentives for the poorest sectors of the population, etc.) Construction and renovation of social housing Abandonment of previously planned company tax increases Payment facilities for SMEs Tax exemption on foreign dividends Partial immediate financing through increased duties on tobacco and alcohol 	<p>GBP 20 billion (around 1.5% of GDP) injected by 2011, including GDP 16.3 billion in the 2009-2010 budget</p> <p>Increase in public debt from 37% of GDP in 2008 to 57.4% in 2013</p> <p>Financing measures planned in 2011-2012</p>
	Early January 2009	<ul style="list-style-type: none"> "New Deal" construction programme (schools, hospitals, infrastructure, renewable energies): target = creation of 100,000 jobs "Golden hello" (subsidy of up to GBP 2,500 to hire and train a person on unemployment benefits for over 6 months) Training of 35,000 apprentices Government guarantee on loans to SMEs (up to GBP 22 billion) 	GBP 10.6 billion
	Total		GBP 31.5 billion (2.2% of GDP)

Produced by the Banque de France.

Presentation of business strategy by Christian Noyer, with Jean-Paul Redouin and Jean-Pierre Landau, on 10 December 2008



THE BANQUE DE FRANCE'S BUSINESS STRATEGY AND ITS IMPLEMENTATION



The financial crisis has brought the Bank's tasks to the fore and highlighted the robustness of its functioning.

The strategic choices made by the Bank over the past few years enabled it to demonstrate its responsiveness and efficiency throughout 2008:

- thanks to its presence on financial markets, the Banque de France was able to follow on a day to day basis the crisis-related events, to thoroughly comprehend the problems encountered by counterparties (access to liquidity) and to put forward specific proposals to alleviate tensions on the money market;
- the crisis has demonstrated the effectiveness of the close links between the banking supervisors and the Banque de France;
- it has highlighted the credibility of the Bank's work on economic conditions and financial stability;
- the Bank's long-standing expertise in financial analysis underpinned the Government's decision to make the Banque de France, through its branch network, the "natural" intermediary of the credit mediator in the French *départements*;
- the quality of services rendered in the framework of the relations between private individuals and financial sphere strengthens the role of the Banque de France through its household debt commissions.

I | The Bank's business strategy

I | I Six areas of development for 2008-2012

The Treaty on European Union, the Statute of the European System of Central Banks (ESCB) and French national legislation provide a robust and lasting foundation for the tasks of the Banque de France. These tasks are conducted within a changing environment, linked to the developments in the global economy, changes in the financial system, European financial integration and the enlargement of the Eurosystem (16 members since 1 January 2009).

In order to rise to the challenges it has to face in the performance of its tasks, the Banque de France has defined six strategic priorities for 2008-2012.

1|1|1 Being a leader in the field of economic and monetary analysis

To achieve this objective, the Banque de France must maintain, or even strengthen, its capacity to prepare and explain monetary policy and establish its influence in the following areas: economic studies, including in microeconomics, research and public statistics.

This role should not be restricted to the national sphere. The Banque de France should be recognised as one of the leading institutions in the area of monetary and financial affairs both in the euro area and in the European and international fora in which it takes part (see chart: The Banque de France's participation in European and international groupings, section 2|2|).

The Banque de France will develop its research capacities not only by recruiting around 30 economists and researchers over 2008-2010 but also by tightening its links – vectors of cross-fertilisation – with academic circles. In this respect, the partnership established with the Toulouse School of Economics has enormous potential.

Achieving this objective also involves promoting its work vis-à-vis a broad public. Today, more than ever, the Banque de France is concerned with financial education. In this respect, it intends to update and develop its range of publications in order to ensure a better dissemination of its analyses and studies, its message on monetary policy and its presentation of economic facts, making them easily understandable by all.

The reorganisation carried out in 2008 to redefine the structures of the Directorate General Economics and International Relations and create a Directorate General Statistics reflects the importance and the autonomy of the statistics function in the institution, with a responsibility for the coordination, promotion of tools and products and wider dissemination (see section 2|1).

1|1|2 Being a major player in the area of financial stability

As a key player in the area of financial stability, the Banque de France needs to be able to detect the emergence of risks that could represent a systemic threat if they are not correctly dealt with. The Banque de France strives constantly to reduce the identified risks of vulnerability, primarily in the field of regulated financial corporations, but also by analysing the role of unregulated players. It is essential that the Bank be able to rapidly and efficiently assess and manage systemic crises in co-operation with all the players concerned at the national, European and international level.

The close links between banking supervisors and the central bank are clearly a major asset. Indeed, it enables the Bank to have at its disposal a comprehensive management and control panel, and therefore be much more responsive. Market data, i.e. the information obtained from market participants, derived from the transactions conducted by the Banque de France directly on markets or obtained from financial institutions, may be cross-checked with prudential data. This whole set of data provides an extremely wide and reliable overview of what happens in times of tension and crisis.

These close links between the Banque de France and the *Commission bancaire* are therefore a source of efficiency. Synergies are also developed between the operational directorates and the studies departments.

The Banque de France is also charged with the oversight of means of payment, securities settlement and exchange systems, which enables it to have a more comprehensive overview of the situation.

In this respect, the Deletré report on the organisation and functioning of the supervision of financial activities in France, submitted in January 2009 to Christine Lagarde, the Minister of the Economy, Industry and Employment, confirms the pivotal role played by the Banque de France in this area. The planned merger between the certification and supervisory authorities of the banking and insurance sectors, in particular between the *Commission bancaire* and the *Autorité de contrôle des assurances*

et des mutuelles (ACAM – the Insurance Supervisory Authority) does not call into question the principle of maintaining close links between the supervision of financial institutions and the Banque de France.

The Larosière report, submitted on 25 February 2009 to Mr Barroso, the President of the European Commission, contains a series of proposals along the same lines: while stressing the importance of the macroprudential dimension, the report suggests that the supervision of systemic financial risks at the European level be handed over to an authority with close links to the European Central Bank.

1|1|3 Taking up the challenge of the construction of European supervision

The Banque de France continues to take an active part in all the work and proposals that aim at:

- adapting the prudential regulation of capital and risks in the framework of Basel 2, and supplementing it, in particular regarding liquidity;
- increasing the harmonisation of this regulation, its implementation and its control, for example by giving more weight to the Committee of European Banking Supervisors (CEBS) and by harmonising reporting requirements;
- strengthening the co-operation between authorities, in Europe, by developing the role of the colleges of supervisors for the control of cross-border groups.

This close co-operation is essential for establishing the European system of decentralised supervision. In this respect, the Larosière report not only suggests strengthening the powers of the current Level 3 committees, including the Committee of European Banking Supervisors (CEBS) for the banking sector, but also entrusts national supervisory authorities or the colleges of supervisors in charge of controlling cross-border groups with the responsibility of supervising financial sector institutions.

1|1|4 Being a leader or co-leader of common Eurosystem infrastructures

The Eurosystem is developing and creating new common infrastructures necessary for optimal liquidity management. In this framework, the

goal of the Banque de France in terms of design, development and management of the Eurosystem's IT infrastructures focuses on four main priorities:

- the valuation of collateral used by banks for refinancing operations: the Banque de France is involved in the creation of a European platform for collateral management, in co-operation with the National Bank of Belgium and De Nederlandsche Bank, which builds on its experience of valuation hubs;
- market operations: the Banque de France and the Banco de España plan to set up a European platform for processing market operations, in conjunction with other central banks. As a first step, in 2008, the Banque de France was entrusted with the task of introducing a software tool for the management of foreign exchange reserves at the European level;
- securities transactions: after having contributed to the setting-up of TARGET 2 (Trans European Automated Real-Time Gross Settlement Express Transfer System), the developments of which it oversees, the Banque de France is also involved in the TARGET 2 Securities project, a European platform for settling securities transactions in central bank money within the euro area;
- lastly, the Bank plans to set up a new IT centre complying with the new standards, in particular with regard to security, in order to be able to host Eurosystem infrastructures.

1|1|5 Strengthening the Bank's cash activities

In 2012, the supply of new euro-denominated banknotes will no longer be governed by a system of quotas but by a centralised system of tenders, except for NCBs with their own printing works that decide not to take part in the new system. The challenge for the Banknote Manufacturing Directorate General, the industrial department of the Banque de France, is to continue to secure a significant share of the production of euro banknotes by improving its level of competitiveness with a view to participating in the Eurosystem's system of tenders in 2012. Three priorities have been set:

- completing the renovation of the production facilities to a state-of-the-art technical level with the capacity to meet the future deadlines for the second series of euro banknotes;

- continuing the systematic improvement of productivity by reducing the rate of imperfect banknotes produced, 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.

As regards banknote circulation, a key priority is to ensure the soundness of the cash industry. The challenge is to prevent default risk by maintaining a strong responsiveness in the event of contingencies and to promote the external recycling of banknotes, while developing appropriate means of control.

In the next four years, the objective is to develop strong cash centres and to adapt the Bank's branch network to the changes in cash flows. In particular, new highly-industrialised cash processing centres will be set up in areas where cash flows tend to concentrate.

1|1|6 Improving the quality and efficiency of services to the community within the framework of the Public Service Contract

In the wake of the crisis, the expectations of the public authorities and private individuals have grown vis-à-vis the Banque de France. The latter's objective is to meet requests in the most efficient and responsive manner and at the lowest cost. The Bank network, at the departmental level, is particularly involved, given its active participation in the departmental commissions charged with monitoring the financing of the economy and its support to the work of the credit mediator, Mr Ricol.

The bill of the Ministries of the Economy and Justice, which aims to strengthen the role of the household debt commissions, could give rise to new challenges in terms of involvement.

These broad guidelines have been fully confirmed for 2009. Of course, the Banque de France will focus more specifically on easing the current financial turmoil and reducing its impact on companies and households.

In addition, in its strategic planning the Banque de France has taken account of the implications of the general review of public policies, launched in 2007, and the impact of the law on the modernisation of the economy of 4 August 2008.

In 2008, the Bank's results improved on account of its sound management. This extra leeway will enable the Bank to make the necessary investments for the implementation of its medium-term strategy. It will only retain this leeway if the efforts made to rationalise structures and modernise management tools are pursued.

1|2 Two cross-sectoral strategies

When exercising its tasks, the Banque de France must also take into account the responsibilities incumbent on public institutions and general government in terms of modernisation and sustainable development.

Two major cross-sectoral strategies were thus added to the six strategic priorities.

1|2|1 The constant modernisation of processes

To reach its strategic goals, the Banque de France requires state-of-the-art processes and tools at its disposal. The plans to modernise the Banknote Manufacturing Directorate General and restructure the Bank's branch network have been completed. New investment has been programmed in order to further enhance the soundness of the cash industry, in particular with the creation of industrial cash processing centres, and to set up IT infrastructures necessary for the Eurosystem's major projects in the areas of market operations and payment systems. Another priority of the Bank is to bring its real estate stock into compliance with sustainable development standards. It is also in the process of modernising its management tools in order to improve the way in which it manages performances and steers the implementation of its strategy. In 2008, the Bank also redefined methods and procedures for cost calculation.

In 2008, the Bank rationalised its structures and organisations mainly in the following areas: statistics, cash management and branch network activities. The Bank's presence at the departmental level was confirmed. It will pursue its work on the medium-term strategy for the branch network at a later stage.

One element that will have to be taken into account will be the possible regional reorganisation by the Government in the wake of the mission conducted by Mr Balladur.

In addition, the Bank continued to review the cost-benefit ratios for its tasks and overhaul its processes both in the network and at the head office. As regards support functions, it conducted a series of reengineering studies to improve the pooling of resources and examine the conditions for outsourcing some low value-added activities.

ISO 9001 certifications were obtained in operational fields such as banknote production, currency in circulation, payment systems, banking services and within support functions such as information systems, internal auditing and printing. In 2008, OHSAS 18001 assessments were conducted in several areas in order to improve occupational health and safety management.

Quality approaches with or without certification are now being rolled out in an increasing range of areas. They are all implemented with a constant objective of operational excellence and a search for productivity gains.

1|2|2 Sustainable development at the heart of the Bank's tasks and deliberations

A number of considerations in recent years have led the Banque de France to take the issue of sustainable development into account in its work and discussions. The main ones are the following:

- a potentially more stringent legal framework: the Banque de France wishes to contribute to the international objectives in this area as they are expressed in France, in particular through the *Loi d'orientation politique énergétique* of 2005. In this regard, it adopted in 2008 an anticipatory stance with respect to future legal provisions following the high-level environmental conference known as the *Grenelle de l'environnement*: obligation to cut energy consumption, eco-responsible real estate renovation, sustainable procurement planning, etc.
- the emergence of new concepts: carbon currency, ethical banking, ethical investment funds, solidarity-based savings, socially responsible

investment, etc. mainly in the financial and banking sectors. They not only need to be taken into account in central banks' analyses and deliberations, but they are also likely to contribute to the emergence of a financial industry that includes fundamental concepts such as transparency, accountability, the long-term horizon, simplicity, etc. In this context, microfinance, the Observatory of which is managed by the Banque de France, also takes on a new dimension;

- the expectations of the public: these expectations, expressed by different economic players, have been taken on board by non-governmental organisations (NGOs), which have acquired a genuine expertise in banking issues and promote "sustainable finance" by analysing the behaviour of banks with regard to sustainable development. The public is sensitive to the indirect impact of the banking sector, via its loans, on society and the economy. The recent crisis has given rise to greater demand for "responsible" banks whose lending policy should not only meet financial criteria, but also social, ethical and environmental criteria.

In this context, adopting a sustainable development strategy for a central bank means taking a fresh look at its way of functioning and its tasks. This does not mean putting an extra burden on its daily activities and way of functioning, but rather "doing things differently to do them better".

A comprehensive sustainable development strategy

In the past few years, the Banque de France has gone from simply integrating environmental concerns into some of its activities to conducting a comprehensive sustainable development strategy; it has set about actively positioning itself and going further by:

- making the reduction of its carbon footprint a strategic priority and a means of differentiating itself, or even positioning itself, within the Eurosystem;
- specifying its position or its view on the new concepts and the new risks that they bring to light;
- analysing the impact of this strategy on the central bank's tasks;
- establishing an in-depth dialogue on the issues at stake with the internal and external parties involved.

Box 12

The history and future of corporate social responsibility (CSR)¹

Extracts from the speech by Christian Noyer

« [...] My first question is whether CSR is a stable concept or one that is still evolving? This concept broadly stems from that of sustainable development, which is defined as development that meets present needs without compromising the ability of future generations to meet their own. Its blueprint was set out at the 1992 UN Conference on Environment and Development in Rio de Janeiro (the first Earth Summit). It is based on the principle of development that is economically efficient, socially equitable and ecologically sustainable. CSR, whose initial objective was accountability, still largely appears to be an evolving paradigm closely linked to the current transition towards a new economic model.

[...] My second question is: will the concept of CSR, whose global spread has been promoted by globalisation, result in new forms of managerial responsibility?

[...] Banks, for instance, are seeking to better understand, beyond their direct impact (environmental footprint), their indirect role through the projects, investments and businesses they choose to fund, i.e. through the financing of a more sustainable economy.

[...] Some experts have even introduced the concept of "sustainable finance". This is the notion whereby the banking sector commits to ensuring transparency, long-term governance, well-informed choices and sustainable markets.

[...] The current financial crisis has left no doubt as to the fact that financial institutions exert a substantial indirect impact on society and its economy. This impact may be considerable in both directions and go far beyond the mere financing of projects or management of risk.

Perhaps confidence in the financial sector could be rekindled thanks to such notions, with a return to fundamentals: simplicity (of products in particular, circuits and funding of companies or virtuous projects), transparency, ethics and balance.

My third question is: can CSR give rise to an alternative, or complementary, regulatory approach that could reinforce global regulation policies?

This would imply that the taking into account of CSR in management models would result in a certain form of self-regulation, for example with recognised codes of conduct.

[...] In the light of this collective awareness of the environmental (finite and fragile natural resources), economic and societal implications, central banks perform their task of preserving financial stability while taking into account and anticipating events. This approach, as recent developments have shown, has to be increasingly systemic and co-operative, involving companies, banks, governments and central banks. The interactivity between the players and the combination of their respective responsibilities should constitute a virtuous basis for a "sound financing of a sustainable economy". "Sound financing of a sustainable economy" and "financial stability" are mutually reinforcing concepts [...].

¹ ICCA Symposium – EABH (Institute for Corporate Culture Affairs – European Association for Banking History) – 27 October 2008

As in all companies, this comprehensive sustainable development strategy is made up of three interconnected components:

An “environmental” component: reducing the Banque de France’s carbon footprint

The guiding principle consists in reducing the institution’s carbon footprint, i.e. the depletion of natural resources and greenhouse gas emissions.

A “social” component: putting human beings at the heart of the Bank’s activities

This aspect concerns the way in which activities are carried out both internally and externally. The guiding principle is first and foremost to conduct a human resource management policy that is respectful of human beings.

An “economic” component: taking a fresh look at the tasks of the Banque de France in its capacity as a central bank

This aspect concerns the very nature of the Banque de France’s tasks. The guiding principle is to look at these tasks through the prism of sustainable development i.e. both in a long-term perspective (as opposed to short-termist approaches) and with a view to greater social responsibility.

Environmental projects and achievements in 2008

The Bank’s master plan for reducing the carbon footprint (*Schéma directeur de réduction de l’empreinte environnementale – SDREE*), drawn up in 2008, is the benchmark for a broad involvement at all levels.

The SDREE covers all sectors of activity and sets out the main priorities with regard to the environmental component of sustainable development, in particular:

- the reduction in the consumption of natural resources;
- the alignment of real estate assets with environmental standards, both for new buildings and renovations;
- the implementation of eco-responsible procedures both for purchases and services.

It includes both technical recommendations to steer the Bank’s actions and behavioural recommendations that everyone may implement. The SDREE is

Box 13

Launching of the carbon footprint project

In the second half of 2008, the Banque de France launched a carbon footprint project in order to measure its greenhouse gas emissions. This project aims at identifying and analysing activity flows (mainly energy, transport, supplies and services) of its different establishments (head office for 2009). Five sites were initially chosen as pilot sites (Chamalières, Vic-le-Comte, Marne-la-Vallée, Paris and Lille).

If the project yields conclusive results in the course of 2009, the carbon footprint assessment will be extended to the whole branch network. The methodology adopted, which is that of the French Environment and Energy Management Agency (ADEME), covers the overall perimeter of the Bank and will involve, once the data have been collected and processed, drawing up recommendations for the reduction of CO² emissions, in proportions at least equal to that of the European energy-climate package.

The Banque de France, anxious to anticipate the EU’s target of a 20% reduction in greenhouse gas emissions between 1990 and 2020, intends to continuously reassess its processes.

based on a joint commitment by the Bank and its staff, the changes in behaviour leading to a reduction in resource consumption of almost 30%. The idea is to set an example both at the individual and collective level.

Concrete, measurable results have already been obtained with regard to the reduction or the shift in energy consumption at the Bank’s banknote production sites, and the systematic inclusion of energy performance indicators in construction work (Avignon) and real estate renovation (Strasbourg, La Rochelle, etc.). Other large-scale projects are underway:

- a new eco-responsible IT platform (Green IT): launching of preliminary studies with a view to bringing the Bank’s IT support centres together in a “positive energy” building (a building that produces more energy than it consumes);
- a plan to reorganise working spaces at the Bank’s head office, taking into account the sustainable development dimension: renovation of buildings, comfort of the users.

- a Company Transport Plan: analysis of staff means of transport in 2008 (home-workplace and assignments at three pilot sites), supplemented by an action plan to be drawn up by June 2009;
- preparation of a guide for the promotion of sustainable procurement;
- a carbon footprint project: objective of measuring greenhouse gas emissions generated directly or indirectly at the head office, the Directorate General Banknote Manufacturing and a pilot branch (Lille) by end-2009;
- an energy audit of all the tertiary buildings of the branch network in order to subsequently draw up a strategic plan for real estate management.

A renewed social dimension

An existing policy

The company VIGEO was entrusted with the task of assessing the "social responsibility" of the Bank in 2007. This work highlighted the fact that social responsibility was a major value for the Bank. The VIGEO report also noted that the Bank was rather ahead within the corporate world in terms of its social policy, in particular with regard to fighting inequality.

A large number of achievements...

- several company agreements on disabled people and special efforts through the *Centre d'adaptation et de réinsertion par le travail* (CART). This centre is a model in terms of integration of mentally disabled people;
- creation of an Observatory on the prevention of health risks at work;
- initiatives with regard to the fight against addictions;
- commitment against harassment;
- setting up of a psychological helpline for Bank staff;
- initiatives in favour of social diversity (500 high school students from Priority Education Areas (ZEP) will be received in Bank branches as from 2009).

... and several programmes underway

- health risks at work;
- new scheme for fighting gender discrimination;
- new agreement on disability under negotiation.

An economic dimension heightened by the financial crisis

Review of the Bank's tasks

In the first half of 2008, the Banque de France conducted a review of its tasks taking sustainable development into account, with regard to central bank activities (preparation and implementation of monetary policy, management of payment media and systems, economic and financial studies, banking supervision, cash management), activities in connection with the Bank's branch network (the regions, companies, households) and even certain support activities linked to operational activities. The Bank's objective was to examine how it could integrate sustainable development into its tasks and identify areas with real value added in terms of "social responsibility".

Priorities

This review highlighted several priorities, in particular:

- improving the public's financial education and its access to information by setting up websites for the general public devoted to household debt and banking regulations and practices ("Infobanque"), and by linking up to the network of interactive terminals in order to provide access to a wide range of public services (first experiment underway in the Auvergne);
- integrating sustainable development into the Bank's research work and studies by developing research on energy market developments and the impact of extreme events, by examining the risks that the new instruments such as carbon certificates represent for financial stability, and by broadening its expertise with respect to money laundering and the financing of terrorism;
- generalising the certification of the Bank's products and processes (ISO 9001, ISO 14001, OHSAS, etc.).

As the Governor of the Banque de France stated at the ICCA symposium on the history and future of corporate social responsibility on 27 October 2008, these projects are the start of a comprehensive and iterative process for an enterprise attuned to its partners that should result in a complete review of its tasks. During this symposium, the Banque de France stressed the major indirect role played by the banking sector with regard to sustainable development through the activities, investments and projects they choose to finance, i.e. through the financing of a more sustainable economy.

A specific form of governance

The specific nature of the Bank's comprehensive sustainable development strategy is that it puts special emphasis on the involvement and interaction of both internal and external stakeholders in the reform process to be carried out.

A special organisational structure was decided on at end-2008 and is progressively being set up:

- a "strategic committee for sustainable development" chaired by the Governor of the Banque de France and charged with setting broad guidelines;
- an "operational committee for sustainable development" placed under the responsibility of the Secretary General and charged with preparing and following up decisions, as well as promoting the formulation and implementation of concrete projects;
- the operational committee relies on two working groups "Reduction of the carbon footprint" and "Tasks, products, services and R&D";
- an "external consultative commission", which will enable the Bank to interact more and be more in line with external stakeholders (NGOs, companies, local authorities, etc.);
- an internal "sustainable development laboratory" charged with steering and co-ordinating the work of a network of sustainable development reference people in every Directorate General and region;

In 2009, the Banque de France will draw up a "sustainable development charter" with a view to formalising this governance and its commitments.

2| Implementing the strategy

2|1 Organisation of the departments

In 2008, the Banque de France carried out a reorganisation of its head office departments, which meets some of the strategic priorities described in Section 1|1. The purpose of this reorganisation is to:

- strengthen the Bank's position on the European and international scene with regard to studies and research;
- reinforce its capacity to analyse and take preventive measures in the area of financial stability;
- develop its statistical tools, in particular for company analysis;
- modernise its management methods. In this respect, a clearer distinction between operational functions and support functions should enable the Bank to be more efficient in implementing its broad guidelines and meeting its objectives.

2|1|1 The reorganisation of the Directorate General Economics and International Relations

The structure of this Directorate General is now as follows:

- the new *Microeconomic and Structural Analysis Directorate* (DEMS), charged with analysing the behaviour of economic agents, the performance of the productive system (in particular from the point of view of foreign trade) and structural policies;
- the *Economics and International and European Relations Directorate* (DERIE), in charge of co-ordinating the Bank's European and international activities, was broadened to include the Macroeconomic Analysis and International Syntheses Division in order to better integrate economic research within the numerous international fora where the following issues are discussed: global imbalances, international macroeconomic assessment and exchange rate fluctuations. This new structure will also contribute to facilitating the Bank's work on the enlargement of the European Union and the euro area;

• thanks to its two other directorates, the **Business Conditions and Macroeconomic Forecasting Directorate** (DCPM) and the **Monetary and Financial Analysis Directorate** (DEMFI), the Banque de France is able to conduct its own economic assessments based on a monitoring of the business environment and make its own macroeconomic forecasts for France and the euro area, and therefore make itself heard within the Eurosystem.

To focus on these objectives, the Directorate General Economics and International Relations (DGEI) has parted with the following activities: statistics and services provided to the entire Bank, such as publications and translations.

2|1|2 Creation of the Directorate General Statistics (DGS)

The Directorate General Statistics (DGS) was created by grouping together different divisions within a specialised operational unit with sufficient technical and human resources. Its creation contributes to the unlocking of synergies with the other members of the ESCB, the development of a set of tools common to all data-producing divisions and the pooling of data. It is also aimed at improving the efficiency of the collection and production of data and strengthening the Bank's authority in this area.

The Directorate General Statistics is made up of three directorates:

- the **Sectoral Surveys and Statistics Directorate** (DESS) processes the collected statistical information on companies with a view to analysing the French business environment and providing the data necessary for drawing up the balance of payments. It is notably charged with monitoring foreign direct investment in France and French investment abroad;
- the **Balance of Payments Directorate** (DBDP) is responsible for drawing up France's balance of payments, France's contribution to the balance of payments of the euro area and the European Union, international banking statistics, and monitoring securities issuance and holdings. It carries out the exchanges of data with other organisations and provides internal and external users with time series;

• the **Monetary and Financial Statistics Directorate** (DSMF) is charged with drawing up and disseminating the French contribution to euro area monetary and financial aggregates, and compiling the statistics necessary for monitoring residents' investment and financing behaviour. It is also responsible for drawing up the national financial accounts.

The Banque de France took advantage of this reorganisation to create a new division within the DSMF, the Institutional Investors Analysis and Statistics Division, charged with collecting and analysing the information received from insurance companies, mutual funds and securitisation structures. This initiative has confirmed the importance given to analyses of the activity of these non-banking financial sectors, particularly in the context of the financial crisis that started in 2007.

Overall, the purpose of the creation of the DGS is to improve the quality of the statistics produced by the Bank, for the benefit of all users, i.e. internal users, the ESCB and the public. At the national level, the DGS monitors the sources of financing of companies, in close co-operation with the Companies Directorate, and of private individuals.

2|1|3 Creation of the Directorate General Cash Management and Branch Network Activities

The Directorate General Cash Management and Branch Network Activities was created for the purpose of grouping within a single structure the main activities conducted in the network with regard to currency in circulation, relations with companies and with private individuals. It is composed of five directorates:

- the Banknote and Coin Issuance and Circulation Directorate and the Banknote and Coin Maintenance and Relations with Institutional Clients Directorate, which made up the Directorate General Banknote and Coin Management;
- the Branch Network Directorate, the Companies Directorate and the Directorate for the Supervision of Relations between the General Public and the Financial Sector, which came under the General Secretariat.

The Banking Mediation Committee and the General Secretariat of the Advisory Committee on the Financial Sector were brought into this Directorate General to enable the Bank to gain a better overview of relations between private individuals and the financial sphere.

2|1|4 Reorganisation of the General Secretariat

The General Secretariat was reorganised to focus its action on support functions:

- organisation/IT;
- real estate/logistics/security;
- budget/management control/accounting;
- strategy/communication: the Press and Communication Directorate was brought into the General Secretariat to make up this new function.

2|1|5 The strengthening of the “financial stability” function

A new Macrofinancial Studies Division was created within the **Financial Stability Directorate** (Directorate General Operations) to strengthen the Bank's capacities in the area of financial stability.

In practice, the motives underpinning the creation of this division are three-fold. The first objective is to contribute to the identification of macroprudential risks and the assessment of financial stability policies. The second is to analyse the systemic implications of the regulation of the financial sector. The third is to contribute to a better understanding of the interactions between the financial sphere and the real economy. The new division is thus closely involved in the work being conducted on the definition of macroprudential policy.

The Macrofinancial Studies Division will work closely with the Directorate General Economics and International Relations and the General Secretariat of the *Commission bancaire*.

2|2 Salient features of activities in 2008

The position of the Banque de France in the financial and economic landscape is highlighted by its active contribution to the decisions taken within the framework of the Eurosystem and numerous European and international bodies and by the three key objectives that underpin the legitimacy of its actions:

- monetary stability;
- financial stability, both within the framework of the Eurosystem and in terms of its responsibility as a central bank;
- the provision of specific services to public authorities, companies and private individuals, as well as to the banking and financial sector.

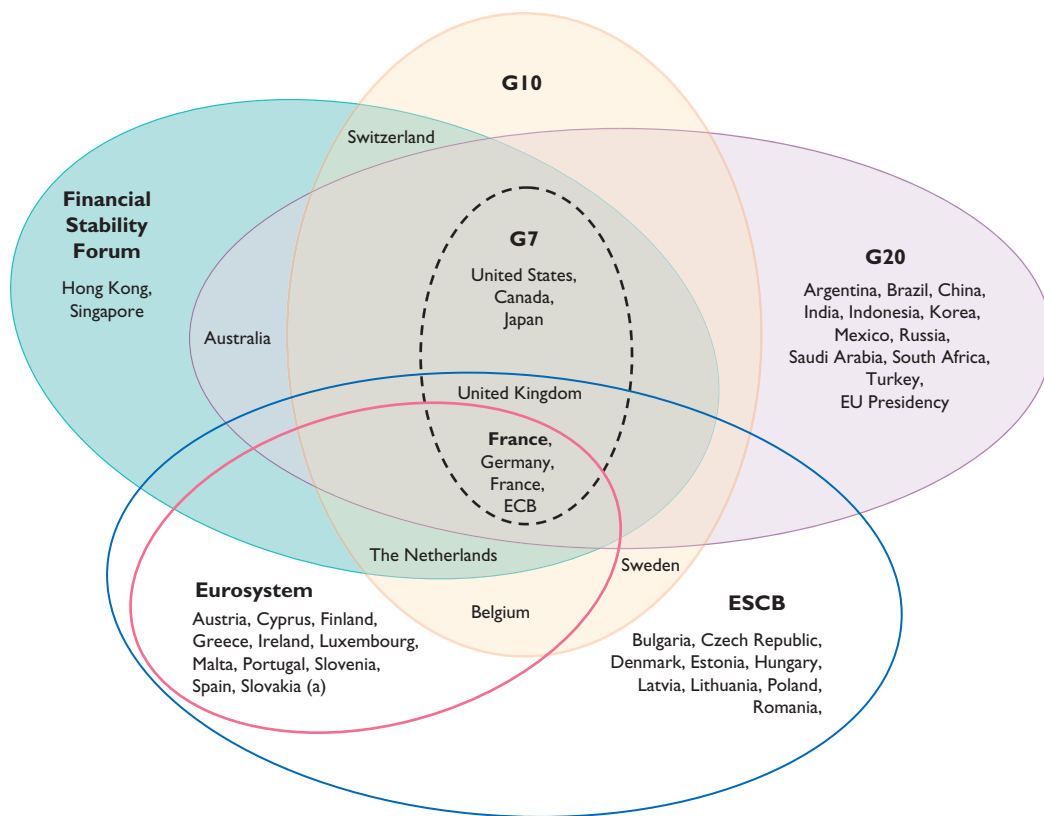
2|2|1 An active contribution within the framework of European and international bodies

In 2008, the Banque de France took an active part in all the work conducted within the framework of international bodies, in particular on the financial crisis, the means of containing it and the reforms to be implemented.

European relations

The Governor of the Banque de France is a member of the ECB Governing Council, the Eurosystem's decision-making body, which comprises the governors of the national central banks of euro area countries (16 since Slovakia joined on 1 January 2009) and the six members of the ECB Executive Board. The Governing Council organised an unusually large number of meetings and teleconferences in 2008 to ensure the liquidity of the money market and deal with the rise and then fall of inflationary pressures.

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



Notes: Basel Committee = G10 + Spain.
 The European Union presidency participates in the G7 when it is held by a country that does not belong to the G7.
 (a) Since January 2009

The decisions of the Governing Council are prepared by a series of committees, in which all national central banks take part. Over a hundred Banque de France representatives regularly participate in these committees and in various related working groups. In 2008, three committee and working group meetings were organised in France by the Banque de France.

The Banque de France is also a member of the EU Economic and Financial Committee (EFC), which prepares the work of the Ecofin Council and brings together the Economy and Finance Ministers of the Member States. It also takes part in the informal Ecofin Council, which includes central bank governors. The Banque de France's involvement was particularly significant in the second half of 2008, during the French presidency of the European Union.

International and bilateral relations

The Banque de France is a member of the major international fora. In this capacity, it took an active part not only in the international management of the financial crisis but also in the discussions on the reform of the international financial architecture.

In the framework of the G20, it put forward its analyses on the reform of the international financial and accounting regulatory system and international co-operation in the areas of supervision and information exchanges. Within the International Monetary and Financial Committee and the G7, it took part in the discussions on the reform of the IMF, its role, its instruments and governance. In addition, it contributed to the work on the reform of the role and instruments of the development banks.

In order to strengthen the mechanisms and instruments for preventing crises, the Banque de France is taking part in the drawing-up of a new, more efficient and responsive international framework for macro-financial supervision involving all of the players concerned (in particular the IMF and the Financial Stability Forum). This framework is expected to take into account the interactions between regulatory, financial and macroeconomic aspects in the detection of crises.

The Governor of the Banque de France participates in the meetings of Franc Zone ministers and 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 2008 provided an opportunity for analysing the impact of the rise in food prices on the Franc Zone economies and the effects of the global financial crisis.

As regards technical co-operation, the second twinning project between the Banque de France and the Bulgarian National Bank, in partnership with De Nederlandsche Bank and the Banca d'Italia, came to an end in 2008. The Banque de France continued to maintain close co-operation with some central banks (BEAC and BCEAO, bilateral agreement with the Bank of Morocco) and took an active part in projects conducted by the ECB (in particular in Egypt and Russia).

Key data for 2008

- 23 meetings of the ECB Governing Council and 18 teleconferences.
- 17 other European meetings (Economic and Financial Council, informal Ecofin, French-German Economic and Financial Council).
- Some thirty meetings of international (IMF, BIS, G7, G10, G20, OECD, FSF) and regional (e.g. the Franc Zone) organisations and bodies.
- 85 short-term assignments, 4 long-term secondments and 34 study visits in the framework of technical co-operation.
- 53 training seminars and 24 study visits arranged for 1,750 trainees from foreign central banks.

2|2|2 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.

The preparation of monetary policy relies on powerful statistical tools and an in-depth analysis capacity, two requirements that justified the creation of the Directorate General Statistics (DGS) and the reorganisation of the Directorate General Economics and International Relations (see above).

Active participation in tasks relating to official French and European statistics

Tasks carried out in the area of statistics

In this area, the Banque de France:

- draws up the French components of the monetary and financial and balance of payments statistics that the ECB then aggregates for the whole of the euro area;
- produces a large body of financial statistics pertaining to national accounting;
- draws up France's balance of payments and international investment position;
- conducts a "monthly business survey".

Key data for 2008

- 32,000 statistical series released on the French version of the Bank's website.
- 17,600 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.
- 15,000 companies surveyed to produce the monthly business survey.
- 1,085 companies reporting monthly and 11.5 million items of information processed to compile the balance of payments.
- 380 monthly reporting banks for the production of monetary statistics.
- 449 asset management companies participating in the quarterly centralisation of portfolios of some 10,900 mutual funds.

Due to the financial crisis, it became increasingly important to assess the economic and financial situation in France. The Directorate General Statistics conducted an early and precise analysis of the changes in the distribution of loans to companies and households and the developments in the issuance of securities during the cyclical downturn. The DGS also set up a statistical monitoring framework to enable the public authorities to monitor the commitments by French banks in terms of credit granted to the French economy in the framework of the public support mechanism for the financing of the economy (SFEF).

Greater emphasis on studies and research

The Directorate General Economics and International Relations has gradually been reinforcing its teams of economists. Its production of original research documents (*Working Papers*) increased by 20% between 2007 and 2008 and the number of articles published in international scientific journals also posted a strong rise.

In 2008, the Banque de France organised several international symposia and seminars, which brought together renowned researchers from central banks and French and foreign universities. It also held its international symposium, organised every two years. This year's theme was "Globalisation, inflation and monetary policy".

The Banque de France Foundation carried on its monetary, financial and banking research programme. In the framework of its Visiting Scholars programme,

Key data for 2008

- 36 *Working Papers*, over 60 articles in the Bank's *Monthly Bulletin* and other publications.
- 26 articles published in scientific journals with selection panels.

Banque de France Foundation

- 15 research seminars.
- Seventh *Journées on "International Macroeconomics and Finance"*.
- Creation of the "Young researcher in economics" prize.

it received academics from French and foreign universities wishing to collaborate on studies with Banque de France teams and organised 15 research seminars.

The Foundation organised its seventh *Journées on "International macroeconomics and finance"* on 5 and 6 December 2008. This event was co-organised by economists from the Banque de France (international economics unit), the Paris School of Economics (PSE) and the Centre for Economic Policy Research (CEPR). The Foundation also created a "Young researcher in economics" prize to promote economic research at French universities.

Improving the operational framework of monetary policy

The changes to the Bank's operational framework of monetary policy are dealt with extensively in Chapter 1 "The implementation of monetary policy in the context of the financial crisis".

Operational activities based on back office tools of the highest standard

As regards markets and securities, the changes to the operational framework (in particular regarding monetary policy, with the "3G" collateral management system for French and foreign institutional clients, see below) were founded on a complete overhaul of the securities back office of the Bank. The objective of this reform was to bring depository function tools into line with the highest European standards and its efficiency was successfully tested in the context of a very considerable increase in the number of tender procedures and the amount of collateral used.

Further diversification of the foreign exchange investment strategy and development of the range of services offered

Diversified foreign exchange assets

In 2008, 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 actively managed in trading books or, in some cases, invested in securities held to maturity.

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.

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-2008

- EUR 81.6 billion in foreign exchange reserves.
- 2,491 tonnes of gold, worth EUR 49.7 billion.
- EUR 31.9 billion in foreign currency holdings.

In the same way as national foreign exchange reserves, these portfolios are actively managed, in accordance with benchmark portfolios defined by the ECB.

A greater range of financial services

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 continued to grow considerably in 2008 thanks to the strengthening of ties with existing clients and the development of new contacts (about 12 new clients in 2008). The range of financial services is diversified: it includes the opening of interest-bearing cash accounts, both in euro and foreign currencies, the opening of securities accounts in euro, lending/borrowing operations in several currencies, foreign exchange operations and sales/purchases of euro-denominated securities. 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 2008, the Banque de France sold 103 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.

Production and management of banknotes and coins

Production of banknotes

The good results for banknote production recorded in 2006 and 2007 were confirmed in 2008, with an increased volume of banknotes delivered, an improvement in industrial performances (fall in the rate of imperfect banknotes produced, increase in productivity of equipment and productivity per employee) and a consolidation of operating income.

In 2008, the volume of banknotes produced and delivered was higher than that recorded the previous year. Banknote production continued to benefit from the combined effect of a high quota of euro banknotes (1,580 million notes) assigned to the Banque de France as part of the pooling system¹ and a sustained export market amounting to an average 600 million banknotes annually.

As regards human resources, 2008 was marked by two major events:

- the Bank's paper mill and printing works were awarded the occupational health and safety OHSAS 18001 certification, in addition to the renewal of the Quality ISO 9001 and Environment ISO 14001 certifications;
- the reform of the management framework of contract staff – which involve setting up a new pay and career management system – as a result of the increased recruitment of this category of staff.

Table 9 Banknote Manufacturing
 Results in 2007 and 2008

(Annual volumes in billion banknotes, staffing levels in full-time equivalent terms at 31 December)

	Annual volumes manufactured and delivered	Headcount
Results 2007	2.04	944
Results 2008	2.24	959

¹ 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 2008, the Banque de France produced EUR 5, EUR 10 and EUR 20 banknotes.

At European level, the Directorate General Banknote Manufacturing contributed 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 entrusted this group with the design and production of a pilot series of EUR 50 banknotes, which will be the first denomination to be issued at the start of the next decade.

In the medium term, the operational priorities of the Directorate General Banknote Manufacturing are focused on the consolidation of its financial break-even, especially in view of the implementation in 2012 of the Eurosystem's centralised system of tenders for the supplying of euro banknotes.

Management of banknotes in circulation

In 2008, the Banque de France and the IEDOM put 7.7 billion euro banknotes into circulation, worth EUR 178 billion. This represents a 1.5% increase on the previous year. The number of banknotes returned to these institutions also posted a slight rise (up by 0.9%) to stand at 7.5 billion banknotes, worth EUR 178 billion. The volume of banknotes handled by these issuing institutions grew at a slower pace in 2008, after having increased by 2.9% and 4.0% respectively in 2007. This can be attributed to the gradual development of banknote recycling by private operators:² at end-2008, 2,770 bank branches were authorised to recycle banknotes, compared with less than 2,000 a year earlier.

In this context, the banknote authentication and fitness sorting activity remained sustained: the annual volume of banknotes processed amounted to 7.6 billion banknotes, enabling the Banque de France to clear its stock of banknotes received in 2007.

In 2008, the net issuance of euro banknotes³ in France rose by 12.5% to stand at EUR 69.9 billion.

This increase, which was more pronounced than that recorded in 2007 (8.7%), is due to the increased demand for banknotes in October caused by the climate of uncertainty in the wake of the financial crisis. In the euro area, this demand resulted in a EUR 35 billion

Chart 27 Volumes of euro banknotes handled by the Banque de France and the IEDOM

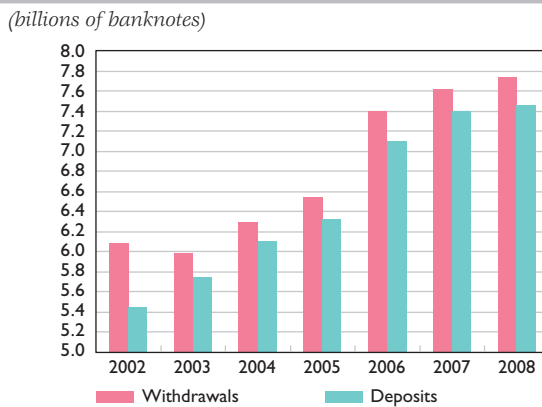


Chart 28 Net issuance of banknotes in France

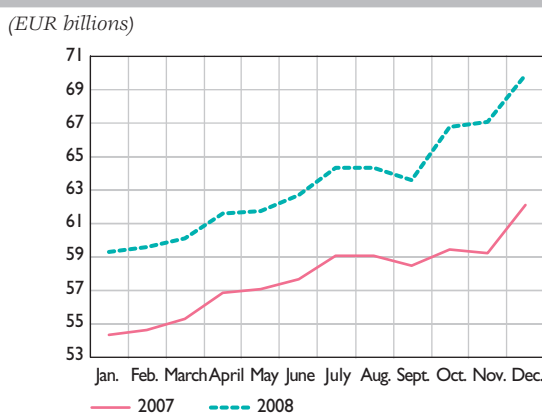
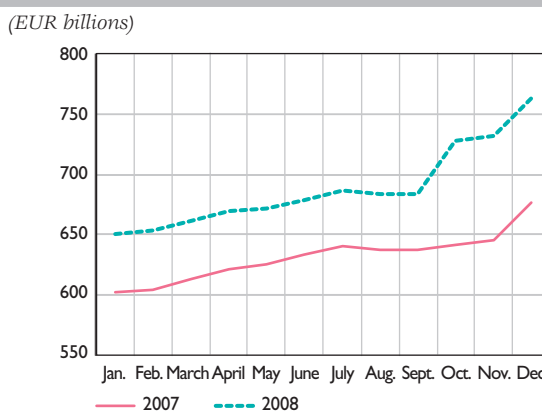


Chart 29 Net issuance of banknotes in Europe



2 Banknote recycling by a private operator consists in the re-issuance by the latter of the banknotes received from its own clients without transiting through the central bank. This operation, which is strictly governed by European regulations, is conditional on the signing of an agreement with the central bank, the private operator being subject to controls by the bank (see box 14).

3 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.

Box 14

The recycling of euro banknotes and coins in 2008¹

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

The system of inspection, which was put in place in 2006, is now totally operational. At end-2008, 40 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. Overall, at 31 December 2008, there were 169 sites in France handling coins for delivery to the Banque de France.

71 workshops were the subject of on-site inspections by the Banque de France. The inspections carried out identified a number of malfunctions (inadequacy of equipment, operating and internal control procedures, etc.) that were gradually rectified. Having identified several serious shortcomings, the Banque de France gave notice to six of these sites to bring their processing procedures into compliance with the requirements of the agreements. These problems were resolved.

In addition, following the notification of a new counterfeit in January 2008, the operators adapted their equipment.

Agreements regarding the automatic distribution of banknotes not withdrawn 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 that will come to an end on 31 December 2009.

Since then, most credit institutions have started to work on the possibility of recycling banknotes in-house in the framework of the target system laid down by the standard agreements. In general, this has resulted, often after a series of experiments, in the signing of an agreement. Most of the institutions concerned have invested in back office equipment, which are efficient and easy to set up, or bank counter equipment (automatic cash-recycling machines). Some, however, have preferred to recycle via equipment integrated into the ATM.

At the end of 2008, 44 agreements concerning the "distribution by ATMs of banknotes not directly drawn from a Eurosystem central bank" had been signed. 2,770 bank branches were distributing via ATMs banknotes not drawn from a central bank. These banknotes were covered by 42 agreements regarding processing operations signed by the credit institutions themselves. In addition, 7 banknote processing agreements were signed by service providers of these institutions.

In 2008, the Banque de France carried out 71 on-site inspections of bank branches and workshops processing banknotes for the replenishment of ATMs.

Training bank employees in the authentication of banknotes

In accordance with the provisions of Article R122-6 of the Monetary and Financial Code, the Banque de France continued to give support to banks that requested it in training staff charged with the manual distribution of banknotes in bank branches. In 2008, 1,145 credit institution staff members were trained along these lines by the Banque de France.

Implementation of the Decree in overseas departments

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

Three agreements concerning the delivery by ATMs of recycled banknotes have been signed (Réunion, Martinique, Guadeloupe).

At end-2008, six agreements covering the automatic processing of euro coins were in force in respect of eleven production sites. The IEDOM conducted four on-site inspections.

¹ Report produced pursuant to Articles R121-3 to R123-2 and R162-5 of the Monetary and Financial Code implementing Article 6 of Council Regulation (EC) 1338/2001 of 28 June 2001 (entered into force on 17 January 2006).

increase in banknote circulation, including 2.2 billion in respect of net issues in France.

At end-2008, banknote circulation in the euro area amounted to EUR 763 billion, up by 12.7% on the previous year, compared with a 7.7% rise in 2007. By convention, 19.0%⁴ of this banknote circulation, corresponding to EUR 145 billion, is recorded on the Bank's balance sheet.

In terms of net issuance, France remained in fourth position in the Eurosystem,⁵ behind Germany (EUR 328 billion), Italy (EUR 140 billion) and Spain (EUR 83 billion).

Compared to other euro area countries, France continues to stand out in using a great number of medium-value denominations: the growth in net issuance in France, in nominal terms, is mainly fuelled by that of denominations used for everyday transactions (EUR 5, 10, 20 and 50), which rose by 13.8%, compared with 9.2% in the Eurosystem. Net issuance of denominations used for hoarding purposes (EUR 100, 200 and 500) posted a lower increase than the euro area average (8.6%, as against 15.5% for the Eurosystem).

As part of the decentralised pooling system and the adjustment of banknote stocks between euro area central banks, the Banque de France supplied foreign central banks with 423 million banknotes and imported 74 million.

Developments in the volume of coins handled by the Banque de France and the IEDOM in 2008 were more marked than for banknotes: whereas withdrawals rose by a small amount (1.1%, i.e. 24 million coins), deposits increased sharply, by 5.5%, i.e. by 67 million coins. In this context, the growth in net issuance of euro coins in France in nominal terms continued to decline to 4.1% in 2008 from 5.8% in 2007. At end-December 2008, net issuance of coins in France thus stood at EUR 2.4 billion.

French franc banknotes continued to be returned to the Banque de France in 2008, with a surge in activity recorded at the beginning of the year due to the end

Key data for 2008

- 2.2 billion banknotes delivered by the Directorate General Banknote Manufacturing, of which 1.6 billion in euro.
- 7.6 billion banknotes sorted.
- 7.7 billion banknotes distributed by the Banque de France.
- 7.5 billion banknotes received at the Banque de France.
- 0.9 billion coins put into circulation.

of the exchange period for the Montesquieu 200 franc note on 28 February 2008. Over the year, exchanges of French franc notes reached a volume of 1.8 million banknotes with a value of FRF 333 million (i.e. EUR 50.7 million).

2|2|3 The Banque de France and financial stability

Banking supervision and co-operation with market authorities

Key role of banking supervision

The main task of the banking authorities chaired by the Governor of the Banque de France (*Comité des établissements de crédit et des entreprises d'investissement* – CECEI – for the administrative authorisations delivered to credit institutions, and the *Commission bancaire* for prudential supervision) is to ensure the safety of public deposits and, more generally, to safeguard banks' soundness. In order to ensure the latter, it is essential that the French banking and financial system be prudently managed and strictly supervised.

The quality of banking supervision is enhanced by the fact that the banking authorities are closely linked to the Banque de France. Indeed, the supervision of credit institutions is one of the many tasks carried out by the central bank, which enable it to have an all-encompassing yet precise view of the financial sector, be it knowledge of the markets, household debt statistics or companies' financial situation. In this regard, the Governor of the Banque de France sits

⁴ 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.

⁵ Outstandings, excluding national currencies.

on the Boards of the *Autorité des marchés financiers* (AMF – Financial Market Authority), and the *Autorité de contrôle des assurances et des mutuelles* (ACAM – Insurance Supervisory Authority). The Banque de France performs secretarial duties for the *Comité consultatif de la législation et de la réglementation financières* (CCLRF – Advisory Committee on Financial Legislation and Regulation), which gives its opinion on any text on the subject, at the request of the Minister of the Economy, Industry and Employment.⁶

As regards prudential supervision, a programme of on-site inspections was carried out in 2008 (including, in particular, the supervision of the valuation of complex products, securitisation, proprietary trading and management for third parties, and liquidity management). In addition, a reorganisation took place to launch a series of new investigations in the large banking groups both in France and in some of their establishments abroad, following the heavy market losses incurred by some institutions, and in subsidiaries of foreign banks in order to measure the extent to which they have been impacted by the problems encountered by their parent companies. These investigations focused mainly on the impact of the crisis on Value at Risk (VaR) models, exposures on monoline insurers and the internal control of operational risk related to market activities.

In addition, in the framework of recommendations made by international political and financial authorities on the difficulties arising from the crisis, the *Commission bancaire*, together with the other supervisory authorities (AMF, ACAM, *Autorité des normes comptables*) and professional organisations, was led to clarify the exercise of banking activities, in particular with regard to the fair valuation of certain financial instruments, accounting reclassification and the quality of banks' financial disclosure, in order to restore market confidence.

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. In this respect, it was closely involved, via its General Secretariat – a department of the Bank – in the national and international adaptations of the main regulatory texts in this area, in particular the national

transposition measures for the European Third Money Laundering Directive of 25 October 2005.

In 2008, European co-operation between banking supervisors – which is more than ever necessary during a crisis – was stepped up. The supervision of major cross-border institutions was increased and extended to other groups. The first on-site inspections involving supervisors from several European countries under the authority of a head of mission were conducted in two major French groups. As regards crisis management in the European Union, the *Commission bancaire* signed the tripartite co-operation agreement drawn up by banking supervisors, insurers, financial markets, central banks and ministries of finance, which clarifies the operational responsibilities of each signatory. Lastly, the General Secretariat of the *Commission bancaire* continued to offer its expertise to the Interim Working Committee on Financial Conglomerates, which studied the concentration risk and liquidity transfers within these groups.

The Committee of European Banking Supervisors (CEBS) carried out several key projects following the requests made by the European Commission (liquidity risk, hybrid instruments, large exposures, etc.). The CEBS also pursued its work on financial and regulatory reporting (FINREP and COREP) with a view to simplifying its content and harmonising the national adaptations.

At the international level, the co-operation fora, such as the Basel Committee, the Joint Forum and the Financial Action Task Force (FATF), were extremely active in 2008. Within the Basel Committee particularly, the General Secretariat of the *Commission bancaire* took part in various projects, mainly related to the worsening of the financial turmoil:

- the analysis and management of liquidity risk by banks, in particular during a crisis, and the means of supervision used by supervisory authorities, in particular for the supervision of transnational groups;
- the strengthening of Basel 2 (tightening of requirements relating to securitisation and the trading book; setting-up of more stringent stress tests; enhancing of transparency and valuation methods);

⁶ The Credit Institutions and Investment Firms Directorate provides the secretariat for the CCLRF and the CECEI.



- the use of fair valuation and its monitoring by supervisors.

The work of the Joint Forum focused on credit risk transfer, concentration risk in financial conglomerates and the marketing of financial products for non-professional investors.

Given the principal trends in the organisation of banking activities in France in 2008, the CECEI was led to examine the following projects: the creation of secure refinancing structures, innovations in the area of payment media, the merger or development of mutual bank networks, investment advice and the reception and transmission of orders.

Key data for 2008

Commission bancaire

- 129 on-site inspections in the framework of the programme of on-site inspections for 2008.
- Around 20 additional inspections in response to the financial crisis, concerning market risk, monoline exposures and liquidity risk.
- Participation of managers and executives of the SGCB in 228 bilateral, sectoral and international meetings concerning the financial crisis.
- Participation in 271 meetings with French and foreign supervisory authorities in the framework of off-site supervision (up by more than 50%).

CECEI

220 decisions, including 17 authorisations and 50 withdrawals of authorisation.

The salient features of 2008 in the area of banking and financial regulation were the preparation of the future Electronic Money Directive and the transposition into French law of the Payment Services Directive (leading to the creation of a new type of institution, a payment institution) and the Acquisitions Directive.

Financial stability

Activities relating to financial stability at the heart of current events

The Banque de France was very closely involved in the numerous initiatives in connection with the crisis at the national, European and international level, in particular in the analysis of financial sector vulnerabilities and market developments and the drawing up of possible responses. It contributed to the work of the G20, the BIS and the FSF through a large number of studies and other papers. It also closely monitored the work of the French Presidency of the European Union on financial regulation (review of the Lamfalussy process, work on several Directives – the Capital Requirements Directive (CRD), Solvency 2, rating agencies, etc.).

This work was co-ordinated by the Financial Stability Committee, an internal Banque de France body chaired by the two Deputy Governors. The Committee carried out several assessments of the consequences of the crisis for liquidity-providing central banks and bank regulators.

The Banque de France also helped to explain the financial mechanisms of the crisis at numerous seminars and conferences open to specialists and the general public (at universities and *grandes écoles* and in the framework of presentations organised by Bank branches). On 3 September 2008, the Banque de France, in partnership with the Toulouse School of



Conferences and seminars
on the financial crisis

Economics, organised an international conference on “extreme events”, which brought together researchers, financial industry experts and representatives from the official sector. More generally, this partnership enables researchers and Banque de France experts to work closely on issues of financial stability and regulation.

The Bank published two issues of its *Financial Stability Review* in 2008. The first focused on liquidity-related problems in periods of financial turmoil. The second was devoted to valuation and its implications in terms of financial stability, in particular the impact of mark-to-market valuation and the knock-on effects of pro-cyclicality. Both issues include a large number of contributions from economists and experts from academia, public institutions and financial institutions. The issue on liquidity was launched at a conference chaired by the Governor of the Banque de France at the Palais Brongniart. To launch the issue on valuation, a conference, chaired by Governor Noyer, was organised in Washington alongside the autumn meetings of the IMF. It drew a wide audience, around a panel of speakers including central bank governors, economists

and professionals. A conference on valuation, aimed at academics and the financial community, was held several days later at New York University.

Particular attention was also paid to educational publications. The second issue of *Documents et débats* devoted to the financial crisis (published in March 2009) was circulated to all economics teachers and French Members of Parliament. A new on-line publication, *Focus*, was launched, the first issue being devoted to the “Assessment and outlook for sovereign wealth funds”.

In a context marked by continued financial turmoil, the Banque de France, which is responsible for overseeing the issuance of negotiable debt securities, closely monitored the developments on this market, in particular the outstanding amount of certificates of deposit issued by credit institutions. The outstanding amount of negotiable debt securities (for all segments, i.e. certificates of deposit, commercial paper issued by companies and negotiable medium-term notes) increased from just over EUR 471 billion in July 2007 to roughly EUR 580 billion at end-2008. It represents the largest market for short-term securities in continental Europe. It ranks third worldwide, behind the US and British markets, but has shown considerable dynamism since July 2007: outstandings (excluding negotiable medium-term notes) were up by 26% between July 2007 and end-2008, while, over the same period, outstandings of commercial paper in the United States and euro-commercial paper in London fell by 26% and 13% respectively.

In addition, the Banque de France continued to play a prominent role in promoting the STEP label designed to promote the integration, recognition, development and quality of short-term securities markets in Europe. This label, created in 2006, benefited from the ECB

Key data for 2008

Financial stability

- 4 meetings of the “Paris Robustesse” group.
- 30 articles published in the *Financial Stability Review*.

Supervision and development of the negotiable debt securities market

- 337 financial memoranda analysed in the framework of the annual updating exercise then posted on the Banque de France’s website, and 150 ad hoc updates.

Governing Council decision of 15 October 2008 to add STEP-labelled certificates of deposit to the list of eligible collateral, provided they fulfil certain conditions. The outstanding amount of STEP securities increased significantly, climbing from EUR 320 billion at end-2007 to EUR 380 billion at end-2008 (negotiable debt securities accounting for 68% of the total). The ECB publishes statistics of outstanding amounts and yields on its website, on the basis of data provided by various suppliers, in particular the Banque de France.

Operational continuity objective

Ensuring financial stability also means preparing for operational shocks likely to significantly and lastingly affect the smooth functioning of the Paris financial centre. In the framework of the *Paris Robustesse* group – which brings together representatives from the main credit institutions, payment systems and regulatory and supervisory authorities – the Banque de France set up an emergency committee charged with crisis management and recovery at the collective level.

This committee was at the heart of a test conducted on the Paris financial market in June 2008, like those carried out in the major financial centres of London and New York. The Banque de France, the French Banking Federation, around 15 large banking groups and institutions, market infrastructures and representatives from the Ministry of the Economy, Industry and Employment took part in this exercise, which consisted in simulating a major operational crisis.

The security of means of payment and transfer systems

Implementation of major projects

The salient features of 2008 were the successful migration of TARGET2, the launch of TARGET2 Securities, and the first step towards the creation of a Single Euro Payments Area with the introduction of the SEPA credit transfer scheme.

• TARGET2

TARGET2 is the Eurosystem's settlement system for large-value payments. It was developed and is operated on behalf of the Eurosystem by the Banque de France – which supervised the entire project – together with the Deutsche Bundesbank and the Banca d'Italia. The different banking communities were

Key data for 2008

TARGET2-BDF:

- 27,200 daily transactions with a value of EUR 381.3 billion.
- 15% of TARGET2 traffic.

successfully migrated to TARGET2 in three successive stages (November 2007, February and May 2008). The French banking community was connected to TARGET2 on 18 February 2008. Despite the turmoil on financial markets and the sometimes very large volumes of activity (over 50,000 transactions settled in T2-Banque de France on 15 December 2008), the system has worked perfectly, recording an availability rate of 99.9%. The liquidity management tools made available to participants undoubtedly contributed to ensuring users' confidence in the system.

The Banque de France also developed and now manages the information and decision-support system of TARGET2 used by all participating central banks.

• TARGET2 Securities

The purpose of TARGET2 Securities is to facilitate the creation of a single financial market through the setting-up of a European platform for the settlement of securities transactions in central bank money. In 2008, the Eurosystem identified T2S user requirements, in close co-operation with stakeholders. On 17 July, the ECB Governing Council confirmed the launching of the project and entrusted the Banque de France, the Deutsche Bundesbank, the Banca d'Italia and the Banco de España with the task of developing the future platform. To this end, the four central banks defined and set up a transnational organisational framework with a view to delivering the T2S platform by 2013. Within this, the Banque de France was put in charge of the management of the project and functional co-ordination, and of the development of the settlement engine, a statistical database and the T2S archiving platform. So far, work has focused on defining the platform's general specifications in order to be able to communicate them to the market in early 2009. Furthermore, work on setting up the governance structure and pricing rules of the future platform continued in 2008.

• **SEPA (Single Euro Payments Area)**

In 2008, the European harmonisation of cashless payments in the framework of the SEPA project entered a new phase with the introduction of the SEPA credit transfer scheme on 28 January 2008 and the implementation of interoperability principles by the card payment systems. In December 2008, SEPA credit transfers accounted for 1.8% of all transfers in Europe.

The Banque de France participates actively in steering France's migration to SEPA within the National SEPA Committee that it chairs jointly with the *Fédération bancaire française* (French Banking Federation). On 25 November, this committee published the first report on France's migration to SEPA.⁷ In addition, the Banque de France was closely involved in drawing up a harmonised legal framework facilitating the use of SEPA payment instruments and transposing the Payment Services Directive, which is expected to come into force on 1 November 2009.

Oversight of means of payment

The progress of European integration has serious implications for the framework for oversight activities. In January 2008, the Eurosystem published an Oversight Framework for Card Payment Schemes – Standards.⁸ Benefiting from its experience at the national level, the Banque de France took part in its preparation. This framework has become a common benchmark for Eurosystem central banks for conducting their oversight activities and therefore ensures equal treatment for all card payment systems across Europe. In 2008, an assessment of these systems was launched; the Banque de France is working together with other central banks with regard to the international systems and alone with regard to the French systems. Security standards for the other types of European-wide payment instruments are also being defined.

In 2008, the Banque de France also pursued its efforts to strengthen the security of online banking services and online card payments, which are growing strongly and are expected to grow further as SEPA payment instruments become increasingly widespread. The Bank noted with satisfaction that a number

of solutions designed to enhance authentication (e.g. single use access codes generated via card readers or sent by SMS) are available and are starting to be used by French banks.

Lastly, as the previous years, the Banque de France analysed the quantitative and qualitative data communicated by payment instrument issuers and operators in order to assess the extent to which they meet the security objectives it previously defined.

Oversight of transfer systems and market infrastructures

Despite the size of the shocks and the sometimes very large volumes of activity – both being the result of the financial crisis – the transfer systems on the Paris market continued to function well. This situation is largely due to the improvements that have been made to their organisation in recent years which have significantly contributed to their resilience. The crisis has helped market participants become fully aware of the significance and scale of the interdependencies between transfer systems, as well as between the latter and financial players. These interdependencies were identified in a report⁹ of the Committee on Payment and Settlement Systems of the BIS drawn up by a working group chaired by the Banque de France.

At the European and international level, the Banque de France took part in adapting oversight standards and frameworks. In particular, it chaired a working group of the Committee on Payment and Settlement Systems of the BIS in charge of drawing up an up-to-date and common methodology for implementing the different sets of standards.

In 2008, the Banque de France monitored and assessed the new transfer systems. In France, the clearing system for retail payments CORE became operational in January 2008, in order to process the new SEPA credit transfers. The Banque de France made sure that national payment instruments within the previous SIT system (*Système interbancaire de télécompensation*) were properly migrated to CORE between June and October 2008. It also oversaw the establishment of a protection mechanism against settlement risk, which will enable settlements to be made even if

⁷ Available on the National SEPA Committee website <http://www.sepafrance.fr/fr/content/le-rapport-annuel-de-migration-de-la-france-%C3%A0-sepa>.

⁸ Available on the ECB website: <http://www.ecb.int/press/pr/date/2008/html/pr080111.en.html>.

⁹ "Interdependencies of payment and settlement systems", June 2008, available on the BIS website at: <http://www.bis.org/publ/cpss84.htm>.

the participant with the largest settlement obligation fails. This mechanism is expected to be operational in early 2009. The Banque de France also took part, within the framework of the Eurosystem, in monitoring the actions taken by TARGET2 operators regarding the items identified as requiring particular attention in the 2007 assessment. This assessment had concluded that the system was fully compliant with the core principles for systemically important payment systems.

2|2|4 The other tasks specific to the Banque de France

Services to public administrations

Tasks carried out in the context of relations with public administrations

- *Services to private 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 2008

- *Over 15,000 technical opinions delivered by Banque de France commissions for monitoring and granting assistance to companies.*
- *The Banque de France contributed to the work of local economic bodies by taking part in around 3,000 meetings, including 750 devoted to the new credit mediation activity.*
- *At 31 December 2008, 56 partnership agreements had been signed with regional and local authorities in order to facilitate the marketing of economic and financial assessments of companies (GEODE) and 326 assessments were carried out within this framework.*
- *28 ACSEL (Localised Cyclical and Structural Economic Analysis) analyses were conducted.*

The Public Service Contract signed between the Banque de France and the State covers a large range of the tasks carried out by the Bank that do not lie within the remit of the European System of Central Banks.

Data on non-financial corporations

The Companies Directorate is in charge of assessing companies' financial situation on the one hand, and monitoring economic developments and labour pools in the regions on the other.

Given the deterioration in the economic climate, the Companies Directorate had to collect a greater amount of data than usual (companies' accounting records, bank outstandings, notification of non-payment of bills, information from the court registries, etc.) in order to help the Bank improve and continuously update its assessment of the business environment and provide the public authorities with specific information meeting their requirements. Every month, a summary table of bank outstandings broken down by business category is drawn up and sent to the Ministry of the Economy, Finance and Employment. A similar document, highlighting local features, is also sent to the regional directors of the Banque de France in order to supplement the data already at their disposal for monitoring economic developments in their region. These data on credit outstandings are complemented by sectoral data on failures and payment incidents.

The economic context also gave rise to increased efforts to integrate qualitative data (environment, strategy, etc.) into the rating process by specifying the procedures and implementing different frameworks for qualitative analysis, which supplement the data drawn from the financial analysis. At the same time, the methodology for taking account of payment incidents in the rating process was refined. This resulted, all other things being equal, in a smaller number of unfavourable ratings at end-2008.

When the range of eligible assets for Eurosystem monetary policy operations was widened in October, the volume of transferable private claims immediately increased, in the form of a broadening of the group of companies that receive such bank loans.

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 2008

- Over 5 million entities listed in FIBEN.
- 240,000 companies rated on the basis of tax or consolidated statements (4,000 groups).
- Almost 45,000 meetings with company managers.

This group, which, up until then, only included companies classified under the first three rating levels (rating 3), was extended to include companies with a lower rating owing to their less favourable financial position (rating 4+). The Banque de France's rating system was thus one of the levers used to facilitate banks' access to refinancing from the Eurosystem and, as a result, to the financing needed for their lending activities.

At the same time, according to the law on the modernisation of the economy, intercompany trade credit periods are expected to be reduced as from 1 January 2009. The Trade Credit Observatory, the secretariat of which is provided by the Companies Directorate, used the individual company data that it records in order to assess the impact of the implementation of such a reform. These data were also presented in the Annual Report of the Trade Credit Observatory and used to study the derogation requests submitted by some economic sectors to the French Competition Authority.

In addition, in 2008 the Companies Directorate contributed to the Bank's commitment to sustainable development. It took a major step forward in the rationalisation process of its information systems: it developed an IT project for dematerialising the collection of companies' accounting records, which is expected to be implemented at end-2009.

The management of the Treasury's account and of payment means on behalf of the Treasury

The new account-keeping application EVCLI entered the production phase on 3 December 2007. In 2008, the Internet client interface (BDF Direct) was only made available to the Agence France Trésor. Treasury accountants shall be able to consult their accounts and take orders in 2009.

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 2008

Transactions performed on behalf of the State:

- 174 million cheques collected,
- 307 million direct debits presented,
- 252 million credit transfers initiated.



Credit mediation: seminar with René Ricol, Henri Jullien and the departmental mediators held on 2 January 2009

Services provided in the area of relations between private agents and the financial sphere

National payment incident databases

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 private individuals 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;
- 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 2008

- 65.7 million consultations of the FCC.
- 2.4 million individuals registered in the FICP.
- 161.5 million consultations of the FNCI.

Overindebtedness and access to banking services

In 2008, the Banque de France published the results of a survey showing the typology of overindebted households and the main procedures for processing cases of overindebtedness by the household debt

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:

- it has provided the secretariat for the household debt commissions since the creation of the mechanism for dealing with situations of overindebtedness;
- 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 Microfinance, created in September 2006, and contributes to the analysis and development of its practices.



Meeting in Caen on 28 January 2009

Key data for 2008

- 188,500 cases submitted to the household debt commissions.
- 32,000 applications for access to banking services.

commissions. This study included for the first time information on persons involved in a personal recovery procedure. It was produced within the framework of the Public Service Contract signed between the Banque de France and the State, like the quarterly overindebtedness barometer. This barometer is a summary table made up of a set of representative indicators and is drawn up within the framework of a consultation process conducted in collaboration with the *Comité consultatif du secteur financier*.

In addition, a new function for the automatic input of data into the National Register of Household Credit Repayment Incidents (FICP) was added to the IT application for processing cases of overindebtedness, which was implemented throughout the Banque de France's branch network in 2007.

In 2008, the number of applications to the household debt commissions was up by 3% on the

previous year. The average processing time of the out-of-court settlement phase by the household debt commissions' administration stood at 3.4 months at end-2008, which goes beyond the commitment set out in the Public Service Contract (4 months).

The procedures for obtaining access to banking services, which enable natural or legal persons without a bank account to open one, were enhanced, in accordance with the law on the modernisation of the economy.

Services to regional and local authorities and public economic bodies and administrations

One of the most salient features of 2008 was the creation of a credit mediation mechanism, which came into force in early November. Under this new framework, the directors of the Bank's departmental branches have the status of departmental credit mediators.

In 2008, the Banque de France also examined the financial situation of around 3,500 companies. This task derives more or less directly from the Public Service Contract, which, in Article 2 on the monitoring of local economic developments, refers to the Bank's participation in the procedures for examining companies' financial difficulties.



Press conference by Christian Noyer
on 24 January 2008

GOVERNANCE, HUMAN RESOURCES AND FINANCIAL MANAGEMENT

I | Governance

I | I | Executives bodies

I | 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 independence of the Banque de France, as a member of the European System of Central Banks (ESCB), implies the independence of the Governor, who is a member of the Governing Council of the European Central Bank (ECB), and of the Deputy Governors. In accordance with Article L.141-1 of the *Monetary and Financial Code*, the Banque de France, represented by its Governor and Deputy Governors, 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.

The Governor chairs the Executive Committee, which is composed of the heads of the business areas, and the Careers Committee, which gives its opinion on the appointment of the Bank's senior executives.

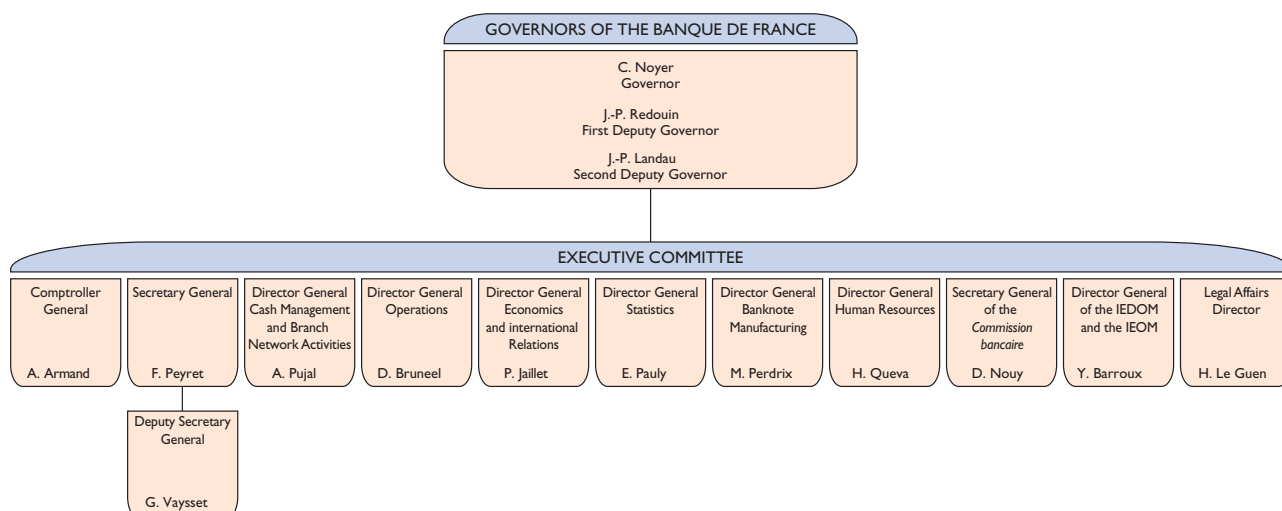
The Governor is also Chairman of the *Commission bancaire*, the Credit Institutions and Investment Firms Committee (*Comité des établissements de crédit et des entreprises d'investissement*), the Banking Mediation Committee and the Observatory for Payment Card Security. In 2008, under the law on the modernisation of the economy (LME) he was entrusted with the position of Chair of the Observatory for Regulated Savings.

I | I | 2 | 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 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, is made up of the Deputy Governors, the Directors General, and the Deputy Secretary General for Strategy and the Legal Affairs Director. With a view to increasing integration with the Bank, the Director General of the French overseas departments note-issuing bank (*Institut d'émission des départements d'outre-mer - IEDOM*) and the French overseas note-issuing bank (*Institut d'émission d'outre-mer - IEOM*) is also a member of the Executive Committee.

The management bodies of the Banque de France





1st row (left to right)

Hervé Queva, Director General of Human Resources; **Danièle Nouy**, Secretary General of the Commission bancaire; **Jean-Paul Redouin**, first Deputy Governor; **Christian Noyer**, Governor; **Jean-Pierre Landau**, second Deputy Governor; **Élisabeth Pauly**, Director General Statistics; **Frédéric Peyret**, Secretary General

2nd row (left to right)

Gilles Yaysset, Deputy Secretary General; **Didier Bruneel**, Director General Operations; **Pierre Jaillet**, Director General Economics and International Relations; **Alain Armand**, Comptroller General; **Armand Pujal**, Director General Cash Management and Branch Network Activities; **Michel Perdrix**, Director General Banknote Manufacturing; **Hervé Le Guen**, Legal Affairs Director
(Yves Barroux, Director General of the IEDOM and the IEOM, does not appear in this photograph as he was on an assignment when it was taken)

The Executive Committee

The Executive 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 directly concerned. It may meet as a Careers Committee to express an opinion on the appointment of Head Office managers and regional managers.

1|1|3 Operational management bodies

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, which is chaired by the Governor, advises the latter on the Bank's portfolio investment strategy (for both euro —and foreign—

currency denominated portfolios). In particular, it issues opinions on the volume of investment, its allocation by asset type 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 maintains 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, which is responsible for defining the Bank's short and medium-term policy with respect

to IT investment, and the Real Estate Investment Committee, which is in charge of managing the Bank's real estate assets.

1|1|4 The College of regional managers and the branch network

The Banque de France network (see map in Appendix) currently has 96 *département* branches (of which 22 regional head offices), associated to which are 21 economic centres and 7 household debt centres. The services related to cash in circulation are undertaken in 71 of these establishments and in 4 specialised centres.

In order to ensure that the requirements of the users of public services provided by the Bank are met (household debt, access to payment incident databases and the right to basic banking services), and in accordance with the Public Service Contract concluded with the Government, 85 customer service and information offices have been set up in towns where the Banque de France, after closing its branches during 2004-2006, retains neither an economic centre nor a centre for processing applications to the household debt commission. These non-permanent offices are located on the premises of other administrative bodies, such as town halls or *sous-préfectures*.

The organisation of the Banque de France's branch network now functions at two levels:

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

Regional managers are responsible for fostering initiatives and promoting good practices in all operational fields. They are also in charge of allocating budget resources within the branch network, using

financial control instruments and the various initiatives relating to risk monitoring and control. Regional managers are assisted by centres of expertise and a specific structure in charge of supervising operations and procedures, i.e. the regional risk monitoring and control division.

In view of their responsibilities, the regional managers are the prime contacts of the Governors and Head Office managers of the Banque de France for any questions relating to the branch network. The College of Regional Managers, chaired by the Director General Cash Management and Branch Network Activities, and his Deputy responsible for the branch network, has meeting every two months, which are also attended by the five regional inspectors.

1|2 Decision-making and control bodies

1|2|1 The General Council

Pursuant to Article L.142.3 of the *Monetary and Financial Code*, 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, Industry and Employment and a representative elected by Banque de France staff. A Censor, or his/her alternate, appointed by the Minister of the Economy, Industry and Employment, 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 performs the main functions of an executive board at the Banque de France. It deals with issues relating to the management of activities that are not within the remit of the ESCB. 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.



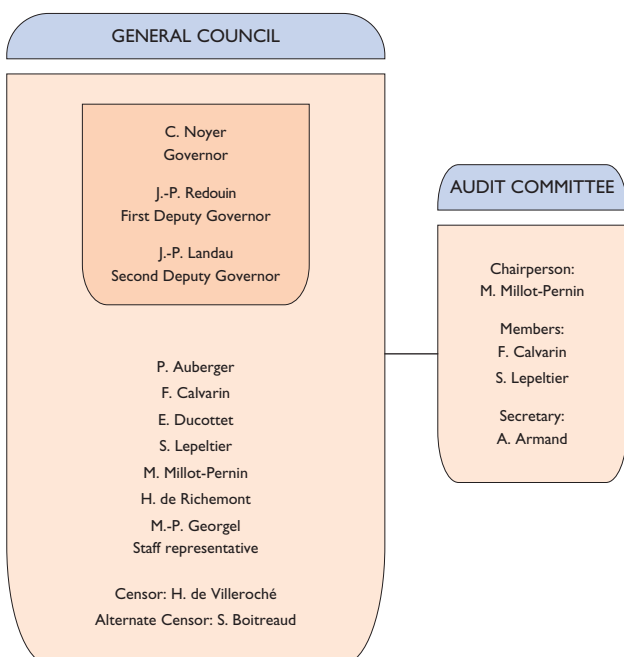
1st row (left to right)

Monique Millot-Pernin; Jean-Paul Redouin; Christian Noyer; Jean-Pierre Landau; Élisabeth Ducottet

2nd row (left to right)

Henri de Richemont; Marie-Paule Georgel; Philippe Auberger; Serge Lepeltier; François Calvarin; Hervé de Villeroché

The General Council



It also draws up the Bank's expenditure estimates and annual accounts and makes proposals for the allocation of profits and the State's share of the dividends.

In accordance with the above-mentioned principles, the General Council is responsible in particular 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 major projects underway. It also scrutinises the draft report on the implementation of the *Public Service Contract*.

In the framework of the State reform and taking into consideration the distribution of powers between the ECB and the national central banks, the law on the modernisation of the economy of 4 August 2008 abolished the Monetary Committee of the General Council. Furthermore, the law changed the General Council's budgetary responsibilities. The General Council must now provide the Banque de France

with the necessary means to perform the tasks with which it has been entrusted arising from its participation in the ESCB. As is the case for the Bank's Governors, the members of the General Council other than the Governor and the Deputy Governors are independent: Article L.142-3 stipulates that the General Council shall ensure that the professional activities performed by their members comply with the principle of independence of the Banque de France.

1|2|2 Audit Committee

The Banque de France Audit Committee was set up by virtue of the decision of the General Council of 22 October 2004. 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. As a result of the laws of 20 February 2007 and 4 August 2008, changing the Bank's governing authorities, the Committee's composition was reviewed at the beginning of 2009. The responsibilities and operating rules of the Audit Committee, specified in a charter appended to the General Council decision, were revised at the same time.

In accordance with Directive 2006/43/EC of 17 May 2006, the Audit Committee is charged with informing the General Council on issues relating to financial reporting, external and internal auditing, internal control and risk management. In all these fields, the Audit Committee may hear any member of Banque de France management or auditors.

The Audit Committee met three times in 2008. Its work focused mainly on the following:

- with regard to financial reporting, the Bank's auditors presented their report to the members of the Committee on the closing of the 2007 annual accounts;
- with regard to internal auditing, the Committee took note of the main conclusions of the internal audit and the progress report on the action plans drawn up by the audited units and has examined the audit programme for 2009, for which it has given its approval;

- lastly, in respect of internal auditing and risk control, the Committee examined the development in the operational risk management system and has took of its main findings. In this area, the Committee also examined the market and credit risk control system.

1|3 Risk control and internal audit

1|3|1 Internal audit

The internal audit has competence over 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 therefore structured accordingly. The internal audit implements its annual work programme using a risk-based approach with a view to, in accordance with the terms in its charter, ensuring the quality of management, risk control and internal audit processes. It also oversees the implementation of corporate social responsibility within the bank. 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 (IIA) serve as a reference both with regard to the organisation and the conduct of audit missions; in 2008, an independent external evaluator (the IFACI, the French equivalent of the IIA) conducted an assessment to ensure that the organisation and practices of the Bank's internal audit comply with all the standards.

The work of the internal audit is also in line with the framework of the ESCB. The Comptroller General, the Director of the Head Office Audit and his Deputy are permanent members of the ESCB Internal Auditors Committee (IAC) that meets regularly 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 the audit missions. In 2008, the Banque de France chaired one of the task forces set up within the IAC to guide the auditing on the subject of "Monetary policy and market operations". The conclusions of the IAC task forces are submitted to the Audit Committee and to the ECB 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 (BIS). They also participate in benchmarking exercises aimed at identifying best professional practices. Furthermore, a large number of delegations of internal auditors from issuing banks in developing countries attend training sessions in Paris, while Banque de France inspectors conduct on-site technical assistance missions abroad.

Lastly, on 12 and 13 June 2008, the Bank hosted its first conference of internal audit managers from central banks of French-speaking countries, chaired by the Comptroller General, assembling around 20 Internal Audit Managers. The work notably focused on general issues relating to the role of the audit function in the governance of central banks as well as more specific questions and the internal auditing process itself.

1|3|2 Risk Prevention

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

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

The organisation works as follows:

- in each Directorate General, risk managers are in charge of updating the mapping of operational risks and assisting in the implementation of risk-reduction action plans; in addition, in each regional branch, a risk management and control unit is responsible for ensuring that the control mechanisms are properly implemented in the branch network;
- within the Risk Prevention Directorate, attached to the Comptroller General, a special unit is in

charge of providing assessments, co-ordinating and reporting to the Bank's authorities, while another unit is responsible for information security;¹

- the Internal Control Co-ordination Committee (3CI), which meets twice yearly, comprises the Directors General, the Legal Affairs and Audit Directors and risk managers, and is chaired by the Comptroller General. It is charged with supervising work aimed at enhancing risk control in all of the Banque de France's fields of activity;
- every year, the report on risk analysis and the action plans based on an updated general risk map are presented to the Executive Committee.

Two events marked 2008: in May, the Banque de France hosted the annual conference of the International Operational Risk Working Group (IORWG), which assembles the risk control managers of central banks and banking supervisory authorities worldwide. Furthermore, in November, the ECB Governing Council validated the overall risk management methodological framework applicable to all of the Eurosystem-related NCB activities, a project in which the Banque de France played a significant role. The Council of Governors appointed a Bank representative to chair the working group mandated to implement this common methodological framework within the ESCB's various Committees, for the first year of its implementation.

2| Human resources management

2|1 Staff levels

2|1|1 Total staff

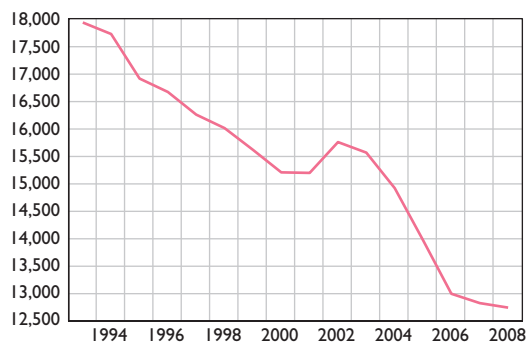
At 31 December 2008, the Banque de France employed a total of 12,746 full-time equivalent staff, down by 0.6% on the previous year.² Between 1993 and 2008, staff numbers fell by 28.9%.

¹ In the area of information security, the new risk management method was applied in 2008 to all new computer applications.

² The table on total staff levels is provided in the Appendix.

Chart 30 Total number of staff

(full-time equivalent positions at 31 December)



While the statutory staff can be broken down almost equally between men and women, this is not the case in all hierarchical categories, particularly among the managerial staff. Among contract staff, the large share of men is attributable to the overriding proportion of men among the security personnel.

Statutory employees are mainly in the 30-49 age bracket, with the average age standing at 46.7 in 2008.

Some 43% of staff members work at the Head Office, 49% in the branch network and 8% in banknote manufacturing.

Chart 31 Male/female breakdown of total staff

(full-time equivalent positions at 31 December)

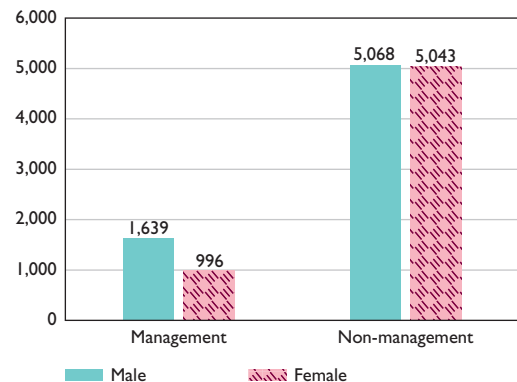
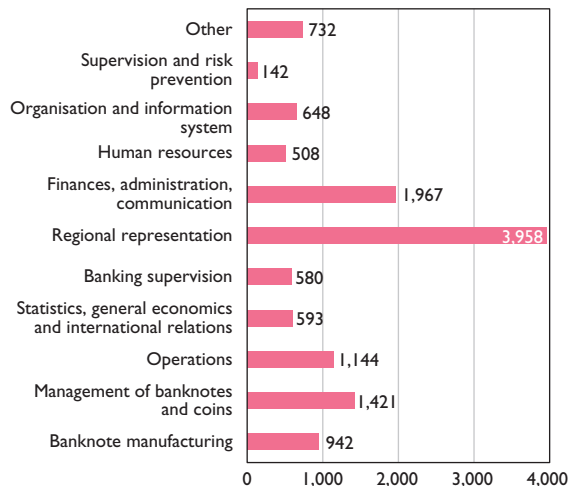


Chart 32 Average number of staff by field of activity

(full-time equivalent positions)



2|1|2 Secondments and temporary assignments of Banque de France staff with external organisations

In 2008 the Bank pursued its policy of seconding and assigning staff to external organisations. At end-2008, staff secondments and assignments were as follows:

- 58 members of the Bank's staff to various French organisations, including the Autorité des marchés financiers (AMF –Financial Markets Authority) and several ministries;
- 84 members of the Bank's staff to European institutions, international organisations and embassies, and in particular to the European Central Bank (35 staff members), the International Monetary Fund (IMF) and the Bank for International Settlements (BIS).

2|2 Skills development and prospects in terms of new positions

2|2|1 Reform of the internal promotion system

A new framework for internal promotion enabling staff to develop their career within the Bank without taking internal competitions has been



defined. This framework aims to capitalise on staff members' professional experience and potential by offering professional development prospects throughout their career.

The framework consists of three steps: a selection based on aptitude tests and an interview with a panel, attribution of a new associated with occupational mobility and assessment of the employee's performance in the new position.

2|2|2 Development of professionalism

The development of professionalism and skills is a priority for the Bank. To this end, 35 professional development paths corresponding to specific functions or certification paths have been established. Furthermore, training programmes for the development of managerial, relational and behavioural skills have been significantly reformed.

2|2|3 Manpower and skills planning

In 2008, a grid was established to match job types to functions in the manpower and skills planning framework. This grid will be updated periodically. The approach notably consists in conducting, for collective purposes, forward-looking analyses of developments in terms of manpower and skills requirements, and implementing action plans aimed at ensuring a more appropriate match between future activities, the skills employed and the distribution of staff between the various functions.

Furthermore, an Observatory for manpower and skills was set up and entrusted, in particular, with defining the principles and procedures for collecting and analysing information on manpower and

skills, anticipating the consequences of internal developments and contributing to the validation of professional experience and training.

2|3 Corporate social responsibility activities

2|3|1 Psychosocial risk factors

The Bank's approach is placed within the context of the national interprofessional agreement on stress in the workplace, which aims to detect, anticipate and prevent problems related to *stress*.

The prevention of psychosocial risk is one of the main focuses of the *Observatoire paritaire des risques de santé au travail* (Joint Observatory for Health Risks in the Workplace) set up in 2006.

Several actions have been carried out in this area. In particular, a hotline has been set up to support staff members, 24 hours a day 7 days a week. In the event of persistent difficulties in a particular unit, a work and organisational psychologist intervenes, and following events of a traumatic nature, psychological support in crisis management is provided.

Furthermore, psychosocial risk has been analysed with a view to establishing a management and prevention policy.

2|3|2 Implementing a "social barometer"

An annual survey or "social barometer", carried out by a survey company, was set up to measure developments in the staff's perception of the areas affecting the



Bank's image, working conditions and management, human resources management, communication and lastly, developments in the Bank's strategy. The results of the first survey were distributed to Bank staff.

In general, the results concerning the Bank's image, and the overall satisfaction and pride of working for the Bank were positive. In particular, working conditions and management were judged to be positive, with the prevailing sentiment that skills are used well. However, the survey reveals that there are concerns regarding professional development prospects.

In order to draw some lessons from this survey, the methods of presentation to the staff of the strategy and priorities for 2009 were revised, giving a more extensive role to management in this area.

2|3|3 Draft corporate agreements on disabilities and gender equality within the workplace

Seven successive corporate agreements testify to the Bank's long-standing commitment to people with disabilities in the workplace. Negotiations over a draft corporate agreement for the 2009-2011 period aim to pursue the recruitment of people with disabilities for everyday positions, implement the framework or measures necessary to compensate for disabilities and maintain people with disabilities in their jobs, raise awareness in the units that they join, involve the supervisory staff in the integration process and increase the recourse to firms employing disabled persons.

A taskforce has been set up to apply the Bank's policy in this area and make sure that the corporate agreement is implemented; it also has the cross-disciplinary role of examining this issue and proposing solutions.

Moreover, in 2008, the Bank entered into negotiations with a view to signing an agreement concerning gender equality in the workplace. This is not a new issue at the Bank. A framework was thus established to promote gender equality, notably based on recruitment by competitive examinations, the duration of leave related to the birth or adoption of children, and the choice to work part time. Furthermore, the Bank set up a working group in 2004 to discuss, on the basis of the annual report, comparisons between the situation of men and women and gender equality implementation conditions at the Bank, and propose measures in order to improve specific situations.

However, the Bank plans to extend this action and define in an agreement the principles and actions that will help to improve equality throughout employees' careers. This agreement is a step towards obtaining the "Equality" label.

2|4 Developments in corporate social spending

New agreements have been proposed to the social fund managers, aiming to gradually redistribute the Bank's contributions to the various social activities by encouraging the assessment of the optimal use of these funds, based on rationalising fund and taking into consideration developments in staff members' needs. The bank has set an objective to reduce spending by EUR 15 million by the end of 2011. It is on the basis of this objective that the social expenditure budget has been allocated for 2009 by the General Council, following consultations between the unions and management.

The first results were obtained in 2008 with a significant reduction in staff members allocated to social organisations, the closure of co-ops and closure

and disposal plans for a number of insufficiently used holiday and sports centres. The savings amounted to almost EUR 5 million in 2008, compared with 2007 and further savings are expected in 2009.

3 | Financial management: analysis and results

Net profit for the year ended 31 December 2008 totalled EUR 2,460 million, up EUR 144 million on 2007. Profit before tax (which came to EUR 1,509 million) and exceptional items reached EUR 4,185 million, up 10% on 2007. This favourable result was mainly attributable to the increase in the Bank's financial income and to the moderate increase in operating costs in a context of extensive use of resources due to the financial crisis.

Two factors contributed to the rise in net income:

- the significant increase in dividends paid by the IEDOM (+ EUR 31 million) and above all by the European Central Bank (+ EUR 249 million), which had interrupted its dividend payment for three years in order to consolidate its provision for foreign exchange rate and interest rate risks;
- growth in earnings resulting from the development of activities with institutional customers, mainly foreign central banks that use Banque de France services for the investment of their foreign reserve assets.

Conversely, the financial crisis has depressed other earnings somewhat, which have nonetheless remained stable overall, in spite of the increase in the Bank's investment volumes.

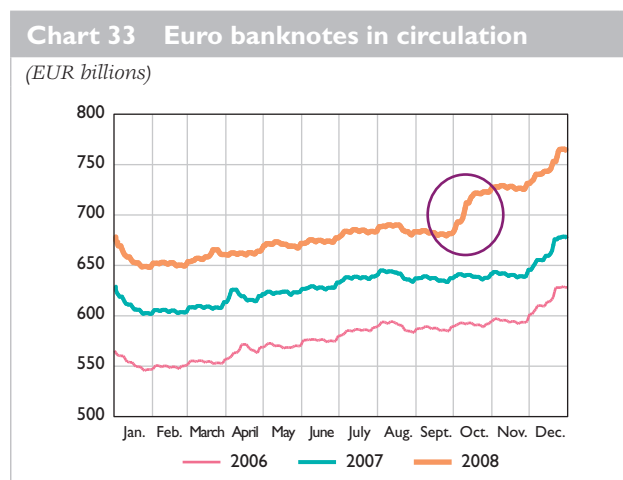
3 | I The financial crisis had a mixed impact on income

With the exception of the dividends and income from activities with institutional customers, the bulk of earnings in 2008 were from investments, in

the form of loans to credit institutions or securities portfolios, of income from banknote issuance. This monetary income stood at EUR 5,003 million in 2008, up by EUR 26 million compared with 2007. This small increase was mainly due to the relative stability in the average interest rates on the Bank's investments in 2008, since the interest rate cuts that followed the exacerbation of the financial crisis were not implemented until the end of the year. The intensification of the financial crisis in the fourth quarter also led to a sharp increase in the demand for banknotes and the money market almost came to a standstill, leading the Eurosystem central banks to significantly increase lending to credit institutions in order to support the financial sector and, consequently, the economy as a whole. This increased activity brought with it a rise in financial risks and had a mixed impact, although limited overall, on the Bank's income formation.

3 | I | I Increased demand for euro banknotes

Continuing the trends that had prevailed over previous years, euro banknote circulation increased at a fairly sustained rate during the first nine months of 2008. In October, the rate of circulation accelerated sharply in the wake of bank failures, with an upsurge in the total number of banknotes in circulation by almost EUR 50 billion during the month of October.



In accordance with the allocation mechanism defined within the Eurosystem, the Banque de France books as a liability its share in the total value of banknotes in circulation corresponding to its share in the ECB's capital key. The latter stood at EUR 148 billion at the end of 2008, up by EUR 16 billion year-on-year.

3|1|2 Increase in bank refinancing

The increase in currency in circulation led to a rise in the refinancing needs of the banking system. Since the euro area's money market is integrated, the growth in euro-denominated refinancing operations should be assessed at the Eurosystem level.

Net lending by the Eurosystem for the refinancing of euro area credit institutions thus increased sharply as of October 2008, standing at EUR 351 billion at the year end, thus offsetting the tightening impact of the rise in demand for banknotes on bank liquidity.

Moreover, the failure of Lehman Brothers and the ensuing fears of a contagion to other institutions in the United States and Europe triggered a major crisis of confidence in the entire global financial system as of October 2008. Credit institutions' wariness of lending to each other brought the interbank market to a standstill

Chart 34 Net bank refinancing and banknote circulation in euro at the Eurosystem level

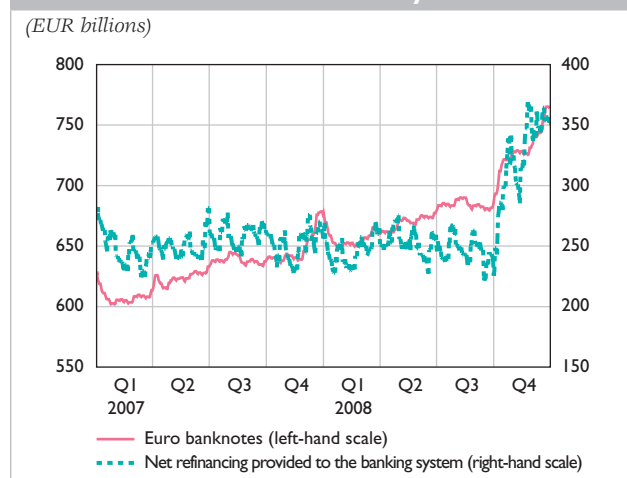
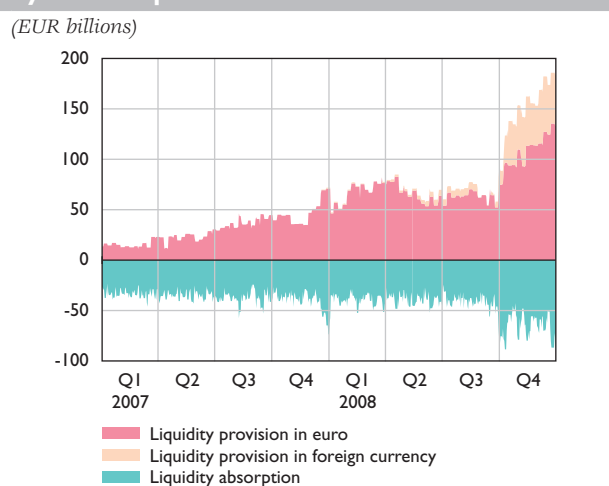


Chart 35 Liquidity provision or absorption by the Banque de France



—particularly in the euro area— obliging central banks to play a predominant role in the circulation of liquidity.

The daily record of bank refinancing by the Banque de France shows the magnitude and the suddenness of the crisis. Outstanding loans denominated in euro and foreign currency granted by the Banque de France to French credit institutions increased from EUR 72 billion to EUR 185 billion from one year-end to the next, whilst deposits with the Bank reached EUR 91 billion.

3|1|3 Stability of monetary income

In this context of rapid growth in the refinancing granted to the banking system, the income derived by the Banque de France from these operations remained paradoxically stable (EUR 3,308 million in 2008, versus EUR 3,264 million in 2007).

Three main factors offset the increase in volume of loans granted to credit institutions:

- the reduction in key interest rates coincided with the upsurge in loan outstandings (see chart below);
- the ECB reduced the spread between the Eurosystem's interest rate on deposits and the interest rate on

banking sector refinancing to zero, providing liquidity at a fixed-rate as of mid-October 2008, thus limiting the intermediation margin generated by the Eurosystem's central banks when credit institutions reinvested the excess liquidity that they had previously borrowed;

- lastly, five counterparties of three Eurosystem central banks that had undertaken refinancing operations defaulted. The risk of depreciation of securities lodged as collateral by defaulting counterparties (mainly illiquid structured securities) have led the Eurosystem's central banks to make an appropriate provision, in proportion to their share in the ECB's capital key, pursuant to Article 32.4 of the Statute of the ESCB. The size of the total provision amounted to EUR 5.7 billion and constituted an expense of EUR 1,184 million in the bank's 2008 accounts.

Furthermore, loans to credit institutions denominated in foreign currency, which have increased the volume of financial assets denominated in foreign currency on the Bank's balance sheet, were carried out for central banks issuing the currencies concerned and therefore the impact of these transactions on the Bank's profit and loss account was neutral.

Income related to holding foreign exchange reserves contracted very slightly (EUR 1,695 million, versus EUR 1,714 million in 2007), in a context where average returns fell slightly during the full year.

Lastly, the Banque de France continued with its gold sales, in the framework of the agreement reached between 15 European central banks, selling 103 tonnes in 2008, generating a capital gain of EUR 1,226 million, transferred to the revaluation reserve in accordance with the agreement on the management of foreign exchange reserves signed between the State and the Banque de France. In total, since the beginning of the programme of sales initiated in 2004, 516 tonnes of gold have been sold for EUR 7.8 billion, increasing the volume of the Bank's interest-bearing investments and contributing to raising its financial income.

3 | 2 Continuing efforts to modernise the Bank

The improvement in the Bank's results also reflects the impact of the structural reforms that have been implemented over the past few years.

The reform of the Banque de France's regional branch network and improvements in the industrial processes used in banknote manufacturing have helped to reduce the Bank's operating costs. The number of full-time equivalent staff has been cut by around 2,900 in 5 years, constituting a reduction of 18%.

This has resulted in a steady reduction in the Bank's break-even point, i.e. the minimum return on assets necessary to cover expenses, which has decreased by 170 basis points since 2003, dropping from 2.77% to 1.08% in 2008.

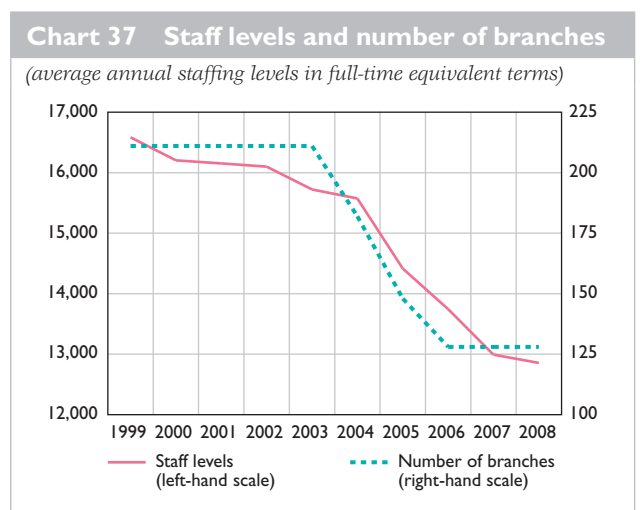
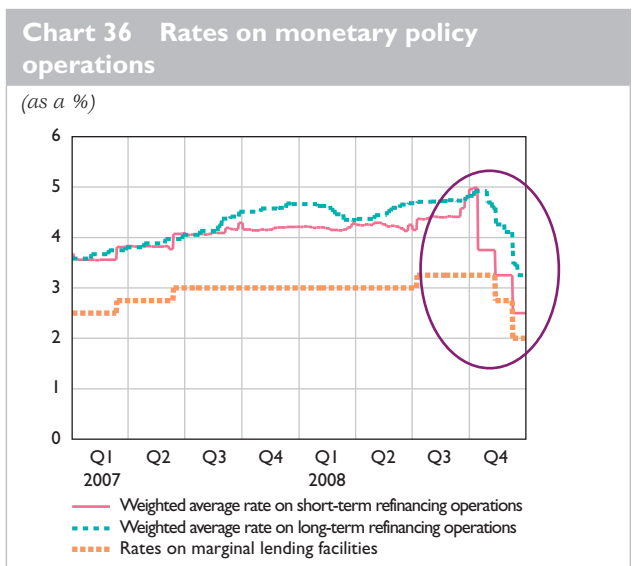
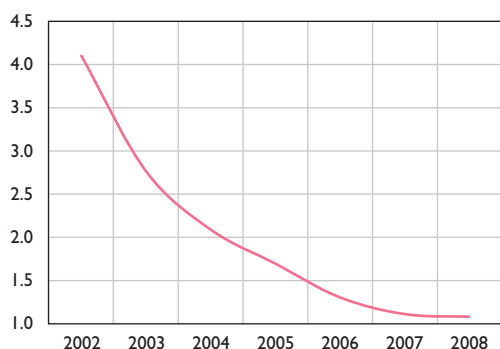


Chart 38 Developments in the Banks' break-even point

(as a %)



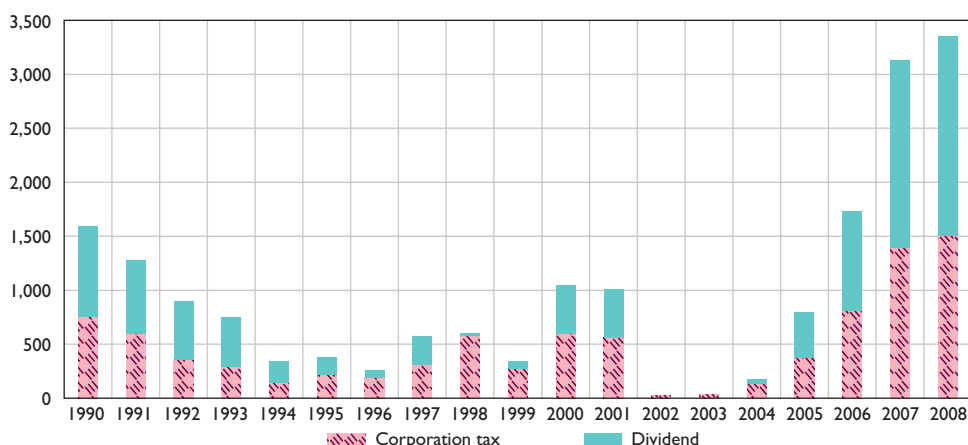
Furthermore, the Bank has strengthened its financial position by continuing to increase provisioning for social purposes for both working employees and retirees and allocating its fund for general risks given its exposure to the increase in financial risks.

During its session on 10 April 2009, the General Council agreed to pay a dividend of EUR 1,845 million to the State. Taking into account the corporate income tax charge amounting to EUR 1,509 million, payments to the State during 2008 totalled the exceptionally high amount of EUR 3,354 million.

Comprehensive information on the annual accounts is provided in the Appendix and preceded by the report on the Bank's assets, liabilities and results.

Chart 39 Payments to the State

(EUR millions)





Trading room
at the Banque de France

THE ACCOUNTS OF THE BANQUE DE FRANCE

I | Report on assets, liabilities and results

The accounts for the year ending 31 December 2008 were approved by the General Council at its meeting of 10 April 2009. The Bank's net profit stood at EUR 2,460 million, a moderate 6% increase compared with 2007. Against the backdrop of the financial crisis, which made substantial demands on the Bank's resources, this increase primarily reflects continuing efforts to modernise the institution and to control operating costs.

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

The Bank's financial position improved significantly from one year-end to the next as a result of the strong increase in net resources (up by EUR 40.4 billion).

This increase can primarily be attributed to the growth in banknotes in circulation and to the particularly large positions of banks and the French Treasury vis-à-vis the Bank against the backdrop of the virtual freezing of financial markets.

Financial position			
<i>(Year-end amounts, EUR millions)</i>			
	2008	2007 Pro forma	Change 2008/2007
Nets assets	192,769	152,390	40,380
Net sources of funds from banknote operations	142,502	127,167	15,335
Net bank refinancing	23,749	13,636	10,113
Net position with customers	17,772	4,683	13,090
Other	8,746	6,904	1,842
Net liabilities	192,769	152,390	40,380
Gold and net foreign exchange position	30,426	32,159	-1,733
Euro-denominated portfolios	77,857	44,301	33,557
Position with the Eurosystem	84,486	75,930	8,556

During the year ending 31 December 2008, the Bank increased its euro-denominated portfolios, which posted growth of EUR 33.6 billion from one year-end to the next.

I | I I Net resources from banknote operations

Net resources from banknote operations			
<i>(Year-end amounts, EUR millions)</i>			
	2008	2007	Change 2008/2007
Banque de France's share of banknotes in circulation	141,664	126,172	15,492
Banknotes put into circulation by the Banque de France	69,902	62,142	7,760
Banknotes put into circulation by the rest of the Eurosystem	74,960	66,710	8,250
Advance to the IEDOM	-3,198	-2,680	-519
French franc banknotes	838	995	-157
Net sources of funds from banknote operations	142,502	127,167	15,335

Euro banknotes

In 2008, the worsening financial crisis prompted an increase in demand for euro banknotes within the euro area but also in surrounding countries from October onwards. As a consequence, the amount of euro banknotes allocated to the Banque de France grew very strongly from one year-end to the next, rising by 12.2%, compared with a 7.7% increase during the previous year.

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 their subscription to the capital of the European Central Bank (ECB).

The difference between the share of euro banknotes allocated to the Banque de France and net issues of euro banknotes carried out by the Bank generates, on the assets side, a claim on the Eurosystem (balance sheet item A8.3). This claim bears interest at the marginal rate applied to the Eurosystem's main refinancing operations.

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. The amount of this advance corresponds to a percentage of France's euro banknote allocation, which since 1 July 2007 has been calculated according to the allocation mechanism in force within the Eurosystem. This advance is eliminated in the Banque de France/IEDOM combined accounts.

French franc banknotes

French franc legacy banknotes may still be exchanged at Banque de France branches during a period of 10 years. French franc banknotes that remain in circulation 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 838 million, a fall of EUR 157 million compared with end-2007, owing to notes handed in to the Banque de France and in particular to the repayment to the State of the balance of the Montesquieu FRF 200 banknotes that had not been returned to the Bank by the end of legal tender for these banknotes (March 2008).

1|1|2 Bank refinancing operations

This aggregate item groups together operations with credit institutions conducted in the context of monetary policy; operations carried out with banks as part of the Banque de France's activities with institutional customers are not included in it.

In response to the financial crisis, the action taken by Eurosystem central banks led the Banque de France to provide very substantial amounts of euro but also of foreign currencies to euro area credit institutions. Overall, euro and foreign exchange liquidity provision surged by nearly EUR 113.0 billion from one year-end to the next.

Loans in foreign currencies (USD, CHF) were made to euro area credit institutions on behalf of the central banks of the countries that issue these currencies

Bank refinancing

(Year-end amounts, EUR millions)

	2008	2007 Pro forma	Change 2008/2007
Assets	184,974	72,097	112,877
Net monetary policy operations	134,463	71,055	63,408
Foreign exchange lending to euro area institutions	50,511	1,042	49,469
Liabilities	208,723	85,733	122,990
Banks' current accounts	90,843	73,698	17,145
Net position of French credit institutions with the euro area	67,369	10,993	56,376
Counterpart of foreign exchange lending (debt with the ECB)	50,511	1,042	49,469
Net bank refinancing	23,749	13,636	10,113

and were fully backed by foreign exchange swap transactions with the ECB, which acts as intermediary with these central banks.¹ The impact of these transactions on the Bank's profit and loss account is neutral.

In parallel, net euro-denominated financing increased strongly (up by EUR 63.4 billion from one year-end to the next), well in excess of the net liquidity needs of French banks; this was accompanied by a sharp rise in the latter's net lending position vis-à-vis the euro area (up by EUR 56.4 billion from one year-end to the next) and by an increase in their current accounts on the Bank's books at year-end (up by EUR 17.1 billion).

1|1|3 Operations with institutional customers

Operations with institutional customers

(Year-end amounts, EUR millions)

	2008	2007 Pro forma	Change 2008/2007
Assets	105,643	67,084	38,559
Lending to the French Treasury (advance in respect of coins)	0	42	-42
Back-to-back investment of customer deposits (other than the French Treasury)	105,643	67,042	38,601
Liabilities	123,415	71,766	51,649
French Treasury current account	13,045	309	12,736
Customer deposits	110,370	71,457	38,913
Net position with customers	17,772	4,683	13,090

¹ The counterpart of these swap transactions constitutes a non-interest-bearing liability in euro vis-à-vis the ECB (see note 2 of the Notes to the annual accounts).

Operations with the French Treasury

The advance in respect of coins was fully repaid by the Treasury in 2008. However, the balance on the Treasury's account reached the exceptional amount of EUR 13.0 billion at year-end.

Other operations with institutional customers

The Banque de France provides non-euro area central banks with a range of services that, in particular, allow them to invest a proportion of their foreign reserves and to carry out foreign exchange transactions.

The Banque de France's volume of business conducted with institutional customers increased by EUR 38.9 billion from one year-end to the next.

Institutional customers' deposits and the back-to-back operations are recorded in dedicated accounts.²

Net gold and foreign exchange reserves decreased by EUR 1.7 billion from one year-end to the next, primarily as a result of exchange rate fluctuations.

Gold reserves

The Banque de France's gold reserves decreased by 103 tonnes and stood at 2,491 tonnes at year-end. Sales of gold were 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. Nevertheless, the value of the Bank's gold reserves increased by EUR 2.2 billion from one year-end to the next, with the sharp rise in gold prices (up by 9.4%) more than offsetting the reduction in the quantities held.

Following the entry into force of the second rider to the agreement between the State and the Bank of 29 December 2007, realised gains on sales of gold totalling EUR 1.2 billion were assigned to the revaluation reserve of State foreign exchange reserves. The gold revaluation account opened on 1 January 1999, which books unrealised capital gains from that date, stood at EUR 30.0 billion at year-end.

1|1|4 Gold and foreign exchange transactions

Gold and foreign exchange transactions			
<i>(Year-end amounts, EUR millions)</i>			
	2008	2007 Pro forma	Change 2008/2007
Assets	91,791	93,574	-1,783
Gold	49,802	47,557	2,245
Foreign exchange assets	39,666	44,569	-4,903
Relations with the IMF	2,323	1,448	875
Liabilities	61,365	61,416	-50
Foreign exchange liabilities	8,356	11,874	-3,519
Counterpart to SDR allocations	1,195	1,167	29
Revaluation accounts	31,318	26,971	4,348
Revaluation reserve of State gold reserves	18,499	18,499	0
Revaluation reserve of State foreign exchange reserves	1,996	2,904	-908
Total gold and foreign exchange	-30,426	-32,159	1,733

NB: Foreign exchange assets have been recalculated to neutralise foreign exchange liquidity loans, which have no effect on the Bank's profit and loss account. This provision of foreign exchange liquidity to euro area credit institutions by Eurosystem central banks³ is included in the bank refinancing aggregate item.

Foreign exchange assets and operations with the International Monetary Fund

Foreign exchange assets net of liabilities decreased by EUR 1.4 billion from one year-end to the next owing to exchange rate fluctuations and arbitrage transactions involving foreign exchange assets.

The claim on the IMF stood at EUR 2.3 billion (up by 60%). This rise stemmed from new lending granted by the IMF on the one hand, and the 3% appreciation in the exchange rate of Special Drawing Rights (SDRs) against the euro, on the other.

Currency arbitrage and reimbursements of SDRs generated EUR 308 million of net foreign exchange gains, taken to the revaluation reserve of State foreign exchange reserves. Unrealised losses were taken to the profit and loss account and covered by drawing on the revaluation reserve of State foreign exchange reserves.

² See note 28 of the Notes to the annual accounts.

³ See notes 2, 17 and 28 of the Notes to the annual accounts.

1|1|5 The Banque de France's euro-denominated portfolios

These comprise monetary portfolios and own funds investment portfolios.

Euro-denominated monetary portfolios⁴

The increase of EUR 32.9 billion in 2008 took place within the framework adopted by the Eurosystem in 2003, which allows NCBs to build up their portfolios within annually-reviewed limits.

Own funds investment portfolios

Euro-denominated portfolios			
<i>(Year-end amounts, EUR millions)</i>			
	2008	2007	Change 2008/2007
Euro-denominated monetary portfolios	73,250	40,364	32,885
Available-for-sale	16,812	14,503	2,309
Held-to-maturity	56,438	25,861	30,576
Own funds investment portfolio	4,608	3,936	671
Available-for-sale	2,428	1,638	791
Held-to-maturity	938	1,058	-119
Participating interests	1,241	1,241	0
<i>o/w ECB capital</i>	836	836	0
Euro-denominated securities	77,857	44,301	33,557

The increase in these portfolios, which stood at EUR 4.6 billion at end-December, reflects the expansion of own funds resulting from decisions regarding the appropriation of 2007 profits.

1|1|6 Net position with the Eurosystem

The Bank has several claims on the Eurosystem, notably:

- the claim reflecting the share of banknotes put into circulation by the rest of the Eurosystem that is allocated to the Banque de France under the allocation mechanism defined within the Eurosystem;

- the claim arising from gold (15%) and foreign exchange assets (85%) transferred to the ECB; it is denominated in euro and 85% of this claim bears interest, with the remaining non-interest-bearing 15% corresponding to the gold transfer. These claims are remunerated at the marginal rate applied to the Eurosystem's main refinancing operations.

The other claims on the Eurosystem consist of income receivable from the ECB in respect of the net pooling of monetary income (EUR 88 million in 2008 compared with EUR 49 million in 2007) and in respect of the payment by the ECB of a share of its seigniorage income (EUR 249 million in 2008).

Net position with the Eurosystem			
<i>(Year-end amounts, EUR millions)</i>			
	2008	2007	Change 2008/2007
Claim on the Eurosystem for banknotes in circulation	75,572	67,312	8,260
Claim on the ECB for gold and foreign exchange assets transferred	8,577	8,569	8
Other claims on the Eurosystem	337	49	288
Net position with the Eurosystem	-84,486	-75,930	-8,556

1|1|7 Other transactions

Other items			
<i>(Year-end amounts, EUR millions)</i>			
	2008	2007	Change 2008/2007
Capital, reserves and retained earnings	3,820	3,367	453
Provisions for liabilities and charges	1,984	675	1,309
Fund for general risks	870	670	200
Fixed assets	-890	-896	6
Other liabilities	502	771	-269
Net profit for the year	2,460	2,317	143
Total	8,746	6,904	1,842

The net balance on other transactions was EUR 8.7 billion, constituting an increase of EUR 1.8 billion from one year-end to the next.

⁴ From an accounting standpoint, this aggregate item comprises balance sheet item A7 "Euro-denominated fixed-income securities" and the portion of A4 "Euro-denominated claims on non-euro area residents" consisting of securities issued by non-euro area entities. 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.

This rise can be attributed to the increase in reserves appropriated from 2007 net profit and, above all, the establishment in 2008 of a provision amounting to EUR 1,184 million designed to cover the share borne by the Banque de France of risks arising from monetary policy operations conducted by the Eurosystem with five defaulting counterparties.

I | 2 Breakdown of profit

Net profit for 2008 amounted to EUR 2,460 million, up by EUR 144 million on 2007.

I | 2 | 1 Net income from activities

The rise in net income from Banque de France activities, which stood at EUR 6,195 million in 2008, is mainly attributable to the increase in non-monetary income from euro transactions and the interim distribution of EUR 249 million in respect of the ECB's seigniorage income. Monetary income from euro and foreign exchange transactions remained at high levels and varied little, with the interest rates only falling at the end of the year.

Net monetary income from euro transactions

Net monetary income from euro transactions is the largest component of income for the Banque de France. It represents the excess of income derived from euro monetary transactions (refinancing of the banking system, securities portfolios, sharing of Eurosystem monetary income) over the interest paid on deposits from credit institutions (minimum reserves and deposit facilities). This income⁵ includes the net result of the pooling of the Eurosystem's monetary income and the interest on intra-ESCB balances corresponding to adjustments to banknotes in circulation.

The intensification of the financial crisis led the Eurosystem to step up activity with a view to supporting the financial sector and, at the same time, resulted in an increase in the former's financial risk profile. In autumn 2008, five counterparties of three Eurosystem central banks (Deutsche

Net income from activities

(Year-end amounts, EUR millions)

	2008	2007	Change 2008/2007
Net income on activities of the Banque de France	6,195	5,644	551
Euro monetary income	3,308	3,264	44
Income from refinancing of the banking system	712	1,187	-475
Pooling of monetary income	2,819	2,272	547
Provision for risk on monetary policy operations	-1,184		-1,184
Income from available-for-sale and held-to-maturity portfolios	2,476	1,096	1,380
Interest on claims arising on transfer of reserve assets to the ECB	289	281	8
Interest paid on minimum reserves	-1,632	-1,414	-218
Other interest-bearing accounts	-172	-159	-13
Foreign currency monetary income	1,695	1,714	-19
ECB and IEDOM dividends	330	50	280
Net profit from non-monetary activities	862	616	246

Bundesbank, Banque centrale du Luxembourg and De Nederlandsche Bank) defaulted on refinancing operations. These counterparties had submitted eligible collateral mainly consisting of asset backed securities (ABS) whose liquidity became limited due to the exceptional market conditions prevailing at that time. The Governing Council of the ECB decided that any shortfall, if it were to materialise, should eventually be shared in full by the Eurosystem NCBs in accordance with Article 32.4 of the Statute of the ESCB, in proportion to the prevailing ECB capital key shares of these NCBs in 2008. The Governing Council also decided, as a matter of prudence, that the NCBs should establish their respective shares of an appropriate total provision in their annual accounts for 2008 as a buffer against risks arising from the monetary policy operations conducted with the counterparties mentioned above. The size of the total provision amounts to EUR 5.7 billion, with EUR 1,184 million attributed to the Banque de France.

This provision for risks arising from monetary policy operations offset the EUR 1.2 billion-rise in net monetary income from euro transactions.

⁵ 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 88 million in 2008, an increase of EUR 49 million relative to 2007.

The latter resulted from the increase in the volume of the Bank's interest-bearing investments in a context where interest rates, despite falling very sharply in the fourth quarter of 2008, remained very high overall over the course of the year. The interest rate on the main refinancing operations remained on average in 2008 slightly higher than that observed in 2007 (4.01% compared with 3.94%).

Net monetary income from foreign exchange transactions

Foreign currency portfolios financed by monetary liabilities generated, in 2008, a profit of EUR 1,695 million, down EUR 19 million on the previous year. This decline can chiefly be ascribed to the lower return on these assets at the end of the year.

ECB and IEDOM dividends

Unlike the three previous years in which the ECB had entirely used its available income to reconstitute its provision against foreign exchange and interest rate risk, in 2008 it paid Eurosystem NCBs interim dividends as part of its seigniorage income. The Banque de France thus received income of EUR 249 million in 2008.

Moreover, the dividend paid by the IEDOM in 2008 in respect of the year ended 31 December 2007 stood at EUR 81 million, which constitutes an increase of EUR 31 million.

Net profit from non-monetary activities

Non-monetary activities generated a net profit of EUR 862 million, up EUR 246 million on the previous year.

This increase can mainly be attributed to the expansion in income generated by services to institutional customers while other income from services, including the sale of goods to other central banks (exports of banknotes other than euro banknotes) and the provision of services to commercial banks (including management of payment media and databases) remained stable. Income from the provision of services to the State fell by EUR 9 million.

Income from the portfolios in which the Bank's own funds and the Employee Reserve Fund are invested amounted to EUR 206 million, down by EUR 19 million on the previous year.

1|2|2 Operating expenses

Operating expenses			
<i>(EUR millions)</i>			
	2008	2007	Change 2008/2007
Operating expenses	-2,011	-1,850	-161
Staff costs and pension expenses	-1,362	-1,345	-17
Taxes other than income tax	-54	-34	-21
Provisions, depreciation and amortisation	-138	-115	-23
Capitalised production	40	62	-23
Other operating expenses	-496	-419	-77

Operating expenses stood at EUR 2,011 million in 2008, up by EUR 161 million on 2007.

Staff costs rose by EUR 17 million due to the increase in pension expenses while staff costs related to working employees remained stable (the impact of the reduction in staff numbers offset that of the overall pay rise).

The increase in taxes (EUR 21 million) can be ascribed to the rise in professional tax and the social solidarity contribution.

Depreciation and amortisation expenses also rose (EUR 23 million) whereas credit to the profit and loss account arising from the transfer to the balance sheet of capitalised production costs came down by the same amount thanks to the completion of several major IT projects.

Other net operating expenses increased by EUR 77 million. This rise can largely be ascribed to the growth in provisions to cover employee-related liabilities for both working employees and retirees.

1|2|3 Profit for the year

Main profit and loss account balances			
<i>(EUR millions)</i>			
	2008	2007	Change 2008/2007
Net income on activities of the Banque de France	6,195	5,644	551
Operating expenses	-2,011	-1,850	-161
Profit before tax and exceptional items	4,185	3,794	391
Net transfer to fund for general risks and accelerated tax depreciation	-215	-135	-80
Exceptional items	0	54	-54
Corporate income tax	-1,509	-1,396	-113
Profit for the year	2,460	2,317	144

After an additional contribution of EUR 200 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 1,510 million, net profit for the year ended 31 December 2008 amounted to EUR 2,460 million.

At its meeting of 10 April 2009, the General Council of the Banque de France examined the accounts for 2008

and decided on the appropriation of profits. One such appropriation is automatic, as it results from the legal requirements that apply to the Banque de France: 5% of net profit to the reserve set up under Article 28 of the decree of 3 December 1993. This reserve, which stands at EUR 408.4 million, is capped at the amount of the Bank's capital, i.e. EUR 457 million. It will reach this ceiling in 2009 after receiving an allocation of EUR 48.95 million in respect of the net profit of 2008.

In accordance with the methods for financing the pension obligations defined in the framework 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 440 million to a special reserve.

The dividend paid to the State amounted to EUR 1,845 million.

The balance of EUR 0.57 million was carried forward as retained earnings.



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2 | Annual accounts

2|1 Balance sheet and profit and loss account

Balance sheet at 31 December 2008				
(EUR millions)				
Notes to annual accounts		ASSETS	2008	2007 Pro forma
1	A1	Gold	49,802	47,557
2	A2	Foreign exchange assets (excl. relations with the IMF)	86,986	45,533
		2.1 Foreign exchange assets held with non-euro area residents	21,393	29,616
		2.2 Foreign exchange assets held with euro area residents	65,593	15,917
3	A3	Relations with the IMF	2,323	1,448
		3.1 Financing provided to the IMF	1,629	768
		3.2 Acquisitions of Special Drawing Rights	694	680
5	A4	Euro-denominated claims on non-euro area residents	5,793	3,487
4	A5	Euro-denominated loans to euro area credit institutions in the framework of monetary policy operations	134,463	71,055
5	A6	Other euro-denominated loans to euro area credit institutions	20,711	3,925
6	A7	Euro-denominated securities issued by euro area residents	68,740	39,141
	A8	Relations within the Eurosystem	85,322	76,766
		8.1 Participating interest in ECB	836	836
7		8.2 Claims arising on the transfer of reserve assets to the ECB	8,577	8,569
8		8.3 Claims on the Eurosystem for euro banknotes in circulation	75,572	67,312
9		8.4 Other claims on the Eurosystem	337	49
10	A9	Advance to the IEDOM	3,198	2,680
11	A10	Claims on the French Treasury	0	42
12	A11	Other euro and foreign currency denominated financial assets	86,882	63,814
13	A12	Miscellaneous	7,504	3,959
14	A13	Fixed assets	1,295	1,301
		13.1 Tangible and intangible assets	890	896
		13.2 Participating interests (other than interest in the ECB)	405	405
Total assets			553,019	360,708
Notes to annual accounts		LIABILITIES	2008	2007 Pro forma
15	P1	Banknotes in circulation	144,862	128,852
4	P2	Euro-denominated liabilities to euro area credit institutions in the framework of monetary policy operations	90,843	73,698
		2.1 Current accounts	67,693	49,260
		2.2 Other liabilities	23,150	24,437
	P3	Other euro-denominated liabilities to euro area credit institutions	139	40
	P4	Euro-denominated liabilities to non-euro area residents	21,566	10,737
2	P5	Foreign exchange liabilities	8,356	11,874
3	P6	Counterpart to SDR allocations	1,195	1,167
17	P7	Relations within the Eurosystem	117,880	12,035
18	P8	Euro-denominated liabilities to other euro area residents	17,112	4,290
		8.1 Treasury's account	13,045	309
		8.2 Other liabilities	4,067	3,981
19	P9	Items in course of settlement	279	574
20	P10	Banking transactions	74,465	54,366
21	P11	Miscellaneous	14,637	7,021
22	P12	Provisions for liabilities and charges	1,984	675
23	P13	Revaluation accounts	31,978	27,558
	P14	Fund for general risks and accelerated tax depreciation	948	733
24	P15	Revaluation reserve of State gold reserves	18,499	18,499
24	P16	Revaluation reserve of State foreign exchange reserves	1,996	2,904
25	P17	Capital, reserves and retained earnings	3,820	3,367
	P18	Profit for the year	2,460	2,317
Total liabilities			553,019	360,708

2008 Profit and Loss Account

(EUR millions)

Notes to annual accounts			2008	2007 Pro forma
	1.	Net income on activities of the Banque de France	6,195	5 644
30	1.1.	Net interest income	6,236	4 973
		1.1.1. Interest and related income	14,404	8 666
		1.1.2. Interest and related expenses	-8,168	-3 694
31	1.2.	Net income/loss on financial transactions	207	54
		1.2.1. Net of realised gains/losses and unrealised losses on foreign exchange	-908	-1 679
		1.2.2. Net of charges to/releases from the revaluation reserve of State foreign exchange reserves	908	1 679
		1.2.3. Net of other income and expenses on financial transaction	207	54
	1.3.	Commission	9	6
		1.3.1. Commission (income)	44	54
		1.3.2. Commission (expense)	-35	-48
32	1.4.	Income from equity securities and participating interests	364	105
33	1.5.	Net result of pooling of monetary income	-1,096	49
34	1.6.	Net of other income and expenses	475	458
	2.	Operating expenses	-2,011	-1,850
35	2.1.	Personnel and related expenses	-1,362	-1 345
	2.2.	Taxes other than income tax	-54	-34
	2.3.	Provisions, depreciation and amortisation	-138	-115
	2.4.	Net of other operating income and expenses	-456	-357
		Profit before tax and exceptional items (1 + 2)	4,184	3,794
	3.	Net charge to the fund for general risks and accelerated tax depreciation	-215	-135
36	4.	Extraordinary items	-	54
		4.1. Extraordinary income	-	54
		4.2. Extraordinary charges	-	-
37	5.	Corporate income tax	1,509	-1,396
		Profit for the year (1+2+3+4+5)	2,460	2,317

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)

Fixed income and variable yield securities are recorded in asset item A2, when they are denominated in foreign currencies, or in asset items A4 or A7, when they are denominated in euros, and depending on whether they are issued by residents or non-residents. However, euro-denominated securities linked to the Bank's own funds, provisions and customer deposits recorded in liability items P4 or P10, are recorded in asset item A11. Securities held in the pension reserve fund of Banque de France employees are recorded in asset item A12 (see Note 29).

Fixed income securities that the Banque de France has decided to hold to maturity are recognised in the accounts at amortised cost but may be subject to impairment in the event of the risk of non-recovery.

The other fixed income securities that may be sold before their maturity, and variable yield securities, are revalued line by line at their market price 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. Gains and losses arising from sales realised during the year are calculated on the basis of the weighted average price of each line of securities; they are booked in the item 1.2.3 "profits or losses on financial transactions" of the profit and loss account.

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.

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 item 1.2.3 of 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 (item 14) and unrealised losses are booked as expenses on financial transactions (item 1.2.3 of the profit and loss account). Unrealised gains and losses are not netted. Unrealised losses are amortised over the remaining life of the contract. The interest is recorded in item 1.1 of 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 of the profit and loss account "Net balance of foreign exchange realised gains and losses and unrealised losses". At the end of the year, the premium amounts booked to the profit and loss account during the year are transferred to the revaluation reserve of State foreign exchange

reserves in the same way as realised foreign exchange gains and 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 (item P14). Unrealised losses are booked in item 1.2.3 of the profit and loss account. Unrealised gains and losses are not netted.

Synthetic instruments

A synthetic instrument is a financial instrument created artificially by combining two or more instruments with the objective of reproducing the cash flows and valuation models of another instrument.

At the end of the year a synthetic instrument that replicates a fixed income security that is not intended to be held to maturity is marked to market using the market prices of the instruments that make it up. The unrealised gain or loss of the synthetic instrument is calculated for the net amount of the unrealised gains and losses of the instruments that make it up.

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 between different synthetic instruments are not netted. Gains and losses arising from sales realised during the year are booked, if need be, in item 1.2.3 "profits or losses on financial transactions" of the profit and loss account.

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. In accordance with CRC Regulation No. 2002-10, the useful lives of long-term assets are reviewed regularly and modified as required.

Accelerated tax depreciation is applied for assets that can be depreciated more rapidly for tax purposes than for accounting purposes.

Banknotes in circulation

See note 15.

Fund for general risks

A fund for general risks was established in 1998 to cover any general risks inherent in the activities of a central bank. This fund is booked as a liability in item P14, with counterparty entries for charges and releases from this fund through item 3 of the profit and loss account.

Pension scheme

See note 29.

Change of presentation

Up until now, all securities that the Bank had the intention of holding to maturity were booked in item A11, whether or not they were linked to specific resources. Pursuant to an ECB Governing Council decision dated 11 December 2008 and with an objective of improving the accounting transparency of the balance sheet, investment securities not linked to specific liabilities were transferred as at 31 December 2008 from asset item A11 to the items that account for claims in foreign currencies or in euro. These are asset item A2 for securities in foreign currencies and A4 or A7 for securities in euro.

For the purposes of comparison, the 2007 balance sheet was restated pro forma according to the same principles.

Post balance sheet events

Change in the Banque de France's share in the ECB capital as of 1 January 2009

Under Article 29 of the ESCB Statute, the capital subscription of each member NCB to the ECB is calculated according to two criteria with equal weight: the weighting of each member state in the population of the EU and its weighting in the GDP of the EU, as calculated by the European Commission. These weightings are adjusted every five years.¹The second adjustment subsequent to the creation of the ECB was realised on 1 January 2009; on this date the Banque de France's share in the capital of the ECB fell from 14.3875% to 14.2212%.

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.

In the tables below, items may not add up to the total due to rounding.

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.

It was in this context that the Banque de France continued with its gold sales, selling 103 tonnes, and at 31 December the gold stock was 2,491 tonnes. Despite these sales, the sharp increase in the price of gold (see Note 23) resulted in an increase in the euro exchange value of the reserves at the year-end.

¹ They are also adjusted when a new country joins the EU.

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.

Foreign exchange assets and liabilities (excl. relations with the IMF) Asset item A2 and Liability item P5		
(EUR millions)		
	2008	2007
ASSETS		
Foreign currency assets		
Overnight deposits	493	282
Fixed-term deposits	7,876	5,834
USD liquidity providing program	47,320	964
Securities received under repurchase agreements	5,831	14,720
Fixed income securities	25,063	23,347
Accrued interest receivable	404	387
Total	86,986	45,533
LIABILITIES		
Foreign exchange liabilities		
Securities delivered under repurchase agreements	8,353	11,861
Accrued interest payable	3	13
Total	8,356	11,874

Fixed income securities denominated in foreign currencies comprise securities that the Bank has the intention of holding to maturity and securities that may be sold. These two portfolio categories are subject to different valuation rules that are described in the section on accounting principles and valuation methods. Securities intended to be held to maturity totalled EUR 9,803 million at 31 December 2008, compared to EUR 7,558 million at 31 December 2007.

The item "foreign currency assets" also includes claims on euro area residents denominated in foreign currency, taking the form of securities repurchase agreements; and, for an equivalent value in euros of EUR 47,320 million (EUR 964 million in 2007), loans that were granted in the framework of the temporary reciprocal currency arrangement (swap line) put in place by the US Federal Reserve System and the ECB. Under this programme, the US Federal Reserve System provided the dollars to the ECB through a EUR/USD swap. 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-interest-bearing 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 drawing rights under the reserve tranche that corresponds to the fraction of France's quota in the capital of the IMF settled in gold and other foreign currency assets, uplifted for net euro usage by the IMF, notably, for euro-denominated drawings and repayments by member countries vis-à-vis France.

The EUR 862 million increase observed in 2008 is entirely as a result of an increase in the net euro usage; IMF drawings on France's quota, intended to fund new loans, exceeded repayments of previous drawings.

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.

Relations with the IMF Asset item A3 and Liability item P6		
(EUR millions)		
	2008	2007
ASSETS		
Financing provided to the IMF	1,628	766
Acquisitions of Special Drawing Rights	693	676
Accrued interest receivable	3	6
Total	2,323	1,448
LIABILITIES		
Counterpart to SDR allocations	1,193	1,160
Accrued interest payable	2	7
Total	1,195	1,167

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.

Main refinancing operations are open market operations that play a key role in steering interest rates, bank liquidity management and signalling the stance of monetary policy. They are conducted through weekly tenders in the form of temporary sales of assets (repurchase agreements) for a one-week maturity.

Longer-term refinancing operations (LTROs) are carried out through monthly tenders. At the end of 2008, outstanding LTROs had one-month and six-month agreed maturities.

Since October 2008 these two types of financing of credit institutions have been carried out at fixed rates.

Marginal lending facilities are overnight facilities granted in the form of repurchase agreements to Banque de France counterparties at their request. Interest is paid on these facilities at a rate fixed by the Eurosystem.

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

The deposit facility allows Banque de France counterparties to make overnight deposits. The interest rate on the deposit facility is set by the Eurosystem and provides a floor for the market rate.

Finally, Eurosystem may ask counterparties to invest cash assets in the form of remunerated fixed-term deposits with the national central bank of the Member State in which the counterparty is established. These **collections of fixed-term deposits** are only considered for fine-tuning with a view to withdrawing

liquidity from the market. Deposits accepted from counterparties have a fixed maturity and interest rate.

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

Asset item A5

(EUR millions)

	2008	2007
Main refinancing operations	16,750	24,751
Longer-term refinancing operations	116,117	46,118
Fine-tuning operations	–	–
Structural operations	–	–
Marginal lending facility	1,106	–
Margin calls paid	–	–
Accrued interest receivable	490	186
Total	134,463	71,055

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

Liability item P2

(EUR millions)

	2008	2007
Current accounts	67,616	49,169
Remaining liabilities	23,136	24,432
Deposit facilities	23,136	–
Collection of fixed-term deposits	–	23,000
Margin calls received	–	1,432
Accrued interest payable	91	96
Total	90,843	73,698

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 A4 and A6 according to whether the counterparty is located within or outside the euro area.

Claims in euro on non-euro area residents

Asset item A4

(EUR millions)

	2008	2007
Securities held until maturity	4,621	1,217
Other claims	1,063	2,251
Accrued interest receivable	109	19
Total	5,793	3,487

Note 6: Asset item A7 “Euro-denominated securities issued by euro area residents”

This item includes all euro-denominated securities issued by residents of the euro area, other than those that are specifically linked to:

- capital and customer deposits, which are recorded in asset item A11 (see Notes 12 and 28);
- the Employee Reserve Fund, which is recorded in asset item A12 (see Note 29)

Euro-denominated securities issued by euro area residents

Asset item A7

(EUR millions)

	2008	2007
Securities held until maturity	50,798	24,305
Other securities	16,781	14,273
Accrued interest receivable	1,161	563
Total	68,740	39,141

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)

	2008	2007
Claims arising on the transfer of reserve assets to the ECB	8,288	8,288
Accrued interest receivable	289	281
Total	8,577	8,569

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 2008. 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 includes 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) as well as the ECB's interim distribution of profit (see Note 15 on banknotes in circulation).

Other claims on the Eurosystem

Asset item A 8.4

(EUR millions)

	2008	2007
Other claims on the Eurosystem	88	49
ECB interim dividends	249	–
Total	337	49

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 balance of the Banque de France claim on the French Treasury in respect of coinage was repaid in 2008.

Note 12: Other euro and foreign currency denominated financial assets

Other euro and foreign currency denominated financial assets		
Asset item A11		
<i>(EUR millions)</i>		
	2008	2007
Fixed income securities held until maturity (a) (b)	61,172	33,209
Other fixed income securities and variable-yield securities	3,029	2,321
Other operations	22,537	28,012
Accrued interest receivable	144	272
Total of other euro- and foreign currency-denominated financial assets	86,882	63,814

(a) In 2008, 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 60,422 million. Of which deposit-backed securities EUR 60,423 million (see Note 28).

Asset item A11 includes, notably, securities linked to customer deposits, recorded in liability items P4 and P10, capital and provisions.

Securities portfolios				
Extract from Asset item A11				
<i>(EUR millions)</i>				
	2008			2007
	Fixed income securities held until maturity	Other securities	Total	Total
Fixed income securities				
Government securities	60,530	163	60,693	56,299
Securities issued by public bodies	184		184	4,927
Other issuers	460		460	4,988
Accrued interest receivable	156		156	655
Net balance sheet value	61,329	163	61,493	66,869
Equities and other variable-yield securities				
French and foreign mutual funds				
Capitalisation mutual funds		862	862	994
Capitalisation mutual funds		1,952	1,952	1,134
Other variable-yield securities		52	52	90
Net balance sheet value		2,866	2,866	2,217

Note 13: Miscellaneous

Miscellaneous		
Asset item A12		
<i>(EUR millions)</i>		
	2008	2007
Deferred income, accrued expenses, etc.	4,136	541
Accrued income	990	545
Prepaid expenses	14	14
Other items	3,132	-18
Miscellaneous	3,368	3,418
Total	7,504	3,959

The other accruals accounts include, notably, the impact of the revaluation of off-balance sheet foreign exchange positions held in relation to the temporary reciprocal currency arrangement (swap line) put in place between the US Federal Reserve System and the ECB (see Note 28). As far as the swaps are concerned, the overall impact of these operations (on- and off-balance sheet) on the net foreign exchange gains or losses is nil.

Note 14: Fixed assets

Fixed assets				
Asset item A8.1 and A13				
<i>(EUR millions)</i>				
	31 Dec 2008	Increase (a)	Decrease (a)	31 Dec 2007
Participating interest in the ECB (gross value)	831			831
FX translation difference on participating interest in the ECB	5			5
Participating interest in ECB (balance sheet value)	836			836
Non-ECB participating interest (gross value)	405			405
<i>Intangible fixed assets (gross value)</i>	<i>517</i>	<i>123</i>	<i>62</i>	<i>457</i>
<i>Amortisation</i>	<i>315</i>	<i>48</i>	<i>4</i>	<i>272</i>
Net value of intangible fixed assets	202	76	58	185
<i>Tangible fixed assets (gross value)</i>	<i>2,096</i>	<i>215</i>	<i>166</i>	<i>2,047</i>
<i>Depreciation and provisions</i>	<i>1,408</i>	<i>91</i>	<i>19</i>	<i>1,336</i>
Net value of tangible fixed assets	688	124	147	711
Total tangible and intangible fixed assets (net value)	890	200	205	896

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

Information relating to subsidiaries and participating interests at 31 December 2008

Asset item A8.1 and A13.2

(EUR millions)

	Asset item	Listed	% share capital held	2008 Shareholders' equity	2008 profit/loss equity	2008 book value
Bank for International Settlements	A13.2	No	9.16	13,892	603	405
European Central Bank (a)	A8.1	No	20.64	19,529	1,322	831
La Prévoyance immobilière	A13.2	No	98.20	na	na	ns
Banque de France Gestion	A13.2	No	99.99	2	4	ns

ns: not significant

na: not available

(a) The interest in the capital is the BdF's share in all of the NCBs that are members of the euro area. It is this key that is used for the allocation of dividends.

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.

Following the entry of Malta and Cyprus into the euro area on 1 January 2008, the central banks of these two countries have had to pay their full contribution to the capital of the ECB which increased from EUR 4,127 million at 31 December 2007 to EUR 4,137 million on 1 January 2008.

The Banque de France's share in the ECB's capital key remained unchanged at 14.3875%.

Share of the Banque de France in the capital of the ECB (%)

(en %)

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

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.²

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).

For a five-year period from the year of adoption of the euro,³ intra-Eurosystem balances resulting from euro banknote allocation are being adjusted in order to avoid significant changes in the NCBs' income positions compared to previous years. These 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 reference period⁴ 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. These adjustment amounts will reduce each year until the first day of the sixth year following euro adoption, after which income on banknotes will be allocated fully between the NCBs in proportion to their paid-up share in the ECB's capital. The adjustment period for Cyprus and Malta will end on 1 January 2013.

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.⁵

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

3 The year of adoption of the euro corresponds to the year in which euro banknotes became legal tender in the member country concerned; this was in 2008 for the central banks of Cyprus and Malta.

4 The reference period is the 24 months that commences 30 months before the date on which euro banknotes have legal tender in the member states concerned.

5 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.

This income is distributed in full unless the ECB's net profit is less than the income earned on euro banknotes in circulation or 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. For 2008, the ECB Governing Council decided that an amount of EUR 1,339 million would be retained by the ECB. The remaining amount distributed to NCBS is included in item 1.4 "Income from equity securities and participating interests". The portion allocated to the Banque de France in the form of an interim distribution of profit totalled EUR 249 million.

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

Euro-denominated liabilities to non-euro area residents Liability item P4		
(EUR millions)		
	2008	2007
Euro-denominated liabilities to non-euro area residents	21,485	10,635
Accrued interest payable	81	102
Total	21,566	10,737

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 2 with other NCBS in the ESCB. These liabilities also include non-interest bearing debt of EUR 50,510 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 Notes 2 and 28).

Euro-denominated liabilities to the Eurosystem Liability item P7		
(EUR millions)		
	2008	2007
Euro-denominated liabilities to the Eurosystem	117,684	11,935
Accrued interest payable	195	100
Total	117,880	12,035

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.
 - the account of other Government agencies.
- 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).

Euro-denominated liabilities to other euro area residents Liability item P8		
(EUR millions)		
	2008	2007
Liabilities vis-à-vis the State	13,036	308
Other liabilities	4,059	3,981
Accrued interest payable	18	12
Total	17,112	4,290

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.

For the record, 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		
<i>(EUR millions)</i>		
	2008	2007
Overnight deposits	13,538	505
Other banking transactions	59,954	53,205
Accrued interest payable	973	657
Total	74,465	54,366

Note 21: Miscellaneous

Miscellaneous Liability item P11		
<i>(EUR millions)</i>		
	2008	2007
Deferred income, accrued expenses, etc.	10,534	2,617
Accrued expenses	399	283
Deferred income, etc.	10,134	2,334
French franc banknotes in circulation	838	995
Miscellaneous	3,275	3,409
Total	14,637	7,021

This item includes mainly:

- the other accrual accounts that incorporate the revaluation impact of off-balance sheet foreign exchange positions held in relation to retail banking

operations (see Note 20). Their impact on the profit and loss account is cancelled out by the revaluation of foreign exchange positions in the balance sheet, the overall foreign exchange position from these activities being close to zero.

- the capital of the Banque de France Employee Reserve Fund (see Note 29);

- 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 to cover various social obligations to retired employees (death benefits, etc.) that are not funded by the pension scheme;

- provisions for major repairs.

In 2008, the Bank created a provision in relation to its complementary health plan. This provision covers the Bank's implied commitment, following the opening of negotiations with staff representative bodies with a view to introducing a compulsory plan, to fund a portion of the complementary health plan for personnel.

Finally, in accordance with the general accounting principle of prudence, the ECB Governing Council has deemed it appropriate to establish a buffer totalling EUR 5,736 million against counterparty risks

in monetary policy operations. In accordance with Article 32.4 of the ESCB Statute, this buffer will be funded by all NCBS of participating member states in proportion to their subscribed capital key shares in the ECB prevailing in 2008. As a result, a provision for EUR 1,184 million, equivalent to 20.6431 % of the total provision, was created.

Provisions for liabilities and charges				
Liability item P12				
(EUR millions)				
	2008	Increase	Decrease	2007
Provisions for restructuring	193		51	244
Provisions for changing the age pyramid	24			24
Provisions for retirement benefits	134	32		102
Provisions for the complementary health plan	150	150		
Provisions relative to monetary policy operations	1,184	1,184		
Other	299	12	18	305
Total	1,984	1,378	69	675

Note 23: Revaluation accounts

Gold and foreign exchange assets and liabilities are revalued at the reference prices indicated by the ECB on 31 December 2008. The unrealised gain on gold was calculated using a price of EUR 19,983 per kilogram of fine gold, compared with EUR 18,269 at end-2007.

The revaluation rates used at 31 December 2008 for the main currencies held were the following:

- 1 euro = 1.3917 US dollars (compared with 1.4721 at end-2007)
- 1 euro = 0.9051 SDRs (compared with 0.9311 at end-2007)

Revaluation accounts		
Liability item P13		
(EUR millions)		
	2008	2007
Revaluation account – gold	30,001	26,825
Revaluation account – foreign exchange	1,105	46
Revaluation account – securities	870	685
Revaluation account – forward financial instruments	2	2
Total	31,978	27,558

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 in 2008 were transferred to the revaluation reserve of State foreign exchange reserves (see Note 31).
- The revaluation reserve of State gold reserves remained unchanged at EUR 18,499 million.

Note 25: Capital, reserves and retained earnings

Capital, reserves and retained earnings		
Liability item P17		
(EUR millions)		
	2008	2007
Capital	457	457
Reserves	3,362	2,910
Statutory reserves	408	293
Long-term capital gains	100	100
Special pension reserve fund (see note 29)	446	109
Other reserves (a)	2,408	2,408
Retained earnings	0	1
Total	3,820	3,368

(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)		
	2008	2007
Securities to be received	2,215	4,955
Securities to be delivered	149	582

Note 27: Financial futures contracts

Notional amount of forward contracts		
(EUR millions)		
	2008	2007
Outright transactions on organised markets		
Interest rate contracts denominated in foreign currency		
Purchases	2,384	3,241
Sales	1,329	–
Interest rate contracts denominated in euro		
Purchases	1,019	4,962
Sales	4,894	7,015
Over-the-counter markets		
Interest rate swaps denominated in foreign currency	679	315
Interest rate swaps denominated in euro	20	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 P10.

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 “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)		
	2008	2007
Euro to be received against foreign currency to be delivered		
Euro to be received	12,911	4,242
Foreign currency to be delivered	12,861	4,167
Foreign currency to be received against euro to be delivered		
Foreign currency to be received	14,170	62
Euro to be delivered	14,005	64
Foreign currency to be received against foreign currency to be delivered	62,139	43,244
Foreign currency to be delivered against foreign currency to be received	70,956	44,321

In addition, at 31 December 2008, the amount remained of the forward contract commitment to deliver dollars to the ECB with a value equivalent to EUR 47 320 million, under the temporary dollar-denominated Term Auction Facility introduced by the Federal Reserve System (see Notes 2 and 17).

In addition, a commitment to deliver Swiss francs to the ECB arose from the mechanism introduced with a view to providing Swiss franc liquidities to Eurosystem counterparties. Swiss francs were made available to the ECB by the Swiss National Bank through EUR/CHF swaps for a countervalue of EUR 3,950 million. The Swiss francs were lent by the Banque de France to Eurosystem counterparties by way of EUR/CHF currency swaps.

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 Reserve Fund", in accordance with the third indent of Article R144-4 of the French Monetary and Financial Code. This reserve fund 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

reserve fund for pensions 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 reserve fund 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.

For the calculation of pension liabilities as at 31 December 2008, new mortality tables have been used; these were mortality experience tables by sex based on the TGH-TGF 2005 statutory tables.

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 2008, as in previous years, a discount rate of 4.5% was applied.

Pension liabilities and funding

(EUR millions)

Liabilities			Funding		
	2008	2007		2008	2007
Liabilities in respect of the special retirement scheme	9,453	9,099	Funding	3,750	3,253
o/w to current workforce	4,248	4,115	o/w Employee Reserve Fund	3,304	3,144
o/w to retirees	5,205	4,984	o/w Special pension reserve	446	109
Liabilities in respect of the additional seniority granted as part of restructuring plans	126	124	Provisions	126	124
Total gross liabilities	9,578	9,222	Total funding	3,875	3,376
Net liabilities	5,703	5,846			

Profit and loss account

Note 30: Net interest income

Net interest income

Profit and loss item 1.1

(EUR millions)

	2008	2007
Interest on foreign exchange assets	1,916	2,092
o/w: Interest held-to-maturities securities	478	311
Interest on claims on the IMF	43	47
Interest on euro-denominated claims on non-residents		
Interest on lending to credit institutions	3,353	1,285
Interest on euro-denominated securities	2,585	1,142
o/w: Interest held-to-maturities securities	1,900	584
Interest on claims arising on transfer of reserve assets to the ECB	289	281
Interest on net claims on the Eurosystem (a)	0	0
Interest on the net euro banknote position	2,731	2,223
Total of other euro- and foreign currency denominated financial assets	3,487	1,396
o/w: Interest on available-for-sale securities	1	ns
Interest on held-to-maturity securities	351	95
Other interest	3,134	1,299
Total interest and related income (A)	14,404	8,464
Interest on euro-denominated liabilities to monetary financial institutions in the euro area	-1,987	-1,592
o/w: Interest paid on minimum reserves	-1,632	-1,414
Interest on euro-denominated liabilities to non-euro area residents	-2,551	-398
Interest on foreign exchange liabilities	-525	-462
Interest on counterpart to SDR allocations	-30	-49
Interest on net claims on the Eurosystem (a)	-2,450	-60
Interest paid on the Treasury account	-46	-8
Other interest	-579	-922
Total interest and related expenses (B)	-8,168	-3,491
Net interest income (C = A + B)	6,236	4,973

(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 2008, the net balance of realised gold and foreign exchange gains and losses and unrealised foreign exchange losses was a gain of EUR 908 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 908 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)

	2008	2007
Net gain/loss on foreign currency denominated securities (a) (b) (c)	306	89
Net gain/loss on euro-denominated securities included in item A7 (b) (c)	-105	-45
Net gain/loss on available-for-sale securities included in item A11	-10	2
Net foreign exchange gain/loss (excluding foreign exchange reserve management)	16	8
Total	207	54

(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 profits and losses on synthetic instruments.

Note 32: Income from equity securities and participating interests

In 2008, ECB income from banknotes in circulation totalled EUR 2,230 million. The ECB, pursuant to a decision of the Governing Council in relation to the establishment of a provision for currency, interest rate and gold price risks, has retained EUR 1,025 million for this purpose. The Bank has received its share (20.6431%) of the balance distributed (EUR 1,206 million) by the ECB, being EUR 249 million (see Note 15), as an interim distribution of profit.

Income from equity shares and participating interests

Profit and loss item 1.4

(EUR millions)

	2008	2007
ECB dividend	249	–
Dividends from other participating interests	99	69
Dividends from available-for-sale securities	16	34
Other income	–	2
Total	364	105

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 5,594 million) and that reallocated to the Bank (EUR 5,682 million) constitutes the net result arising from the calculation of monetary income recorded in profit and loss item 1.5.

At 31 December 2008, the net result from the pooling of monetary income also comprised the provision made in relation to monetary policy operations of EUR 1,184 million (see Note 22).

Note 34: Net of other income and expenses

Net of other income and expenses		
Profit and loss item 1.6		
(EUR millions)		
	2008	2007
Remuneration for services rendered to the State	149	158
Other income (a)	334	363
Total other income (A)	483	471
Total other expenses (B)	-8	-13
Net of other income and expenses (C = A + B)	475	458

(a) This item notably includes fees charged for use of the databases managed by the Banque de France (FNCL, FICP, FCC, FIBEN).

Note 35: Personnel and related expenses

Personnel and related expenses		
Profit and loss item 2.1		
(EUR millions)		
	2008	2007
Salaries, wages and related taxes	-743	-738
Social security expenses	-167	-152
Retirement expenses	-418	-420
Profit-sharing and incentive plans	-34	-35
Total personnel expenses	-1,362	-1,345

Note 36: Extraordinary items

In 2008, contrary to 2007, there were no extraordinary items. In 2007 the extraordinary items comprised

net gains arising on the sale of some of the branches closed as part of the reform of the Banque de France regional network. During 2008 there were no such sales.

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)		
	2008	2007
Income taxes for the year	1,509	1,396
on recurring income	1,509	1,376
on exceptional items	-	20

Other information

Remuneration of management bodies		
(EUR millions)		
	2008	2007
Total remuneration paid to management bodies	3.0	2.9

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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REPORT OF THE AUDITORS ON THE ANNUAL ACCOUNTS

Year ended 31 December 2008

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 2008 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 checking, on a test basis or via other selection methods, 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 the overall financial statement presentation. We believe that the information we have collected 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 2008, 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 indicated in the Notes to the annual accounts, pursuant to the ECB Governing Council's Decision of 11 December 2008, securities held to maturity not backed by specific liabilities were transferred as at 31 December 2008 from item A11 to the asset items that display claims denominated in foreign currencies (item A2) or in euro (items A4 or A7). To enable comparison, the 2007 balance sheet was reprocessed *pro forma* according to the same principle.

.../...

2| Basis for our assessments

The financial crisis, which has been gradually accompanied by an economic crisis, has led to an exceptional increase in volatility, a sharp contraction in liquidity on certain markets and difficulties in assessing the economic and financial outlook. This situation has created specific conditions this year for the preparation of the annual accounts, particularly with regard to accounting estimates. It is in this context that, 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, reviewing the documentation concerning calculations and controls carried out by the Banque de France and the ESCB, 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

We have also performed the other procedures required by the law.

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, 10 April 2009
The Auditors

Mazars

Patrick de Cambourg
Max Dongar

Deloitte & associés

Thierry Aubertin

3| Combined accounts

3| I Combined balance sheet and profit and loss account

Combined balance sheet at 31 December 2008				
(EUR millions)				
Notes to combined annual accounts	Poste	ASSETS	2008	2007 Pro forma
	A1	Gold	49,802	47,557
		Foreign exchange assets (excl. relations with the IMF)	86,986	45,533
	A2	2.1 Foreign exchange assets held with non-euro area residents	21,393	29,616
		2.2 Foreign exchange assets held with euro area residents	65,593	15,317
	A3	Relations with the IMF	2,323	1,448
		3.1 Financing provided to the IMF	1,629	768
		3.2 Acquisitions of Special Drawing Rights	694	680
	A4	Euro-denominated claims on non-euro area residents	5,793	3,487
	A5	Euro-denominated loans to euro area credit institutions in the framework of monetary policy operations	134,463	71,055
	A6	Other euro-denominated loans to euro area credit institutions	20,711	3,925
	A7	Euro-denominated securities	68,740	39,141
	A8	Relations within the Eurosystem	85,322	76,766
		8.1 Participating interest in the ECB	836	836
		8.2 Claims arising on the transfer of reserve assets to the ECB	8,577	8,569
		8.3 Claim on the Eurosystem for euro banknotes in circulation	75,572	67,312
		8.4 Other claims on the Eurosystem	337	49
2	A9	Claims on the French Treasury in respect of coins	0	42
	A10	Other euro and foreign currency denominated financial assets	86,885	63,817
I	A11	Miscellaneous	7,854	4,242
	A12	Fixed assets	1,329	1,330
		12.1 Tangible and intangible assets	915	917
		12.2 Participating interests (other than interest in the ECB)	414	414
Total de l'actif			550,207	358,344
	Poste	LIABILITIES	2008	2007
	P1	Banknotes in circulation	144,862	128,852
	P2	Euro-denominated liabilities to euro area credit institutions in the framework of monetary policy operations	90,843	73,698
		2.1 Current accounts	67,693	49,260
		2.2 Other liabilities	23,150	24,437
	P3	Other euro-denominated liabilities to euro area credit institutions	139	40
	P4	Euro-denominated liabilities to non-euro area residents	21,566	10,737
	P5	Foreign exchange liabilities	8,356	11,874
	P6	Counterpart to SDR allocations	1,195	1,167
	P7	Relations within the Eurosystem	117,880	12,035
	P8	Euro-denominated liabilities to other euro area residents	13,700	1,212
		8.1 Treasury's account	13,175	502
2		8.2 Other liabilities	525	711
	P9	Items in course of settlement	303	769
	P10	Banking transactions	74,465	54,366
	P11	Miscellaneous	14,646	7,033
	P12	Provisions for liabilities and charges	1,997	689
	P13	Revaluation accounts	31,978	27,558
	P14	Fund for general risks	870	670
	P15	Revaluation reserve of State gold reserves	18,499	18,499
	P16	Revaluation reserve of State foreign exchange reserves	1,996	2,904
I	P17	Capital, reserves and retained earnings	4,375	3,832
		17.1. IEDOM capital grant, reserves and retained earnings	137	137
		17.2. Banque de France capital, reserves and retained earnings	4,238	3,695
	P18	Profit for the year	2,538	2,408
Total liabilities			550,207	358,344

2008 Combined profit and loss account

(EUR millions)

Notes to combined annual accounts			2008	2007
	I.	Net income on the activities of the Banque de France	6,261	5,731
2	1.1.	Net interest income	6,366	5,099
		<i>1.1.1 Interest and related income</i>	14,404	8,667
		<i>1.1.2 Interest and related expenses</i>	-8,038	-3,568
	1.2.	Net income/loss on financial transactions	207	54
		<i>1.2.1 Net balance of realised gains/losses and unrealised losses on foreign exchange</i>	-908	-1,679
		<i>1.2.2 Net of charges to/releases from foreign exchange revaluation reserves</i>	908	1,679
2		<i>1.2.3 Net of other income and expenses on financial transactions</i>	207	54
	1.3.	Commission	9	6
		<i>1.3.1 Commission (income)</i>	44	54
		<i>1.3.2 Commission (expense)</i>	-35	-48
	1.4.	Income from equity securities and participating interests	283	55
	1.5.	Net result of pooling of monetary income	-1,096	49
	1.6.	Net of other income and expenses	493	468
	2.	Operating expenses	-2,062	-1,891
	2.1.	Personnel and related expenses	-1,382	-1,360
	2.2.	Taxes other than income tax	-55	-34
	2.3.	Provisions, depreciation and amortisation	-140	-117
	2.4.	Other operating expenses	-485	-380
		Profit before tax and exceptional items (1 + 2)	4,199	3,840
	3.	Net charge to the fund for general risks	-200	-120
	4.	Extraordinary items	-	54
	4.1.	Extraordinary income	-	54
	4.2.	Extraordinary charges	-	0
I	5.	Corporate income tax	-1,461	-1,366
		Profit for the year (1 + 2 + 3 + 4 + 5)	2,538	2,408

3 | 2 Notes to the combined annual accounts

3|2|1 Scope of consolidation

Undertakings excluded from the consolidation

At 31 December 2008, 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 I: Deferred taxes

A net deferred tax asset of EUR 332 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		
<i>(EUR millions)</i>		
	Deferred tax assets	Deferred tax liabilities
Income temporarily exempted from taxation		22
Tax on unrealised gains and losses on mutual funds	110	
Other deferred tax relating to securities	7	
Provisions not deductible for tax purposes	250	
Charges deducted for tax purposes but not yet recognised in the accounts	14	
Other recurring timing differences		27
Total	381	49

The matching entry for this deferred tax asset is split between:

- the tax charge for the year, which is EUR 53 million lower than in the individual annual accounts for fiscal 2008;

- item P17 “Capital, reserves and retained earnings”, which includes the balance of EUR 279 million, representing the net deferred tax asset at the start of fiscal 2008.

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

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**REPORT OF THE AUDITORS
ON THE COMBINED ANNUAL ACCOUNTS**
Year ended 31 December 2008

In accordance with the assignment entrusted to us by the Bank’s 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 2008.

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 or via other selection methods, 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 the information we have collected 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 2008, 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) As explained in the Notes to the annual accounts, pursuant to an ECB Governing Council decision dated 11 December 2008, investment securities not linked to specific liabilities were transferred as at 31 December 2008 from asset item A11 to the items that account for claims in foreign currencies (item A2) or in euros (items A4 and A7). For the purposes of comparison, the 2007 balance sheet was restated pro forma according to the same principles;
- e) 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.

2| Basis for our assessments

The financial crisis, which has been gradually accompanied by an economic crisis, has led to an exceptional increase in volatility, a sharp contraction in liquidity on certain markets and difficulties in assessing the economic and financial outlook. This situation has created specific conditions this year for the preparation of the annual accounts, particularly with regard to accounting estimates. It is in this context that, 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, reviewing the documentation concerning calculations and controls carried out by the Banque de France and the ESCB, 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 332 million as at 31 December 2008. 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, 10 April 2009
The Auditors

Mazars
Patrick de Cambourg
Max Dongar

Deloitte & associés
Thierry Aubertin



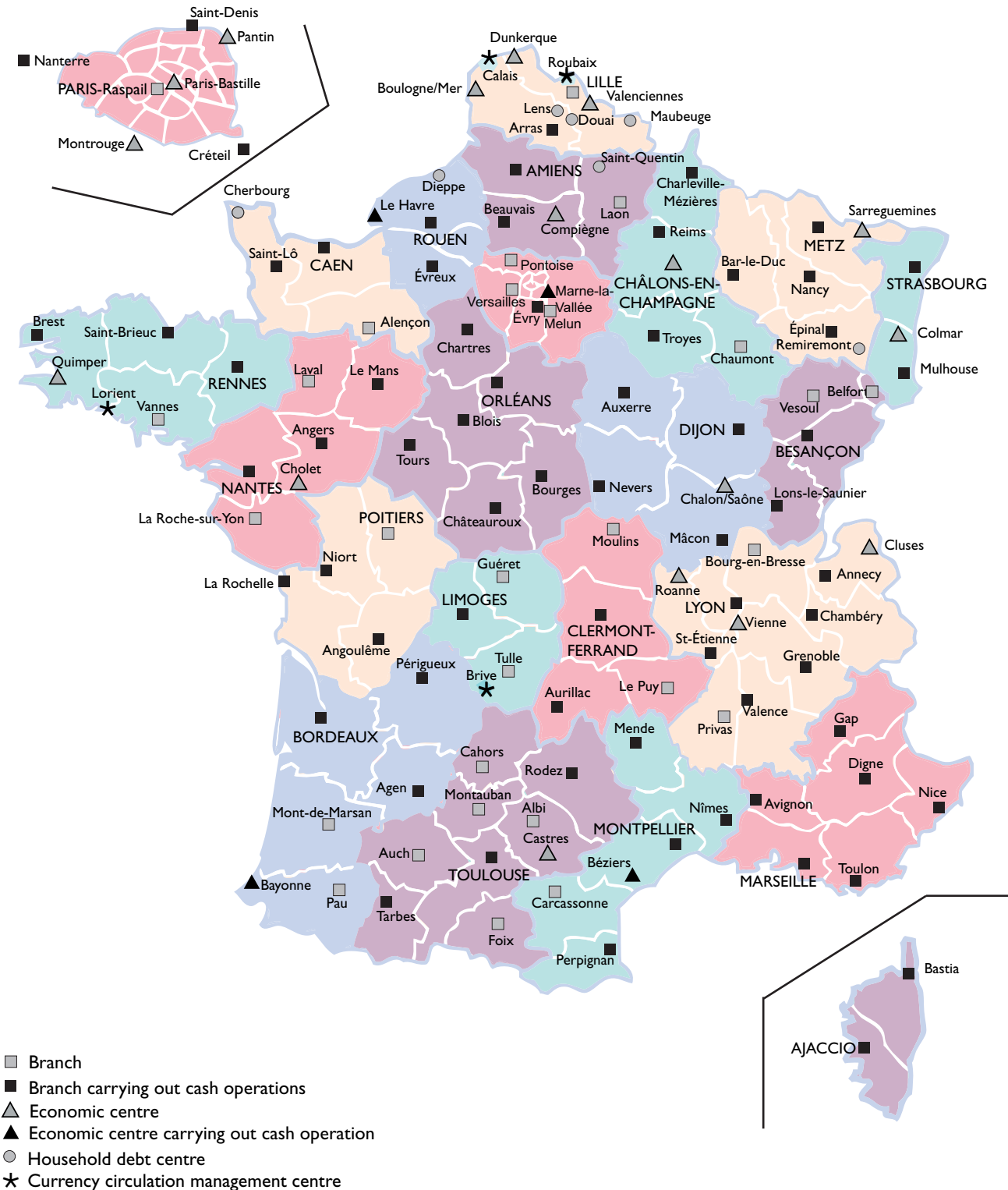
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APPENDIX I

The Banque de France branch network at end-2008

The Banque de France branch network at 31 December 2008



Banque de France staff levels at 31 December 2008

Chart 40 Breakdown of statutory staff by age bracket

(full-time equivalent positions at 31 December)

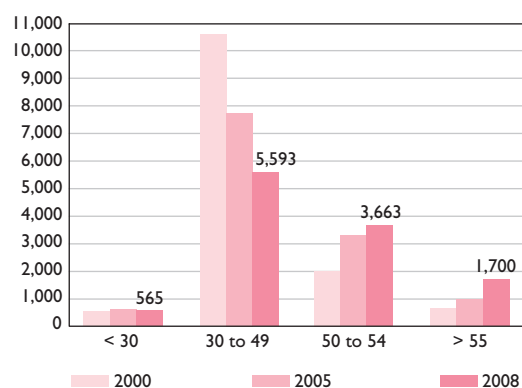
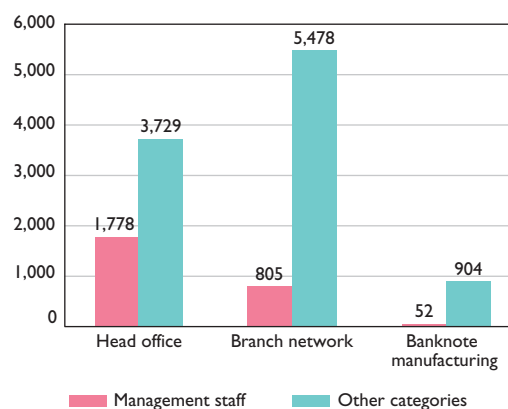


Chart 41 Location of staff

(full-time equivalent positions at 31 December)

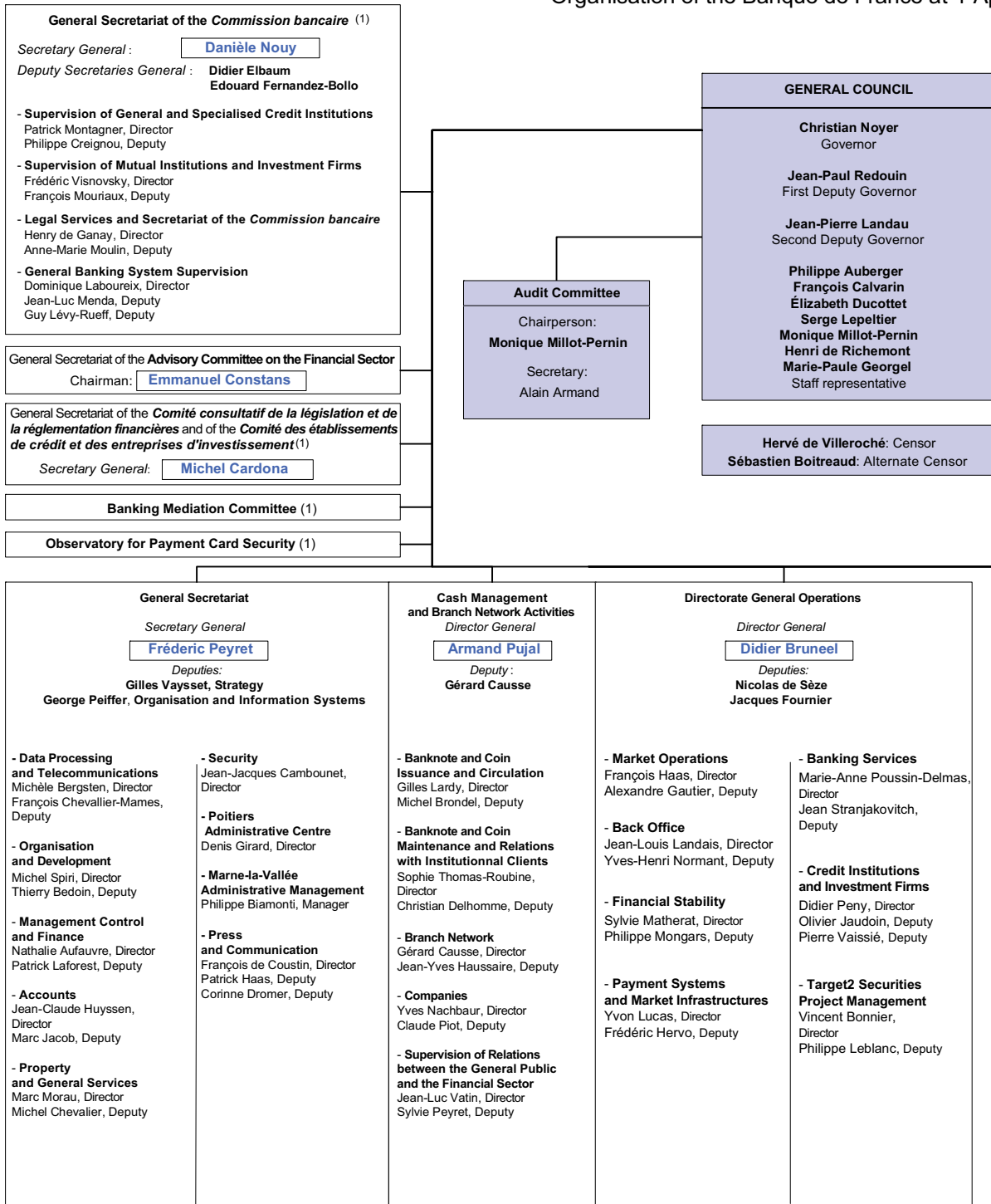


Staff levels

(full-time equivalent positions at 31 December)

	2007	2008
STATUTORY STAFF	11,653	11,521
Male	5,862	5,787
Female	5,791	5,734
Head office	5,243	5,168
Management staff	1,510	1,532
Other categories	3,733	3,636
Branch network	5,636	5,581
Management staff	812	804
Other categories	4,824	4,777
Banknote manufacturing	774	772
Management staff	9	9
Other categories	765	763
CONTRACT STAFF	1,175	1,225
Specially-recruited staff	406	468
Head office	237	284
Banknote manufacturing	169	184
Other staff (excluding occasional staff)	769	757
Security staff	583	574
Cleaning and other staff	186	183
TOTAL	12,828	12,746
Male	6,743	6,707
Female	6,085	6,039

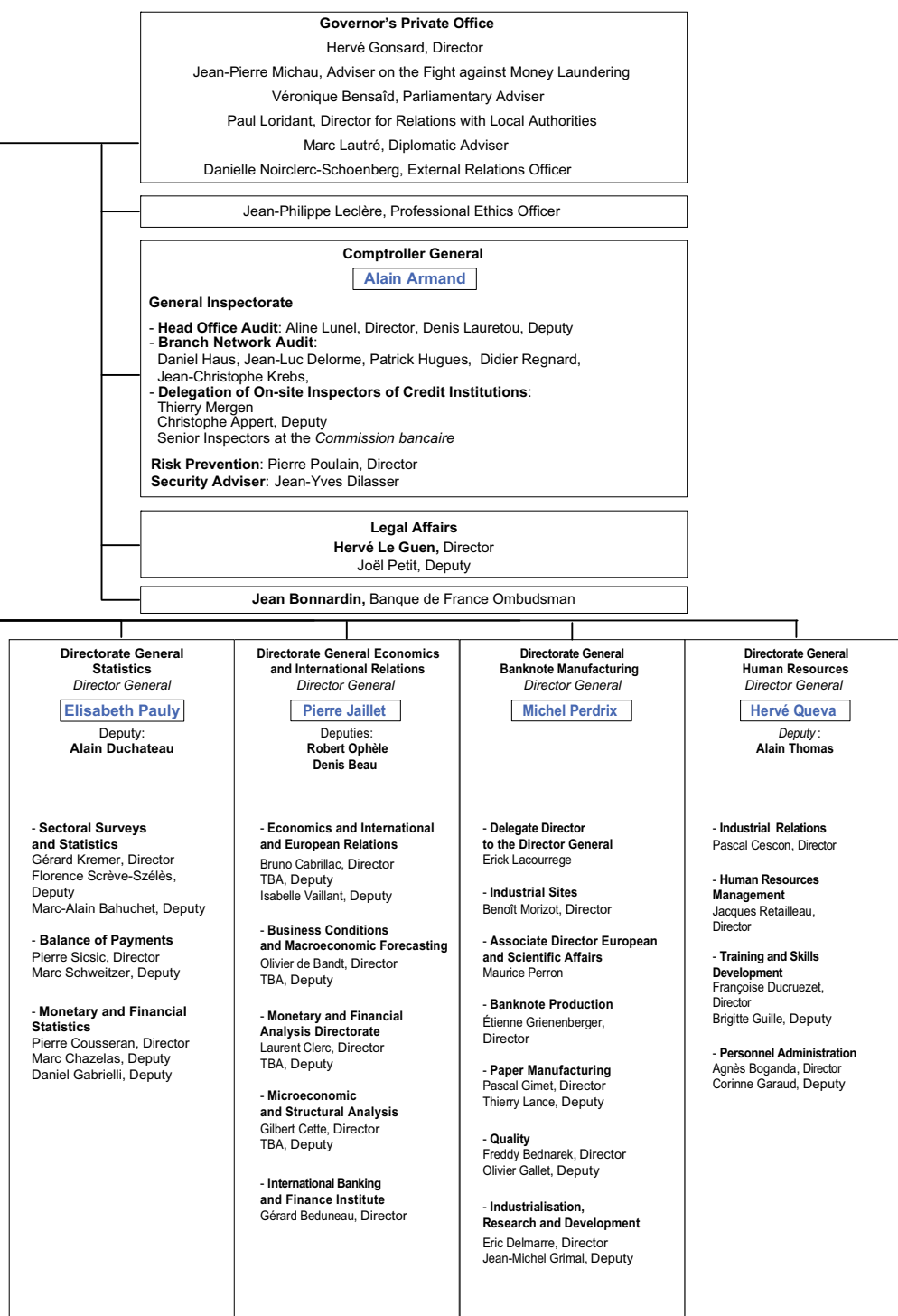
Organisation of the Banque de France at 1 April 2009



Branch Network:

96 *département* directorates including 22 regional head offices

(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.



as well as 21 economic centres, 7 household debt centres and 4 currency circulation management centres.

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