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The Federal Council

Federal Council wants to introduce new tool to strengthen financial sector stability

Bern, 11.03.2022 - The Federal Council is planning to expand its toolkit to strengthen the stability of the financial sector. At its meeting on 11 March 2022, it defined key parameters for a "public liquidity backstop", which would allow the Confederation and the Swiss National Bank (SNB) to bolster the liquidity of a systemically important bank that is in the process of resolution. The Federal Department of Finance (FDF) is to prepare a consultation draft by mid-2023.

The 2007-2009 global financial crisis showed the significance of liquidity for the stability of systemically important banks, and for the entire economy. In order to strengthen systemically important banks' crisis resilience and reduce the risk of economic turmoil, the Swiss legislator is opting for increased capital and liquidity requirements and an improved ability to restructure or liquidate (too-big-to-fail regulations).

For resolution to be successful, there needs to be a credible and practicable resolution plan, sufficient loss absorption by creditors (bail-in capacity) so that the bank can be recapitalised in the event of impending insolvency, and sufficient liquidity. The revised and increased liquidity requirements for systemically important banks, which are due to enter into force on 1 July 2022, should ensure that affected institutions have sufficient liquidity in a wide range of possible crisis situations. This will make them more resilient compared to non-systemically important banks, as required by the Banking Act.

However, even with higher liquidity requirements, situations are conceivable in which a systemically important bank's liquid assets are not enough to perform successful resolution. Already now, the SNB provides second-line additional liquidity in the form of emergency liquidity assistance (ELA).

Confidence-building measure

In the future, in order to increase market participants' confidence in the ability of a recapitalised and solvent systemically important bank to survive, it is planned to provide a third line of temporary additional liquidity via a public liquidity backstop. This is a public measure designed to provide rapid and subsidiary liquidity to a systemically important bank domiciled in Switzerland in the event that this should be necessary for successful resolution. The public liquidity backstop helps to ensure existing or new market participants' willingness to maintain or engage in business relations with the affected bank. Its existence therefore has a preventive effect, before liquidity assistance is even needed. This tool should not be confused with a state bailout of a systemically important bank.

Internationally, a public liquidity backstop is part of the standard crisis toolkit. It increases the chances of a systemically important bank's resolution being successful, and would put Switzerland's systemically important banks on an equal footing with their foreign competitors.

According to the key parameters defined by the Federal Council today, the public liquidity backstop is to be anchored in law. Liquidity assistance for a systemically important bank would be provided by the SNB in the form of a state-guaranteed loan. Moreover, the backstop should have privileged creditor status in bankruptcy, in order to avoid potential losses for the Confederation, and should be predicated on a loss-recovery and sanctioning mechanism.

The Federal Council has instructed the FDF to prepare a consultation draft by mid-2023.

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