

BANK OF FINLAND
76TH YEAR BOOK 1995

REPORT ON ACTIVITIES IN 1995



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The Governor's Review

Finland's commitment to economic discipline, which has a positive influence on monetary stability and sustainable growth, could be seen in many ways in the course of 1995. The Government's decisions on consolidation of public finances and the moderate pay settlements reached in the autumn, along with the appreciation of the markka and a decline in food prices following Finland's accession to the EU, set the stage for a lowering of inflation expectations and a substantial easing of monetary policy.

Finland's total output growth of well over 4 per cent in 1995 ranked among the highest in Europe. However, the growth did slow markedly around the middle of the year. Exports continued to be the main contributor to output growth. On the whole, Finnish export markets expanded rapidly in 1995, but the pace decelerated in the latter half of the year, notably in Europe. The markets for forest industry products in particular weakened in the last few months of the year, albeit in part for reasons of a temporary nature.

The growth of domestic demand also continued at a fairly brisk pace, owing to private consumption and manufacturing investment. Nevertheless, demand in the job-creating services sector remained quite sluggish, as did the demand for housing. Because investment in the manufacturing sector was financed mainly out of retained earnings and because households and companies that focus on domestic markets continued to repay their debts, the demand for credit was highly subdued. Sluggish demand for credit has in turn slowed the improvement in profitability in the banking sector.

Because of export growth and an improvement of about 10 per cent in the terms of trade, the current

account recorded a sizable surplus last year. However, declining export growth in volume terms and in particular a pickup in import volume growth in the latter part of the year signalled the end of the peak phase of foreign debt repayment and an increasing focus of domestic demand on imported goods and services and away from job-creating domestic output.

Inflation remained fairly subdued in 1995, mainly because of temporary factors. The appreciation of the markka led to a decrease in import prices, and there was a substantial fall in food prices following Finland's entry into the European Union.

In spite of robust economic growth, unemployment fell only slightly. Although employment increased to some extent in manufacturing, continued recession in the construction and service sectors proved to be a significant deterrent to the reduction of unemployment.

The early part of 1995 saw a continuation of the moderate tightening of monetary policy that had started in 1994 in response to the rise in long-term interest rates and the strengthening of inflation expectations in the course of 1994. The Bank of Finland raised the tender rate in February and in June by a total of 0.5 percentage point. This was done in response to increased price and cost pressures stemming from pay settlements reached in autumn 1994 and increases in export prices. By emphasizing its commitment to the objective of price stability, the Bank of Finland sought to prevent inflation expectations from spreading throughout the economy.

The narrowing of the differential between Finnish and international long-term interest rates pointed to a gradual dampening of inflation expectations as early as mid-year. Nonetheless, it was not

until the tail end of the year that confidence among money and foreign exchange market participants in a stable economic performance improved to an extent sufficient to provide more room for monetary policy manoeuvrability. Confidence was boosted, in particular, by a moderate pay settlement covering a period of more than two years, which was reached in the autumn, as well as by decisions made on fiscal consolidation and cuts in nonwage labour costs. These measures helped to improve the outlook for achieving price stability, continued steady economic growth and increasing employment. The exchange rate remained stable and long-term interest rates declined further.

During the last quarter of the year, the Bank of Finland lowered the tender rate on four separate occasions, altogether by 1.75 percentage points, and at the end of the year the tender rate stood at 4.25 per cent. The base rate, too, was lowered twice, by 0.5 percentage point in all. In connection with the lowering of the tender rate, the Bank of Finland – in contrast to earlier practice – also published its outlook on inflation and on those factors that influence the inflation outlook.

Growth prospects for the current year are still good, even though slackening growth in the export markets and fiscal stringency on the part of the central government may act to curb total output growth to some degree. Inflation will remain subdued in the next few years, although the temporary dampening factors will no longer exert any influence. This, together with the consolidation of central government finances, will create a good basis for maintaining a low level of interest rates.

The major, and very difficult, challenge facing economic policy is to stimulate job-creating domestic demand in such a way as to sustain price competitiveness in the export sector and a surplus on the current account.

For 1996 the emphasis of employment policy must be on structural change and reform. Moderate pay developments, fiscal consolidation, low inflation, exchange rate stability and the resultant low level of interest rates are necessary but not sufficient conditions for a significant reduction in unemployment.

It is important that structural reform not be brushed aside in an excessive burst of optimism or artificial stimulation of consumer demand. The requirement for a continued surplus on the current account in order to reduce foreign indebtedness means that Finland will need a permanently higher saving rate than the average rate for the last twenty or thirty years. Because of current-account restraints and the sensitivity of interest rates to inflation, improving employment requires that domestic consumer goods and services become increasingly competitive relative to imported goods and foreign services.

In addition to wage restraint, competitiveness can be improved by structural changes in taxation, income transfers and labour markets.

It should be emphasized that the need for continued discipline in economic policy, wage restraint and structural reform is imposed on Finland by its own needs and circumstances, not by the requirements of EU membership.

* * *

The financial result posted by the Bank of Finland for 1995 is weak, as has been the case in the last several years. In the 1990s, the Bank has incurred major losses because of its participation in the management of the banking crisis and because of exchange rate losses stemming from the appreciation of the markka against the major reserve currencies.

Extreme volatility in financial performance in connection with exchange rates and interest rates is an inevitable part of central banking in circumstances such as those that Finland has been facing in recent times. On the other hand, central bank participation in the management of a banking crisis in a capacity other than that of temporary lender of last resort is exceptional. In this case it was necessary, because at the onset of the banking crisis the government did not have the organizational and operational framework needed to manage the crisis. In this situation, the Bank of Finland was obliged to take over a large amount of real estate and other assets. Asset management companies now operating as the Sponda Group were set up later to manage the assets. The ownership of companies involved in business and investment activities is not within the purview of a central bank.

Central bank participation in such matters is not consistent with the principle of central bank independence nor with Finland's obligations under its agreement with the EU. In fact, the Government has, on a proposal of the Parliamentary Supervisory Board, initiated measures aimed at transferring to government responsibility the assets and claims still held by the Bank of Finland as a result of the Skopbank takeover and compensating the Bank for the interest lost on capital tied up in the Skopbank operation. This decision means that all the asset management companies responsible for the final settlement of the banking crisis will be pooled together under government supervision.



Economic Developments

Finland's membership in the EU started off on a favourable note. The economy grew rapidly, particularly at the beginning of the year. The markka appreciated and long-term interest rates declined. Right at the beginning of the year, food prices fell as a result of Finland's EU membership. Competition intensified in sectors which had previously been sheltered, which also helped to restrain inflationary pressures.

Economic policy continued to be aimed at price stability and a stemming of the growth of government indebtedness. These policy aims are also well suited to the requirements of EU membership. Finland's new Government, appointed after the general election in March, announced a programme of cuts in government expenditure covering the whole period up to the next general election. The programme was also confirmed as part of Finland's convergence programme, which was adopted in September and submitted subsequently to the EU Commission and Council of Ministers.

Decisions on consolidation of central government finances, moderate pay settlements reached in the autumn, a lowering of inflation expectations and declining long-term interest rates have laid the ground for sustainable growth. They moreover provide a good basis for the decision concerning Finland's participation in Stage Three of EMU.

Economic slowdown in Europe towards the end of the year

Employment improved only slightly in the EU countries in 1995 even though economic growth was robust in the first half of the year (Chart 1). In the second half of the year there was a slowing of the growth. Although the slowdown was partly attributable to temporary factors, such as a reduction in inventories, there was clearly an increase in uncertainty at the end of the year.

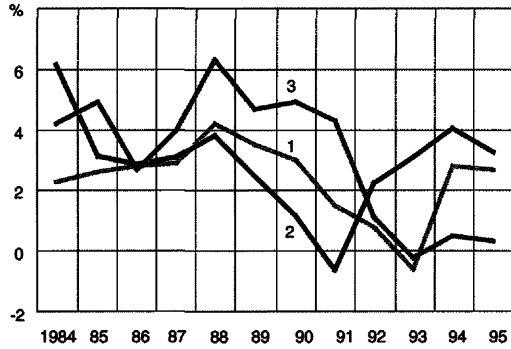
The public sector deficit, which had expanded during the recession, decreased in relation to GDP, though not as fast as targeted. The rate of inflation was slower than expected in Europe, and inflation differentials narrowed. The dampening of inflationary pressures provided room for monetary easing in many European countries.

The relatively rapid economic expansion in the USA, which has continued for four years, pushed the unemployment rate below 6 per cent. The rapid tightening of monetary policy in 1994 seems to have lowered inflation expectations and reduced price pressures. Thus the rise in consumer prices remained subdued in 1995 in spite of rapid economic expansion and occasional depreciation of the dollar. Therefore, the central bank was able to lower interest rates when the first signs of an economic slowdown were detected.

**Chart 1.
ECONOMIC DEVELOPMENTS
IN THE INDUSTRIAL COUNTRIES**

Gross domestic product

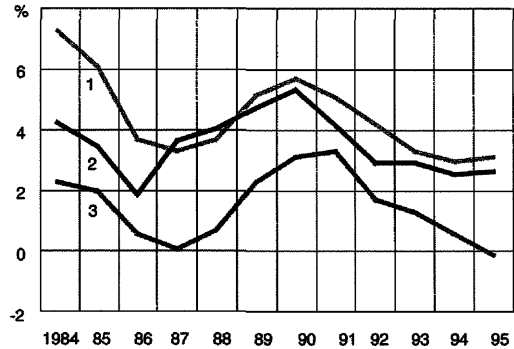
Volume change from the previous year, %



- 1. EU
- 2. USA
- 3. Japan

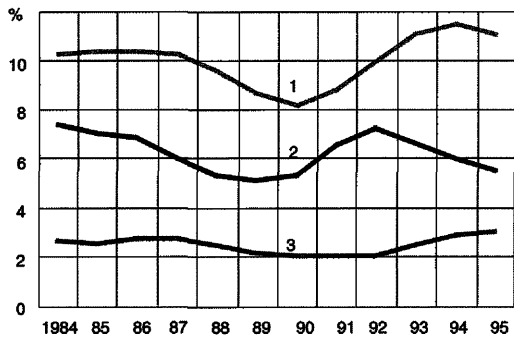
Consumer prices

Change from the previous year, %



- 1. EU
- 2. USA
- 3. Japan

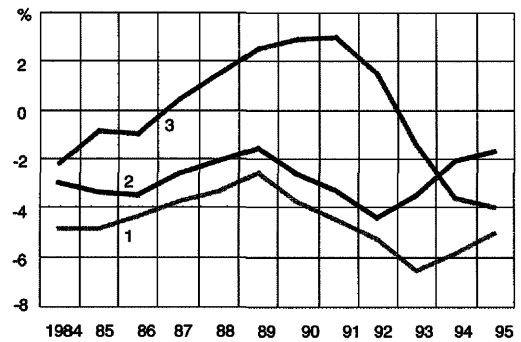
Unemployment rate



- 1. EU
- 2. USA
- 3. Japan

Public sector net lending

% of GDP



- 1. EU
- 2. USA
- 3. Japan

Like the EU countries, the USA is also striving to reverse the growth of public sector indebtedness. In 1995, the deficit fell below 2 per cent of GDP. The decrease was however smaller than in the previous two years (Chart 1).

The Japanese economy has now been stagnant for three years. Fiscal policy was lax in 1995, and the public sector deficit continued to grow. Because of slow growth and because of problems in the banking sector, the central bank lowered its interest rates nearly to zero. Despite a sizable interest rate differential, the yen appreciated rapidly in the spring when trade negotiations between the USA and Japan came to a standstill. However, towards yearend the yen's exchange rate against the dollar returned to its level as at the beginning of the year.

Finnish export markets and exports developed favourably

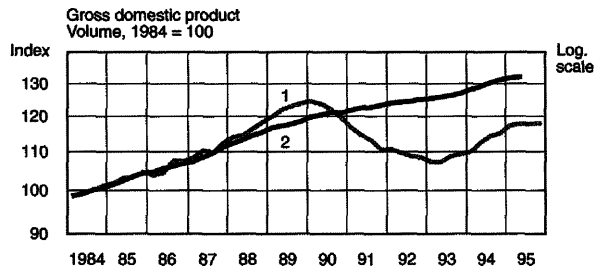
World trade continued to grow rapidly in 1995. International trade was fuelled in particular by rapid growth of US and Japanese imports. In industrial countries trade grew as demand focused on investment in machinery and equipment. In the first half of the year, demand in Europe was boosted by corporate investments while growth in consumption and housing construction remained modest. Dampening of import demand in Latin America as a result of the Mexican crisis was more than offset by demand in the dynamic Asian economies.

Because the growth of imports was relatively slow in Germany and the United Kingdom, the growth of Finnish export markets (export-weighted world trade) was clearly slower than that of world trade. But Swedish imports grew rapidly due to an increase in manufacturing sector investment and in export production.

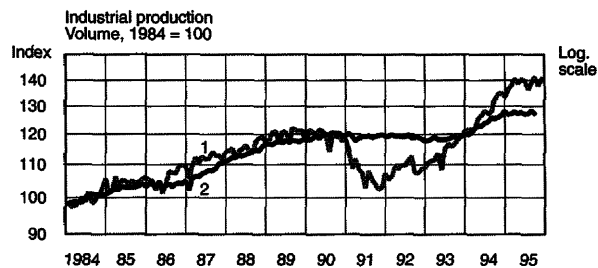
Trade flows between industrial countries were hardly affected by the wide fluctuations in exchange rates in the course of 1995. But the weakening of the dollar during the year lowered the prices in other currencies of some raw materials, especially oil; the depreciation of the Swedish krona lowered world market prices of sawn goods, which in Europe are often invoiced in Swedish kronor.

The volume of Finland's merchandise exports continued to grow vigorously until the summer months of 1995, after which the growth began to level off. On average, exports grew by 6 per cent

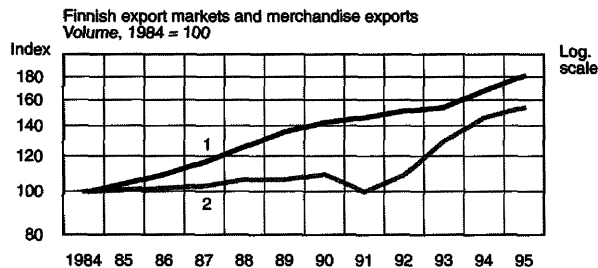
Chart 2. DOMESTIC AND INTERNATIONAL ECONOMIC DEVELOPMENTS



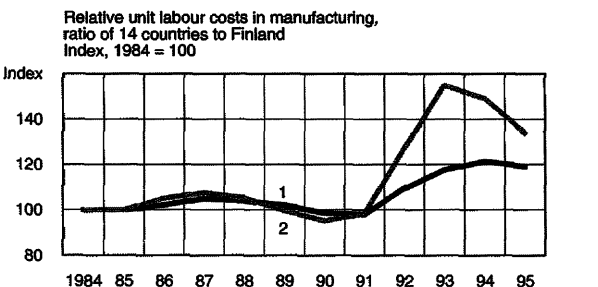
1. Finland
2. OECD countries



1. Finland
2. OECD countries



1. Finnish export markets¹
2. Finnish merchandise exports



1. In national currencies
2. In common currency
¹ Export-weighted, world trade.

from the previous year, ie by less than the growth of export markets (Chart 2). The main factors underlying export growth were continuing strong price competitiveness and a product range that suited international demand. In the course of the year, capacity constraints began to deter export growth in many companies, particularly in the metal and engineering industries. At the end of the year, restrictions were placed on exports of certain forest-based products in order to stabilize sales prices.

The very rapid export growth in the metal and engineering industries was in part attributable to vigorous growth in exports of electronics products. Machinery exports also increased due to a global boom in investment, even though the growth figure was lowered by the postponement of a couple of vessel deliveries until 1996.

Towards yearend, the market for some forest industry product groups started to weaken substantially. Exports of sawn goods met with difficulties

already in the spring, and cutbacks were also experienced in the production of fine paper in the autumn. However, the average export prices of chemical pulp and paper products rose very rapidly; in December export prices of this product group were still 27 per cent higher than a year earlier in spite of the markka's appreciation. In addition to a good market situation, the rise in paper product prices was attributable to the fact that investments in new capacity have remained very subdued globally during the current cyclical upswing.

The rise in export prices in 1995 was fuelled not only by paper products but also by the strengthening of export prices of basic metals. As import prices of oil and oil products fell at the same time, the terms of trade were almost 10 per cent better at the end of 1995 than a year earlier. Thus the terms of trade returned to the level reached in the previous cyclical peak in 1989.

Domestic economic performance

	average				
Exports	4.5	10.0	16.7	13.3	8
Private investment	-5.3	-19.6	-19.5	-0.3	12 ½
Private consumption	0.6	-4.9	-2.9	1.8	4 ½
Total domestic demand	0.1	-5.6	-5.5	3.6	5
– of which: public	0.8	-2.2	-7.0	0.8	½
Imports	3.0	1.1	0.8	12.6	10 ½
GDP	0.6	-3.6	-1.2	4.4	4 ½
	change %				
Earnings	5.8	1.9	0.7	2.0	4 ½
Unit labour costs	3.3	-2.1	-4.6	-2.9	3
Export prices	2.6	4.7	6.4	1.5	7.0
Import prices	2.1	7.6	10.1	-0.2	-0.1
Consumer prices	4.0	2.9	2.2	1.1	1.0
– December to December	..	2.3	1.5	1.6	0.3
Underlying rate of inflation	0.6	2.9	2.6	1.3	..
– November to November	..	3.1	2.7	0.8	-0.5
Unemployment rate, %	9.2	13.1	17.9	18.4	17.2
	per cent of GDP				
Gross investment	21.8	16.7	14.3	15.4	16 ½
Gross saving	19.6	12.1	13.0	16.7	20
Current account = financial balance	-2.2	-4.6	-1.3	1.3	3 ½
– business sector	-2.2	-3.0	2.0	5.0	4 ½
– financial institutions	0.4	-0.1	1.1	0.4	½
– households	-0.2	4.2	3.4	1.9	3
– public sector	-0.1	-5.7	-7.9	-6.0	-5
Net foreign debt	35.5	48.2	54.7	52.5	44

Consumption boosted domestic demand

Domestic demand grew by 5 per cent in 1995, owing to an increase in private consumption and manufacturing investment. By contrast, the recession continued in the construction sector, which was particularly apparent in housing construction. Markka appreciation buoyed demand by increasing disposable income in the household and sheltered sectors. The lowering of interest rates however occurred too late to have an impact on domestic demand in 1995.

Households' real disposable income increased by almost 7 per cent in 1995, though this was partly attributable to the fact that tax refunds were paid twice during the year. The increase in real income derived from a substantial increase in nominal income and sustained low inflation. Households' future prospects were brightened by wage increases and reduced risk of unemployment. As a result, private consumption grew vigorously, by about 4½ per cent.

By contrast, households' activity in the housing market continued to be subdued as the post-recession reluctance to make long-term commitments persisted. The previous year's rise in long-term interest rates tended to maintain the concern that interest rates might start to rise again, which also made households reluctant to borrow. The autumn 1994 pay settlements kindled fears in the spring of a resurgence of inflation, which would in turn put upward pressure on interest rates. On account of this, housing prices declined somewhat in the course of 1995. Even though household indebtedness continued to decrease, a great many households are still burdened by excessive debt (Chart 3).

The financial position of the corporate sector also improved and indebtedness decreased in 1995 (Chart 4). A high capacity utilization rate and a rise in export prices substantially improved the financial results of industrial companies. Domestic costs did not rise as rapidly as in previous cyclical peaks and thus indebtedness in the manufacturing industries is now clearly lower than it was on average in the 1980s (Chart 5).

Investment activity in the manufacturing industries picked up considerably in 1995. Strong profitability and a shortage of capacity increased companies' propensity to invest. Some pending projects were also put on stream when Finland decided

Chart 3.
HOUSEHOLD SECTOR
(incl. nonprofit institutions)

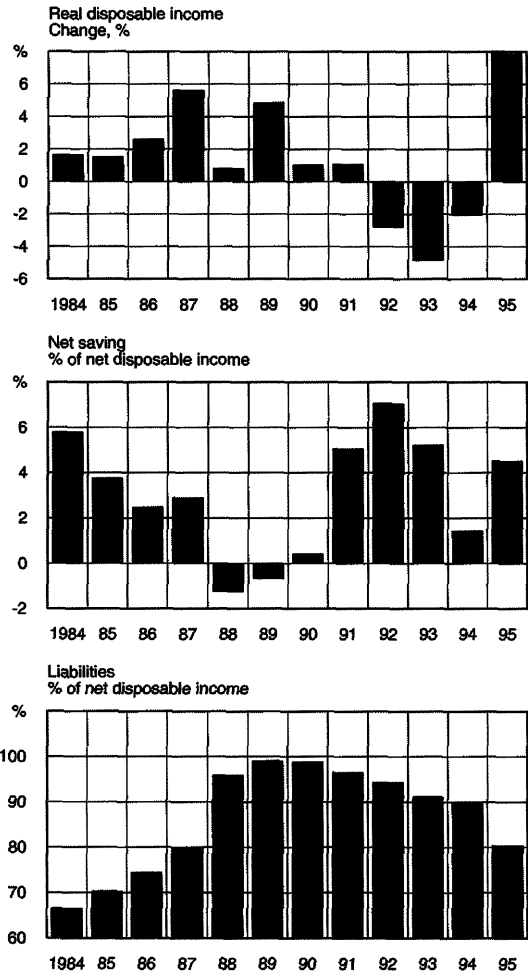
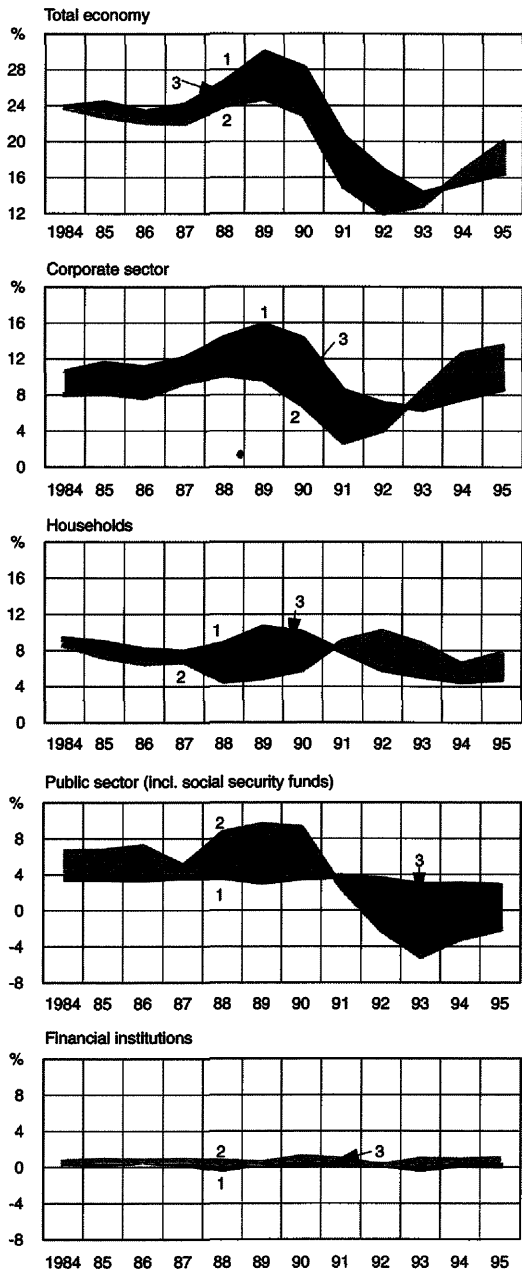


Chart 4.
SAVING AND INVESTMENT RATES

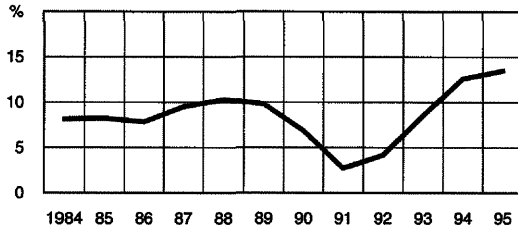
Gross saving and investment,
% of GDP
Saving - investment = net lending



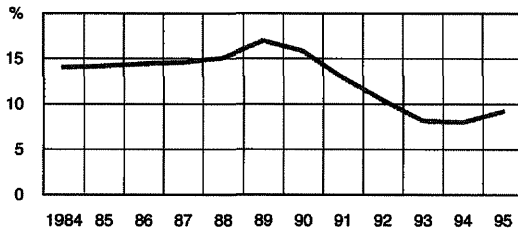
1. Investment
2. Saving
3. Financial position by sector;
whole economy = current account deficit/surplus

Chart 5.
BUSINESS SECTOR

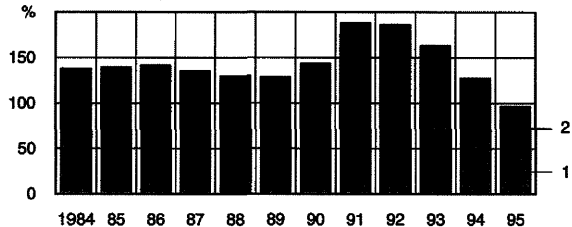
Gross disposable income
% of GDP



Investment in productive capacity
% of GDP

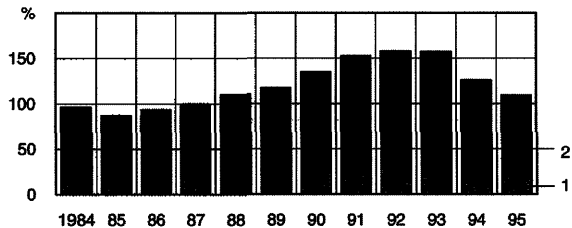


Indebtedness ratio of industry
% of value added



1. Foreign currency debt
2. Markka debt

Indebtedness ratio of other subsectors
% of value added



1. Foreign currency debt
2. Markka debt

to join the EU. In 1995, the investment ratio for manufacturing industries was about the same as in the 1980s, but now companies had little need to borrow.

Companies in non-manufacturing industries improved their financial position somewhat, owing to rationalization and higher consumer demand. However, the level of indebtedness of these companies remained higher than in the mid-1980s. In many sectors, companies operating in the domestic market continued to be burdened by excess capacity relative to demand, so that investment activity remained subdued.

Like the corporate sector, the public sector has had to rationalize operations. Public demand (investment and consumption) increased slightly in 1995 while the ratio of public expenditure (excluding financial investment) to GDP declined.

Rapid growth of total output continued

As in recent years, growth in total output in 1995 was buoyed mainly by the export sector, but output also rose to some extent in other sectors (Chart 6). Total output growth was well over 4 per cent. Output growth in manufacturing began to slow towards the end of the year, partly due to temporary factors. In some manufacturing sectors, capacity constraints curbed output growth. Production stoppages in the forest industry reduced output in the latter half of the year.

Because investment activity in manufacturing focused on machinery and equipment and because households were reluctant to purchase housing, the construction sector remained in a recession. Some large investment projects launched in the manufacturing sector were not yet fully reflected in output figures. Activity in the construction sector expanded only in regard to renovation work.

There was hardly any improvement in employment in the service sectors and other sectors serving the domestic market. The large pay increases at the end of 1994 together with the wide tax wedge were among the factors impeding an improvement in the employment situation. The manufacturing sector was the only sector in which employment clearly expanded. Due to an increase in the labour supply, the unemployment rate decreased by less than would have been expected on the basis of the increase in employment. Thus the unemployment rate decreased only slowly and remained high, at 17.2 per cent on average (Chart 7).

Chart 6.
PRODUCTION

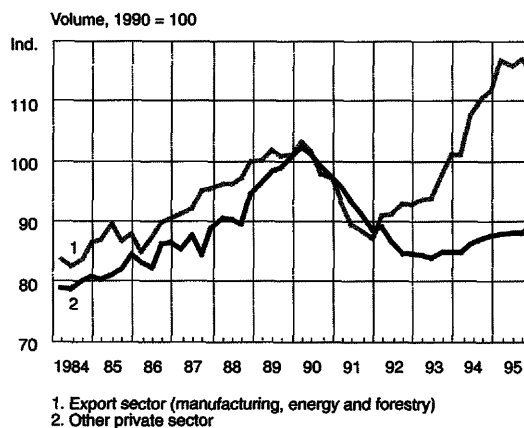
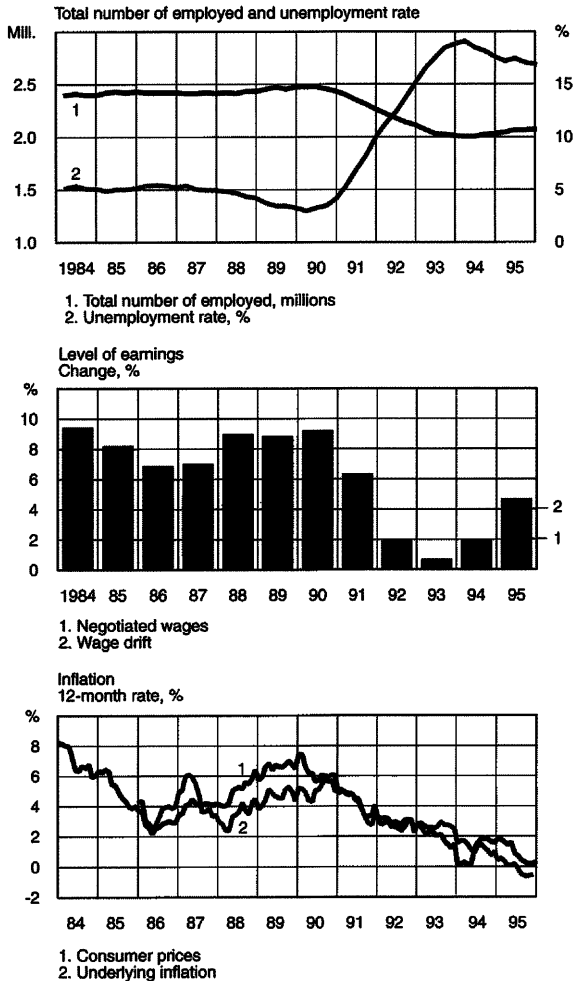


Chart 7.
LABOUR MARKET, WAGES AND PRICES



Because of the persistently high unemployment rate, the Government submitted an employment programme to Parliament. The main feature of the programme was the lowering of indirect labour costs by 1.5 percentage points on average. The programme also aims at enhancing labour market flexibility.

Inflation remained low

The major influence on consumer prices was the drop in food prices that followed Finland's entry into the EU. Food prices had already begun to decline at the end of 1994. The decline was most noticeable in the early months of 1995 and again in the autumn. Thus EU membership will still have a significant, though temporary, effect on twelve-month changes in the consumer price index in 1996. Had it not been for the decline in food prices, the increase in indirect taxes would have raised the rate of increase in consumer prices from just under 2 per cent to about 3 per cent in the first half of 1995.

In the first half of 1995, rising labour costs and inflation expectations stemming from the implementation of autumn pay settlements posed a potential threat to price stability. There were concerns that robust profits would, as usual, spill over into domestic costs, and indeed the level of economy-wide earnings did rise by an average of about 4.5 per cent from the previous year (Chart 7). The increase in productivity did not quite compensate for the rise in labour costs and the resulting rise in unit labour costs led to a clear increase in inflationary pressures.

The inflationary pressures were however muted by the appreciation of the markka, which resulted in a modest decline in import prices. The prices of consumer goods and oil in particular fell substantially. The markka's appreciation also curbed the pass-through of cost increases to prices. Thus, exchange rate developments worked in conjunction with lower food prices to hold down inflation expectations.

Declines in food and import prices have a stronger impact on the indicator of underlying inflation than on the consumer price index. This is because the indicator excludes the effects of housing prices, interest rates and indirect taxes. Indeed, the twelve-month change in underlying inflation has been negative since the summer months.

Over the course of 1995, the low (about 2 per cent) inflation target won increasingly broader acceptance. Both sides of the labour market considered it essential to achieve a long-term pay settlement that would keep wage costs under control. This resulted in a centralized, slightly over two-year, wage agreement covering virtually all wage and salary earners. Thus inflationary pressures arising from contractual wages will remain clearly more modest in 1996–1997 than they were in 1995.

Growth of central government deficit came to a halt

The central government continued to borrow heavily in the early part of the year as temporary factors boosted expenditures and reduced revenues. The central government's financial position however improved towards the end of 1995, and the net borrowing requirement, FIM 63–64 billion, was smaller than in the previous year. Central government revenue increased by 10 per cent on the previous year and expenditure increased by 7 per cent.

Interest expenditure on central government debt continued to grow. By contrast, income transfers to households decreased by more than 4 per cent, to about FIM 42 billion, partly because of an improvement in the employment situation. The rapid growth in total wages and salaries and a pickup in consumption increased central government revenue. Total revenue from income and property taxes was 15 per cent higher than in the previous year.

The new Government, which took office in March 1995, took a number of measures to stop the build-up of public sector debt. These measures however had only a minor impact on borrowing in 1995. According to the Government programme, the central government's discretionary expenditures will be cut by some FIM 21 billion by the time of the next general election. If expenditure cuts beginning in 1991 are included, total savings will amount to as much as 8 per cent of the value of total output in 1999 (Chart 8). The employment programme drawn up in the autumn will not be a major burden on central government finances.

Including the surpluses posted by local governments and social security funds, the general government deficit in 1995 amounted to some 5.5 per cent of GDP. According to the same convergence criteria, the general government debt stood at 60 per cent of GDP at the end of the year (Chart 9). By contrast,

Chart 8.
CUTS IN CENTRAL GOVERNMENT OUTLAYS,
1991-1999

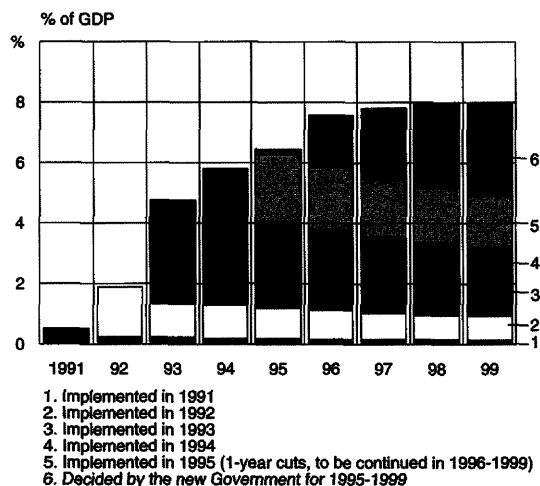


Chart 9.
PUBLIC FINANCES
(% of GDP)

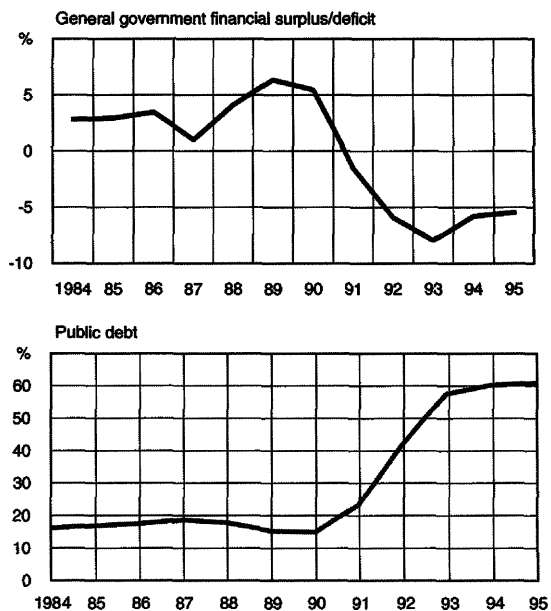
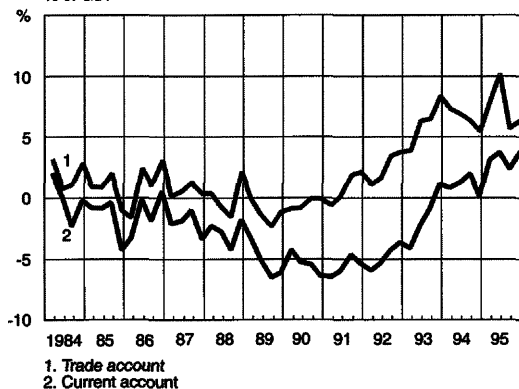
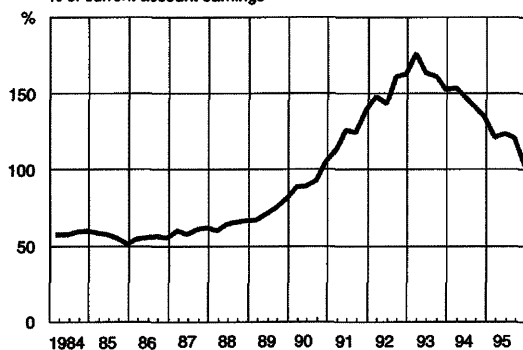


Chart 10.
EXTERNAL BALANCE

Trade account and current account
% of GDP



Net foreign debt
% of current account earnings



central government debt continued to grow rapidly, to FIM 359 billion, which was 65 per cent of GDP.

Consolidation of the central government financial position requires cuts in public expenditure over several years. Without such cuts, it will be impossible to change the tax system so as to improve the employment situation and narrow the tax wedge. The new Government announced a programme of expenditure cuts spanning the whole period up until the next general election. The same measures were also included in Finland's convergence programme as submitted in September to the EU Commission and Council of Ministers. The programme was favourably received at the ECOFIN meeting in October. According to the programme, Finland will meet the deficit criterion for Stage Three of EMU as early as 1996 and the public debt criterion in 1999 or, in the fast growth scenario, as early as 1997.

Current account posted a surplus

The trade account showed a surplus of FIM 42 billion in 1995, which was considerably larger than in the previous year. Towards the end of the year, the growth in export volume came to a halt while imports, boosted by domestic demand, continued to grow throughout the year. Even though the volume of imports grew more than that of exports, the trade account surplus remained large because of a notable improvement in the terms of trade.

Of the other items in the current account, the services balance strengthened noticeably from the previous year. Earnings from transport grew more rapidly than expenditures stemming from increased travel abroad. The appreciation of the markka and decrease in foreign debt strengthened the investment income account. Membership fees paid to the EU were of the same magnitude as subsidies received from the EU.

The current account surplus in 1995 amounted to FIM 19 billion, which was clearly more than in the previous year. This surplus enabled Finland to reduce its net foreign debt, which is large by international standards. The ratio of current account surplus to GDP was about 3.5 per cent (Chart 10). For domestic sectors, the strengthening of the current account surplus meant a considerable strengthening of the financial position of the private sector (especially companies) in comparison with the previous year (Chart 4).

Monetary Policy

The environment was generally favourable for the conduct of monetary policy during 1995. Inflation expectations subsided, and despite some disturbing international factors the markka remained stable. The external balance continued to strengthen, and yields on long-term bonds declined substantially.

The rise in inflation expectations that accompanied the strong performance of the economy in the early part of the year and the increase in inflationary pressures stemming mainly from the cost side limited the room for monetary policy manoeuvring through the first three quarters of the year. The Bank of Finland raised the tender rate in February and June, but during the latter half of the year it became possible to loosen monetary policy. Of particular importance were certain decisions made regarding central government finances and the labour markets. Consistency in the conduct of economic policy provided the preconditions for achieving a stable economy: low inflation, strong competitiveness, consolidation of central government finances and an improving employment situation. Because the credibility of economic policy had improved and inflation expectations had subsided, conditions were favourable for a decline in the level of interest rates. Hence the Bank of Finland lowered both the tender rate and the base rate in the latter part of the year.

Interest rate policy eased and the markka appreciated towards the end of the year

The cautious monetary tightening that had started in 1994 continued as the Bank of Finland raised the tender rate by 0.25 percentage point to 5.75 per cent in February (Chart 11) and again by 0.25 percentage point in June. The rate increases were necessary because inflation expectations had risen and cost pressures had increased. Long-term interest rates were at their highest at the beginning of the year, after which they declined steadily. Short-term rates, on the other hand, peaked in June and declined in the latter half of the year.

Because actual inflation remained low and the credibility of the inflation objective improved, economic agents began to revise downward their inflation expectations and the markets began to expect lower interest rates (Chart 12). It was also anticipated that the inflation rate would remain subdued in the coming years despite the presence of temporary price pressures. Because, in addition, central government finances had improved and exceptionally modest wage settlements had been concluded, there was room in the autumn for an easing of monetary policy. This opportunity was used to cut the tender rate by 1.75 percentage points to 4.25 per cent in

October–December. The base rate was cut from 5.25 per cent to 5 per cent at the beginning of November and again to 4.75 per cent as from 15 December.

The ultimate target for monetary policy remained unchanged throughout the year: an inflation rate of about 2 per cent over the medium term. Policy-instrument settings were based on the Bank of Finland's outlook for future inflation. In forming the outlook for prices, various forecasts and indicators of economic performance were utilized. More precise evaluations than earlier were published for example in the regular quarterly article of the Bulletin 'Economic developments, inflation and monetary policy' as well as in a separate press release in October. In the course of the year the tender rate became firmly established as a key instrument of monetary policy.

The disturbances that occurred in the international currency markets had no noticeable effect on the value of the markka. As the Bank of Finland intervened to a lesser extent than in previous years, the value of the markka was freely determined by market forces. In terms of both the trade-weighted currency index and the ECU basket, the markka appreciated substantially in the course of the year. In the beginning of the year and in the autumn, interventions were carried to prevent the markka from depreciating too rapidly; in April and August upward pressure on the markka was restrained (Chart 13). The Bank of Finland's forward position increased in the beginning of the year and in August when forward transactions were used to partially offset liquidity-draining effects of capital movements. In March–May and in the latter part of the year, with calm prevailing in the foreign exchange markets, the forward contract portfolio was allowed to shrink as forward contracts matured. The central government did not borrow from abroad in net terms in 1995, which in part enabled a decrease in the Bank of Finland's foreign exchange reserves and forward position. Towards the end of the year the Bank of Finland restricted fluctuations in the markka's value to a somewhat narrower range than before. As measured by the trade-weighted currency index, the markka appreciated by about 3 per cent during the year.

Chart 11.
KEY INTEREST RATES

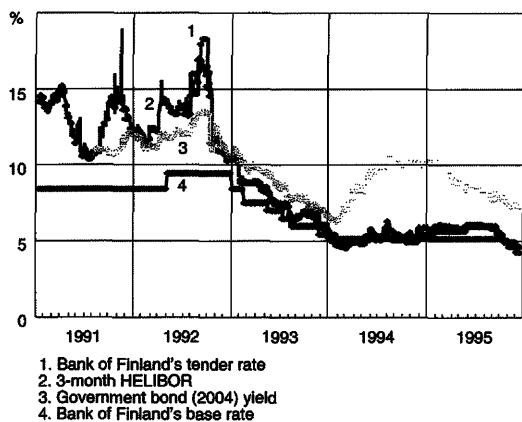
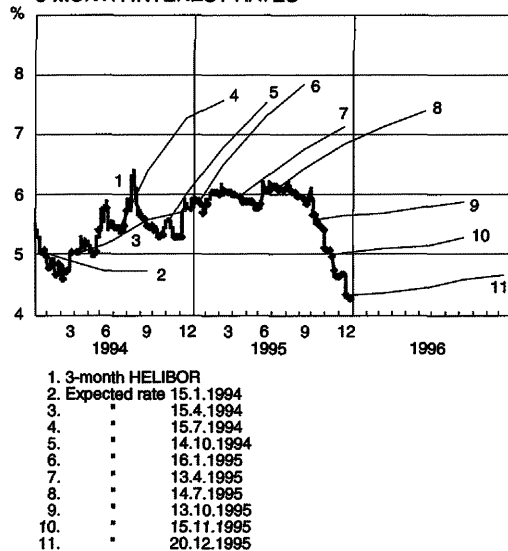


Chart 12.
ACTUAL AND EXPECTED
3-MONTH INTEREST RATES¹



¹ Expected rates based on forward rates.

Disturbances in the international money and currency markets

The international money and currency markets experienced some turbulence in late 1994 and early 1995 as Mexico's economic problems came to a head. In January–April the US dollar depreciated by about 13 per cent against the Deutschemark and 19 per cent against the Japanese yen (Chart 14). In Europe the effects of the Mexican crisis were felt most poignantly in January in the Spanish, Italian and Swedish money markets.

The disturbance in the currency markets peaked at the beginning of March. Exchange rates between the currencies in the European exchange rate mechanism (ERM) approached the system's fluctuation limits (Chart 15). The Spanish peseta came under such heavy downward pressure that the Monetary Committee of the European Union, at the request of Spain, held a meeting on 5 March. It was decided to devalue the peseta by 7 per cent and the Portuguese escudo by 3.5 per cent against the other ERM currencies.

At the end of March the German central bank cut its discount rate by 0.5 percentage point to 4 per cent and its monetary policy benchmark repo rate from 4.85 per cent to 4.5 per cent. The central banks of Switzerland, Belgium, Austria and Holland followed the German example by cutting their rates (Chart 16). In Germany money supply growth was at the time below the target range and inflation was slowing.

In the first half of July the United States' central bank (Federal Reserve), as expected, cut its target short-term interest rate, the federal funds rate, by 0.25 percentage point to 5.75 per cent. Prior to the cut, the rate had been raised seven times in succession. The discount rate was held unchanged at 5.25 per cent. The reason for the rate cut was the presence of signs that US economic growth was slowing. The central banks of Japan, France, Denmark and Canada moderately eased their monetary policy in line with US policy. As interest rates in the US declined, long-term rates also declined in Europe.

The easing of monetary policy continued in August when the German central bank cut its rates by 0.5 percentage point: the discount rate to 3.5 per cent and the Lombard rate to 5.5 per cent. The main reasons for the cuts were the decline in the M3 mon-

Chart 13.
BANK OF FINLAND'S MONEY MARKET
OPERATIONS AND INTERVENTION
IN THE FOREIGN EXCHANGE MARKET

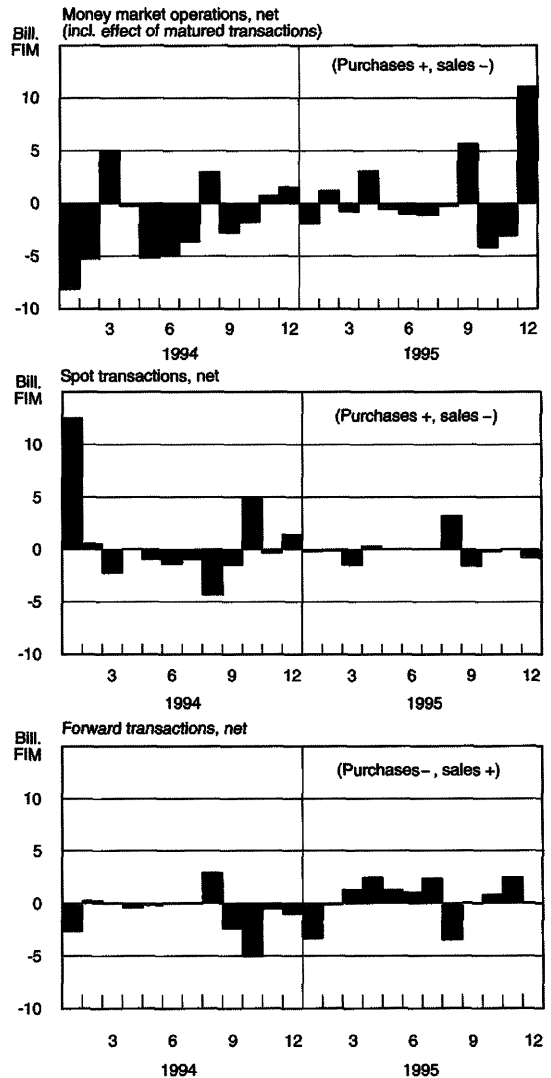
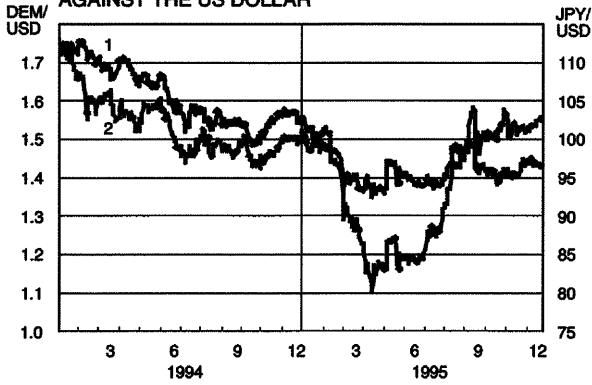


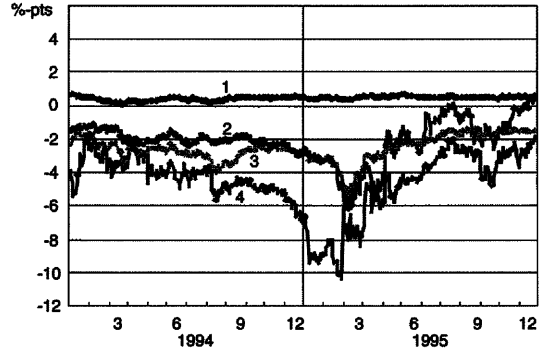
Chart 14.
DEUTSCHEMARK AND YEN EXCHANGE RATES
AGAINST THE US DOLLAR



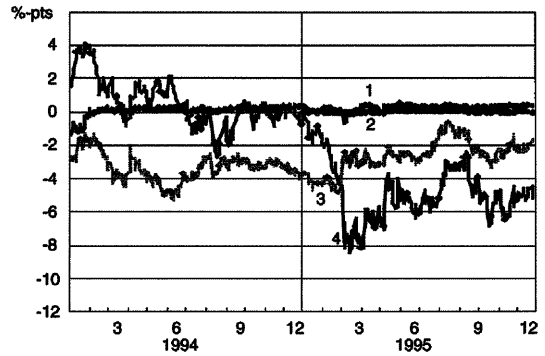
- 1. DEM/USD (left scale)
- 2. JPY/USD (right scale)

Rising curve means dollar appreciation.

Chart 15.
DEVIATIONS OF ERM-CURRENCY EXCHANGE RATES
FROM THEIR CENTRAL DEM RATES



- 1. Netherlands
- 2. France
- 3. Denmark
- 4. Spain



- 1. Belgium
- 2. Austria
- 3. Portugal
- 4. Ireland

Rising curve means currency appreciation.

etary aggregate and the favourable inflation picture. Nearly all countries participating in the ERM followed the Bundesbank's example.

In early August the dollar began to strengthen against the other major currencies. The magnitude of the dollar's fluctuations can be seen in the fact that at the end of August the dollar was 21 per cent stronger against the yen that it had been at mid-April, at its weakest point. Against the Deutschemerk the dollar appreciated 7 per cent in the first half of August.

Discussions on the third stage of Economic and Monetary Union and of which countries would be eligible had an impact on the currency markets in the autumn. At the beginning of October the French franc started to weaken rapidly against the Deutschemerk. Interest rates in France, Spain and Italy rose substantially again at the end of October. The problems of the French Government in connection with its programme of spending cuts were not reflected in the money markets.

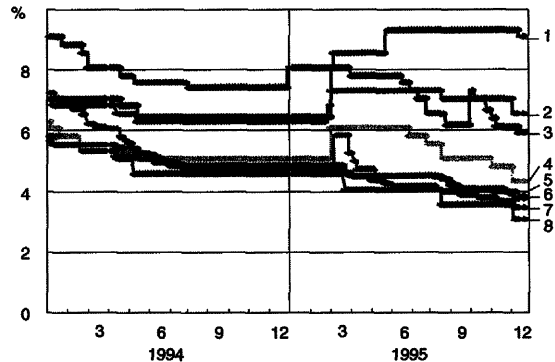
During the latter part of the year signs of slower-than-forecast economic growth in the European economies provided room for a significant decline in long-term interest rates. Because inflationary pressures were subdued at the time, expectations firmed for another easing of central banks' monetary policy. And on 14 December the Bundesbank cut both its discount and Lombard rates by 0.5 percentage point, to 3 per cent and 5 per cent respectively, and set its repo rate at 3.75 per cent.

The international money and currency markets were susceptible to disturbances throughout the year. The main problem was the exchange value of the dollar, especially against the yen. The central banks supported the dollar on numerous occasions. The banking crisis in Japan also cast a shadow over the international capital markets. Discussion of the eligible countries and timetable for EMU again demonstrated that as the starting date for Stage Three approaches the markets become more and more sensitive to this type of discussion.

The Bank of Finland cut the tender rate in the latter part of the year

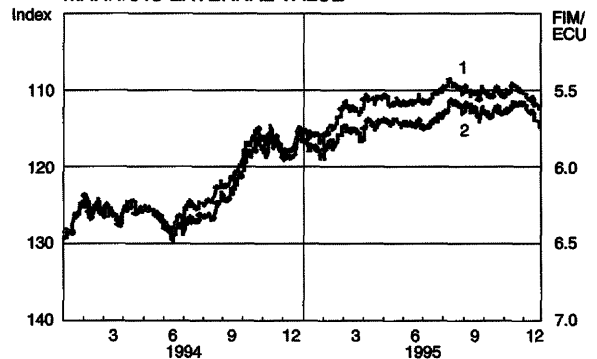
The disturbances in the international money and currency markets in the early part of the year did not have a significant impact on Finland (Chart 17). The strengthening in the external value of the markka during 1994 derived from the surplus

Chart 16.
ERM-COUNTRIES' CENTRAL BANK RATES



1. Spain: repo rate
2. Ireland: short-term facility rate
3. France: repo rate
4. Denmark: discount rate
5. Belgium: tender rate
6. Austria: refinancing rate
7. Netherlands: special advance rate
8. Germany: discount rate

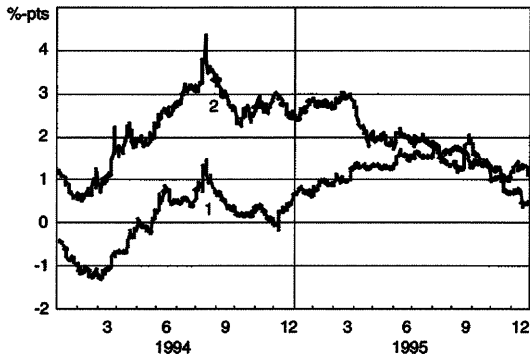
Chart 17.
MARKKA'S EXTERNAL VALUE



1. Trade-weighted index, 1982 = 100
2. Markka's exchange rate against the ECU

Rising curve means markka appreciation.

Chart 18.
DIFFERENTIAL BETWEEN DOMESTIC AND
FOREIGN INTEREST RATES



1. 3-month HELIBOR less 3-month euro-DEM rate
2. Finnish government bond (2004) yield less German
10-year government bond yield

on the current account and robust growth of the economy as well as from a general increase in confidence in the Finnish economy. Finland had succeeded in consolidating its central government finances, and entry into the EU at the beginning of the year helped to increase confidence in the economy. The disturbances in the international markets were reflected only mutedly in the Finnish markets, mainly by way of Sweden. In January the external value of the markka weakened by about 1 per cent as measured by the trade-weighted currency index; the level of interest rates remained stable.

The Bank of Finland had raised the tender rate in its volume tender in December 1994. The central role of the tender rate as an instrument of monetary policy was strengthened in 1995. The Bank of Finland raised the tender rate in February by 0.25 percentage point to 5.75 per cent. The backdrop for the increase was a substantial rise in both inflation expectations for a few years ahead and cost pressures. Rises in export prices, wages and domestic raw materials prices entailed an increased danger of inflation.

Short-term interest rates rose in February, in line with the tender rate increase, while yields on long-term bonds declined somewhat due in part to a decline in international, particularly US, long-term rates. The longest-term rates however stayed above 10 per cent in Finland. The differential vis-à-vis the German three-month rate widened by about 0.3 percentage point in January–February, to nearly 1 percentage point. The differential on long-term rates was about 2.8 percentage points at the end of February (Chart 18). The markka nonetheless appreciated substantially in February, by 3.8 per cent as measured by the trade-weighted currency index. The main reason for the appreciation was the weakening of the dollar and the Swedish krona.

The quick formation of the Government as well as the positive reception afforded its programme of spending cuts resulted in a decline in long-term bond yields of more than 1 percentage point in April. The interest rate differential vis-à-vis Germany narrowed correspondingly to 2 percentage points. Because of declining long-term interest rates, the yield curve had flattened out considerably since the beginning of the year. This reflected not only increasing confidence in Finland's economic policy but also declining inflation expectations.

Market confidence in Finland's economic policy could be seen in the foreign exchange market. At the end of April the markka's exchange value as measured by the trade-weighted currency index was 4.2 per cent higher than at the end of 1994. The Bank of Finland's policy on intervention in the foreign exchange market continued in the early part of the year on the same basis as had been the case since the markka was floated. The markka's exchange rate was allowed to fluctuate freely in response to market forces, except when the Bank of Finland acted to smooth out exaggerated short-term gyrations.

In June the Bank of Finland raised the tender rate to 6 per cent owing to the presence of price pressures in the economy. The Bank's particular interest here was to prevent inflationary pressures from building up and spreading throughout the economy. The Bank of Finland also wanted to underline its commitment to the inflation target. The surge in export prices, with its various repercussions, could have jeopardized price stability over the long term. The presence of inflationary pressures was also indicated by wage increases already in effect and uncertainty regarding upcoming wage settlements. The Bank of Finland noted that exchange rate movements and wage settlements have a major impact on future price stability, which in turn must be ensured as a necessary precondition for the continuance of job-creating growth. After the tender rate increase, short-term market rates rose to the same level, whereas the timing of increases in long-term rates generally coincided with rate hikes in the international markets.

The markka had remained stable in May-June, but it appreciated during the summer, reaching a high for the period of the float at mid-August. Successful budget negotiations, growing confidence in a moderate wage settlement, low and stable inflation, and a more-favourable-than-expected external balance all helped to push down market interest rates and strengthen the markka in August. At the same time, expectations of lower interest rates increased substantially. The Bank of Finland purchased foreign exchange in the early part of August when the markka was appreciating rapidly and sold foreign exchange right at the end of the month as the markka weakened. The markka depreciated when the Deutschemark surged in the international currency markets. After the currency markets had calmed, the decline in the level of international interest rates

also pulled domestic rates down. Central banks in many EU countries also lowered their rates in August. Long-term rates however fell further in Finland than in many other EU countries. At the end of August Finland's longest-term interest rate was some 1.5 percentage points higher than in Germany and some 2 percentage points lower than in Sweden. The longest-term rate declined to 8 per cent, which was just slightly higher than corresponding rates in Denmark and the United Kingdom.

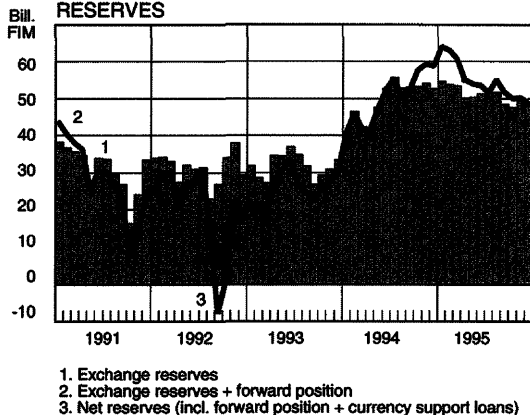
At the beginning of October the Bank of Finland cut the tender rate by 0.5 percentage point to 5.5 per cent and the base rate by 0.25 percentage point to 5.0 per cent. The cuts were based on a favourable inflation performance and an easing of longer-term inflationary pressures. In connection with the rate cuts, the Bank of Finland published a precise forecast of the trend of inflation and of the factors that could affect the trend. This was the first time while the markka has been floating and the inflation target has been in place that the Bank has published its forecast of the trend of inflation. Due to the rise in wages and to the perceived end of the influence of the decline in food prices connected with EU membership, consumer price inflation was expected to accelerate temporarily in late 1995 and during 1996. With a slowing of the rise in costs, underlying inflation was expected to return to the target rate of about 2 per cent in 1997.

The interest rate cut and the published inflation forecast were well received by the markets. The budget and wage settlements and the Government's employment programme had given the markets a positive tone, which was further enhanced by the positive reception afforded Finland's convergence programme for Economic and Monetary Union at a meeting of the Council of the Economic and Finance Ministers (ECOFIN). The credibility of economic policy was strengthened by these actions, and the Bank of Finland continued its policy of lower interest rates by cutting the tender rate by 0.5 percentage point on 1 November and 0.25 percentage point on 20 November. After these cuts, the tender rate stood at 4.75 per cent, a level last seen at the beginning of 1994.

At the end of November the Bank of Finland also lowered the base rate by 0.25 percentage point to 4.75 per cent, effective 15 December.

In December the Bank of Finland lowered its inflation forecast and cut the tender rate to 4.25 per

Chart 19.
BANK OF FINLAND'S FOREIGN EXCHANGE
RESERVES



cent. A weakening international economy and a further lowering of food prices owing to enhanced competition led to a revision of the forecast for underlying inflation to significantly less than 2 per cent per year over 1996–1997. Along with the tender rate cuts in November–December, the interest rate on excess reserves was lowered to 2.25 per cent.

Following the Bank of Finland's policy actions, interest rate differentials vis-à-vis Germany narrowed to less than 0.5 percentage point on three-month instruments and 1.3 percentage points on long-term instruments. The short-term interest rate differential at the end of the year was about the same as at the end of 1994 whereas the long-term differential narrowed by 1.5 percentage points. The one-year HELIBOR rate hit all-time lows when it fell below 4.9 per cent at the end of November and then to 4.5 per cent in December. The yield on the nine-year government bond fell to about 7.4 per cent in November and ended the year at 7.2 per cent. The decline in interest rates had no effect on the external value of the markka. From August until the end of the year the markka's exchange rate against the Deutschemark fluctuated above and below 3:1.

The total external debt declined and the central government's external debt stopped growing

Finland's net external debt, taking into account direct investments, declined by FIM 26.5 billion during the year, to FIM 240.6 billion. The debt fell largely because of price changes in Finnish securities held by foreigners. Price declines in securities amounted to FIM 6.3 billion. Relative to aggregate output, the level of the net debt declined to about 45 per cent.

The foreign exchange reserves (Chart 19) increased at the beginning of the year, owing to capital imports by the central government, and were at their highest in January. In the course of the year, the central government changed over almost entirely to markka-denominated financing and paid down its foreign currency-denominated debt. This resulted in a FIM 3.9 billion decline in the foreign exchange reserves in the course of the year.

The central government's net external debt turned down during the year but still accounted for over half of the total external debt. The central government did not import capital from abroad in net

Balance of payments, million FIM

		I	II	III	IV	I-IV
Trade balance	33 339	11 469	14 191	8 400	7 800	41 860
A. CURRENT ACCOUNT	6 627	3 436	5 938	4 743	4 976	19 094
B. CAPITAL AND FINANCIAL ACCOUNT	18 877	-1 745	-7 226	-6 335	-5 267	-20 573
Direct investment	-14 207	369	-2 639	-998	650	-2 618
Portfolio investment	39 217	-14	-3 042	3 411	-411	-57
Loans	8 107	901	-3 056	-4 236	1 752	-4 639
Other	-14 239	-3 001	1 511	-4 512	-7 258	-13 260
A.+B. CHANGE IN FOREIGN EXCHANGE RESERVES (Increase +, decrease -)	25 504	1 691	-1 288	-1 592	-291	-1 480
Memorandum item:: Central government's capital transactions, net	31 165	5 889	-7 021	987	-453	-598

* Preliminary.

terms, as the demand for markka-denominated debt instruments was firm in the domestic markets. Insurance companies in particular expanded their portfolios of central government paper owing to a shortage of alternative safe investment outlets. Foreigners, on the other hand, sold back to Finland their holdings of markka-denominated central government debt to the amount of FIM 2.3 billion.

The foreign debt of the corporate sector increased in April–September because of a significant increase in investment in Finnish securities, especially Nokia shares. Thus the value of Finnish shares held by foreigners grew by over FIM 30 billion. However, as the price of Nokia's shares plummeted in the latter part of the year the amount of these holdings fell again, to FIM 63.7 billion at the end of the year. Private firms continued to pay down their foreign currency-denominated loans during the year. The stock of such loans from domestic banks declined from FIM 46 billion at the end of 1994 to FIM 26 billion. Firms increased their hedging of export receivables in the forward markets by FIM 12 billion in connection with the markka's appreciation.

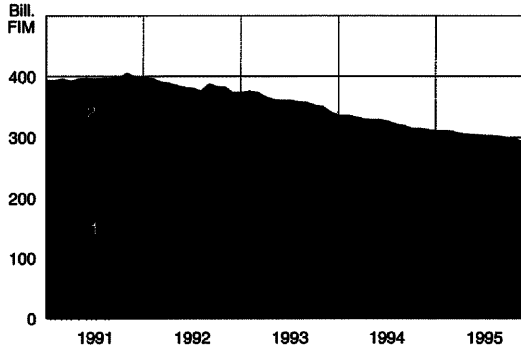
The demand for bank loans¹ recovered slowly and the monetary aggregates recorded moderate growth

The decline in outstanding bank loans, which has continued for several years, slowed in 1995 (Chart 20). The markka-denominated stock stood at some FIM 264 billion at the end of the year. The stock of business loans remained for the third year in a row at slightly over FIM 80 billion. The importance of share and bond issues in firms' financing programmes clearly diminished from the previous two years while the importance of earnings as a source of financing increased. The decline in the stocks of both housing and consumer loans to households came to halt around the middle of the year.

The margin between the average rates on banks' lending and funding was about 4.9 percentage points through most of the year but fell slightly at the end of the year. Interest rates on new loans rose in January–July, reflecting the Bank of Finland's interest rate policy and the rise in market rates. The rise in interest rates was especially visible

¹ Outstanding bank loans at the end of 1995 include lending by Savings Bank of Finland and Siltapankki, both of which were converted into asset management companies in December.

Chart 20.
BANKS' OUTSTANDING LENDING



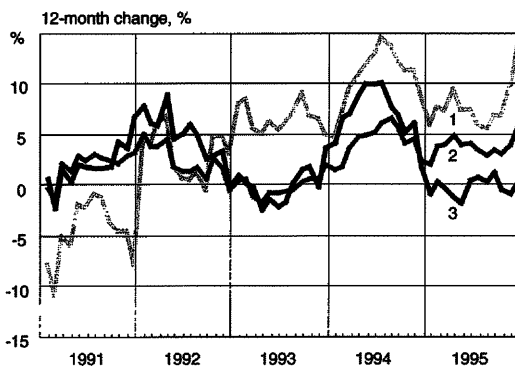
1. Markka lending to the public
2. Foreign currency lending to the public

in business loans, on which the average rate was 8.0 per cent in July. The last time the rate had been as high was in November 1993. The rise in interest rates in the early part of the year did not yet have any impact on new housing and consumer loans to households, the rates on which were fairly stable in the early part of the year, at about 8.5 per cent and 10 per cent respectively. After mid-summer lending rates turned down. This trend was accelerated in the latter part of the year when the Bank of Finland cut its own rates and long-term market rates declined. The banks also cut their prime rates in the latter part of the year. In December the average rate on new loans was 6.2 per cent; the average rate on new housing loans had fallen to 7.5 per cent.

Liquidity in the financial markets remained good throughout the year. Deposit banks' markka funding grew by about FIM 10 billion during the first half of the year but declined moderately in the second half. Markka deposits increased again in the latter part of the year, standing at FIM 291 billion in December.

The abundance of liquidity in the early part of the year was also seen in the monetary aggregates (Chart 21). The growth rate for the money supply was kept high by the continuing high level of economic activity. The modest rise in the level of interest rates and the downturn after the peaking of the economic cycle, along with the dampening of inflation, resulted in a corresponding slowing of the growth of the money supply during the second half of the year. The twelve-month growth rate for the narrow money stock (M1) was about 9 per cent in April; by August the rate had slowed to 5.5 per cent. The broad monetary aggregates grew sluggishly as has been the case in recent years. M2 grew at nearly a 3 per cent annual rate in August; M3 declined in the early part of the year, after which it grew modestly. In the latter part of the year the growth of M1 accelerated. In December the twelve-month growth rate was 13.9 per cent for M1 and 6.0 per cent for M2. A number of different seasonal factors affected the monetary aggregates in the course of the year. On the other hand, changes in the money supply had a less pronounced effect on the monetary aggregates than in previous years owing to the cessation of central government borrowing in foreign currencies.

Chart 21.
MONETARY AGGREGATES



1. M1 (narrow money)
2. M2 (broad money)
3. M3 (broad money + bank CDs held by the public)

Minimum reserve system revised

The Bank of Finland during the year made a number of changes in its monetary policy instruments. The most important change affected the minimum reserve system: the fulfilment of reserve requirements is now based on monthly averaging. Some minor changes were also made in the calculation of the reserve base.

A bank's minimum reserve requirement is the portion of its deposits from the public which it is required to deposit at the central bank. Accounting guidelines for credit institutions were changed at the beginning of 1995 in accord with EU directives. In this connection, the calculation of the reserve base was changed. The change was effected with the intent of keeping the level of deposits the same as before. In order to simplify the reporting of the reserve base, the items included were made to coincide more precisely with balance sheet items and the deductible items, which had proven to be troublesome, were eliminated.

In many countries, reserves are deposited in banks' current accounts at the central bank, which are available to the banks for making payments. The reserve requirement is fulfilled on an averaging basis in that the monthly average of daily balances on a bank's current account must be at least as large as the minimum reserve requirement. The Bank of Finland decided to apply this format as from the beginning of October 1995.

Meeting reserve requirements on the basis of averaging affects the steering of interest rates. The fact that banks can analyse the markets, take a view on interest rates and meet their reserve requirements in light of their own self interests means that interest rates (especially the overnight rate) will be less volatile. Averaging also makes it easier for banks to manage their liquidity and lessens the need for active central bank management of liquidity.

Changes in the standing facilities

The changeover to averaging in the minimum reserve system also brought changes to the standing facilities because banks no longer hold call money deposits per se at the Bank of Finland. The banks' deposits in their current accounts at the Bank of Finland are now their reserve deposits. In the new system, excess reserves arise when a bank's monthly

average of daily current account balances exceeds its reserve requirement. The rate of interest paid on excess reserves is not linked to the tender rate but is separately determined by the Bank of Finland.

Also in connection with the changeover to averaging in the minimum reserve system, the Bank of Finland changed the conditions for granting liquidity credit so that a bank can obtain liquidity credit even if its current account is not overdrawn.

Averaging also meant a change in the collateral arrangements for banks' central bank credit. Previously, minimum reserve deposits were used as collateral for both intraday limits on current accounts and liquidity credit. When the reserve deposits were shifted into current accounts they could no longer be used as collateral. The banks were obliged to lodge collateral with the Bank of Finland, consisting mainly of Treasury bills and Bank of Finland certificates of deposit (CDs). At the end of the year there was about FIM 65 billion worth of these instruments in circulation. Thus the markets had an abundance of assets for use as collateral.

Revision of the criteria for counterparties in money market operations

The Bank of Finland changed its criteria for selecting counterparties for its money market operations as from 1 June 1995 so that credit institutions that are subject to minimum reserve requirements and otherwise qualified can be accepted as counterparties. A counterparty must meet certain technical requirements, such as having a current account at the Bank of Finland and a link to the Helsinki Money Market Center, and be an active and significant participant in the money market. Counterparties to outright bilateral transactions must also observe the money market rules and code of conduct. The rules cover market trading hours and other general operating procedures.

Emphasis in money market operations shifted to central government paper

As from 1 June 1995 issues of the central government became the main instruments eligible for use in the Bank of Finland's money market operations. In its direct money market operations, the Bank of

Finland normally approves only Treasury bills and its own CDs. In repo deals, benchmark government bonds and short-term debt issues of Asset Management Company Arsenal are also approved. The outstanding amount of instruments eligible for money market operations was about FIM 248 billion at the end of 1995.

In connection with the revision in eligible instruments, the use of the 'haircut' was adopted for repo deals. Haircuts are widely applied internationally to protect the lender (purchaser of securities) against interest rate and liquidity risks that arise from the possibility that the lender might be obliged to sell the securities in the market in the event that the counterparty is unable to repay the debt (ie buy back the securities). A haircut is a given percentage markdown in the market price of a security in determining its value as collateral. In other words, the security – as collateral – is not valued at its full market value.

Monetary and exchange rate policy preparations in connection with Economic and Monetary Union

The Bank of Finland participated in the work of the Council of the European Monetary Institute (EMI) and its subcommittees, working groups and Committee of Alternates as well as the European Union's Monetary Committee in preparation for Stage Three of the EU's Economic and Monetary Union.

In the area of monetary policy, preparatory work was done in respect of the monetary policy framework for the European System of Central Banks (ESCB). The aim was to develop instruments and procedures that will enable the ESCB to implement its monetary policies in the third stage of EMU. The efforts focused on the comparison of alternative operating modes. Common features of the different alternatives were credit and deposit facili-

ties at the European Central Bank (ECB) at above- or below-market rates and open market operations. The alternatives differed in respect of reserve requirements and averaging as well as the frequency of open market operations. The preparatory work also included discussions on the appropriate degree of centralization or decentralization in the conduct of monetary policy and alternative ways of achieving it, as well as on the amount of time different countries will need for the preparatory work.

In the area of exchange rate policy, preparatory work was done on the transfer of assets to be included in the foreign exchange reserves from the member states' central banks to the European Central Bank, on the management of the ECB's and central banks' foreign exchange reserves as well as on the exchange market intervention and exchange rate arrangements vis-à-vis member states not participating in the third stage of EMU. Analyses and discussions were carried out inter alia on whether foreign exchange intervention should be centralized or decentralized, how foreign exchange reserves should be managed in the central banks and ECB, and how to ensure sufficiently stable exchange rates between all EU member states also during the third stage of EMU.

The Council of the European Monetary Institute reviewed the progress that had been made in preparations for Stage Three and issued directions regarding the continuation of the process. In the area of monetary and exchange rate policy, the Council also monitored developments in economic performance and policy in the EU area and discussed developments in exchange rates, the use of the ECU in the private sector and the operations of the European Monetary System (EMS). Monetary and exchange rate policy matters were also dealt with in the EMI Committee of Alternates and the EU Monetary Committee.

Financial Markets

Sluggish income generation and slow progress in cutting costs held back an improvement in bank profitability despite more favourable business conditions in the economy as a whole. As companies and households repaid their debts, banks' net income from financial operations as well as other income (from commissions, fees and securities trading) declined. In fact, banks had to continue cutting costs and reducing excess capacity in order to ensure profitable performance under increasingly competitive market conditions.

The relative significance of the capital market in domestic financial intermediation increased again in 1995. The strongest growth occurred in the bond market, spurred almost exclusively by new issues of markka-denominated government bonds. Firms were not very active in tapping the stock market for new risk capital. Wide fluctuations in share prices led to a pickup in derivatives trading.

Bank profitability improved slowly

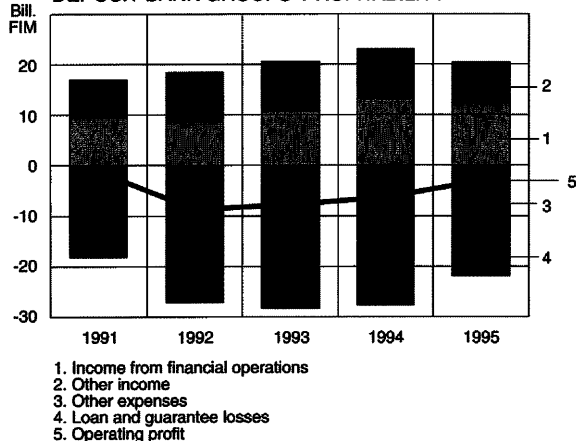
The losses posted by domestic deposit bank groups was reduced by 50 per cent compared to 1994 (Chart 22). However, the combined operating loss still amounted to FIM 2.8 billion. The bulk of this was due to nonrecurrent losses in connection with the merger of Unitas and Kansallis-Osake-Pankki.

The main factor contributing to the improvement in results was a decrease in loan and guarantee losses. These declined by more than one-third to FIM 6.2 billion, as nonperforming assets accumulated at a markedly slower pace than in recent years (Chart 23). Including the asset management companies (Arsenal, Siltapankki, Savings Bank of Finland), the combined loan losses of the banking sector amounted to FIM 9.8 billion. The contraction in nonperforming assets however came to halt around the middle of the year, at FIM 22 billion, because of problems encountered by some large corporate customers and loan arrangements related to debt restructuring.

Despite lower operating losses, banks' net income from financial operations and other income declined significantly during the year. This was due to sluggish credit demand and a narrowing of the margin between banks' markka lending and funding rates. Good corporate profitability and efforts to improve capital structures, accompanied by households' willingness to reduce their debt burden, led to a further contraction in the stock of outstanding bank loans. Companies reduced their stock of foreign currency-denominated loans in particular.

The narrowing of the interest-rate margin reflected a clear post-recession rekindling of competition in the banking sector, which was reinforced by

Chart 22.
DEPOSIT BANK GROUPS' PROFITABILITY ¹



¹ Excl. Arsenal, Siltapankki ja SBF.

increased activity on the part of foreign rivals. The interest rate margin narrowed by nearly 0.5 percentage point in 1994 but stabilized at some 4.9 percentage points in early 1995 (Chart 24). The margin narrowed again as a result of a fall in interest rates later in the year, as lending rates, in line with market rates, came down more quickly than deposit rates.

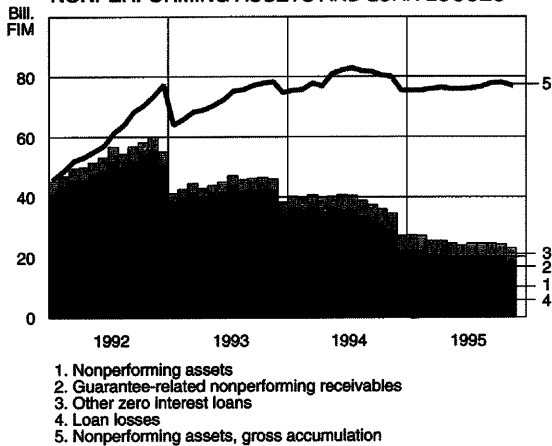
Foreign credit institutions' activities in the Finnish market started to increase significantly in 1994, when the agreement on the European Economic Area and EU-related legislation came into force. There was a further pickup in the level of activity after Finland's accession to the European Union in 1995. Whereas before 1994 there were two (separately-owned) branches of foreign credit institutions operating in Finland, the number had risen to nine by the end of 1995. And by the end of 1995, another 28 EU-based credit institutions had indicated their intention to provide services in Finland without establishing a branch or subsidiary. Thus far, foreign competition has focused on wholesale banking, foreign exchange dealing, securities broking and especially large-customer banking services.

The total amount of banks' other income was substantially reduced by losses incurred in securities trading by the New York branches of Postipankki and Kansallis-Osake-Pankki. Even if these losses are omitted, banks' underlying profitability (profit before loan and guarantee losses) weakened compared to 1994. In addition to the decrease in net income from financial operations, domestic banks clearly lost market share in foreign exchange dealing and securities broking, and the increase in competition was evident in the narrowing of guarantee commissions. Banks' other income was also held down by sluggish credit demand.

Despite a decrease in loan losses, bank profitability did not improve sufficiently. Cost savings from restructurings were not large enough to prevent a weakening of banks' underlying profitability. Therefore, banks will need to improve their cost efficiency, as planned, in order to adapt to an increasingly competitive market in which earnings are lower than before.

Abundant liquidity in the corporate sector and caution on the part of households, together with a pickup in overall economic activity, were reflected in an increase in outstanding bank deposits. Markka deposits have exceeded markka lending for a considerable period already.

Chart 23.
DEPOSIT BANK GROUPS'
NONPERFORMING ASSETS AND LOAN LOSSES ¹



¹ Excl. Arsenal, Siltapankki and SBF.

The use of market-rate-based reference rates continued to increase

Banks continued to rapidly increase their use of HELIBOR and prime rates as lending reference rates, whereas the share of lending tied to the base rate and long-term reference rates declined (Chart 25). The share of lending tied to prime rates expanded particularly rapidly after Postipankki and Merita Bank (Kansallis-Osake-Pankki and Union Bank of Finland) had lowered their prime rates in June 1995 after having increased them in late 1994. Lending tied to prime rates is mainly composed of household loans; lending to companies and financial institutions is almost exclusively HELIBOR-tied or fixed-rate.

During 1995 the amount of deposits tied to the base rate continued to decline, whereas deposits tied to prime rates, tax-exempt transaction accounts and fixed-rate deposits increased in relative importance (Chart 26). The large holdings of tax-exempt transaction accounts has helped to contain banks' funding costs. On the other hand, the interest rates on these accounts respond little to changes in market rates. The constantly growing use of banks' own reference rates for loans and deposits has however reduced their exposure to interest rate risk.

Structural changes in the banking sector

Finland saw an exceptionally large banking merger in 1995. Kansallis-Osake-Pankki and Union Bank of Finland announced on 14 February that they would combine their operations. In March the banks' annual shareholder meetings decided on the merger, and on 1 June Merita Bank commenced operations. In balance sheet terms, the new bank is Finland's largest and ranks among the largest in the Nordic countries as well.

Merita Bank and the cooperative bank group each hold approximately 40 per cent market shares of household loans, which makes them fairly equal rivals in this market. In corporate lending, Merita has the largest share by far, about 50 per cent. However, conditions are likely to remain quite competitive because of the nationwide branch networks of the cooperative banks and Postipankki as well as the presence of foreign rivals. In fact, there were no signs during the year of weakening competition as a

Chart 24.
INTEREST RATE MARGIN BETWEEN
MARKKA LENDING AND MARKKA DEPOSITS

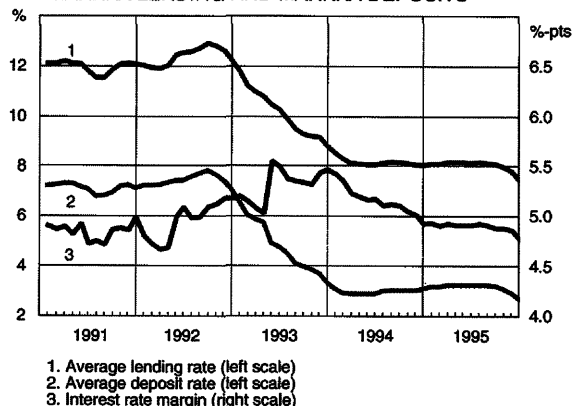


Chart 25.
INTEREST RATE LINKAGES OF
MARKKA BANK LENDING

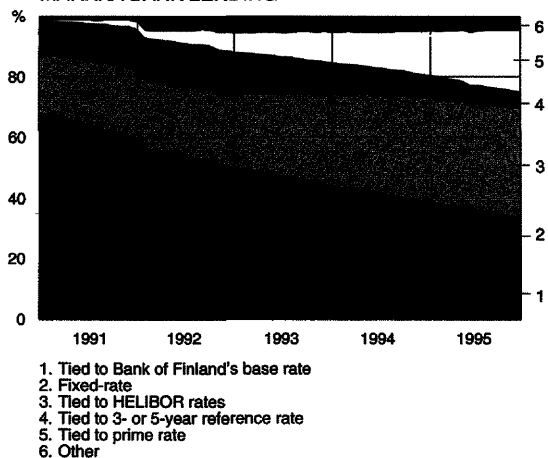
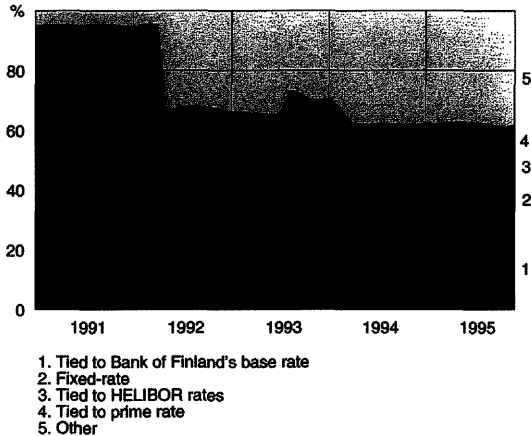


Chart 26.
INTEREST RATE LINKAGES OF
MARKKA BANK DEPOSITS



result of the big merger; competition appears to have tightened further in the banking sector.

The other important structural changes in the banking sector were related to the cleanup of the banking crisis. Siltapankki and Savings Bank of Finland had their banking licences cancelled and were converted into asset management companies. In addition, Siltapankki was transferred into the Arsenal Group.

The Council of State decided in June on the sale of Skopbank's sound parts as well as the shares of Industrialization Fund of Finland Ltd and SKOP Finance Ltd to the Swedish bank Svenska Handelsbanken at a consideration of FIM 4.4 billion. Also included in the deal were Skopbank subsidiaries Finnish Real Estate Bank Ltd and the credit card company Aktiiviraha Oy. It is intended to change Skopbank later into an asset management company.

Bank support in 1995

The settlement of the savings bank crisis and an improvement in the financial performance of the other banks led to an easing of the solvency problems of the banking system. The banks did not require new capital support from the government in 1995. Asset Management Company Arsenal Ltd however availed itself of another FIM 8 billion in capital support to cover its losses.

The Bank of Finland's role in the management of the banking crisis concerns assets transferred to its asset management companies in connection with the takeover of Skopbank in 1991. At that time Sponda Oy took over Skopbank's shareholdings and real estate and Solidium Oy became the majority shareholder in Oy Tampella Ab. The Bank of Finland committed more than FIM 15 billion to these arrangements.

The Bank of Finland's asset management companies have sought to manage the transferred assets, disposing of them as soon as possible, and to see to it that society's losses remain as small as possible. At the end of 1995 the Bank of Finland was holding some FIM 4.5 billion worth of loans to asset management companies. The time needed for liquidizing the assets has proved to be longer than originally foreseen, in particular as regards real estate.

By a decision of the Cabinet Economic Policy Committee on 9 January 1996, the government will undertake to purchase the Sponda Group from the

Bank support 1991–95, million FIM

	Bank of Finland		Council of State		Government Guarantee Fund		Total	
	Capital	Guarantees	Capital	Guarantees	Capital	Other	Capital and other	Guarantees
1991 Scopulus, Sponda and Solidium	4 330						4 330	
1992 Scopulus, Sponda and Solidium	9 444	600					9 444	600
Skopbank			580		3 000		3 580	
Savings Bank of Finland			1 094		11 400		12 494	
Cooperative banks			1 108				1 108	
Postipankki			903				903	
Kansallis-Osake-Pankki			1 726				1 726	
Unitas			1 749				1 749	
Okobank			422				422	
Security fund of the savings banks					500		500	
Other			160				160	
1993 Scopulus, Sponda and Solidium	-2 722	-100					-2 722	-100
STS-Bank (Siltapankki)					3 036		3 036	
Savings Bank of Finland			-844		-2 656		-3 500	
Skopbank			350	300	700		1 050	300
Kansallis-Osake-Pankki				1 800				1 800
Unitas ¹				1 000				1 000
AMC Arsenal Ltd			3 442		1 558		5 000	
Security fund of the commercial banks and Postipankki Ltd					-357		-357	
Security fund of the cooperative banks ¹				900				900
Security fund of the savings banks					-345		-345	
1994 Sponda	-1 220	-500					-1 220	-500
AMC Arsenal Ltd			6 000	28 000			6 000	28 000
Savings Bank of Finland					-686	232	-454	
Skopbank				-174	450	256	706	-174
1995 AMC Arsenal Ltd					8 000	-579	7 421	
Skopbank				-36				-36
Security fund of the savings banks					-155		-155	
Total	9 832	0	16 690	31 790	24 445	-91	50 876	31 790

¹ Decision in principle.

Bank of Finland and to compensate the Bank for interest expenses in connection with the Skopbank operation.

Financial markets legislation revised

The Council of State in April 1994 set up a working group to prepare legislative reforms as required by the EU **deposit guarantee directive**. The working group was also asked to assess the changes in the structure and scope of Finland's deposit guarantee scheme that will be required in order to ensure the stability of the Finnish financial markets and the international competitiveness of Finnish credit institutions.

The working group submitted an interim report in November 1994 proposing a reform of the Credit Institutions Act so as to bring it in line with the deposit guarantee directive. The proposed reforms were approved by Parliament and became effective 1 July 1995. The new provisions concern inter alia time limits for security fund compensation payments, voluntary extra deposit protection for branches of foreign credit institutions and disclosure requirements.

In its final report, submitted in April 1995, the working group recommended a two-phase package of measures for improving financial market stability and the functioning of the credit market. The package included some quick measures for enhancing risk awareness and risk pricing in the financial markets as well as a proposal for a comprehensive long-term reform of the deposit guarantee scheme. A new working group was set up to draft the reform programme by the end of June 1996.

The **Interest Rates Act** was amended as from 1 May 1995 so that the fixed 16 per cent penalty interest rate on overdue payments was replaced by a variable rate linked to market rates. The reference rate used in setting the penalty interest rate is calculated by the Bank of Finland each year according to conditions prevailing at the end of November. The reference rate is based on the three-month market rate. The reference rate for the following calendar year, as confirmed by the Bank of Finland, is published in the Statutes of Finland no later than 14 days prior to the end of the year.

A **working group on cooperative banks re-organization and risk monitoring** in early May 1995 submitted a proposal on revising cooperative

banking legislation so as to allow cooperative banks to form a more coherent group based on the principle of shared responsibility. Cooperative banks belonging to the group would share responsibility for each other's commitments and would not as such be subject to certain legal provisions which apply to individual credit institutions; capital adequacy, liquidity and large exposures would be monitored on a consolidated basis.

The validity of the **Foreign Exchange Act** was extended by three years as from the beginning of 1996. The contents of the act were left unchanged except for the supervision of credit institutions' exchange rate risks, which was transferred from the Bank of Finland to the Financial Supervision Authority by a provision added to the Credit Institutions Act.

In January the Ministry of Finance set up a working group to prepare inter alia changes in legislation governing credit institutions so as to bring it in line with the most recent EU legislation. The working group initially focused on amendments to the Credit Institutions Act as required by the EU's **capital adequacy directive (CAD)**. The next item on the working group's agenda is the 'BCCI' directive issued in June 1995. The directive strengthens the position of auditors in the supervision of credit institutions and obligates them to inform the authorities immediately of any irregularities that surface in the course of carrying out their duties. The working group will continue to function until June 1996.

Central government borrowing increasingly markka denominated

Growth in the outstanding amount of bonds was almost entirely due to the increased focus of central government borrowing on the domestic market (Chart 27). The central government's net financing requirement in 1995 was approximately FIM 64 billion, almost all of which was raised in the domestic markets. The bulk of markka issues consisted of benchmark bonds floated in the wholesale market, totalling FIM 39.9 billion. Yield bonds, which are aimed at households, were issued to the value of FIM 19.4 billion. At the end of the year, outstanding benchmark bonds amounted to FIM 98.7 billion and outstanding yield bonds to FIM 43 billion.

Corporate bond issues were very modest in comparison with previous years. This can be attributed to strong corporate profitability, which made

internal financing easier, and high long-term interest rates in the early part of the year. Nor has the relatively illiquid secondary market for corporate bonds favoured the issuing of bonds.

Increased central government markka financing cannot be considered a constraint on private sector access to the bond markets. In fact, the fall in domestic long-term interest rates in 1995 may be expected to boost bond financing activity. The expansion of the market for benchmark government bonds will also help to develop the domestic corporate bond market by providing the latter with a riskless reference rate and by attracting investor interest in the Finnish bond markets in general.

The market for benchmark bonds continued to expand

The year saw one new primary dealer in the market for benchmark government bonds, the Finnish branch of Swedish Skandinaviska Enskilda Banken. The merger of Kansallis-Osake-Pankki and Union Bank of Finland into Merita Bank and the sale of a part of Skopbank's business to Svenska Handelsbanken reduced the number of primary dealers by two. Hence, at the end of the year, there were nine primary dealers, ie one less than a year ago.

The steady increase in the stock of benchmark bonds was not reflected in correspondingly higher trading volumes for benchmark bonds (Chart 28). The volume of transactions reported by primary dealers in 1995 was FIM 53.9 billion, which was slightly more than in the previous year. The slowing in the growth of trading volume was a result of the steady decline in interest rates through most of the year, which meant that investors did not need to make as large adjustments in their portfolios as was the case when interest rates were more volatile. Nor were foreign investors as active in markka bond markets as they had been in the previous year. Markka-denominated bonds totalling some FIM 4.2 billion in net terms were sold back to Finland in 1995.

In 1995 a large part of the new benchmark bonds in fact ended up in the portfolios of domestic insurance companies, occupational pension institutions and other pension funds. Even though the investment policies of these institutions favoured benchmark bonds in 1995, central government borrowing cannot be based on the presumption that this practice will continue indefinitely. Accordingly, widening the in-

Chart 27.
MARKKA-DENOMINATED BOND ISSUES

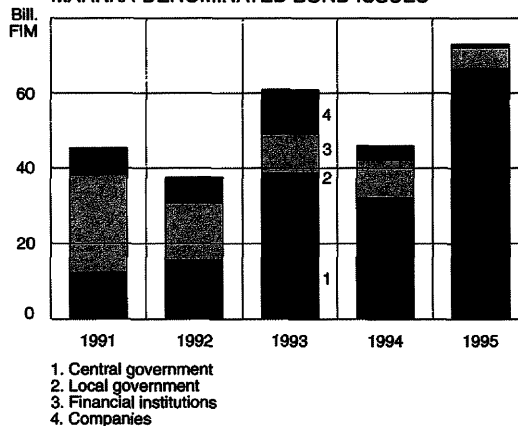
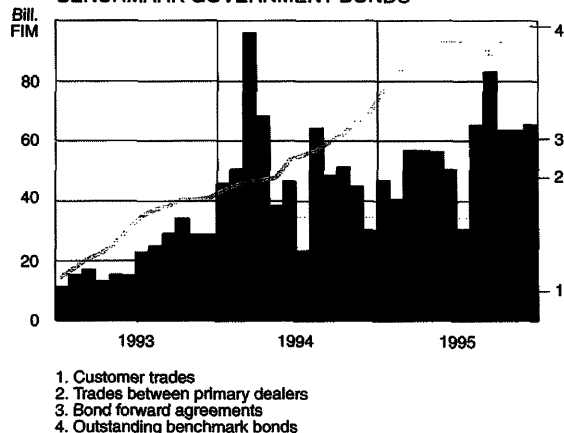


Chart 28.
BENCHMARK GOVERNMENT BONDS



vestor base and, in particular, increasing foreign investors' interest in the market for benchmark bonds will be prime objectives in the years ahead.

Trade in bond forwards, which was started a year ago, did not pick up to any appreciable extent either. But, compared to the previous year, trading focused more on customer contracts than on transactions between primary dealers. The structure of the bond forwards market was simplified in summer 1995 when the Helsinki Money Market Center Ltd and the Finnish Options Market reached an agreement on centralized clearing and settlement of bond forwards at the Finnish Options Market. In 1995 the Finnish Options Market settled 89 per cent of primary dealers' bond forward trades.

Several development projects in the debt markets

With central government borrowing focusing on the domestic market, the need for developing the markka-denominated securities market was further highlighted. Because of its involvement in the primary dealer system for benchmark government bonds, the Bank of Finland has taken an active part in the development of the domestic debt market. A representative of the Bank serves as chairman of the primary dealer committee.

The need to develop the domestic money and capital markets owing to increased central government markka-denominated borrowing also led to closer cooperation between the authorities in 1995. A joint working group composed of representatives of the Ministry of Finance, the State Treasury and the Bank of Finland began to look at policy and technical issues concerning the markets. The group's task is to monitor and expedite the implementation of projects aimed at developing the domestic capital market.

Several projects were in progress to further develop the market for benchmark government bonds. In the course of the year, preparatory work was done in connection with the conversion of benchmark bonds into book-entry form, and an amended version of the Act on the Book-Entry Securities System became effective 15 December 1995. The first issue in book-entry form was a serial bond issued in December 1995 and maturing in 2010.

Work was done on the development of the market for repos (repurchase agreements) based on benchmark bonds. The Bank of Finland's weekly

repo auctions with primary dealers were discontinued on 1 June. The auctions were no longer necessary since the State Treasury had introduced its own repo arrangement. Under the new arrangement primary dealers can temporarily acquire these securities from the State Treasury's own portfolio, which will help to prevent extreme price volatility and thereby improve the efficiency of the market. The arrangement also offers primary dealers a new way of financing their trading portfolios while providing the State Treasury with a new collateralized cash management vehicle.

The Ministry of Finance in April 1995 set up a working group to investigate problems concerning the stamp duty with the aim of furthering the development of the repo market in benchmark bonds. The working group proposed that repurchase agreements based on benchmark bonds concluded with a market maker and settled by a clearing house be exempted from the stamp duty. A bill submitted to Parliament later in the year extends the exemption from stamp duty beyond benchmark bonds to apply *inter alia* to all repurchase agreements based on public issues of local governments, financial institutions and companies as well as contracts based on short-term money market instruments, except for commercial paper. Legislation amending the Stamp Duties Act and the Securities Markets Act came into force on 1 January 1996.

In the course of 1995, preparatory work was also continued on legislative proposals regarding securities markets and securities broking firms as required by the EU's investment services and capital adequacy directives. This work was based on a report issued by a working group on investment services that had convened in the previous year. Under the new legislation, debt market trade and the market makers will come under more extensive statutory regulation. The legislative proposals however take into account the fact that the Securities Markets Act provisions originally intended for the stock market have been mitigated in respect of the money and bond markets. The aim is to ensure that the wholesale markets, which are for professional investors, are not burdened with unnecessary restrictions that impede established market practices and cause extra expenses. It is also sought to emphasize the importance of self-regulation in these markets.

The Government bill would give the Bank of Finland the possibility of strengthening the rules for debt instruments trading if necessary for the Bank's fulfilment of its responsibilities. The right to approve

the rules does not mean that in case of a possible breach of the rules the Bank of Finland would exercise power of sanction on other market participants; in this respect trade is supervised by the Financial Supervision Authority. The Bank of Finland's right to approve rules is necessary mainly because the rules must provide a sound basis for carrying out monetary policy, notably in the short-term money market.

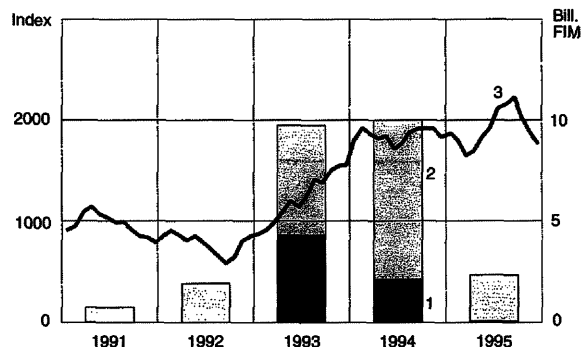
The project for a national securities centre continued to make progress in 1995. The project aims at setting up a single national securities centre that would combine all the activities of the Helsinki Money Market Center Ltd and the Central Share Register of Finland Cooperative with the clearing and settlement operations of the Helsinki Stock Exchange and the self-regulating activities of the Securities Association. Other participants in the project, besides the Finnish government and the Bank of Finland, have been the Central Share Register of Finland, the commercial banks and Helsingin Arvosuuskeskus Oy (a book-entry securities centre in Helsinki). As part of the project, the Finnish government in late 1995 established, with a modest capital base, a limited company which will operate as Finland's securities centre. It is intended to expand the company's ownership base in 1996.

Only modest growth in the stock market

For the stock market 1995 was a year of volatile price movements (Chart 29). Share prices declined moderately at the beginning of the year but assumed a steep upward trend in early April in response to a fall in long-term interest rates. But the rise came to a halt in mid-September, when market expectations of continued robust economic growth started to gradually fade away. Later in the year the Helsinki Stock Exchange all-share index rebounded to the level at which it had started the year.

Likewise, acquisition of new risk capital by listed companies was modest in comparison with previous years. Part of the reason for this was the large number of share issues in the preceding two years, which reduced the need for new share offerings. The paucity of external funding is also explained by the exceptionally good profitability of listed companies. A total of FIM 2.3 billion worth of new risk capital was raised in 1995. In addition, over FIM 2 billion was raised through initial public offerings.

Chart 29.
SHARE PRICES AND ACQUISITION OF
RISK CAPITAL BY LISTED COMPANIES



1. New risk capital: financial institutions, bill. FIM
2. New risk capital: other companies, bill. FIM
3. HEX all-share index, 28.12.1990 = 1000

Share turnover on the Helsinki Stock Exchange however did reach another new high. About 50 per cent of the turnover was concentrated in the shares of a single company, Nokia. Nokia's significance was also highlighted by the fact that its share of the total capitalization of the stock market actually rose above 40 per cent in the course of the year. Without Nokia, the performance of the Stock Exchange all-share index would have been much more modest than it actually was, particularly in the early part of the year.

The importance of foreign investors increased further in the Finnish stock market in the course of 1995. Foreign investors purchased Finnish shares to the value of about FIM 10 billion in net terms, and their holdings of Finnish listed shares at the end of the year accounted for about one-third of the total market capitalization of listed companies.

Wide fluctuations in share prices also set the stage for a pickup in the market for stock-related derivatives. Turnover on the derivatives exchanges in standardized stock and stock index derivatives, as measured by premium payments, increased by 163 per cent from the previous year.

Mutual funds still played a minor role in the Finnish capital market. Total assets held by these funds have remained at the level of some FIM 5 billion. The year saw a slight shift of fund capital from equity funds to fixed income funds that invest mainly in bonds. It was not yet possible to establish money market mutual funds, which specialize in money market instruments with maturities of less than one year. However, improvement of the situation was discussed during the year in connection with the reform of the law on mutual funds.

New Community legislation is being drafted on financial market institutions

In the course of 1995, an EC Council working group dealt with issues connected with the reorganization or winding up of a credit institution. The proposed directive would include provisions for choosing the applicable law in case a credit institution faces a reorganization or liquidation proceeding.

The need for intensified supervision of financial conglomerates which combine operations of banks, securities broking firms and/or insurance companies has recently been underlined, but practical solutions have been elusive. The question has

been discussed inter alia in the EU's banking supervision committee, and it will also be considered in a special EU Commission expert working group.

Preparatory work on revising the directive on undertakings for collective investment in transferable securities was continued in the early part of the year on the basis of an EU Commission proposal submitted in 1994, but unanimity on the matter was not reached between the member states. However, it is to be expected that an EU Council working group will receive a new Commission proposal in 1996. One of the objectives of the reform is to extend Single Market legislation to apply to both money market mutual funds specializing in money market investments and funds of funds (master-feeder funds).

The economic and finance ministers of the EU member states in autumn 1995 came to a common understanding on a proposed directive on investor protection. Pursuant to the directive, each member state should ensure that within its territory there is at least one investor protection scheme including investment service firms as members and guaranteeing small investors minimum protection comparable to that provided by deposit insurance in case an investment service firm is unable to meet its obligations to investor clients. The directive is designed to protect small investors. A member state may, if it so chooses, exclude professional investors from such protection. The proposed directive has been submitted to the European Parliament for a second reading.

Financial market preparations for Stage Three of EMU

In the course of 1995, the Bank of Finland participated in the EMI's technical work in preparing the financial markets for Stage Three of Economic and Monetary Union and a single currency. The issues addressed included inter alia requirements imposed by the implementation of a single monetary policy on the financial markets, notably on clearing and settlement systems for securities transactions. The European Monetary Institute's Banking Supervisory Sub-Committee discussed not only the development of cooperation in financial supervision between the EU countries but also the potential supervisory role of the European Central Bank and the European System of Central Banks in Stage Three of Economic and Monetary Union.

Payment Systems and Maintenance of the Currency Supply

In connection with Finland's accession to the EU, the Bank of Finland participated in 1995 in various projects concerning the development of payment systems which were carried on by working groups of the European Monetary Institute (EMI) and the European Commission. In Finland, similar cooperation also commenced with the banks. The Bank of Finland and the Financial Supervision Authority worked together in the planning of payments systems supervision. Toimiraha Oy, the Bank's subsidiary responsible for developing a multipurpose prepaid card (electronic purse), was sold in November to a company owned by three Finnish banks.

One of the key events in connection with Stage Three of Economic and Monetary Union is the issue of new notes and coin, which is part of the changeover to the single currency. The Bank of Finland participated in the Working Group on Printing and Issuing a European Banknote, which was established by the EMI Council and is responsible for the preparation of European banknotes. The working group is planning the themes and designs for the banknotes as well as their security features and technical specifications. Later on, the preparations will focus on issues related to the currency supply.

Cooperation between EU member states regarding payment systems

Cooperation among EU member states is very close in the area of payment systems. Working groups of both the Commission and the Council worked during the year on the drafting of a directive on cross-border payments between member states. Cooperative work was done on legal and other issues related to the finality of payments as well as on preparations for linking the payment systems of EU central banks. The role of central banks in small-value payment systems and their supervision was also a topic of discussion.

The EU Council's part in the preparation of a directive concerning cross-border payments between member states was completed following a political agreement on the content of the directive reached at a meeting of the Council of the Economic and Finance Ministers (ECOFIN) in September. The member states will be required to adapt their national legislation to the directive within two and a half years after its final approval. The purpose of the directive is to increase the efficiency of cross-border payment transactions between member states by introducing provisions on settlement times and liability issues and on the transparency of payment terms. The directive will apply only to retail pay-

ments between member states. A separate working group under the Commission is considering legal principles related to cross-border payments, concerning liability and other issues, and is expected to submit its proposal in 1996.

Since the plan on European monetary union was accepted in connection with the Maastricht Treaty, the linking together of the payment systems of the member states' central banks has become a topical issue. The effective interlinking of the payment systems of the countries participating in the third stage of monetary union will enable these countries to develop a single money market and is thus an important preparatory step in the changeover to a single monetary policy. The Union-wide payment system which will emerge as a result of the interlinking of the national payment systems is called TARGET (Trans-European Automated Real-time Gross settlement Express Transfer). The TARGET system will be introduced right at the start of Stage Three of the EMU, after which all payments related to monetary policy are to be settled through TARGET. The system may also be used for other payments on a voluntary basis.

The TARGET system is being planned by the EMI Working Group on EU Payment Systems and its subordinate task forces, in which the Bank of Finland is represented, as are the other member states' central banks. In May, the EMI Council published its first report on the TARGET system based on the work of the working group. The report describes the operating principles of the proposed payment system. The system will be created by linking together each member state's real-time gross settlement system (RTGS system). The Interlinking Task Force, which is under the working group, is studying the technical specifications required to perform the interlinking.

Another EMI task force, the Group of Experts on RTGS, is considering the operating hours of the TARGET system, its pricing principles and certain technical issues related to the provision of intraday liquidity. Furthermore, the Task Force on Securities Settlement Systems is focusing on technical issues related to the transfer of collateral for intraday liquidity provided by central banks.

Although several details connected with the changeover to the single currency are still open, it has been agreed that the Interlinking system will only be used for payments denominated in the sin-

gle currency. While the principal objective of creating the Target System is to serve the needs of the single monetary policy and thus the countries participating in monetary union, it has been decided that non-participating EU countries can also join the system and use it for sending and receiving payments denominated in the single currency throughout the EU area.

As Finland's RTGS system (the Bank of Finland's interbank funds transfer system) was already in operation prior to entry into the EU, the changes in Finland's payment systems that will come as a result of single monetary policy are small as compared with many other member states. The most important reforms planned by the Bank of Finland in the course of last year concerned the linkage of the Bank's system to the system connecting the national systems.

The position of central banks in respect of retail payment systems and their supervision was discussed by EMI's Task Force on Retail Payments. In the opinion of the Task Force, cooperation between member states' central banks is necessary if the implementation of monetary policy or financial stability so require and if payment system solutions on a purely national basis would distort competition in the single market. For example, the member states' central banks have agreed on a joint position according to which issuers of electronic cash should be credit institutions as referred to in the Second Banking Co-ordination Directive.

Closer cooperation between the Bank of Finland and the banks in matters concerning payment systems

During the report year, the Bank of Finland and the Finnish banks intensified their cooperation in the management of risks inherent in payment transactions by establishing a Payment Systems Management Group, a Payment Systems Cooperation Group and a number of technical task forces including representatives of the Bank of Finland, the Finnish Bankers' Association and the banks.

The working groups aim at finding methods of operation that will reduce the exposure of payment intermediating banks to the risk of possible insolvency of a payment-system participant. Limiting the participants' exposure to this risk reduces the danger of payment defaults spreading from one bank to another in a crisis situation.

The main themes of the discussions were the payment and settlement of banks' customer payments via the RTGS system and the ways to improve risk management in connection with the netting of payments. The working groups also considered legal issues related to payment transactions. The groups will continue their work in 1996.

Payment systems supervision was developed further

The Bank of Finland and the Financial Supervision Authority initiated a joint study on matters related to the supervision of payment systems. The parties aimed at specifying the key areas for supervisory cooperation and at finding suitable solutions for its practical organization.

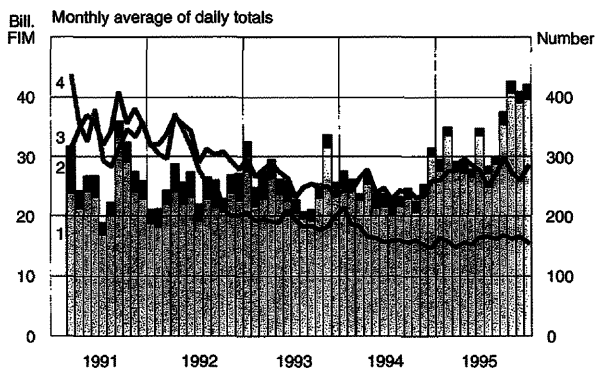
The cooperation focused on determining minimum standards for the management of risks connected with payment transfers and for the security of the payment systems. Future cooperation in the development of legislation on payment systems was also discussed.

Banks take over the development of the electronic cash system

At the beginning of November, Toimiraha Oy, the Bank's subsidiary for developing the Avant electronic cash system for low-value payments, was sold to Automatia Rahakortit Oy. The latter company was established by Merita Bank, Okobank and Postipankki. According to the banks, their aim is to launch in 1996 a multipurpose prepaid card that will be reloadable at ATMs.

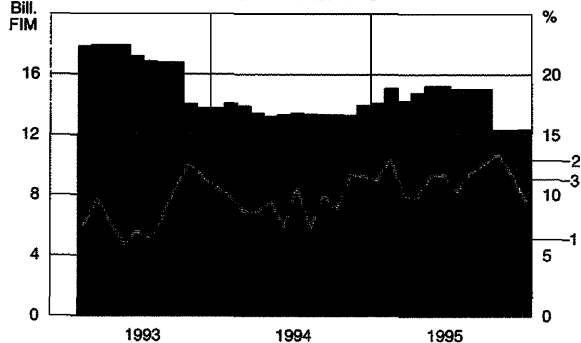
The sale of Toimiraha Oy to the banks reflects the Bank of Finland's line of thought by which it has now completed its part in the development of the electronic cash system. The Bank of Finland's objective was to lay the foundation for a reliable and open national electronic cash system, and as this foundation is now considered to be in place, it was appropriate that the Bank should withdraw from ownership of the company that had developed the system. The banking sector thus becomes responsible for the issuance of electronic cash, which is in harmony with EMI recommendations and with the usual practice around the world. The banks' existing customer network will enhance the prepaid card's prospects of becoming a widely accepted payment medium in the future.

Chart 30.
PAYMENT TRANSACTIONS IN THE BANK OF FINLAND'S INTERBANK FUNDS TRANSFER SYSTEM



1. Transactions between account holders, bill. FIM
2. Transactions between the Bank of Finland and account holders, bill. FIM
3. Transactions between account holders, number
4. Transactions between the Bank of Finland and account holders, number

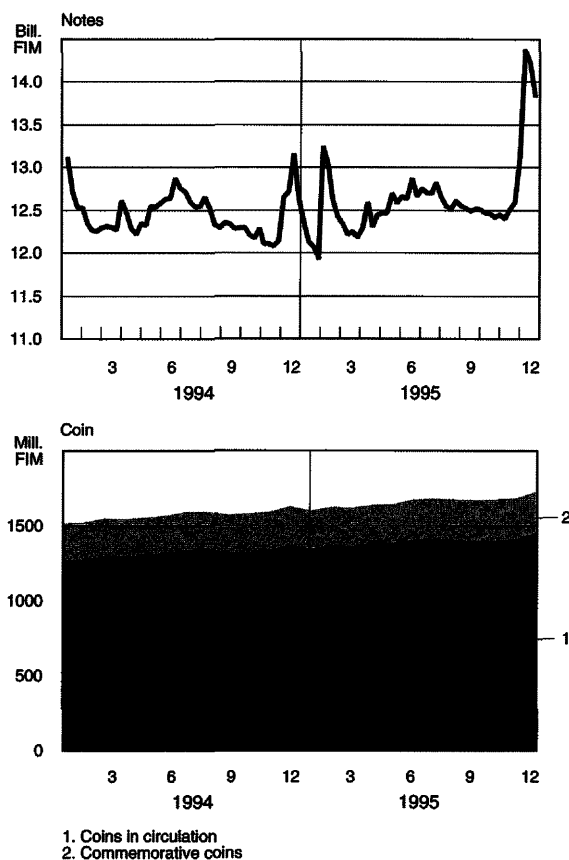
Chart 31.
BANKS' INTRADAY CREDIT LIMITS



1. Collateralized part of limits, bill. FIM
2. Uncollateralized part of limits, bill. FIM
3. Average usage rate of limits, %

The Bank of Finland, in cooperation with other authorities, commenced to examine the need for legislation governing electronic cash.

Chart 32.
VALUE OF NOTES AND COIN IN CIRCULATION



The banks' need for current account overdrafts diminished

Along with the introduction of averaging provisions in the minimum reserve system, the banks' minimum reserve deposits were transferred to their current accounts at the Bank of Finland. The minimum reserve deposits, which had previously been frozen in special minimum reserve accounts, can now be used for making payments provided that the monthly average of daily account balances meets the reserve requirement. The revision brought about a notable decrease in the banks' need for intraday credit, and the banks in fact applied for new intraday credit limits in connection with the reform. The new intraday credit limits entered into force on 2 October 1995, ie simultaneously with the introduction of the averaging provisions (see Appendices, Table 18).

The revision also entailed changes in the collateral coverage of banks' intraday credit limits on their current accounts. With the transfer of minimum reserves to banks' current accounts, the reserves are no longer available for use as collateral, and the banks are required to post book-entry securities which are approved by the Bank of Finland as collateral. In 1995 most banks were required to post collateral equivalent to 25 per cent of their intraday credit limits, but as from the beginning of 1996, the collateral requirement for all banks is 100 per cent.

The number and average size of payments between the account holders increased to some extent compared to 1994 (Chart 30). The increase was partly due to the fact that a new branch of a foreign-owned bank joined the system in the latter half of 1994. In connection with the revision of the minimum reserve system, the total amount of the credit limits decreased by about FIM 2.7 billion from the beginning of October (Chart 31).

The amount of notes in circulation remained stable; the amount of coin increased

During most of the year, notes in circulation amounted to about FIM 12.5 billion. However, the payment of two tax refunds during the year caused

the amount of notes to rise in February and December (Chart 32). In December, the increase in notes was also affected by normal seasonal variation.

The amount of notes in circulation peaked on 15 December at FIM 14 391 million and was at its lowest, FIM 11 979 million, on 31 January 1995. Over the year, the amount of notes increased by FIM 1 193 million, mainly in the form of 1 000 markka and 100 markka notes (see Appendices, Table 15).

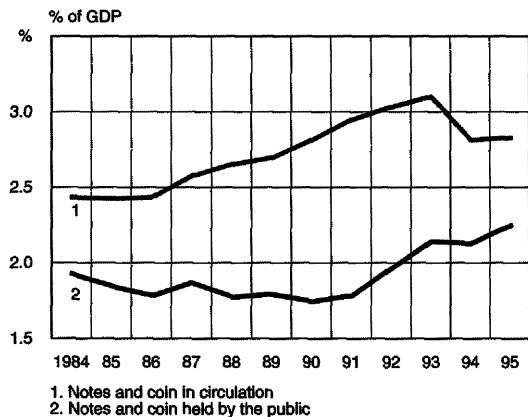
The amount of coin in circulation rose from FIM 1 640 million to FIM 1 743 million during the year. The amount of ordinary coin in circulation increased by FIM 84 million and the amount of commemorative coin by FIM 19 million.

In relation to GDP, the amount of currency in circulation remained virtually unchanged during the year (Chart 33). At the end of 1994, the amount of currency in circulation in Finland was less than 3 per cent of GDP, ie the lowest of the EU countries apart from Luxembourg. In most EU countries, the corresponding ratio ranged from 3 to 7 per cent. The amount of currency in circulation depends inter alia on the sophistication of the payment system, the structure of the banking system and the use of banknotes for savings both at home and abroad.

The amount of currency in circulation, measured as the average of end-of-month figures, has remained relatively stable, having grown by only 4.4 per cent from 1991 to 1995 (Chart 34). During the same period, the amount of currency held by the public increased from FIM 8 831 million to FIM 11 059 million, ie by 25 per cent. According to a survey conducted by the Bank of Finland in autumn 1995, private companies held about 14 per cent of this amount, ie FIM 1.5 billion. This amount was less than a half of the amount households were estimated to hold as active balances according to a survey conducted two years earlier. These surveys indicated that payments in cash accounted for about 40 per cent of the total value of households' payments and for nearly 20 per cent of the total value of the payments received by companies.

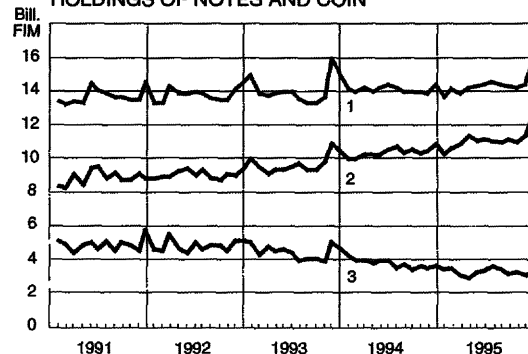
Banks' cash holdings have decreased from FIM 5 753 million at the end of 1991 to FIM 3 210 million, ie by 44 per cent. This decrease was partly due to the termination of the till-money credit facility in June 1993, when the Bank of Finland ceased to finance the cash held in banks' tills. Another factor in the reduction in banks' cash holdings is the contraction of their branch networks. The reduced

Chart 33.
NOTES AND COIN IN CIRCULATION



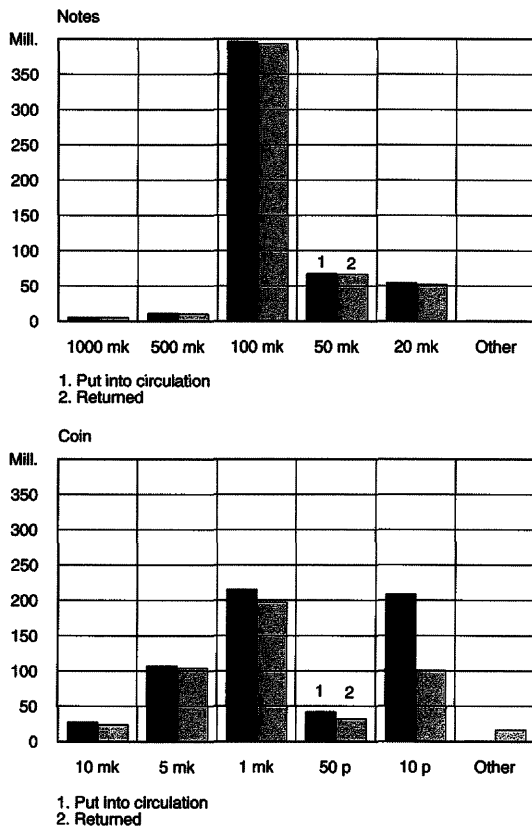
1. Notes and coin in circulation
2. Notes and coin held by the public

Chart 34.
HOLDINGS OF NOTES AND COIN



1. Notes and coin in circulation
2. Notes and coin held by the public
3. Banks' cash holdings

Chart 35.
FLOW OF NOTES AND COIN THROUGH
THE BANK OF FINLAND, 1995



number of bank branches and the economic recovery have actually increased the public's need for cash holdings.

Several new commemorative coins were issued

Four commemorative coins were issued in the course of 1995, one being a special EU version of the ordinary 10 markka coin. The reverse of the EU commemorative coin is the same as that of the ordinary 10 markka coin, but the obverse features a flying swan and the 12 stars of the EU. The number of coins struck was 500 000.

In January, a silver coin in the denomination of 100 markkaa was issued to commemorate the centenary of the birth of the Finnish academician and biochemist Artturi Ilmari Virtanen. The coins struck numbered 43 000. In June, a gold coin in the denomination of 2 000 markkaa was issued commemorating 50 years of peace. The issue was limited to 6 900 coins. To commemorate the 50th anniversary of the founding of the United Nations, a silver coin in the denomination of 100 markkaa was issued in October. The number of coins struck was 43 000. The special EU version of the ordinary 10 markka coin was also minted as a gold and silver coin with a gold alloy centre and an outer ring of silver.

The special version of the 10 markkaa coin, the 2 000 markka gold coin and the commemorative coin for the 50th anniversary of the United Nations together form a commemorative coin series called '50 Years of Peace 1995'.

Flows of notes increased

The flow of notes from the Bank of Finland to the banks increased from the previous year by 19 per cent in markka terms and the return flow increased by 15 per cent, ie by much more than the 9 per cent increase in notes in circulation. In 1995, the Bank of Finland issued notes to the value of FIM 55 607 million and received returned notes amounting to FIM 54 414 million.

The number of notes issued also increased, from 448 million to 536 million, ie by 20 per cent (Chart 35). The number of notes returned to the Bank of Finland increased from 463 million to 530 million notes, ie by 14 per cent. The growth was particularly noticeable in the number of 100 markka

notes returned to the Bank, which increased from 330 million notes to 394 million notes, ie by 19 per cent. This was due to the fact that the banks ordered a larger share of the sorted notes needed for ATMs directly from the Bank of Finland instead of loading the ATMs with notes that had been returned to the bank branches.

In 1995, the notes in circulation passed through the Bank of Finland 5.7 times on average. Compared with the other EU countries, the velocity of circulation is high: corresponding figures for other EU countries range from 1.5 to 3.5.

The velocities of the different notes were as follows: 1.3 for the 1 000 markka note, 2.4 for the 500 markka note, 7.6 for the 100 markka note, 4.9 for the 50 markka note and 2.9 for the 20 markka note.

The flows of coins were smaller than in 1994 because the replacement of the old 5 and 1 markka coins by coins of the new series, which had begun in November 1993, was for the most part completed by the end of 1994. In 1995, the Bank of Finland put into circulation coins with a total face value of FIM 1 092 million and received returned coins amounting to FIM 988 million. The Bank issued 603 million coins, ie 19 per cent less than in 1994, and received 477 million returned coins, which was 32 per cent less than a year earlier. One reason for the decrease in the coin flows to and from the Bank of Finland was the introduction by the Bank of a coin handling fee at the beginning of March.

The Bank reduced its coin supplies

Under the Treaty of Maastricht, central banks of EU member states are not allowed to finance the public sector. As the State has the sole right to mint coins and the face value of the coins is credited to the State's account, coins held by the Bank of Finland constitute a non-interest-bearing claim on the State, which is regarded as a form of interest subsidy to the State. However, according to an EU Council regulation, the financing prohibition is not contravened if the coins held by the central bank account for no more than 10 per cent of the total amount of coin in circulation.

Before Finland joined the EU, the amount of coin held by the Bank of Finland clearly exceeded 10 per cent of the total value of coin in circulation. In 1995, the Bank's share was kept below 10 per

cent. On 31 December 1995, the total value of coin held by the Bank of Finland was FIM 139 million, which was 8.0 per cent of the total amount of coin in circulation.

Preparations for the transfer of the obligation to redeem coins

The Cabinet Economic Policy Committee decided on 9 January 1996 that the State will repay its debt to the Bank of Finland in connection with the obligation to redeem coins. It is the obligation of the State to redeem at face value any coins that have been turned over to the Bank of Finland for issuance.

Old notes and coin were returned slowly

At the end of 1993, the Bank of Finland annulled the validity of all notes of the 1945 – 1980 types. In 1995, the amount of annulled notes in circulation decreased from FIM 303.0 million to FIM 252.8 million. At the end of the year, the total value of 500 markka notes of the 1975 type still in circulation was FIM 54 million, and the total value of 100 markka notes of the 1963 and 1976 types still in circulation was FIM 77 million.

At the end of 1993, the Ministry of Finance annulled the validity of all coins issued before 1963, and all coins in penni denominations issued after 1963 with the exception of 50 and 10 penni pieces of the 1990 type. In 1995, the amount of annulled coins still in circulation decreased from FIM 114.2 million to FIM 111.1 million. The major part of the decrease was due to the return of the old 50 and 20 penni coins, which totalled FIM 2.3 million.

Few counterfeit notes

In 1995, only a few single counterfeit Finnish banknotes were in circulation, all of which were of the 1986 type (without the marking 'Litt.'). In addition, several dozens of pictures of 100 markka notes of the 1986 'Litt. A' type, cut out from a magazine, were detected.

The Bank of Finland and the Central Criminal Police arranged training in the recognition of genuine banknotes for bank employees and other persons whose jobs involve the handling of money.

Currency supply services made subject to a charge

A coin handling fee was introduced by the Bank of Finland on 1 March 1995. The fee is FIM 5 for a bag of 1 000 coins returned to the Bank or for a package of coins purchased from the Bank. The 5 markka, 50 penni and 10 penni coins are available in packages of 1 000 coins and the 10 markka and 1 markka coins in packages of 800 coins. The coin handling fee covers costs only, in accordance with the Act on the Grounds for Levying Government Fees. The purpose of the fee is to increase the efficiency of the maintenance of the coin supply by decreasing the frequency with which coins are transported to the Bank of Finland for handling. The fees charged in 1995 totalled FIM 4.5 million.

The Bank of Finland and the banks that use the Bank's data system for currency supply services have agreed on which of the costs arising from the use and maintenance of the system are to be reimbursed to the Bank of Finland. In 1995, these reimbursements amounted to FIM 7.5 million. Again, in accordance with the Act on the Grounds for Levying Government Fees, these reimbursements cover costs only.

Preparation of the European banknotes

According to the Treaty of Maastricht, the European Monetary Institute is responsible for the technical preparation of the European banknotes. The Bank of Finland participated in a working group established by the EMI to carry out the technical preparation of the European banknotes. The Working Group on Printing and Issuing a European Banknote cooperates with the Mint Directors' Working Group, which is preparing the European coins.

The working group on the European banknote studied various issues related to member states' means of payment and their production and handling. On the basis of these studies, the EMI Council decided that the highest value for a European coin will be 2 monetary units and the lowest value for a banknote will be 5 units. It is assumed that there will be seven notes in the denominations of 5, 10, 20, 50, 100, 200 and 500 monetary units. There were two options regarding the appearance of a banknote: completely identical or identical on one side with a limited national feature on the other side.

The planning of the themes and features to be depicted on the notes continued throughout the year. In developing the themes, EMI is advised by experts in history, psychology, art and graphic design. The working group on the European banknote is at the same time considering the technical specifications, sizes and security features of the banknotes.

During the year, the EMI's working group on the European banknote also discussed matters related to the production and issuance timetable for European banknotes. In this connection, preliminary analyses were done concerning necessary modifications in ATMs and other machines that use and handle banknotes and the lead times required. According to a timetable approved at the Madrid Summit Meeting in December, European banknotes and coins will be issued no later than three years after the beginning of Stage Three of Economic and Monetary Union. The issuance will be followed by a six-month transition period during which national banknotes and coins will maintain their legal tender status alongside the European currency.

Other Activities

International cooperation

Activities related to the European Union

Finland became a member of the European Union at the beginning of 1995. In joining the EU, Finland also joined the Economic and Monetary Union (EMU) during Stage Two. At the same time, Finland became a member of the European Monetary Institute (EMI), which is the main body involved in preparations for EMU. Thus, Finland became a fully-fledged member of the EU institutions dealing with economic, monetary and exchange rate policies following a six-month period as an observer.

Since the start of Stage Two at the beginning of 1994, the EMI has been in charge of EU Member States' monetary and foreign exchange policy cooperation and preparatory work for Stage Three of EMU. The EMI Council – composed of the President of the EMI, Mr Alexandre Lamfalussy, and the Governors of the central banks of the Member States – is the highest authority in these matters. Issues concerning the Council are prepared by the Committee of Alternates and various subcommittees and working groups. These bodies in turn have expert working groups to deal with certain specific matters. The Committee of Alternates, subcommittees and working groups are composed of representatives of the central banks of the Member States.

Ms Sirkka Hämäläinen, Chairman of the Board of the Bank of Finland, is a member of the EMI Council and Mr Matti Vanhala, Member of the Board of the Bank of Finland, is a member of the Committee of Alternates. All in all, the Bank of Finland was represented in some twenty subcommittees or working groups of the EMI.

The EMI preparations for Stage Three progressed according to the plan approved by the EMI Council. The monetary policy, foreign exchange policy and banking supervisory subcommittees as well as the working groups on European banknotes, accounting, information systems, statistics, payment systems and legal issues did preparatory work in their respective fields of competence. Further information on EMI's activities is available in its Annual Report.

In its first annual report, published in April 1995, the EMI reported on economic, monetary and foreign exchange policy developments in the EU and on its own tasks and activities. In November, the EMI published its reports on the changeover to the single currency and on progress on economic convergence. Both the Annual Report and the single currency report were translated into Finnish at the Bank of Finland under commission to the EMI. Upon recommendation by the EMI, the report on progress towards convergence was also translated into Finnish.

The Bank of Finland and the Ministry of Finance each sent one representative to the meetings of the EU Monetary Committee and its Committee of Alternates and to the meetings of the EU Economic Policy Committee. Mr Matti Vanhala and Mr Esko Ollila, both members of the Board of the Bank of Finland, participated respectively in the work of the Monetary Committee and the Banking Advisory Committee. The Bank of Finland was also represented on the Committee on Monetary, Financial and Balance of Payments Statistics and in several working groups of the EU Council and Commission dealing with financial markets issues.

The Bank of Finland was also involved in the preparation of EU matters in Finland. After the completion of Finland's accession negotiations, the task of preparing for Finland's integration into the EU was reorganized. The focus is now on preparing official positions and providing support for Finland's representatives in the work of the EU. Bank of Finland representatives participated in the work of the Committee of Secretaries General and five of its preparatory subcommittees. The Bank of Finland's representative on the Committee of Secretaries General was Mr Esko Ollila, Member of the Board. The Bank of Finland also had a representative on each of the preparatory subcommittees dealing with the following matters: economic and monetary policy; international finance issues; taxation; financial services and capital movements; and insurance services. The economic and monetary policy subcommittee dealt extensively with EU-related matters. The Bank of Finland also cooperated with EU coordinators of various ministries. Mr Matti Vanhala, Member of the Board, participated in the working group on economic matters dealing with Finland's preparations for the Inter-Governmental Conference of 1996.

Bank for International Settlements (BIS)

The Bank for International Settlements operates as a bank for the central banks and serves as their organization for international cooperation. The governors and experts of central banks convene monthly in Basle to discuss current monetary and economic policy issues and to exchange information on market developments and other matters of concern to central banks.

The BIS maintains a data bank containing information used in the monitoring of technical assis-

tance provided by the central banks to the economies in transition. The BIS also carried out the practical arrangements for the coordination meetings on technical assistance presided over by the International Monetary Fund. A representative of the Bank of Finland participated in these meetings.

The Bank of Finland carried out Finland's part in a global survey on foreign exchange and derivatives markets conducted by the BIS.

International Monetary Fund (IMF)

In 1995, the IMF focused its activities on enhancing the monitoring of member countries' economic policies. The importance of this objective was underlined when uncertainty in the financial markets stemming from Mexico's economic problems threatened to foment an international financial crisis.

In February the IMF, together with the USA and some other countries, put together an extensive package of international financial support for reform of the Mexican economy. The stand-by arrangement, which amounted to just over SDR 12 billion, was the largest ever granted to a single member country.

In February, the IMF revised the principles applied in the monitoring and surveillance of member countries' economies. The latest revision (they are done every two years) was carried out immediately after the Mexican financing operation. The new principles emphasize the importance of improved communication. On-going dialogue between the Fund and member countries requires an improvement in the availability of up-to-date information. The IMF also intends to standardize the economic performance data which member countries publish regularly.

The June G-7 summit meeting in Halifax, Canada supported the strengthening of the IMF's surveillance function.

In September, the Interim Committee of the IMF approved a proposal of the Executive Board on an Emergency Financing Mechanism. The Interim Committee also welcomed the proposal put forward by the G-10 countries to enhance the IMF's ability to borrow from member countries. The proposed facility would supplement the present General Agreement to Borrow (GAB), increase the number of participant countries and double the amount of available financing.

The IMF continued to provide technical assistance to the economies in transition during the year

under review, and experts from the Bank of Finland also continued to take part in related short- and longer-term assignments.

A team of IMF officials visited Finland in June within the framework of Article IV consultations. During the visit the Fund's economists analyzed the state of the Finnish economy. A consultation report was drawn up on the basis of the visit and was discussed in September by the Executive Board of the Fund.

Within the IMF, the Nordic and Baltic countries have formed a joint constituency since 1992. Mr Jarle Berge from Norway held the position of Executive Director in 1995. Norges Bank, the central bank of Norway, was responsible for preparing the Nordic and Baltic countries' joint positions for presentation to the Executive Board.

Ms Sirkka Hämäläinen, Chairman of the Board of the Bank of Finland, acted as Finland's representative on the Fund's Board of Governors. Mr Matti Vanhala, Member of the Board, served as her deputy.

Other international cooperation

The Nordic Financial Commission (NFU), the forum for cooperation between the Nordic countries' central banks and ministries of finance, held two meetings during the year under review. The meetings included discussions of the issues to be dealt with by the Executive Board of the IMF; draft statements were prepared. European integration was also included on the agenda. At two coordination meetings, the Nordic and Baltic countries prepared joint positions for presentation to the Executive Board of the IMF.

Within the Organization for Economic Cooperation and Development (OECD), the Bank of Finland participated inter alia in the work of the Economic Policy Committee, the Committee on Financial Markets, the Committee on Capital Movements and Invisible Transactions as well as in the related working parties. The Bank's representatives also participated in meetings of experts monitoring conditions in the economies in transition.

A representative of the Bank of Finland participated in cooperative efforts involving different areas of state administration through which the OECD has sought to determine where it should focus its operations so as to obtain maximum effectiveness within the constraints of a tight budget.

A representative of the Bank of Finland also worked with a delegation of officials in preparing joint statements for OECD negotiations on a Multilateral Agreement on Investment (MAI).

Investment of the foreign exchange reserves

There were no major changes in 1995 in the general principles applied to the investment of foreign exchange reserves. The management of reserve assets is guided by the central bank's long-term tasks and objectives and by the intended use of the reserves. The reserves were invested in major international financial markets with the primary objectives of value preservation, liquidity maintenance and, within these constraints, a good rate of return. Since the holding period of foreign exchange reserves is uncertain and reserves must be readily available for financing interventions, maintenance of an ample supply of liquidity is one of the major concerns in portfolio decisions.

As an investor, the Bank of Finland is highly risk-averse. The main risks associated with the investment of reserves are exchange risk, credit risk, liquidity risk and interest rate risk. The management of investment risks is an integral process, in which the level of any one individual risk cannot be changed without simultaneously affecting the level of other risks. Minimizing all risks simultaneously is impossible.

The principal means by which risks associated with foreign exchange reserves can be reduced are portfolio diversification, emphasis on the best available investment vehicles and counterparties, and use of investment benchmarks. Compliance with agreed investment principles and risk limits is monitored continuously.

The most important source of uncertainty affecting the reserves is exchange rate risk. In order to minimize changes in the value of the reserves due to exchange rate fluctuations, the Bank of Finland diversified its currency holdings among major investment markets. The currency distribution, though reviewed regularly, is normally stable over long periods. No modifications in the distribution were considered necessary in 1995. The most important investment currencies were the Deutschmark, US dollar, French franc, pound sterling, Japanese yen and Dutch guilder.

The liquidity of the reserves is secured by the use of a wide range of mostly default-free negotiable investment instruments. The bulk of the reserves was invested in bonds issued by the governments of the above countries and in repurchase agreements collateralized by such bonds. Part of the reserves was invested in short-term foreign currency deposits, gold and SDRs. Only major, highly creditworthy international credit institutions are accepted as counterparties.

The most important influence on the returns earned on foreign exchange reserves in 1995 was the sharp decline in international interest rates, which followed a yearlong surge in rates. The slowing of economic activity and favourable development of inflation created room for an easing of monetary policy in the USA and in Germany and Holland of the European investment markets. Although key interest rates were raised in France to defend the currency and in the early part of the year in the UK to stem inflation, bond yields also declined substantially in these markets. In the latter half of the year, the central banks of France and England also lowered their key short-term rates. Nonetheless, the interest rate differentials of France and the UK vis-à-vis Germany tended to widen in the course of the year. In Japan key interest rates were lowered to a record low level because of the halt in economic growth and because the yen remained strong and the banking crisis and deflationary pressures continued. The decline in yields on debt obligations with maturities exceeding one year resulted in capital gains on reserves in all six investment markets.

The foreign exchange reserves decreased during the year, mainly due to repayments on the government's foreign debt, but were still large as a result of the government's large capital imports in previous years.

In connection with the signing of the EMS agreement, 20 per cent of the gold and dollar reserves were swapped against official ECUs with the EMI. The Bank of Finland however manages these swapped reserves on behalf of the EMI as part of its normal foreign exchange reserves management.

The main items of the convertible reserves at the end of 1994 and 1995 and changes in the course of the year are shown below:

	Reserves	Reserves	Change
	29 Dec 1995	31 Dec 1994	
million FIM			
Gold	1 742	2 180	-438
Special drawing rights	1 569	1 537	32
IMF reserve tranche	1 685	1 354	331
ECU-claim on the EMI	3 363	-	3 363
Foreign currency claims	40 506	47 672	-7 167
Total	48 865	52 743	-3 878

Economic analysis and research

Monthly reports on economic developments compiled jointly by economics-related departments at the Bank of Finland are a key element in the Bank's monitoring of the economy. Analysis focused on the maintenance of price stability and the influencing factors. Analysis of actual economic developments was closely related to forecasts used in assessing future developments in the Bank's operational environment and the pressures they exert on monetary policy. Forecasting and monitoring as required by EU cooperation were upgraded by the use of the NIGEM model of the international economy developed by the UK's National Institute for Economic Research. The model is used for forecasting developments in the major EU economies and can also be used for projecting the effects of economic policy measures.

The Bank of Finland's economic research focuses on macroeconomic issues related to monetary policy planning and on the functioning of financial markets, including issues concerning payment instruments and payment systems.

Macroeconomic research concentrated on the effects of monetary policy on the economy as a whole and the complex problems involved in inflation forecasting. In addition to individual studies, work continued on the construction of a new version of the Bank of Finland's macroeconomic simulation model (BOF4). The Bank of Finland also published a study of the labour market, which attracted a great deal of public interest. The paper discusses the effects of taxation on employment and wages.

In the area of financial markets, research focused on the measurement of banking competition, the pricing of deposits and bank services and com-

panies' demand for cash, which was studied with the aid of a survey. The survey of companies' financing needs and availability of financing was continued in cooperation with the Ministry of Trade and Industry and the Confederation of Finnish Industry and Employers. The Research Department used comprehensive statistical data to study the factors that affected banks' behaviour at different stages of the Finnish banking crisis. In addition, work continued on an extensive statistical study of Finnish economic history. The aim of this study is to compile a consistent set of basic statistics describing the functioning of the Finnish financial markets from the 1860s to the 1990s.

Research on economies in transition has become an established part of the Bank's research activities, and international awareness of this work is growing. Monitoring, analysis and research continued to focus on economic developments and the transition process in Russia and the Baltic states. Another area of concern was the development of the EU's relations with Eastern economies and activities of international organizations in economies in transition, with special emphasis on issues concerning the monetary and financial systems of Russia and the Baltic states. Publishing activity continued at a brisk pace. An English-language book was published on the history of the bilateral payment system between Finland and the Soviet Union, which should also serve as a reference source for future research.

Information and publications

The Bank of Finland attempted to provide clear and transparent information on the objectives, rationale and measures connected with monetary policy. The Bank waged an anti-inflationary campaign by means of an inflation leaflet aimed at the general public and several articles on inflation in its Finnish language publication *Markka & talous* (The Markka and the Economy).

The importance of the Bank's communication function has increased in today's changing national and international environment. A survey of *Markka & talous* readership was conducted in Finland in order to find out how well the Bank is getting its message across to the reader.

Of the periodicals published by the Bank of Finland, *Markka & talous* appeared four times and the English language publication *Bank of Finland*

Bulletin 11 times. The *Year Book* and *Finnish Bond Issues 1994* were published in the spring. The Bank's four research series were combined into two series. Series A comprises studies intended for the general public. A new series E replaces series B, C and D and includes theses and analytical research papers. Two publications were issued in series A and three in series E.¹ The statistical review *Financial Markets* appeared monthly. Thirty-seven papers appeared in the *Discussion Papers* series, which comprises research and analytical work done in the various departments of the Bank. The *Review of Economies in Transition*, which contains studies and reports on developments in Central and Eastern European economies, appeared nine times.

Information management

Information services and production of statistics

In order to obtain advance data on foreign trade needed for the balance of payments, the Bank of Finland was obliged to design and conduct its own survey of firms. This was necessitated by the delay in the release of the official foreign trade statistics of the National Board of Customs because of changes in statistical systems connected with Finland's entry into the EU. The balance of payments publications were supplemented with an annual statistical publication which included long time series and structural data. A comprehensive publication on compilation methods, data collection and time series related to the balance of payments was published in the Bank's series A.

Since Finland's accession to the EU, the Bank of Finland's developmental work concerning the compilation of financial and balance of payment statistics has become part of a joint effort under the auspices of the EMI. The aim of this work is to determine the statistical and related developmental needs of Stage Three of EMU. For this purpose, the Bank of Finland took an active part in the work of the EMI's Working Group on Statistics and its two sub-working groups. On the basis of the Working Group's preparatory work, the EMI Council adopted a proposal on the competence of the future European Central Bank in statistical matters and on the

¹ A list of Bank of Finland publications in 1995 is included in the Appendices.

division of tasks and cooperation with EUROSTAT (Statistical Office of the European Communities) and the national central banks.

The Bank of Finland continued to participate in the work of the EU Finance and Balance of Payment Statistics Committee and the Balance of Payments Statistics working group and the corresponding sub-working groups, as it has done continuously since Finland joined the EFTA and EEA. A representative of the Bank of Finland was involved in the drafting of proposals for an EU-wide compilation system for balance of payments data and a message standard for data transmission.

In order to improve its information services, the Bank set up a Statistics Desk within its library facility, to which inquiries are directed concerning statistics compiled by the Bank of Finland. A number of charges were introduced on Bank of Finland statistical publications in order to improve cost-effectiveness. The library's new data management system was made available to the staff, and a multimedia studio with interactive information media was set up within the library facility.

Data processing

Preparations for Stage Three of EMU were also launched in the area of data processing. The Bank of Finland was connected to the e-mail system of the central banks of EU member states and changes associated with Finland's entry into the EU were implemented in the information systems. The joint use of monitoring data was improved in cooperation with the Financial Supervision Authority. Utilization of time series data was enhanced by developing the decision support system and by constructing distributed databases which will be updated regularly. The operational reliability of the market information system and back office system was improved through operational changes and platform replacement. The Bank's various activities and related changes were analysed with the aim of drafting IT strategy descriptions for each unit.

In-house operations, organization and staff

Work with EU organizations and EMU preparations tied up a considerable amount of the resources of many of the Bank's units. Development of work

processes was carried on in order to make activities more efficient and increase flexibility. Common modes of operation were adopted for the Bank after thorough discussion by all the units.

The Data Processing and Administrative Departments were reorganized. Joint use of information services and systems was expanded within the Bank and between the Bank and other organizations, for example as regards information banks provide to the Bank of Finland on an official basis.

The salary scheme applied to managers and experts was revised. The revision aimed at better integrating the scheme with the Bank's operational planning and modes of operation and increasing its flexibility as a management tool.

The Bank's operating costs have decreased over the period from 1992 to 1995. The increase in the 1996 budget is primarily due to an increase in note-handling costs (Chart 36).

Bank of Finland's operating expenses and budget, million FIM

	Budgeted 1996	Realized 1995	Realized 1994
Expenses			
Salaries	154.5	146.9	146.8
Social security costs	84.7	84.7	81.6
Travel and training	13.3	10.3	9.2
ADP expenses	24.8	23.0	22.1
Banknote printing	27.1	34.4	49.2
Real estate expenses	27.2	26.3	23.9
Other expenses	30.3	28.4	23.6
Total	361.9	354.2	356.5
Investment			
Investment in equipment and machinery	35.4	17.7	26.0
Investment in real estate	18.1	32.4	37.0
Total	53.5	50.0	63.0
Total expenses	415.4	404.2	419.5
Income			
Sale of services	20.7	22.9	17.2
Return on real estate	33.2	35.9	36.5
Total income	53.7	58.8	53.7
NET RESULT	361.6	345.4	365.8

In the course of the year, the number of staff employed by the Bank increased by 15 persons, all of whom were employed on short-term contracts. At the end of 1995, a total of 796 persons were employed by the Bank of Finland; staff at the head office numbered 679 and that at the branches 117. The total number includes 41 persons on leave of absence and 61 on fixed-term contracts.

Internal exchange of jobs continued as before in the filling of vacancies. It was accelerated when four vacancies opened up when the EMI recruited four of the Bank's experts. Almost 30 persons changed jobs either permanently or for a fixed period.

Training

Training continued to focus on developing the skills required for working in EU and EMI working groups. Training was also aimed at expanding professional skills to facilitate internal jobs exchange.

Internal management development programmes, which support the development of the Bank's activities, were continued. By the end of the year under review, almost all central bank managers and some of those of the Financial Supervision Authority had participated in such programmes.

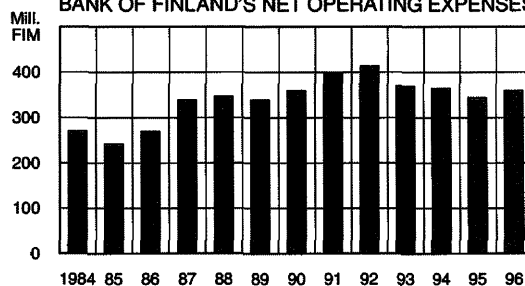
Experts' economic training focused on EU institutions and operating mechanisms and their development. Three four-day seminars on these matters were attended by a total of 75 persons. Other subjects on which courses were arranged included risk management, financial intermediation, financial market analysis, monetary policy and quantitative methods in economics.

Expenditure by the Bank of Finland on training accounted for some 4 per cent of the total wage bill.

The second 18-month Young Professionals training programme commenced in September 1995. The aim is to prepare newly-qualified economists for work in international organizations, the banking sector and public administration. The seven economists accepted into the programme work in various units of the Bank and participate in internal training arranged for experts. In addition, the Young Professionals learn about the main institutions related to central government and business and industry. They also work for a short period abroad.

Training assistance to the central banks of eastern economies was continued. The main target country was Russia, and three one-week special

Chart 36.
BANK OF FINLAND'S NET OPERATING EXPENSES



seminars were arranged for Russian experts in Helsinki. The Bank of Finland and the Financial Supervision Authority also arranged a training seminar on banking supervision at the Russian central bank. Officials of Eesti Pank (the central bank of Estonia) attended a seminar in Tampere arranged jointly by the Bank of Finland and Eesti Pank as well as internal courses organized by the Bank of

Finland. In 1995, training assistance was extended to include other eastern economies. One-week courses and seminars were arranged for experts from the central banks of Albania, China, Belorussia, Ukraine, Poland and other countries. Training for participants from eastern economies was tailored to suit participants' special needs and requests.

Financial Statements

Profit and loss account, million FIM

	1 Jan–31 Dec 1995		1 Jan–31 Dec 1994	
INTEREST INCOME				
Domestic (1)				
Liquidity credits	8.0		1.0	
Certificates of deposit	7.0		91.5	
Securities with repurchase commitments	201.9		72.6	
Net interest on forward transactions	8.1		15.2	
Financing of domestic deliveries (KTR)	15.4		25.5	
Bonds	226.2		250.7	
Loans for stabilizing the money market	–		31.8	
Other	37.5	504.0	37.0	525.3
Foreign (2)				
IMF	107.3		74.2	
Securities	2 129.9		2 215.6	
Other currency claims	739.4	2 976.6	430.2	2 720.0
Total interest income		3 480.6		3 245.2
INTEREST EXPENSE				
Domestic (3)				
Call money deposits	–29.7		–43.9	
Certificates of deposit	–2 046.6		–1 539.6	
Reserve deposits	–4.1		–	
Investment deposits	–34.0		–48.2	
Other	–5.2	–2 119.6	–11.9	–1 643.6
Foreign				
IMF	–43.2		–44.6	
Other	–12.6	–55.9	–1.8	–46.4
Total interest expense		–2 175.5		–1 690.0
INTEREST MARGIN (4)		1 305.2		1 555.2
OTHER INCOME (5)				
Commissions and fees	20.6		14.9	
Other	107.1	127.7	57.7	72.6
OTHER EXPENSE (6)				
Salaries	–146.9		–146.7	
Social security costs	–84.7		–81.5	
Purchase of banknotes	–34.4		–49.2	
Depreciation	–105.1		–63.0	
Other	–88.1	–459.3	–78.0	–418.4

	1 Jan-31 Dec 1995		1 Jan-31 Dec 1994	
EXPENSE AND INCOME RELATED TO FINANCIAL SUPERVISION (7)				
Salaries	-22.4		-18.9	
Depreciation	-0.4		-0.6	
Other	-22.6		-20.3	
Supervision fees charged by the Financial Supervision Authority	45.5	0.0	40.0	0.2
PROFIT BEFORE VALUATION ADJUSTMENTS AND PROVISIONS		973.5		1 209.6
Valuation gain/loss on foreign securities (8)		883.9		-1 459.8
Exchange rate gain/loss (9)		-2 130.5		-5 816.9
Change in pension provision (10)		-95.9		-89.9
Increase (-) / reduction (+) in provisions (In accordance with section 30 of the Act on the Bank of Finland) (10)		369.0		6 157.0
PROFIT FOR THE FINANCIAL YEAR (11)		0.0		0.0

Balance sheet, million FIM

ASSETS

	31 Dec 1995		31 Dec 1994	
Gold and foreign currency claims (1)				
Gold	1 742.1		2 180.5	
Special drawing rights	1 569.0		1 536.9	
IMF reserve tranche	1 685.1		1 353.7	
ECU-claim on the European Monetary Institute	3 363.1		.	
Foreign currency claims	40 505.5	48 864.8	47 672.2	52 743.2
Other foreign claims (1)				
Markka subscription to Finland's quota in the IMF	3 910.8		4 594.6	
Share in the European Monetary Institute	58.2	3 969.1	.	4 594.6
Claims on financial institutions (2)				
Certificates of deposit	–		443.0	
Securities with repurchase commitments	7 075.8		1 037.4	
Bonds	416.5		802.2	
Other	1 338.7	8 831.0	237.9	2 520.5
Claims on the public sector (3)				
Total coinage	1 882.4	1 882.4	1 806.0	1 806.0
Claims on corporations (4)				
Financing of domestic deliveries (KTR)	185.2		315.8	
Other	2 700.3	2 885.5	2 833.2	3 149.0
Other assets (5)				
Loans for stabilizing the money market	4 532.0		4 532.0	
Accrued items	972.2		1 832.1	
Other	141.0	5 645.2	159.4	6 523.5
Valuation account (6)		643.0		–
Capitalized expenditures and losses due to safeguarding the stability of the money market (7)		1 400.0		1 400.0
Total		74 121.0		72 736.8

LIABILITIES

	31 Dec 1995		31 Dec 1994	
Foreign currency liabilities (1)	1 214.2		130.4	
Other foreign liabilities (1)				
IMF markka accounts	3 910.9		4 594.6	
Allocations of special drawing rights	926.5	4 837.5	984.9	5 579.5
Notes and coin in circulation (8)				
Notes	13 867.9		12 675.1	
Coin	1 743.1	15 611.0	1 639.5	14 314.7
Certificates of deposit (9)	27 090.0		35 236.0	
Liabilities to financial institutions (10)				
Call money deposits	-		1 386.6	
Reserve deposits	15 675.7		6 525.7	
Other	1 100.9	16 776.6	-	7 912.3
Liabilities to the public sector (11)				
Current accounts	0.0		0.0	
Deposits of the Government Guarantee Fund	75.2	75.3	93.1	93.1
Liabilities to corporations (12)				
Deposits for investment and ship purchase	994.0	994.0	1 548.5	1 548.5
Other liabilities (13)				
Accrued items	300.0		436.5	
Other liabilities	26.9	326.9	24.2	460.8
Provisions (14)				
Pension provision	1 431.4		1 328.6	
Other provisions	-	1 431.4	369.0	1 697.5
Capital accounts (15)				
Primary capital	5 000.0		5 000.0	
Reserve fund	764.1		764.1	
Profit for the financial year	0.0	5 764.1	0.0	5 764.1
Total	74 121.0		72 736.8	

Appendices to the financial statements

	31 Dec 1995	31 Dec 1994
Note issue, million FIM		
Right of note issue	48 120	52 743
Used right of note issue	15 170	12 911
Unused right of note issue	32 950	39 832
Markka/foreign currency forward contracts, million FIM		
Forward purchase contracts ¹	–	6 079
Foreign currency/foreign currency forward contracts, million FIM (middle rate of purchased currency) ¹	–	4 301
Foreign currency futures contracts, million FIM		
Purchase contracts ¹	38	–
Sales contracts ¹	6 276	1 552
Shares and other interests, nominal value, million FIM (Bank of Finland's holding in parentheses)		
Scopulus Oy	2 (100 %)	2 (100 %)
Sponda Oy	300 (100 %)	300 (100 %)
Setec Oy	40 (100 %)	40 (100 %)
Helsinki Money Market Center Ltd	35 (52 %)	35 (52 %)
Bank for International Settlements	53 (1.67 %)	56 (1.67 %)
Shares in housing companies	1	1
Real estate shares	1	1
Other shares and interests	1	1
Total	433	437
Guarantees, million FIM		
Temporary guarantee commitments in connection with the transfer of risk exposures from Skopbank	13	75
Liability arising from pension commitments, million FIM		
The Bank of Finland's pension liability	1 772	1 762
– of which covered out of reserves	1 431	1 329

¹ Middle rate of the currency as at the last business day of the year.

The Bank of Finland's real estate

Building	Address	Year of completion	Volume cu.m (approx.)
Helsinki	Rauhankatu 16	1883/1961	49 500
	Rauhankatu 19	1954	33 000
	Unioninkatu 33	1848	17 500
	Snellmaninkatu 23	1896/1988	27 500
	Liisankatu 14	1928	48 500
	Ramsinniementie 34	1920/1983	4 500
Joensuu	Torikatu 34	1984	11 000
Kuopio	Kauppakatu 25-27	1912	7 500
	Puutarhakatu 4	1993	11 900
Lahti	Torikatu 3	1929	36 500
Mikkeli	Päiviönkatu 15	1965	7 500
Oulu	Kajaaninkatu 8	1973	17 000
Tampere	Hämeenkatu 13	1942	36 000
Turku	Linnankatu 20	1914	10 500
Vantaa	Suometsäntie 1	1979	311 500
Inari	Saariselkä	1968/1976	2 000

Helsinki 15 February 1996

THE BOARD OF THE BANK OF FINLAND

Sirkka Hämäläinen, Chairman

Harri Holkeri

Esko Ollila

Kalevi Sorsa

Matti Vanhala

Notes to the financial statements

Accounting principles applied

The Bank of Finland's balance sheet follows a sectoral division, depicting the financial relations between the central bank and the foreign and domestic sectors. The valuation principles applied in the balance sheet are explained in the notes to the various items. The valuation principles applied to foreign securities were changed during the financial year. In keeping with the Act on the Bank of Finland, fixed assets, shareholdings and long-term expenditure are entered as expenditure in full in their year of acquisition and thus do not show up in the balance sheet. The Bank of Finland's shareholdings, other interests and real estate are listed in the appendices to the financial statements.

Foreign currency assets and liabilities have been translated into markkaa at the middle exchange rates as at 31 December 1995.

In accordance with section 17, subsection 1, paragraph 2, of the Act on the Bank of Finland, the Parliamentary Supervisory Board confirms the accounting principles applied.

Notes to the profit and loss account

1. Domestic interest income

Domestic interest income, FIM 504 million, includes FIM 202 million in interest income on securities with repurchase commitments and FIM 226 million in interest income on bonds. Domestic interest income decreased by FIM 21 million from the previous year.

2. Foreign interest income

Foreign interest income amounted to FIM 2 977 million, which is FIM 257 million more than in the previous year.

3. Domestic interest expense

Domestic interest expense, FIM 2 120 million, increased by FIM 476 million. Interest expense on CDs issued by the Bank of Finland amounted to FIM 2 047 million.

4. Interest margin

The interest margin amounted to FIM 1 305 million, which is FIM 250 million less than in the previous year.

5. Other income

Other income, FIM 128 million, includes FIM 34 million in gains on the sales of branch real estate and FIM 30 million in rental income on real estate.

6. Other expense

The wage bill amounted to FIM 147 million. Social security costs include FIM 59 million in pensions paid.

In accordance with the Act on the Bank of Finland, acquisitions of fixed assets and other long-term expenditures are entered as expense under depreciation in the year they are incurred by the Bank. Thus depreciation includes all acquisitions of fixed assets and other long-term expenses for the financial year. Expenses for repair and renovation of buildings accounted for FIM 31 million of depreciation and acquisitions of machinery and equipment for FIM 14 million.

7. Expense and income related to financial supervision

The operating costs (salaries, depreciation, other expense) of the Financial Supervision Authority, which operates in connection with the Bank, are shown as separate items in the Bank of Finland's profit and loss account. These costs are covered by supervision fees subsequently collected from the supervised entities.

8. Valuation gain/loss on foreign securities

Valuation gain/loss on foreign securities includes gains and losses on sales of securities and, for securities holdings, the amortized premium or discount and the difference between the acquisition price (adjusted by the amortized premium/discount) and the market value, if the market value is lower. A net valuation gain of FIM 884 million was entered in respect of foreign securities in 1995.

9. Exchange rate gain/loss

Exchange rate gain/loss includes all exchange-rate-induced changes in the values of foreign currency claims and liabilities and off-balance-sheet items, as well as net earnings from foreign exchange dealings. During the financial year, the markka strengthened against the key reserve currencies, ie the Deutschemark, US dollar, French franc, pound sterling, Japanese yen and Dutch guilder. Exchange rate losses totalled FIM 2 996 million, of which FIM 2 131 million was entered in the profit and loss account.

10. Changes in provisions

Employees' pension contributions totalling FIM 7 million were collected from wages during 1995 and transferred to the pension provision. Interest is calculated on employees' pension contributions and on the accumulated pension provision at a rate equivalent to the base rate plus 2 percentage points, and the pension provision is increased by the resulting amount. The pension provision was increased by a total of FIM 102 million.

The provision, FIM 369 million, was run down in its entirety in accordance with section 30 of the Act on the Bank of Finland.

11. Result for the financial year

A result of zero markkaa was reported for the financial year.

Notes to the balance sheet

1. Gold and foreign currency items

As in previous years, gold has been entered at the value of FIM 35/g in the balance sheet. On 31 December 1995, the market price of gold was FIM 54/g. At the end of the year, the Bank's holdings of gold totalled 49 773 kilos, while the corresponding amount at the end of 1994 was 62 299 kilos. The amount of gold in the Bank of Finland's balance sheet was changed and a new balance sheet item, 'ECU-claim on the European Monetary Institute', was added to the foreign exchange reserves. These changes were due to the fact that in connection with Finland's membership of the EU, the agreement on the European Monetary System (EMS) entered into force in respect of Finland on 1 January 1995. Pursuant to the agreement, the Bank of Finland exchanged with the European Monetary Institute 20 per cent of its gold and dollar reserves for ECUs.

The item 'allocations of special drawing rights' under liabilities corresponds to the item 'special drawing rights' under foreign currency claims. Interest is paid on both items at a rate equivalent to the SDR interest rate.

The SDR-denominated reserve tranche and the markka subscription together form Finland's quota in the IMF. The counterpart of the markka subscription is included in the IMF markka accounts under foreign liabilities. The markka subscription and the corresponding markka accounts are linked to the exchange rate of the special drawing right (SDR) in

accordance with the practice applied by the IMF. Other foreign claims also include the contribution to the European Monetary Institute.

Foreign currency claims consist mainly of foreign securities issued or guaranteed by governments and foreign bank deposits. The item also includes foreign sight accounts as well as foreign means of payment held by the Bank of Finland.

The valuation principles applied to securities included in foreign exchange reserves were changed in financial year 1995. Previously the securities were valued at the lower of nominal value and market value. In financial year 1995, securities were entered at the time of acquisition at acquisition cost. Subsequently, the difference between a security's acquisition cost and nominal value (premium or discount) is amortized as profits or losses over the remaining maturity of the security. In the financial statements, the acquisition cost of the securities (adjusted by amortized premium or discount) is compared to the market value at the balance sheet date. If the market value is lower, the securities are entered in the balance sheet at their market value.

Foreign currency liabilities consist of convertible markka claims of international organizations and foreign banks on the Bank of Finland.

2. Claims on financial institutions

Certificates of deposit are discount instruments issued by banks.

Securities with repurchase commitments (repos) are the principal instruments used in money market operations.

Holdings of bonds issued by banking institutions consist mainly of investments. They are valued at nominal value.

3. Claims on the public sector

Total coinage indicates the State's liability to the Bank of Finland arising from its obligation to redeem coins.

4. Claims on corporations

Credits for financing domestic deliveries have been granted either in the form of loans or bonds. Bonds are valued at nominal value. The interest rate ranges from the base rate to the base rate plus 1–2.5 percentage points.

The item 'other' mainly consists of securities classified as investments and valued at nominal value.

5. Other assets

The outstanding amount of loans for stabilizing the money market remained unchanged during 1995, at FIM 4 532 million. A total of FIM 15 582 million of Bank of Finland financing was committed to the takeover of Skopbank and the transfer of Skopbank's risk exposures in 1991–1992. Of this amount, FIM 5 750 million has been recouped, FIM 3 900 million has been entered as losses in the profit and loss account and FIM 1 400 million has been capitalized in the balance sheet.

Accrued items are mainly interest receivables. Accrued items for 1994 include the difference between the nominal value of foreign securities and the lower of acquisition price and market value if the nominal value is lower than these. Owing to a change in valuation principles, a corresponding item is not included in the accrued items for 1995. Other assets also include FIM 109 million in staff housing loans. The interest rate charged on old housing loans is the same as the base rate; the rate on loans granted after 16 February 1993 is the base rate plus 2 percentage points.

6. Valuation account

The valuation account is composed of exchange rate adjustments of FIM 865 million and a valuation adjustment of FIM –222 million. The valuation adjustment derives from the terms and conditions of the gold swap agreement in connection with the European Monetary System (EMS).

7. Capitalized expenditures and losses due to safeguarding the stability of the money market

The losses incurred as a result of the sale of Skopbank's shares and preferred capital certificates to the Government Guarantee Fund in 1992 were capitalized in the balance sheet. No write-offs were made in respect of this item in 1995. The amount still to be written off stood at FIM 1 400 million.

8. Notes and coin in circulation

Notes and coin in circulation consists of notes and coin held by the public and banking institutions.

9. Certificates of deposit

Certificates of deposit issued by the Bank of Finland are valued at nominal value. The difference between the nominal value and the issue price has been entered in accrued items and is allocated to interest expense over the maturity of the instrument.

10. Liabilities to financial institutions

Call money deposits in 1994 constitute the credit balances on current accounts held by banking institutions entitled to central bank financing. The Bank of Finland changed the minimum reserve system so that, with effect from 2 October 1995, the banking institutions subject to the minimum reserve requirement that have access to the liquidity credit facility and a current account at the Bank of Finland fulfil their minimum reserve requirements on the basis of the monthly averages of the balances on their current accounts at the end of each day. The Bank of Finland may pay interest on deposits exceeding the minimum reserve requirement. On 31 December the excess reserve rate was 2.25 per cent.

11. Liabilities to the public sector

This item consists mainly of the Government Guarantee Fund's deposit account and current account at the Bank of Finland.

12. Liabilities to corporations

Deposits for investment and ship purchase comprise statutory deposits made with the Bank of Finland by companies which have made an investment or ship purchase reserve. The deposits are interest-bearing and the rate of interest is determined according to the Investment Reserves Act.

13. Other liabilities

Accrued items consist mainly of accrued interest payable.

Other liabilities include FIM 9 million of notes in circulation in the old denomination.

14. Provisions

The Bank of Finland's pension liabilities total FIM 1 772 million; 80.8 per cent of this amount is covered by the provision.

Other provisions for 1994 include the provision pursuant to section 30 of the Act on the Bank of Finland, which was run down in the 1995 financial statements.

15. Capital accounts

The Bank's primary capital and reserve fund were unchanged.

Auditors' report

We, the Auditors elected by Parliament, have audited the accounts, including the financial statements, and the management of the Bank of Finland for 1995 to the extent required by good auditing practice.

In the course of the accounting year, the Internal Audit Department of the Bank of Finland has carried out the audit of the Bank's accounting and operations. We have examined the reports issued on the internal audit at the Bank.

We have read the Report on Activities of the Bank of Finland, and the Board of Management has provided us with information on the Bank's operations.

The financial statements of the Bank of Finland have been prepared in keeping with the principles on closing the accounts confirmed by the Parliamentary Supervisory Board and current regulations.

On the basis of the above and in the absence of any further comments raised by the audit, we propose that the profit and loss account and the balance sheet be confirmed and the Board of Management discharged from liability for the accounting year audited by us.

Helsinki, 7 March 1996

AUDITORS OF THE BANK OF FINLAND

Kauko Heikkinen

Johannes Leppänen

Iivo Polvi

Chartered Public Finance Auditor,
Approved Auditor

Matti Saarinen

Martti Tiuri

./ Kalervo Virtanen

Authorized Public Accountant

Appendices

Measures concerning monetary and foreign exchange policy and the financial markets in 1995

- February**
- Tender rate**
The Bank of Finland raised its tender rate on 10 February from 5.5 per cent to 5.75 per cent.
- March**
- Increase in the capital of Asset Management Company Arsenal Ltd**
On 23 March, the Government decided to raise the share capital of Asset Management Company Arsenal Ltd by FIM 8 billion. The capital injection was necessary to cover losses incurred during 1995.
- April**
- Long-term reference rates**
On 21 April, the Bank of Finland recommended that the three- and five-year reference rates which it calculates should no longer be used as reference rates for new loans.
- June**
- HELIBOR rates**
The method of calculating the HELIBOR rates was revised as from 1 June. As a rule, the calculation will take into account offers to repurchase their own certificates of deposit coming from all banks which have been accepted by the Bank of Finland as counterparties in money market operations; the highest and lowest rates quoted for each maturity are omitted.
- Counterparties in the Bank of Finland's money market operations and the instruments employed**
On 1 June, the Bank of Finland revised the criteria applied in the selection of counterparties for its money market operations and accorded priority status to risk-free securities.
- Weekly repo auctions discontinued**
On 1 June, the Bank of Finland discontinued the weekly tenders (repo auctions) which it had arranged for market makers in benchmark government bonds.
- Sale of Skopbank to Svenska Handelsbanken**
On the proposal of the Government Guarantee Fund, the Government approved, on 2 June, an arrangement whereby the sound parts of Skopbank were sold to the Swedish bank Svenska Handelsbanken. The deal involved mainly the parent bank Skopbank's good loans and guarantees as well as the share capital of Industrialization Fund of Finland Ltd and SKOP Finance Ltd., which are part of the Skopbank group. Skopbank subsidiaries Finnish Real Estate Bank Ltd and the credit card company Aktiiviraha Oy were also included in the deal.
- Tender rate**
The Bank of Finland raised its tender rate on 9 June from 5.75 per cent to 6.00 per cent.

October

The minimum reserve system

The Bank of Finland revised the banks' minimum reserve system so that as from October 1995 fulfilment of the minimum reserve requirement is based on a monthly average.

Tender rate

The Bank of Finland lowered its tender rate on 5 October from 6 per cent to 5.5 per cent. In addition, the interest rate on banks' excess reserves was cut from 4.0 per cent to 3.5 per cent.

November

Base rate

The Parliamentary Supervisory Board lowered the Bank of Finland's base rate from 5.25 per cent to 5.00 per cent with effect from 1 November.

Tender rate

The Bank of Finland lowered its tender rate from 5.5 per cent to 5.0 per cent on 1 November and from 5.0 per cent to 4.75 per cent on 20 November. The interest rate on banks' excess reserves was cut from 3.5 per cent to 3.0 per cent on 1 November and from 3.0 per cent to 2.75 per cent on 20 November.

The Savings Bank of Finland and Siltapankki became asset management companies

The Ministry of Finance revoked the authorizations of the Savings Bank of Finland and Siltapankki as from 30 November 1995, and the banks became asset management companies. In addition, Siltapankki was transferred to the Arsenal Group.

December

Base rate

The Parliamentary Supervisory Board lowered the Bank of Finland's base rate from 5.00 per cent to 4.75 per cent with effect from 15 December 1995.

Tender rate

The Bank of Finland lowered its tender rate on 19 December from 4.75 per cent to 4.25 per cent. At the same time, the interest rate on banks' excess reserves was cut from 2.75 per cent to 2.25 per cent.

Main statements issued by the Bank of Finland in 1995

Statements concerning the development of the financial markets

- To the Ministry of Finance concerning the memorandum of the working group on investment services, 2 February.
- To the Ministry of Finance concerning the interim report of the working group on the deposit guarantee scheme, 9 February.
- To the Ministry of Finance concerning the proposal of a working group for a law on the regulation of foreign exchange activities and financial markets, 23 February.
- To the Ministry of Finance concerning a proposal for establishing a national securities centre, 22 March.
- To the Ministry of Finance concerning a proposal for amending the Securities Markets Act as regards the clearing and settlement of securities transactions, 30 March.
- To the Ministry of Finance concerning the obligation of an issuer of securities to provide information on a regular basis, 4 May.
- To the Ministry of Finance concerning the establishment of a national securities centre, 21 June.
- To the Ministry of Finance concerning the memorandum of the working group on a centralized entity for the cooperative banks, 29 June.
- To the Ministry of Finance concerning the memorandum of the working group dealing with revision of the deposit guarantee scheme, 29 June.
- To the Ministry of Finance concerning reform of the Mutual Funds Act, 31 August.
- To the Financial Supervision Authority concerning amendments to regulations and guidelines, 29 September and 24 October.
- To the Financial Supervision Authority concerning regulations on the reporting obligation of securities brokers and the publicizing of reports, 22 November.
- To the Ministry of Finance concerning the granting of an authorization to Helsinki Stock Exchange Ltd and the confirmation of its rules and regulations, 24 October.

Statements concerning the support of the banking system

- To the Government Guarantee Fund concerning a purchase offer in respect of the remaining balance sheet items of the Savings Bank of Finland, 9 January.
- To the Government Guarantee Fund concerning the refinancing of Asset Management Company Arsenal Ltd, 31 January.
- To the Government Guarantee Fund concerning the support of Asset Management Company Arsenal Ltd, 7 March and 2 May.
- To the Government Guarantee Fund concerning the sale of Skopbank's business operations, 30 May.

- To the Government Guarantee Fund concerning the guarantee applications of Asset Management Company Arsenal Ltd and Savings Bank of Finland, 25 August.
- To the Ministry of Finance concerning the revocation of the authorizations of Siltapankki and the Savings Bank of Finland, 7 November.
- To the Government Guarantee Fund concerning the conversion of Siltapankki into an asset management company, 7 November.

Other statements

- To the Ministry of Trade and Industry concerning a proposal for a Directive on the harmonization of guarantee activities, 7 February.
- To the Ministry of Finance concerning the memorandum of the working group on pawnbroking, 9 February.
- To the Ministry of Trade and Industry concerning a project aiming at developing the Estonian banking sector, 27 February.
- To Statistics Finland concerning revision of the classification of financial assets, 2 March.
- To the Ministry of Social Affairs and Health concerning an investigation of the employment pension scheme, 9 March and 14 June.
- To the Ministry of Trade and Industry concerning alternatives for channelling OECD consensus-term credits, 11 April.
- To the Ministry of Finance concerning the commemorative coin "50 Years of Peace 1995", 24 April.
- To the Ministry for Foreign Affairs concerning conventions on the protection of investments, 22 June.
- To the state auditors concerning the growth of government cash reserves, 8 August.
- To the Ministry of Finance concerning the EU commemorative coin, 18 August and 26 October.
- To the Ministry of Finance concerning the commemorative coin for the 50th anniversary of the founding of the United Nations, 20 September.

Tables

Discrepancies between constituent figures and totals are due to rounding.

0 less than half the final digit shown

. logically impossible

.. data not available

- nil

_ change in contents of series

Table 1.

Monthly balance sheet of the Bank of Finland in 1995, million FIM

ASSETS	I	II	III
Gold and foreign currency claims	54 805	54 058	53 492
Gold	1 742	1 742	1 742
Special drawing rights	1 370	1 775	1 616
IMF reserve tranche	1 366	1 326	1 329
ECU-claim on the European Monetary Institute	3 700	3 606	3 619
Foreign currency claims	46 627	45 608	45 185
Other foreign claims	4 654	4 653	4 654
Markka subscription to Finland's quota in the IMF	4 595	4 595	4 595
Share in the European Monetary Institute	60	59	59
Claims on financial institutions	1 946	3 275	3 638
Certificates of deposit	445	447	429
Securities with repurchase commitments	499	1 881	2 272
Term credits	-	-	-
Bonds	765	709	699
Other	238	238	238
Claims on the public sector	1 767	1 765	1 763
Total coinage	1 767	1 765	1 763
Claims on corporations	3 140	3 128	3 123
Financing of domestic deliveries (KTR)	307	295	285
Other	2 833	2 833	2 838
Other assets	5 895	5 823	5 878
Loans for stabilizing the money market	4 532	4 532	4 532
Accrued items	1 206	1 113	1 162
Other	157	178	184
Valuation account	-	877	958
Capitalized expenditures and losses due to safeguarding the stability of the money market	1 400	1 400	1 400
Total	73 607	74 980	74 905

IV	V	VI	VII	VIII	IX	X	XI	XII
50 321	50 536	51 407	51 662	51 750	48 395	47 738	50 503	48 865
1 742	1 742	1 742	1 742	1 742	1 742	1 742	1 742	1 742
1 295	1 028	1 278	1 383	1 275	1 457	1 385	1 421	1 569
1 290	1 437	1 425	1 518	1 584	1 579	1 671	1 666	1 685
3 460	3 481	3 477	3 361	3 333	3 323	3 315	3 279	3 363
42 535	42 847	43 484	43 659	43 816	40 294	39 624	42 396	40 506
4 673	4 384	4 381	4 254	4 189	4 186	4 065	4 063	3 969
4 615	4 326	4 323	4 196	4 132	4 129	4 007	4 006	3 911
58	58	58	58	57	57	57	57	58
3 828	3 128	3 871	4 253	3 876	7 315	7 181	6 395	8 831
-	-	-	-	-	-	-	-	-
2 922	2 242	3 019	3 425	3 053	6 261	5 464	5 409	7 076
-	-	-	-	-	-	714	-	-
668	648	614	591	585	541	490	473	417
238	238	238	238	238	513	513	513	1 339
1 773	1 772	1 793	1 797	1 804	1 797	1 801	1 819	1 882
1 773	1 772	1 793	1 797	1 804	1 797	1 801	1 819	1 882
3 123	3 109	3 100	3 091	3 080	3 078	3 063	2 892	2 886
273	259	244	235	224	217	202	192	185
2 851	2 851	2 856	2 856	2 856	2 861	2 861	2 701	2 700
6 006	6 051	5 823	5 791	5 889	5 855	5 559	5 599	5 645
4 532	4 532	4 532	4 532	4 532	4 532	4 532	4 532	4 532
1 306	1 350	1 111	1 092	1 197	1 166	885	915	972
168	169	179	167	160	157	142	152	141
1 889	1 266	1 114	1 855	1 504	2 120	1 981	2 144	643
1 400	1 400	1 400	1 400	1 400	1 400	1 400	1 400	1 400
73 014	71 646	72 889	74 104	73 493	74 146	72 787	74 816	74 121

Table 1. (cont.)

LIABILITIES	I	II	III
Foreign currency liabilities	556	638	242
Other foreign liabilities	5 588	5 559	5 561
IMF markka accounts	4 595	4 595	4 595
Allocations of special drawing rights	993	965	967
Notes and coin in circulation	13 592	14 087	13 846
Notes	11 979	12 451	12 216
Coin	1 613	1 635	1 630
Certificates of deposit	36 282	36 943	37 991
Liabilities to financial institutions	7 230	8 138	7 564
Reserve deposits	6 511	6 521	6 516
Call money deposits	719	1 618	1 048
Other	0	-	-
Liabilities to the public sector	184	68	68
Current accounts	0	0	0
Deposits of the Government Guarantee Fund	184	68	68
Liabilities to corporations	1 479	1 386	1 337
Deposits for investment and ship purchase	1 479	1 386	1 337
Other liabilities	453	700	834
Accrued items	431	676	800
Other	22	24	34
Valuation account	782	-	-
Provisions	1 698	1 698	1 698
Pension provision	1 329	1 329	1 329
Other provisions	369	369	369
Capital accounts	5 764	5 764	5 764
Primary capital	5 000	5 000	5 000
Reserve fund	764	764	764
Net earnings	-	-	-
Total	73 607	74 980	74 905

IV	V	VI	VII	VIII	IX	X	XI	XII
688	740	723	1 071	1 028	959	1 101	1 263	1 214
5 568	5 288	5 275	5 128	5 063	5 056	4 918	4 913	4 837
4 615	4 326	4 323	4 196	4 132	4 129	4 008	4 006	3 911
953	962	952	931	931	927	910	906	927
14 121	14 270	14 374	14 544	14 325	14 229	14 129	14 321	15 611
12 470	12 613	12 686	12 848	12 636	12 546	12 439	12 620	13 868
1 651	1 657	1 688	1 696	1 688	1 684	1 690	1 701	1 743
35 448	34 742	35 555	36 982	36 809	37 321	37 596	38 082	27 090
7 922	7 317	7 353	7 290	7 198	7 504	6 043	7 286	16 777
6 798	6 523	6 646	6 765	6 574	6 557	5 768	7 011	15 676
1 124	794	707	525	624	672	-	-	-
-	-	0	0	0	275	275	275	1 101
101	194	555	53	56	76	76	75	75
1	3	0	0	0	1	0	0	0
100	191	554	53	55	75	76	75	75
1 290	1 252	1 218	1 203	1 187	1 169	1 109	1 070	994
1 290	1 252	1218	1 203	1 187	1 169	1 109	1 070	994
415	383	374	372	366	370	354	345	327
389	347	338	344	336	337	323	305	300
26	36	36	28	31	33	31	40	27
-	-	-	-	-	-	-	-	-
1 698	1 698	1 698	1 698	1 698	1 698	1 698	1 698	1 431
1 329	1 329	1 329	1 329	1 329	1 329	1 329	1 329	1 431
369	369	369	369	369	369	369	369	-
5 764	5 764	5 764	5 764	5 764	5 764	5 764	5 764	5 764
5 000	5 000	5 000	5 000	5 000	5 000	5 000	5 000	5 000
764	764	764	764	764	764	764	764	764
-	-	-	-	-	-	-	-	0
73 014	71 646	72 889	74 104	73 493	74 146	72 787	74 816	74 121

Table 2.

Bank of Finland's foreign exchange reserves and forward exchange position¹, million FIM

	Gold	Special drawing rights	IMF reserve tranche	ECU-claim on the European Monetary Institute	Foreign currency claims	Foreign exchange reserves	Forward purchase contracts, net	Foreign exchange reserves and forward position
1991	2180	932	1 136	.	29 381	33 629	-8 696	24 933
1992	2180	564	1 732	.	25 041	29 517	-10 345	19 172
1993	2180	664	1 747	.	28 882	33 473	-2 885	30 588
1994	2180	1 537	1 354	.	47 672	52 743	6 079	58 822
1995	1 742	1 569	1 685	3 363	40 506	48 865	-	48 865
1995								
January	1 742	1 370	1 366	3 700	46 627	54 805	9 444	64 249
February	1 742	1 775	1 326	3 606	45 608	54 058	9 180	63 238
March	1 742	1 616	1 329	3 619	45 185	53 492	7 458	60 950
April	1 742	1 295	1 290	3 460	42 535	50 321	4 833	55 154
May	1 742	1 028	1 437	3 481	42 847	50 536	3 595	54 131
June	1 742	1 278	1 425	3 477	43 484	51 407	2 477	53 884
July	1 742	1 383	1 518	3 361	43 659	51 662	-	51 662
August	1 742	1 275	1 584	3 333	43 816	51 750	3 517	55 267
September	1 742	1 457	1 579	3 323	40 294	48 395	3 419	51 814
October	1 742	1 385	1 671	3 315	39 624	47 738	2 582	50 320
November	1 742	1 421	1 666	3 279	42 396	50 503	-	50 503
December	1 742	1 569	1 685	3 363	40 506	48 865	-	48 865

¹ At middle spot rates.

Table 3.

Markka's exchange rate against the ECU and the trade-weighted currency index^{1,2}

	Markka's exchange rate against the ECU	Trade-weighted currency index, 1982 = 100
1991	5.00580	101.4
1992	5.80140	116.4
1993	6.69420	132.4
1994	6.19108	123.2
1995	5.70936	111.6
1995		
January	5.87972	115.9
February	5.84352	114.9
March	5.76731	112.4
April	5.72937	111.2
May	5.70402	111.3
June	5.71859	111.5
July	5.71263	110.9
August	5.60862	109.4
September	5.63392	110.3
October	5.64587	110.4
November	5.61404	110.0
December	5.65470	111.2

¹ Prior to the pegging of the markka to the ECU on 7 June 1991, the external value of the markka was expressed in terms of a currency index.

² Daily averages.

Table 4.

Bank of Finland's base rate

Effective	%
1.11.1979	8.50
1.2.1980	9.25
1.6.1982	8.50
1.7.1983	9.50
1.2.1985	9.00
1.1.1986	8.50
1.3.1986	8.00
19.5.1986	7.00
16.5.1988	8.00
1.1.1989	7.50
1.11.1989	8.50
1.5.1992	9.50
1.1.1993	8.50
15.2.1993	7.50
17.5.1993	7.00
15.7.1993	6.50
16.8.1993	6.00
1.12.1993	5.50
1.2.1994	5.25
1.11.1995	5.00
15.12.1995	4.75

Table 5.

Bank of Finland's minimum reserve system¹

	Reserve requirement %			Required reserves, mill. FIM	Excess reserves, mill. FIM	Total reserves, mill. FIM
	On deposits payable on demand	On other deposits	On other items			
1993 ²	2.0	1.5	1.0	6 398	.	.
1994	2.0	1.5	1.0	6 526	.	.
1995 I-IX	2.0	1.5	1.0	6 557	.	.
1995 X-XII	2.0	1.5	1.0	6 530	616	7 146
1995						
January	2.0	1.5	1.0	6 511	.	.
February	2.0	1.5	1.0	6 521	.	.
March	2.0	1.5	1.0	6 516	.	.
April	2.0	1.5	1.0	6 798	.	.
May	2.0	1.5	1.0	6 523	.	.
June	2.0	1.5	1.0	6 646	.	.
July	2.0	1.5	1.0	6 765	.	.
August	2.0	1.5	1.0	6 574	.	.
September	2.0	1.5	1.0	6 557	.	.
October	2.0	1.5	1.0	6 557	140	6 697
November	2.0	1.5	1.0	6 545	196	6 741
December	2.0	1.5	1.0	6 487	1 512	7 999

¹ Daily average as from 2 October 1995, prior to that end-period figure.² As from 1 July.

Table 6.

Banks' liquidity position at the Bank of Finland¹, million FIM

Daily averages	Call money deposits	Liquidity credits	Liquidity position, net
1991	881	985	-103
1992	2 103	437	1 666
1993	831	425	407
1994	1 393	10	1 383
1995 I-IX	1 021	129	892
1995			
January	1 196	0	1 196
February	1 210	4	1 206
March	1 750	0	1 750
April	853	0	853
May	833	2	831
June	607	30	577
July	803	0	803
August	873	204	669
September	1 067	874	193

¹ Call money deposits were disbanded 29 September 1995.

Table 7.

Bank of Finland's standing facilities¹

	Bank of Finland's tender rate		Liquidity credit: interest rate margin, %-points	Liquidity credit: maturity, days	Call money deposits: interest rate margin, %-points	Excess reserve rate
1992 ²	13.85	1992	1.00	7	-3.00	.
1993	7.87	1993	2.00	7	-2.00	.
1994	5.11	1994	2.00	7	-2.00	.
1995	5.63	1995 I-IX	2.00	7	-2.00	.
		1995 X-XII	2.00	7	.	2.25
1995						
January	5.50	1995 January	2.00	7	-2.00	.
February	5.66	February	2.00	7	-2.00	.
March	5.75	March	2.00	7	-2.00	.
April	5.75	April	2.00	7	-2.00	.
May	5.75	May	2.00	7	-2.00	.
June	5.93	June	2.00	7	-2.00	.
July	6.00	July	2.00	7	-2.00	.
August	6.00	August	2.00	7	-2.00	.
September	6.00	September	2.00	7	-2.00	.
October	5.57	October	2.00	7	.	3.50
November	4.90	November	2.00	7	.	2.75
December	4.56	December	2.00	7	.	2.25

¹ The value for the tender rate is the arithmetical mean of the values for calendar days. The values for interest rate margins, maturity and excess reserves are end-of-period values.² July-December 1992.

Table 8.

Domestic interest rates¹, per cent

	HELIBOR						Long-term market rates		Yields on government bonds ²	
	1-month	2-month	3-month	6-month	9-month	12-month	3-year	5-year	5-year	10-year
1991	13.64	13.25	13.07	12.69	12.57	12.53	12.3	12.2	11.76	.
1992	13.49	13.30	13.27	13.08	13.00	12.96	13.1	13.0	12.04	.
1993	7.85	7.77	7.73	7.59	7.51	7.47	8.5	8.9	8.19	8.79
1994	5.11	5.20	5.35	5.78	6.10	6.33	8.5	9.3	8.40	9.07
1995	5.63	5.69	5.76	5.97	6.17	6.34	8.2	8.9	7.93	8.79
1995										
January	5.50	5.67	5.85	6.32	6.82	7.14	9.5	10.3	9.44	10.24
February	5.71	5.85	5.99	6.32	6.68	6.97	9.3	10.2	9.30	10.22
March	5.78	5.92	6.06	6.48	6.79	7.07	9.2	10.1	9.20	10.18
April	5.75	5.84	5.97	6.31	6.55	6.82	8.7	9.4	8.36	9.42
May	5.72	5.78	5.87	6.06	6.22	6.45	8.2	8.9	7.76	8.84
June	5.93	5.98	6.02	6.21	6.40	6.57	8.3	8.9	7.69	8.70
July	5.97	6.06	6.13	6.40	6.63	6.80	8.5	9.0	7.76	8.74
August	5.99	6.04	6.08	6.25	6.41	6.56	8.1	8.6	7.32	8.34
September	5.97	5.95	5.95	5.97	6.00	6.04	7.6	8.1	7.19	7.98
October	5.58	5.59	5.61	5.65	5.70	5.76	7.4	8.0	7.48	7.95
November	4.90	4.91	4.93	4.99	5.05	5.11	6.7	7.5	6.95	7.52
December	4.56	4.53	4.54	4.57	4.61	4.66	6.5	7.3	6.70	7.38

¹ Daily averages.

² The five-year yield is based on quotations for the serial bond 1/92 (15 January 1992–1999) and the ten-year yield on quotations for the housing bond 1/92 (15 March 1992 – 15 March 2002). Starting from 1 June 1993, the 10-year yield is based on quotations for the serial bond 1/93 (15 March 1993 – 15 March 2004).

Table 9.

Bank of Finland's money market operations, million FIM

	Purchases of money market instruments	Sales of money market instruments	Matured transactions, net	Money market operations, net
1991	109 568	-30 380	-81 969	-2 781
1992	76 230	-137 940	60 417	-1 293
1993	86 521	-146 899	50 486	-9 892
1994	35 540	-351 820	295 165	-21 115
1995	50 435	-434 810	393 930	9 555
1995				
January	2 580	-36 050	31 590	-1 880
February	3 490	-36 940	34 710	1 260
March	4 260	-40 440	35 360	- 820
April	2 400	-34 970	35 680	3 110
May	3 710	-32 780	28 590	-480
June	3 060	-35 560	32 400	-100
July	3 385	-36 980	32 530	-1 065
August	3 040	-36 810	33 550	-220
September	9 350	-37 350	33 740	5 740
October	5 380	-37 610	28 110	-4 120
November	4 680	-38 080	30 380	-3 020
December	5 100	-31 240	37 290	11 150

+ increases liquidity in the money market.

- decreases liquidity in the money market.

Table 10.

Bank of Finland's spot transactions¹ in the foreign exchange market, million FIM

	Purchases of foreign exchange (+)	Sales of foreign exchange (-)	Spot transactions, net
1991	35 120	-69 940	-34 820
1992	20 050	-70 640	-50 590
1993	25 120	-45 080	-19 960
1994	20 930	-12 900	8 030
1995	4 910	-5 470	-560
1995			
January	-	-190	-190
February	-	-90	-90
March	-	-1 440	-1 440
April	400	-	400
May	-	-	-
June	-	-	-
July	-	-	-
August	4 000	-780	3 220
September	450	-1 970	-1 520
October	-	-180	-180
November	60	-	60
December	-	-820	-820

+ increases liquidity in the money market.

- decreases liquidity in the money market.

¹ According to trade date.

Table 11.

Bank of Finland's forward transactions^{1,2} in the foreign exchange market, million FIM

	Forward sales of foreign exchange (+)	Matured forward sales	Forward purchases of foreign exchange (-)	Matured forward purchases	Forward transactions, net
1991	15 060	-6 280	-7 560	13 710	14 930
1992	38 710	-35 650	-5 800	4 600	1 860
1993	18 590	-28 110	-11 660	15 190	-5 990
1994	2 990	-1 320	-11 800	1 320	-8 810
1995	-	-	-15 040	20 400	5 360
1995					
January	-	-	-6 690	3 430	-3 260
February	-	-	-1 130	1 040	-90
March	-	-	-	1 350	1 350
April	-	-	-3 780	6 290	2 510
May	-	-	-	1 300	1 300
June	-	-	-	1 110	1 110
July	-	-	-	2 450	2 450
August	-	-	-3 440	-	-3 440
September	-	-	-	-	-
October	-	-	-	860	860
November	-	-	-	2 570	2 570
December	-	-	-	-	-

+ increases liquidity in the money market.

- decreases liquidity in the money market.

¹ According to trade date.² Incl. outright deals; these do not have an immediate impact on liquidity.

Table 12.

Foreign exchange rates: annual middle spot rates, 1990–1995, FIM

Currency	1990			1991			1992		
	Max.	Av.	Min.	Max.	Av.	Min.	Max.	Av.	Min.
1 USD, New York	4.089	3.823	3.532	4.555	4.046	3.539	5.275	4.483	3.840
1 CAD, Montreal	3.523	3.277	3.034	4.030	3.533	3.059	4.171	3.706	3.210
1 GBP, London	7.200	6.808	6.431	8.073	7.131	6.863	9.023	7.875	7.572
1 IEP, Dublin	6.454	6.325	6.201	7.456	6.511	6.214	8.733	7.636	7.201
1 SEK, Stockholm	0.6545	0.6459	0.6369	0.7623	0.6684	0.6430	0.8845	0.7714	0.7369
1 NOK, Oslo	0.6174	0.6110	0.6079	0.7107	0.6236	0.5966	0.8170	0.7222	0.6888
1 DKK, Copenhagen	0.6298	0.6181	0.6066	0.7182	0.6322	0.6074	0.8580	0.7444	0.6968
1 ISK, Reykjavik	0.0669	0.0656	0.0646	0.0778	0.0684	0.0652	0.0873	0.0778	0.0725
1 DEM, Frankfurt a.M.	2.4282	2.3664	2.3343	2.7905	2.4380	2.3237	3.3097	2.8769	2.7122
1 NLG, Amsterdam	2.1524	2.1002	2.0705	2.4766	2.1634	2.0620	2.9440	2.5552	2.4079
1 BEF, Brussels	0.1173	0.1145	0.1121	0.1354	0.1184	0.1129	0.1608	0.1397	0.1310
1 CHF, Zurich	2.8950	2.7576	2.5965	3.1458	2.8208	2.7407	3.6828	3.2000	2.9228
1 FRF, Paris	0.7135	0.7024	0.6912	0.8162	0.7169	0.6863	0.9682	0.8486	0.7947
1 ITL, Rome	0.00324	0.00319	0.00314	0.00370	0.00326	0.00314	0.00423	0.00364	0.00332
1 ATS, Vienna	0.3452	0.3363	0.3316	0.3964	0.3464	0.3301	0.4704	0.4088	0.3854
1 PTE, Lisbon	0.0274	0.0268	0.0265	0.0321	0.0280	0.0266	0.0370	0.0332	0.0309
1 ESP, Madrid	0.0385	0.0375	0.0362	0.0443	0.0389	0.0376	0.0498	0.0438	0.0424
1 GRD, Athens	..	..	..	0.0250 ¹	0.0224 ¹	0.0220 ¹	0.0260	0.0235	0.0220
1 EEK, Tallinn	.	.	.	.	.	.	.	.	.
1 JPY, Tokyo	0.02872	0.02647	0.02466	0.03508	0.03008	0.02677	0.04234	0.03546	0.03098
1 AUD, Melbourne	3.207	2.988	2.697	3.580	3.152	2.758	3.632	3.289	2.757
1 SUR, Moscow, clearing	6.694	6.542	6.414	..	..	..	.	.	.
1 special drawing right (SDR)	5.34498	5.18322	5.07250	6.29360	5.52733	5.13880	7.25239	6.31546	5.70934
1 XEU (ECU), commercial	4.964	4.864	4.779	5.698	5.003	4.777	6.553	5.798	5.526

¹ For seven months.

Currency	1993			1994			1995		
	Max.	Av.	Min.	Max.	Av.	Min.	Max.	Av.	Min.
1 USD, New York	6.061	5.719	5.294	5.7999	5.2184	4.5345	4.8071	4.3658	4.1839
1 CAD, Montreal	4.865	4.434	4.163	4.412	3.824	3.351	3.424	3.181	3.029
1 GBP, London	8.963	8.582	8.039	8.596	7.982	7.363	7.556	6.891	6.515
1 IEP, Dublin	9.101	8.371	7.996	8.284	7.799	7.238	7.476	6.999	6.728
1 SEK, Stockholm	0.8106	0.7350	0.6826	0.7076	0.6758	0.6339	0.6576	0.6123	0.5713
1 NOK, Oslo	0.8585	0.8059	0.7648	0.7744	0.7393	0.6900	0.7148	0.6889	0.6714
1 DKK, Copenhagen	0.9527	0.8822	0.8296	0.8590	0.8207	0.7705	0.7942	0.7790	0.7608
1 ISK, Reykjavik	0.0924	0.0846	0.0788	0.0797	0.0745	0.0682	0.0708	0.0674	0.0648
1 DEM, Frankfurt a.M.	3.6450	3.4584	3.2704	3.3625	3.2169	3.0115	3.1595	3.0471	2.9465
1 NLG, Amsterdam	3.2395	3.0787	2.9102	3.0028	2.8684	2.6862	2.8201	2.7202	2.6334
1 BEF, Brussels	0.1767	0.1655	0.1580	0.1635	0.1561	0.1463	0.1533	0.1481	0.1435
1 CHF, Zurich	4.1700	3.8706	3.6253	4.0067	3.8179	3.5755	3.8405	3.6941	3.5426
1 FRF, Paris	1.0756	1.0096	0.9581	0.9853	0.9406	0.8749	0.9044	0.8748	0.8562
1 ITL, Rome	0.00394	0.00364	0.00337	0.00345	0.00324	0.00290	0.00296	0.00268	0.00247
1 ATS, Vienna	0.5182	0.4916	0.4653	0.4779	0.4573	0.4275	0.4490	0.4331	0.4189
1 PTE, Lisbon	0.0402	0.0356	0.0326	0.0328	0.0314	0.0294	0.0303	0.0291	0.0284
1 ESP, Madrid	0.0512	0.0451	0.0405	0.0408	0.0390	0.0357	0.0361	0.0350	0.0336
1 GRD, Athens	0.0270	0.0250	0.0230	0.0230	0.0215	0.0195	0.0201	0.0189	0.0180
1 EEK, Tallinn	0.4556	0.4323	0.4088	0.4203	0.4021	0.3764	0.3949	0.3809	0.3683
1 JPY, Tokyo	0.05827	0.05168	0.04263	0.05436	0.05106	0.04672	0.05222	0.04663	0.04106
1 AUD, Melbourne	4.306	3.885	3.569	4.102	3.814	3.330	3.683	3.238	3.022
1 SUR, Moscow, clearing	.	.	.	.	.	.	.	.	.
1 special drawing right (SDR)	8.33894	7.98641	7.31083	7.93658	7.46629	6.77181	6.99188	6.61196	5.60843
1 XEU (ECU), commercial	7.101	6.685	6.380	6.475	6.175	5.729	5.919	5.644	5.457

Table 13.

Foreign exchange rates: monthly middle spot rates in 1995, FIM

Currency	January			February			March		
	Max.	Av.	Min.	Max.	Av.	Min.	Max.	Av.	Min.
1 USD, New York	4.8071	4.7358	4.6809	4.7501	4.6433	4.5192	4.4840	4.3769	4.2781
1 CAD, Montreal	3.424	3.352	3.295	3.393	3.315	3.242	3.212	3.111	3.029
1 GBP, London	7.556	7.458	7.398	7.512	7.300	7.144	7.137	7.004	6.911
1 IEP, Dublin	7.476	7.375	7.316	7.417	7.256	7.149	7.097	6.993	6.889
1 SEK, Stockholm	0.6389	0.6344	0.6289	0.6355	0.6288	0.6156	0.6128	0.6021	0.5875
1 NOK, Oslo	0.7148	0.7071	0.6996	0.7117	0.7041	0.6989	0.7049	0.6979	0.6916
1 DKK, Copenhagen	0.7937	0.7851	0.7773	0.7904	0.7832	0.7776	0.7900	0.7770	0.7622
1 ISK, Reykjavik	0.0708	0.0698	0.0690	0.0708	0.0697	0.0687	0.0690	0.0680	0.0660
1 DEM, Frankfurt a.M.	3.1345	3.0930	3.0500	3.1185	3.0913	3.0710	3.1595	3.1138	3.0615
1 NLG, Amsterdam	2.7964	2.7591	2.7231	2.7823	2.7576	2.7397	2.8201	2.7768	2.7317
1 BEF, Brussels	0.1521	0.1501	0.1484	0.1514	0.1501	0.1492	0.1533	0.1509	0.1487
1 CHF, Zurich	3.7238	3.6782	3.6158	3.6980	3.6526	3.6122	3.8338	3.7378	3.6111
1 FRF, Paris	0.9044	0.8946	0.8854	0.8996	0.8889	0.8778	0.8973	0.8790	0.8686
1 ITL, Rome	0.00296	0.00294	0.00291	0.00295	0.00287	0.00270	0.00271	0.00259	0.00253
1 ATS, Vienna	0.4457	0.4396	0.4335	0.4433	0.4393	0.4364	0.4490	0.4424	0.4351
1 PTE, Lisbon	0.0303	0.0300	0.0297	0.0302	0.0299	0.0297	0.0299	0.0296	0.0291
1 ESP, Madrid	0.0361	0.0357	0.0354	0.0359	0.0356	0.0351	0.0350	0.0341	0.0336
1 GRD, Athens	0.0201	0.0199	0.0197	0.0200	0.0197	0.0194	0.0193	0.0192	0.0190
1 EEK, Tallinn	0.3918	0.3866	0.3812	0.3898	0.3864	0.3839	0.3949	0.3892	0.3827
1 JPY, Tokyo	0.04804	0.04752	0.04692	0.04780	0.04725	0.04669	0.04969	0.04833	0.04635
1 AUD, Melbourne	3.683	3.625	3.570	3.603	3.460	3.345	3.308	3.216	3.145
1 special drawing right (SDR)	6.99188	6.94337	6.89688	6.97490	6.86328	6.75995	6.80026	6.72357	6.60866
1 XEU (ECU), commercial	5.919	5.859	5.812	5.893	5.811	5.756	5.756	5.700	5.674

Currency	April			May			June		
	Max.	Av.	Min.	Max.	Av.	Min.	Max.	Av.	Min.
1 USD, New York	4.3244	4.2650	4.2040	4.4171	4.3155	4.2070	4.3662	4.2983	4.2471
1 CAD, Montreal	3.154	3.096	3.043	3.258	3.172	3.093	3.178	3.120	3.084
1 GBP, London	6.998	6.862	6.803	6.927	6.854	6.699	6.921	6.853	6.719
1 IEP, Dublin	7.048	6.948	6.863	7.091	6.999	6.881	7.076	7.004	6.918
1 SEK, Stockholm	0.5876	0.5810	0.5713	0.6006	0.5919	0.5802	0.6001	0.5920	0.5852
1 NOK, Oslo	0.7015	0.6889	0.6844	0.6923	0.6860	0.6812	0.6919	0.6891	0.6866
1 DKK, Copenhagen	0.7942	0.7855	0.7789	0.7883	0.7832	0.7797	0.7900	0.7858	0.7834
1 ISK, Reykjavik	0.0690	0.0676	0.0663	0.0692	0.0673	0.0651	0.0682	0.0678	0.0672
1 DEM, Frankfurt a.M.	3.1455	3.0947	3.0615	3.0895	3.0663	3.0475	3.0825	3.0668	3.0565
1 NLG, Amsterdam	2.8099	2.7641	2.7347	2.7590	2.7390	2.7215	2.7541	2.7406	2.7306
1 BEF, Brussels	0.1530	0.1505	0.1490	0.1500	0.1490	0.1481	0.1501	0.1493	0.1489
1 CHF, Zurich	3.8405	3.7580	3.7206	3.7472	3.6980	3.6497	3.7282	3.7104	3.6883
1 FRF, Paris	0.8981	0.8814	0.8694	0.8750	0.8670	0.8585	0.8799	0.8736	0.8707
1 ITL, Rome	0.00251	0.00249	0.00247	0.00268	0.00261	0.00254	0.00267	0.00262	0.00258
1 ATS, Vienna	0.4472	0.4398	0.4352	0.4389	0.4360	0.4333	0.4386	0.4362	0.4346
1 PTE, Lisbon	0.0298	0.0293	0.0291	0.0292	0.0291	0.0290	0.0292	0.0291	0.0289
1 ESP, Madrid	0.0349	0.0343	0.0338	0.0354	0.0350	0.0344	0.0355	0.0353	0.0350
1 GRD, Athens	0.0192	0.0190	0.0189	0.0190	0.0189	0.0188	0.0191	0.0190	0.0188
1 EEK, Tallinn	0.3932	0.3868	0.3827	0.3862	0.3833	0.3809	0.3853	0.3833	0.3821
1 JPY, Tokyo	0.05222	0.05101	0.04945	0.05152	0.05078	0.05038	0.05121	0.05083	0.05029
1 AUD, Melbourne	3.200	3.139	3.075	3.270	3.143	3.059	3.134	3.094	3.033
1 special drawing right (SDR)	6.79167	6.71986	6.65998	6.79257	6.72395	6.65482	6.75809	6.72042	6.65189
1 XEU (ECU), commercial	5.747	5.671	5.646	5.681	5.647	5.626	5.687	5.665	5.640

Table 13. (cont.)

Currency	July			August			September		
	Max.	Av.	Min.	Max.	Av.	Min.	Max.	Av.	Min.
1 USD, New York	4.3043	4.2488	4.1924	4.3990	4.3000	4.1839	4.4459	4.3717	4.2427
1 CAD, Montreal	3.183	3.121	3.064	3.281	3.173	3.068	3.282	3.240	3.146
1 GBP, London	6.848	6.776	6.700	6.799	6.743	6.685	6.880	6.810	6.712
1 IEP, Dublin	7.031	6.968	6.905	6.960	6.902	6.848	7.013	6.953	6.866
1 SEK, Stockholm	0.5963	0.5917	0.5877	0.6001	0.5949	0.5900	0.6229	0.6127	0.5997
1 NOK, Oslo	0.6934	0.6882	0.6824	0.6842	0.6784	0.6714	0.6904	0.6829	0.6776
1 DKK, Copenhagen	0.7913	0.7852	0.7782	0.7800	0.7680	0.7608	0.7835	0.7710	0.7638
1 ISK, Reykjavik	0.0682	0.0674	0.0666	0.0680	0.0666	0.0659	0.0671	0.0665	0.0655
1 DEM, Frankfurt a.M.	3.0895	3.0587	3.0285	3.0315	2.9773	2.9465	3.0425	2.9902	2.9565
1 NLG, Amsterdam	2.7580	2.7305	2.7026	2.7063	2.6583	2.6334	2.7169	2.6693	2.6387
1 BEF, Brussels	0.1502	0.1488	0.1473	0.1475	0.1448	0.1435	0.1479	0.1454	0.1438
1 CHF, Zurich	3.7189	3.6755	3.6419	3.6510	3.5959	3.5426	3.7692	3.6750	3.5935
1 FRF, Paris	0.8830	0.8788	0.8731	0.8782	0.8654	0.8573	0.8814	0.8670	0.8579
1 ITL, Rome	0.00267	0.00264	0.00261	0.00271	0.00268	0.00264	0.00276	0.00271	0.00263
1 ATS, Vienna	0.4393	0.4349	0.4304	0.4311	0.4234	0.4189	0.4325	0.4251	0.4203
1 PTE, Lisbon	0.0293	0.0291	0.0289	0.0291	0.0287	0.0285	0.0290	0.0287	0.0285
1 ESP, Madrid	0.0358	0.0355	0.0353	0.0353	0.0349	0.0346	0.0352	0.0348	0.0345
1 GRD, Athens	0.0190	0.0189	0.0187	0.0187	0.0185	0.0184	0.0187	0.0186	0.0184
1 EEK, Tallinn	0.3862	0.3823	0.3786	0.3789	0.3722	0.3683	0.3803	0.3738	0.3696
1 JPY, Tokyo	0.05040	0.04871	0.04740	0.04754	0.04547	0.04437	0.04518	0.04353	0.04247
1 AUD, Melbourne	3.159	3.088	3.022	3.319	3.186	3.095	3.385	3.298	3.203
1 special drawing right (SDR)	6.70253	6.61807	6.52500	6.54517	6.49492	6.41787	6.56928	6.40629	5.60843
1 XEU (ECU), commercial	5.690	5.662	5.613	5.634	5.569	5.530	5.629	5.580	5.535

Currency	October			November			December		
	Max.	Av.	Min.	Max.	Av.	Min.	Max.	Av.	Min.
1 USD, New York	4.3129	4.2696	4.1900	4.2886	4.2400	4.1880	4.3657	4.3351	4.2816
1 CAD, Montreal	3.235	3.174	3.055	3.192	3.134	3.090	3.211	3.165	3.134
1 GBP, London	6.826	6.738	6.623	6.761	6.629	6.515	6.795	6.669	6.576
1 IEP, Dublin	6.957	6.890	6.795	6.910	6.814	6.728	7.012	6.893	6.808
1 SEK, Stockholm	0.6414	0.6248	0.6130	0.6565	0.6427	0.6333	0.6576	0.6531	0.6455
1 NOK, Oslo	0.6893	0.6845	0.6801	0.6834	0.6785	0.6744	0.6901	0.6822	0.6750
1 DKK, Copenhagen	0.7826	0.7776	0.7726	0.7781	0.7724	0.7672	0.7867	0.7766	0.7678
1 ISK, Reykjavik	0.0666	0.0661	0.0654	0.0663	0.0656	0.0648	0.0670	0.0663	0.0653
1 DEM, Frankfurt a.M.	3.0365	3.0188	2.9975	3.0185	2.9934	2.9720	3.0455	3.0083	2.9715
1 NLG, Amsterdam	2.7112	2.6953	2.6779	2.6927	2.6724	2.6535	2.7203	2.6866	2.6542
1 BEF, Brussels	0.1477	0.1468	0.1458	0.1469	0.1457	0.1446	0.1482	0.1464	0.1446
1 CHF, Zurich	3.7635	3.7265	3.6885	3.7502	3.7109	3.6718	3.7884	3.7246	3.6544
1 FRF, Paris	0.8706	0.8643	0.8564	0.8721	0.8677	0.8636	0.8907	0.8733	0.8562
1 ITL, Rome	0.00269	0.00266	0.00259	0.00268	0.00266	0.00263	0.00275	0.00272	0.00267
1 ATS, Vienna	0.4318	0.4290	0.4259	0.4295	0.4255	0.4223	0.4327	0.4276	0.4226
1 PTE, Lisbon	0.0289	0.0287	0.0285	0.0287	0.0285	0.0284	0.0292	0.0287	0.0284
1 ESP, Madrid	0.0352	0.0349	0.0346	0.0349	0.0348	0.0346	0.0360	0.0354	0.0349
1 GRD, Athens	0.0185	0.0184	0.0182	0.0183	0.0181	0.0180	0.0184	0.0182	0.0181
1 EEK, Tallinn	0.3796	0.3773	0.3747	0.3773	0.3742	0.3715	0.3807	0.3760	0.3714
1 JPY, Tokyo	0.04301	0.04242	0.04150	0.04225	0.04162	0.04106	0.04297	0.04258	0.04226
1 AUD, Melbourne	3.297	3.237	3.141	3.250	3.160	3.098	3.259	3.213	3.161
1 special drawing right (SDR)	6.45503	6.39697	6.30644	6.42321	6.33703	6.27940	6.49332	6.43793	6.36884
1 XEU (ECU), commercial	5.588	5.546	5.493	5.536	5.496	5.457	5.597	5.530	5.483

Table 14.

Deliveries of notes and coin, million FIM

	1991	1992	1993	1994	1995
Notes delivered by Setec Oy					
1000 markka	9 000.0	4 600.0	2 100.0	–	–
500 "	4 500.0	1 225.0	2 150.0	–	–
100 "	3 107.0	4 030.0	5 000.0	6 000.0	5 000.0
50 "	925.0	1 500.0	1 000.0	–	–
20 "	–	–	400.0	800.0	400.0
10 "	607.5	–	–	–	–
Total	18 139.5	11 355.0	10 650.0	6 800.0	5 400.0
in millions of notes	128.3	77.4	96.4	100.0	70.0
Notes destroyed, in millions of notes	82.3	156.2	116.1	93.8	57.7
Coins delivered by the Mint of Finland					
Ordinary coins					
10 markka	–	–	300.0	199.8	45.1
5 "	49.6	6.7	234.7	95.0	45.1
1 "	15.0	5.0	92.6	152.0	40.0
50 penni	40.2	25.0	9.9	1.5	0.5
10 "	35.0	15.0	12.0	6.0	8.5
Commemorative coins					
2000 markka	–	–	–	–	13.8
1000 "	–	35.0	–	–	–
100 "	25.0	30.0	–	9.1	8.6
10 "	–	–	–	–	0.0
Total	164.8	116.8	649.2	463.4	161.6
Coins destroyed, in millions of coins					
Ordinary coins	474.3	141.4	221.6	289.4	91.5
Commemorative coins	0.1	0.0	0.1	0.0	0.0

Table 15.

Notes and coin in circulation, at the end of the year, million FIM

	1991	1992	1993	1994	1995
Notes					
1000 markka	3 240.6	3 375.8	4 053.0	3 829.2	4 440.1
500 "	2 600.9	2 547.2	2 593.0	2 286.6	2 505.0
100 "	5 921.2	5 806.7	5 489.7	5 195.7	5 540.6
50 "	939.2	867.0	721.3	647.1	692.5
20 "	—	—	283.8	364.2	396.2
10 "	575.4	583.2	272.6	58.7	50.1
5 "	20.8	20.8	20.5	.	.
1 "	7.7	8.0	8.2	.	.
Total	13 305.9	13 208.7	13 442.1	12 381.5	13 624.5
Ceased to be legal tender on 1 January 1994	(9.4) ¹	(9.4) ¹	(9.4) ¹	303.0	252.8
Coins					
Ordinary coins					
10 markka	—	—	208.2	325.7	365.2
5 "	374.2	384.9	433.9	416.2	428.6
1 "	386.7	384.6	387.0	371.3	390.4
50 penni	112.5	117.6	113.6	79.9	85.9
20 "	45.6	36.4	30.7	.	.
10 "	76.9	90.8	96.3	85.6	96.3
5 "	22.1	20.5	19.2	.	.
1 "	7.6	7.6	7.5	.	.
Total	1 025.6	1 042.4	1 296.4	1 278.7	1 366.4
Commemorative coins					
2000 markka	—	—	—	—	13.8
1000 "	—	35.0	35.0	35.0	35.0
100 "	65.9	92.6	90.4	98.1	104.0
50 "	72.8	71.1	71.8	71.3	70.7
25 "	19.9	19.8	19.8	19.7	19.7
10 "	38.3	38.3	38.2	38.2	38.1
Total	196.9	256.8	255.2	262.3	281.3
Total coins	1 222.5	1 299.3	1 551.6	1 541.0	1 647.7
Ceased to be legal tender on 1 January 1994	(15.7) ²	(15.7) ²	(15.7) ²	114.2	111.1

¹ Notes issued before 1963.² Coins issued before 1963.

Table 16.

Notes sorted at the Bank of Finland, in millions

	1991	1992	1993	1994	1995
1000 markka	4.0	4.2	5.6	6.0	4.9
500 "	9.4	9.4	11.1	10.9	10.5
100 "	246.7	255.1	296.3	317.5	396.0
50 "	72.0	62.0	64.8	47.9	68.6
20 "	–	–	0.6	15.8	73.0
10 "	139.8	142.0	116.5	48.8	1.0
Total	471.9	472.7	494.9	446.9	554.0

Table 17.

Bank of Finland interbank funds transfer system

	Account holders, number	Transactions					
		Between banks, number	Value, million FIM	Between the Bank of Finland and the banks, number	Value, million FIM	Total number	Total value, million FIM
1991 ¹	23	72 337	4 753 208	66 733	612 617	139 070	5 365 825
1992	21	81 127	5 465 954	70 825	883 871	151 952	6 349 825
1993	19	66 375	5 941 650	48 831	712 137	115 207	6 653 787
1994	19	62 817	5 880 570	42 544	476 226	105 361	6 356 796
1995	18	69 425	8 087 023	40 596	420 446	110 021	8 507 469
1995							
January	21	5 508	580 936	3 489	37 672	8 997	618 608
February	21	5 562	671 648	3 207	27 757	8 769	699 405
March	19	6 391	639 142	3 449	34 107	9 840	673 249
April	19	5 359	491 646	2 825	39 957	8 184	531 603
May	19	6 016	559 319	3 243	26 836	9 259	586 155
June	19	5 849	703 998	3 474	25 878	9 323	729 876
July	19	5 267	570 324	3 501	24 975	8 768	595 299
August	19	6 246	661 181	3 756	27 489	10 002	688 670
September	18	6 306	745 006	3 568	43 193	9 874	788 199
October	18	6 052	893 295	3 593	45 571	9 645	938 866
November	18	5 758	857 722	3 666	41 132	9 424	898 854
December	18	5 111	712 806	2 825	45 879	7 936	758 685

¹ From 18 March 1991.

Table 18.

Banks' intraday credit limits

End of period	Total limits, mill. FIM	Collateralized part of limits, mill. FIM	Average usage rate of limits ¹ , %
1993	13 325	3 551	8.8
1994	13 961	4 135	9.6
1995	12 357	7 013	11.4
1995			
January	14 100	4 395	11.3
February	15 100	5 395	13.0
March	14 230	5 178	10.0
April	14 746	5 682	9.8
May	15 225	6 176	11.6
June	15 243	6 181	11.7
July	15 078	6 140	10.4
August	15 075	6 139	11.9
September	15 075	6 139	12.6
October	12 349	7 005	13.4
November	12 339	6 995	11.8
December	12 357	7 013	9.6

¹ Average for the period. The usage rate of limits is calculated on the basis of current account balances at hourly intervals in the period from March to August 1993 (trial stage) and at one-minute intervals from September 1993. The rate is calculated on the basis of debt balances only.

Table 19.

Domestic clearing operations

	Debit entries		Credit entries		Total entries	
	Number, thousands	Value, million FIM	Number, thousands	Value, million FIM	Number, thousands	Value, million FIM
1991	..	..	..	..	336 899	1 436 690
1992	200 792	949 717	152 096	610 147	352 888	1 559 864
1993	206 509	1 021 592	150 291	650 571	356 800	1 672 163
1994	222 620	1 063 408	151 362	802 040	373 982	1 865 448
1995	199 646	1 160 644	156 212	811 972	355 858	1 972 616
1995						
January	15 723	93 545	12 976	64 927	28 699	158 472
February	15 256	111 336	12 336	64 754	27 592	176 090
March	16 675	106 449	13 277	65 523	29 952	171 972
April	15 238	80 500	11 519	58 989	26 757	139 489
May	18 495	93 579	13 081	63 691	31 576	157 270
June	17 797	100 110	13 001	82 961	30 798	183 071
July	18 098	82 813	11 816	60 204	29 914	143 017
August	17 514	94 674	12 277	61 736	29 791	156 410
September	16 179	101 020	15 647	62 430	31 826	163 450
October	17 567	107 181	13 620	67 684	31 187	174 865
November	15 872	97 433	13 509	74 774	29 381	172 207
December	15 232	92 004	13 153	84 299	28 385	176 303

Bank of Finland publications in 1995

Markka & talous	Quarterly bulletin in Finnish.
Bank of Finland Bulletin	11 monthly issues (double issue for June–July).
Annual publications in 1995	Bank of Finland Year Book 1994 (available separately in Finnish, Swedish and English). Finnish Bond Issues in 1994 (trilingual edition in Finnish, Swedish and English).
Economic studies in 1995	
Series A, studies intended for the general public	A:93 JARMO KARILUOTO Suomen maksutase. Laadintamenetelmät, tiedonhankinta ja vuosien 1975–92 aikasarjat (Finland's Balance of Payments. Compilation methods, sources and time series from 1975 to 1992; in Finnish) A:94 JUHANI LAURILA Finnish-Soviet Clearing Trade and Payment System: History and Lessons
Series E, doctoral theses and analytical studies	E:1 JUKKA VESALA Testing for Competition in Banking: Behavioral Evidence from Finland E:2 JUHA TARKKA Approaches to Deposit Pricing: A Study in the Determination of Deposit Interest and Bank Service Charges; doctoral thesis E:3 TIMO TYRVÄINEN Wage Determination, Taxes, and Employment: Evidence from Finland; doctoral thesis
Discussion Papers	37 research reports by various departments of the Bank of Finland appeared in the Bank of Finland Discussion Papers series.
Review of Economies in Transition	9 issues, prepared by the Unit for Eastern European Economies, appeared in the series.
Reporting of information for the balance of payments statistics	Instructions for deposit banks (separately in Finnish, Swedish and English). Instructions for enterprises (separately in Finnish Swedish and English). Payment, currency and country codes (separately in Finnish, Swedish and English).
Statistical reports	Financial Markets; published monthly (trilingual edition in Finnish, Swedish and English). Balance of payments statistics; published monthly (trilingual edition in Finnish, Swedish and English). Investment inquiry; published semiannually (separately in Finnish and Swedish). Direct investment in Finland's balance of payments; published semiannually (separately in Finnish, Swedish and English). Portfolio investment in Finland's balance of payments; published quarterly (trilingual edition in Finnish, Swedish and English).
Orders and subscriptions	The Bank of Finland's annual publications and research publications are available at bookshops. Publications required for official use and research purposes may be obtained directly from the Bank of Finland. The address is: Bank of Finland, Document Services/Address register, P.O. Box 160, 00101 Helsinki, tel. (90) 1831. Electronic mail: X.400: S=PUBLICATIONS;A=MAILNET; P=BOFNET; C=FI, Internet:PUBLICATIONS@BOFNET.MAILNET.FI. The Bank of Finland Bulletin, Markka & talous, Discussion Papers, the Review of Economies in Transition, the statistical reports and bulletins subject to charge and a list of the Bank of Finland's publications are also available at the same address.

The management and organization of the Bank of Finland at the end of 1995

Parliamentary Supervisory Board

Executive Committee

Ilkka Kanerva, Chairman

Matti Puhakka, Vice Chairman

Olavi Ala-Nissilä

Kimmo Sasi

Tuulikki Hämäläinen

Mauri Pekkarinen

Johannes Koskinen

Esko Seppänen

Anneli Jäätteenmäki

Board

Sirkka Hämäläinen, Chairman of the Board

Overall management and supervision of the activities of the Bank

General principles of central bank policy

Representation of the Board

Information

Internal Audit Department

International Secretariat

Organization and Management Development

Harri Holkeri, Member of the Board

Accounting Department

Administration Department

Data Processing Department

Legal Affairs

Maintenance of the currency supply

(Payment Instruments Department and
Branches)

Security

Esko Ollila, Member of Board

Budgeting

Financial Markets Department

Payments and Settlement Department

Personnel Department

Chairman of the Board of the Financial
Supervision Authority

Kalevi Sorsa, Member of the Board

Economics Department

Information Services

Publication and Language Services

Research Department

Unit for Eastern European Economies

Matti Vanhala, Member of the Board

Market Operations Department

Monetary Policy Department

Secretary to the Board and
the Parliamentary Supervisory Board,
Heikki T. Hämäläinen

Pentti Koivikko, Director

Reports to Harri Holkeri, Member of the Board

Administration Department

Maintenance of the currency supply

*Branches

*Payment Instruments Department

*Setec Oy, Chairman of the Board of Directors

Personnel Department: pension decisions, housing loans

Codetermination Committee

Employment agreement negotiations

The Financial Supervision Authority, which functions in connection with the Bank of Finland, publishes its own organization chart.

Departments, offices, branches

Accounting Dpt Ossi Leppänen	Accounts Office Tuula Colliander		
Administration Dpt Urpo Levo	Administrative Services Office Anna Posti	Technical Office Harri Brandt	Vantaa Real Estate Office Taisto Lehtinen
Data Processing Dpt Pertti Simola	Banking Services Seija Lomma	Data Centre Kari Helander	Monitoring Services Matti Ahrenberg
	Office and Internal Services Juhani Rapeli	Workstation and Tele-communications Services Kari Sipilä	
Economics Dpt Antti Suvanto	Forecasting Office Marti Lehtonen	Information Management Ilkka Lyytikäinen	Project Office Anne Brunila
Financial Markets Dpt Kaarlo Jännäri Heikki Koskenkylä* Peter Nyberg* Ralf Pauli*	Market Structure Office Heikki Solttila, ad. int.	Payment Systems Office Veikko Saarinen	Securities Markets Office Markku Malkamäki
Information Services Dpt Esa Ojanen	Balance of Payments Office Jarmo Nurminen	Information Management Jorma Hilpinen	Library Merja Alakulppi
Internal Audit Dpt Timo Männistö	Head of Office Anna-Maija Tikkanen		
Market Operations Dpt Markus Fogelholm	Intervention Office Olli-Pekka Lehmuusaari	Investment Office Oili Wuolle	Planning Office Anneli Isopuro
Monetary Policy Dpt Pentti Pikkarainen	Monitoring Office Laura Vajanne	Planning Office Jarmo Kontulainen	
Payments and Settlement Dpt Raimo Hyvärinen	Correspondent Banking Office Jyrki Varstala	Financial Services Office Mauri Lehtinen	Systems Office Hannu Wiksten
Payment Instruments Dpt Antti Heinonen	Bank Vault Manager Kenneth Sainio	Development Manager Kyösti Norhomaa	Systems Manager Seppo Eriksson
	Helsinki-Vantaa Regional Office Kari Lottanen	Kuopio Pekka Konttinen	Oulu Renne Kurth
	Tampere Reino Ylönen	Turku Martti Hagman	
Personnel Dpt Aura Laento Anton Mäkelä*	Personnel Affairs Office Sirpa Ahrenberg		
Publication and Language Services Antero Arimo	Language Services Carita Gabrán, ad int.	Publications Office Antero Arimo**	
Research Dpt Pekka Ilmakunnas Kari Puumanen*			
Unit for Eastern European Economies Pekka Sutela, ad int.			

Special Units

Information Antti Juusela	International Secretariat Kjell Peter Söderlund	Legal Affairs Arno Lindgren	Management Secretarial Staff Heikki T. Hämäläinen	Organization and Management Development Pirkko Pohjoisaho-Aarti	Security Jyrki Ahvonen
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* Adviser to the Board

** In addition to own duties

SETEC OY

Board: Pentti Koivikko, Mauri Jaakonaho, Matti Lehti
Managing Director: Veli Tarvainen
Management Group: Veli Tarvainen, Tom Ahlers, Pekka Kariola, Juhani Salovaara,
Kristian Silfverberg, Tapio Yrjönen

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