Criteria for Central Bank Assets: Lessons from Pre-ECB France

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The Banque de France was founded in 1800 to discount bills and issue currency.[1] Initially, it was a private institution run by its stockholders. The Banque was nationalized in 1936 and its governing council was staffed by officials with a mandate to represent various interests in society. The Banque's autonomy was largely restored in 1973, and the Banque became officially independent in 1994. Whereas the Banque had originally lent appreciable sums to the Treasury, such lending was scheduled to be eliminated beginning in 1993 as part of the move toward monetary union.[2] At that time the monetary policy operations of the Banque were revised substantially. The Banque also operates as a commercial bank, including taking deposits and holding an investment portfolio, although such activities are secondary to its responsibilities as the central bank. While secondary, these activities influence the composition of the Banque de France's assets, shown below.

The Banque's final monetary policy objective was price stability, with growth of a broad monetary aggregate and a stable exchange rate as intermediate objectives. The Banque achieved its near-term interest rate objectives through two types of repurchase agreement arrangements: the seven-day repo and the five- to ten-day repo. The difference between the demand for reserves and the Banque de France's holdings of Treasury bills was largely made up by twice-weekly seven-day repos, at a rate that was usually the market floor.[3] Bids were all serviced at the official rate, but that rate was not always announced, so the tenders could be equal to or greater than the official rate. The repos were conducted with principal market operators that tended to be larger and more sophisticated credit institutions.[4] The principal market operators transmitted bids for all other participating credit institutions. The five- to ten-day repos were similar, but they were offered under a standing facility at an elevated rate that was typically 75 to 150 basis points above the intervention rate and generally acted as the market ceiling. Because of the elevated rate, only a relatively small volume of five- to ten-day repos were usually outstanding. Following reforms to the French monetary and financial system in the mid-1980s, the Banque de France also engaged in fine-tuning operations in the form of the sale or purchase of Treasury bills, in 24- to 48-hour repos or withdrawals of liquidity.[5]

Fine-tuning operations were conducted virtually every day after 1992, for several reasons. First, in that year the Banque significantly lowered reserve requirements, leaving required reserves closer to settlement requirements and therefore reducing the ability of banks to substitute reserves across days within the settlement period.[6] Second, capital mobility increased, necessitating more frequent intervention to keep the intervention rate near its target. And third, the deregulation and modernization of money markets facilitated more frequent intervention.

Permissible Assets

Securities Owned Outright[7]

The Banque de France had the right to buy and sell Treasury bills and all negotiable debt instruments (certificates of deposit, bills issued by finance companies, commercial paper, medium-term notes). However, the market for such instruments needed to be of sufficient depth, and, as of 1994, the Banque did not operate in certificates of deposit or commercial paper; at that time it only owned Treasury bills. Rediscounting ceased in 1971 except for some preferential financing procedures (such as for medium-term export credits) that stopped in 1986.

Collateral for Advances (Repurchase Agreements)[8]

Lending to credit institutions took the form exclusively of repurchase agreements against Treasury bills and private paper—commercial paper or other credit instruments. Private securities had to have an initial maturity of less than two years and could only be issued by companies that had received the Banque de France's most favorable credit rating (3 on a scale of 3 to 6). These private securities were referred to as "mobilization certificates" and were issued by the borrowing institution on behalf of the Banque de France; the Banque retained the certificates until the expiration of the repurchase agreement.

Monetary Reserves

The Banque de France also was the repository of the monetary reserves in the form of gold and foreign exchange. As of the mid-1990s, the Banque did not use purchases and sales of these assets as instruments of monetary policy. Nevertheless, these reserves constituted a significant percentage of its assets.

Recent Composition of Assets

At the end of 1997, the Banque de France had assets equal to Fr 591.2 billion.[9] Gold and international reserves accounted for 57 percent of assets, with gold alone accounting for 25 percent of assets. The largest category of international reserves was foreign exchange assets and investments, which equaled 18 percent of assets. Claims on the European Monetary Institute equaled 10 percent of assets and claims on the International Monetary Fund equaled 4 percent of assets. Lending to credit institutions, exclusively in the form of repurchase agreements, accounted for 21 percent of assets. Treasury bills purchased to implement monetary policy equaled 3 percent of assets. The largest other categories were assets arising from commercial banking activities (largely correspondent accounts), 7 percent; securities in the course of collection (primarily checks delayed by strikes at year-end), 4 percent; and claims on the Treasury other than securities purchased to implement monetary policy, 3 percent.

Depository institutions appeared to have preferred securing repurchase agreements with private rather than public securities.[10] Of the Fr 125 billion in securities obtained through repurchase agreements owned by the Banque de France at the end of 1997, Fr 80 billion (64 percent) were secured by private claims. Fr 40 billion (32 percent) were secured by government securities, and Fr 5 billion were secured by other securities.

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[1] Banque de France, *The Banque de France: History, Organization, Role*, 1986, p. 7.

[2] Banque de France, *Annual Report*, 1997, p. 231.

[3] Banque de France, *Bulletin Digest* No. 10, October 1994, pp. 53–54.

[4] There were 26 principal market operators in 1994.

[5] Christian Pfister, 1997, "French Monetary Policy: Some Implementation Issues," in *Implementation and Tactics of Monetary Policy*, Bank for International Settlements Conference Papers No. 3, p. 121.

[6] In 1990, required reserves equaled 1.2 percent of GDP; in 1997 they equaled 0.1 percent. Pfister, 1997, p. 124.

[7] Banque de France, *Bulletin Digest* No. 10, October 1994, pp. 50–52.

[8] Banque de France, *Bulletin Digest* No. 10, October 1994, p. 52.

[9] Banque de France, *Annual Report*, 1997, p. 226.

[10] Banque de France, *Annual Report*, 1997, p. 239.