

Working  
on trust

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# Guardian of financial stability

## Introduction

Most people in the Netherlands seldom or rarely stop to think and realise that they live in a country with a well-oiled financial system. We feel that it is logical that everybody accepts our euro, that the euro maintains its value and that our purchasing power is not eroded by inflation. We trust that banks, insurers and pension funds will be as good as their word. That trust can only come about through financial stability.

Financial stability is the mission of De Nederlandsche Bank (DNB). For more than two centuries this organisation has worked towards a healthy and strong financial system deserving of the trust of the public and trade & industry.

DNB is both central bank and supervisor of the financial sector. The pillars of its activities are:  
**Monetary policy:** inflation below, but close to 2%  
**Payments:** reliable, secure and efficient payment products and systems, and  
**Supervision:** strong and sound financial firms.

DNB is therefore also dubbed “Guardian of financial stability”.

DNB carries out many of its tasks within a European context. The introduction of the euro, the European standard currency, formed a milestone. DNB stands for a financially stable Europe and works hard on achieving new European milestones.

## Towards the future

The financial world in which DNB operates is changing faster each day. Some developments have been set in motion; others will surprise us tomorrow, the day after tomorrow or next year.

The economy is changing, new financial players enter the market and others leave. National and European laws and regulations are updated all the time. Further European integration lies in store. As a central bank and supervisor we anticipate and quickly respond to new developments. And we prepare ourselves for future developments.

Financial innovations are the order of the day. New financial products may yield economic growth and profit, but also entail risks. Assessing financial risks, and issuing a warning if they seem unacceptable, is and remains a key task of DNB. Good information to the public is indispensable. It ensures that consumers, companies and financial firms are aware of the risks they take themselves and transfer to others.

All these developments greatly influence DNB's future. The financial world is rapidly changing and our activities and priorities change accordingly. But our mission will not change. Stability to us is worth its weight in gold.

## Statistics

DNB is the address for financial sector data in the Netherlands.

DNB cooperates closely with Statistics Netherlands (CBS). CBS focuses on figures about population make-up, production, prices and the labour market, while DNB addresses monetary and financial sector developments.

Of old, DNB has always provided the Dutch Balance of Payments. The Balance of Payments provides an insight into all transactions of the Netherlands and other countries and therefore a picture of our economic ins and outs.

DNB receives up-to-date figures from banks, pension funds and insurers, and investment firms in the Netherlands. That provides a wealth of financial information.

The statistical data can be found on [www.dnb.nl](http://www.dnb.nl)

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## Financial stability

DNB guards financial stability in the Netherlands and thus contributes to a healthy economy and prosperity in our country. A stable system can absorb external shocks without deranging financial markets, financial firms or the economy. Pillars for financial stability are strong and sound financial firms, a stable euro, liquid financial markets, secure and efficient payments and a balanced financial-economic policy. These pillars form the starting point for the policy tasks of DNB. Financial stability is the large common denominator of its work as supervisor and central bank.

### Overview of Financial Stability

DNB analyses the key risks to financial stability and the strength of the financial sector in the Netherlands. It relates developments in the financial environment and infrastructure on the one hand to the situation at financial firms on the other. On the basis of these analyses, DNB develops its vision on financial stability in the Netherlands. DNB publishes its findings in the biannual publication Overview of Financial Stability.

### A wealth of expertise under a single roof

DNB is the central bank and supervisor of the financial sector. That offers a great many opportunities for the exchange of knowledge between experts in many fields, such as supervisors, researchers, pension professionals, financial analysts and policy makers. This cross-fertilisation is taking on more importance in a financial-economic environment that is constantly changing and becoming more global and complex.

### International viewpoint

Financial stability in the world is good for the Netherlands. Conversely, a crisis elsewhere, for example in the Americas or Asia, may also put our stability at risk. DNB therefore looks and operates beyond our national borders. International orientation and cooperation are gaining weight, both inside and outside Europe.

### Eurosystem

Since January 1, 1999, DNB has formed part of the Eurosystem, which also incorporates the European Central Bank and the central banks of the other euro countries. The Eurosystem determines monetary policy and manages the issue of banknotes within the euro countries. Just as DNB in the Netherlands is known as the “Guardian of financial stability”, so the Eurosystem has gained renown as the guardian of stability in Europe.

## Research and advice

DNB gives independent economic advice and thus wants to contribute to a healthy and prosperous future. DNB performs extensive research and uses the findings to give considered advice, for instance, within the Social and Economic Council (SER) and various other advisory agencies and ministries. DNB gives advice on a wide range of topics, including the labour market, the ageing population and the pension system.

Research holds a prominent place within DNB. One of the fields covered by our researchers is the monetary policy of the Eurosystem. Others investigate innovations in the ways we make payments, the role of financial markets and the importance of integrity at financial firms. With its own research, DNB wants to improve the quality of its work, respond appropriately to new developments and perform its advisory role properly. In addition, DNB has selected four key areas in which it wants to excel as a centre of expertise, i.e. the pension system, insurance, the payment system and supervision.

DNB publishes its research findings on its website and in a number of publications. DNB also exchanges knowledge with other experts and knowledge centres, both nationally and internationally. In particular in those chosen fields of expertise, DNB builds on its role as a centre of expertise.

Twice a year DNB makes a forecast of the Dutch economy, using a purpose-built econometric structural model, which maps the key connections in our economy.

### Authorisations

Supervision of a firm starts with granting authorisation. Financial firms need authorisation from DNB to start their business. During regular supervision, DNB closely monitors firms. Should problems arise, for example if a firm threatens to come below the required financial level, DNB has a whole set of instruments to improve the situation. Which instrument is used depends on the seriousness of the situation. Sometimes a firm talk or a fine suffices. If that does not lead to the required result, sterner measures can be taken, such as the appointment of a 'secret receiver', who becomes a co-director behind the scenes. If the worst comes to the worst, DNB can revoke the authorisation.

### Integrity

The supervision of money transaction offices, such as foreign exchange offices, aims at preventing money laundering and the financing of terrorist activities. This supervision is primarily intended to protect the integrity of the financial system.

In the case of trust offices, which in actual practice often act as director of another firm, the aim is primarily to combat criminal activities.

### International cooperation

In many fields the employees of DNB work together with their colleagues from the European Central Bank and the other central banks of the euro area. An example is the design of new euro banknotes. In addition, DNB is a member of the working groups of the Banking Supervision Committee of the European System of Central Banks (ESCB).

At an international level, too, cooperation is high on the agenda. DNB is a member of the Financial Stability Forum. It also participates in the Committee of the Global Financial System, together with the other central banks of the G10 countries. The International Monetary Fund (IMF) is yet another platform in which DNB operates.

## A short history

DNB was founded in 1814 by King William I, who had a clear vision and aim: economic prosperity. A national bank was crucial. DNB helped the economy get back on its feet through lending to trade and industry. In addition, it started the circulation of a uniform means of exchange by issuing banknotes.

A century later, the role of money-lending institution for trade and industry had been taken over by merchant banks. DNB in turn established itself as the lending facility for the private banking sector, thus becoming a true central bank. The role of DNB as supervisor naturally originated from this. After all, it had to gain insight into the reliability of its customers.

The Bank Act 1948 laid down that DNB was responsible for maintaining the value of money. But this had actually been its task all along, as it was the sole institution allowed to issue banknotes and ensure public trust in paper money.

European cooperation led to the rise of the Economic and Monetary Union (EMU) and later to the introduction of a joint European currency, the euro. Since 1999, DNB has formed part of the Eurosystem. This system also incorporates the ECB and the central banks of the other euro countries. The Eurosystem determines the monetary policy and manages the issue of banknotes within the euro countries.

In 2004, DNB merged with the Pensions and Insurance Supervisory Authority of the Netherlands. Consequently, DNB started supervising the soundness and health of the entire Dutch financial sector, ranging from banks to pension funds and from insurers to trust offices.

## Supervision

As supervisor we commit ourselves to stability and trust in the entire financial system. That is why DNB carefully monitors the entire financial landscape, the individual firms, their intercompany relations and any potential risks.

### Financial firms

DNB supervises banks, insurers and pension funds, securities and investment firms, money transaction offices and trust offices. DNB ensures that financial firms adhere to the rules and do not take unacceptably high risks. Attention is paid to financial health, operational management, administrative organisation and internal control. DNB also checks the expertise and integrity of policy makers at financial firms. In short, DNB assesses whether financial firms are properly organised and take care of the money entrusted to them in a responsible and professional way. This is in the interest of savers, the insured, pension beneficiaries and investors, and – in the end – of the entire financial system.

For the supervision of the financial sector, DNB works together with fellow supervisor the Netherlands Authority for the Financial Markets (AFM). AFM is in charge of market conduct supervision and looks at how companies deal with their customers; DNB exercises prudential supervision and particularly looks at the

financial position of companies, the expertise and reliability of the directors and the soundness of the entire financial system.

Financial firms more and more operate across borders. DNB therefore intensively works together with foreign supervisors. And there are international partnerships specially aimed at specific cross-border organisations.

### The system

DNB not only supervises individual firms but also the financial system as a whole. That is necessary, because a problem at one firm may affect others. Any problems in the payment system may spread to financial firms or even to other parts of the economy. DNB wants to minimise the risk of such chain reactions, as they undermine financial stability.

DNB carries out research and makes recommendations for supervision of the financial system. Internationally, it plays an important role in determining international rules and regulations for financial firms.

### One Europe

The introduction of the Single Euro Payments Area (SEPA) is in full swing. The introduction of the euro, the European single currency, was followed as of 2008 by new European payment instruments, such as European transfers, European direct debits and the European bank card with chip. Meanwhile, the national payment systems have also been incorporated into one large European payment system.

## Monetary policy

The main aim of monetary policy is price stability, i.e. a price increase of below, but close to, 2 % in the euro area over the medium term. DNB conducts this policy together with the central banks of the other euro countries and the ECB, known collectively as the Eurosystem. This joint European monetary policy applies to all euro countries: Austria, Belgium, Cyprus, Finland, France, Germany, Greece, Ireland, Italy, Luxemburg, Malta, the Netherlands, Portugal, Slovenia and Spain.

### Independent

The president of DNB is a member of the ECB Governing Council and in that capacity co-decides monetary policy. The Governing Council consists of the governors of all central banks of the euro area and the ECB Executive Board. The Governing Council meets twice a month. Entirely independently, this Governing Council decides what the best monetary policy is for the euro area as a whole. The central bank governors together promote the joint European interest. Their decisions are independent of national and political interests.

### Interest rates as accelerator and brake for the economy

The ECB does not have any direct influence on the prices of goods and services, as those are determined by supply and demand. But it does have an instrument for indirectly influencing supply and demand, and therefore inflation, namely interest rates.

If inflation is about to exceed the 2% mark in the medium term, the Board of Management of the ECB may decide to raise interest rates. A higher interest rate means that it becomes more expensive for families and companies to borrow money. They may therefore decide against taking out a loan, which in turn means that they will have less money to spend. And if they do not buy as much, prices will increase at a slower pace. And that is exactly the idea behind an interest rate increase.

Conversely, the ECB may decide to cut interest rates. This will stimulate consumers and companies to borrow money, with which they buy products and services. In short, the interest rates act as the accelerator and brake of the economy.

### Research

An interest rate decision is based on thorough analyses of all available data. Those analyses are made by employees of DNB and the other central banks of the Eurosystem. They perform economic analyses to identify risks to price stability in the short and medium term. All sorts of factors are taken into account, such as price indices, currency rates, the trade cycle and budgetary policy. They also conduct monetary analyses, which pay attention to the quantity of money in circulation and the loans that banks in the euro area have outstanding. Economic and monetary analyses form the two pillars of the monetary policy of the Eurosystem.

### Management of reserves and currency market operations

DNB manages more than 600 metric tons of gold for the Dutch state. That gold forms our national nest egg. Part of it is stored in the vaults of DNB. But most of the gold is safely tucked away on the other side of the ocean, in the vaults of the Federal Reserve Bank and those of the Canadian and English central banks. Besides gold, DNB also safeguards the foreign reserve assets of the Dutch State. In addition, DNB holds part of the Japanese yen reserves owned by the ECB. The foreign reserve assets may be used to intervene in the currency markets, for instance in order to dampen exchange rate fluctuations or respond to financial crises. In those cases, the central banks may revert to buying or selling foreign currencies.

## Payments

Together with the other central banks of the euro area, DNB manages the issue of banknotes. In addition, DNB monitors security and userfriendliness of payment products such as PIN cards and payments via the internet or by mobile phone. DNB also plays a key role in the payment transactions between banks.

### Banknotes

DNB annually issues 200 million new banknotes. These banknotes are returned to DNB after use and then checked for authenticity and any imperfections. Each day, DNB checks some three to four million banknotes. Those in good condition are brought back into circulation again, whereas dirty and worn notes are taken out of circulation and destroyed. DNB's shredder cuts up some 100 million rejected banknotes each year.

DNB uses detectors to identify counterfeits, which are then meticulously examined. All data are entered into a central system of the European Central Bank (ECB), which is also accessible to Europol and the national police forces. Its aim is to trace the origin of counterfeit notes.

### Payment systems oversight

Payments should be carried out securely, reliably and efficiently. The proper functioning of a payment system or product increases public trust in the system. That is an important pillar for financial stability.

Each day millions of money transactions take place, in cash, by PIN card, credit card, direct debiting and via the internet. These payment products are subject to oversight by DNB, which plays a key role in interbank payments. When two banks are involved in a payment or transfer, the interbank settlement takes place via DNB. Banks can also settle their international payments via DNB. On a regular basis, DNB tests payment systems on the basis of international criteria. If DNB discovers possible risks, it makes recommendations to remove or reduce them.

### Securities systems

The trade in securities and the settlement of securities transactions is becoming increasingly concentrated. Large numbers of transactions and amounts are involved here. DNB assesses whether the systems for securities settlement are secure and efficient.