OESTERREICHISCHE NATIONALBANK
EUROSYSTEM

ANNUAL REPORT 2007

Stability and Security.

A Chronology of Highlights

The OeNB and Austria	2007	The OeNB and the Euro Area, ESCB and EU
Basel II enters into force on January 1, 2007, page 58 Changes in the supervisory reporting system go into effect, page 58	JANUARY	Bulgaria and Romania become EU Member States, page 46 and 49 Slovenia introduces the euro, page 45 Euro cash surpasses U.S. dollar cash in circulation (in euro terms), page 82
	FEBRUARY	
IT Division delivers Tender Operations System (TOP) for the Eurosystem, page 94	MARCH	Governing Council of the ECB increases key interest rates by 25 basis points to 3.75%, page 28 50th anniversary of the signing of the Treaty of Rome, page 43
	APRIL	
OeNB holds 35th Economics Conference on the topic "Human Capital and Economic Growth," page 89	MAY	European Commission and ECB publish convergence reports on Malta and Cyprus, page 46
	JUNE	Governing Council of the ECB increases key interest rates by 25 basis points to 4.00%, page 28 European Commission reports on Bulgaria and Romania under the Cooperation and Verification Mechanism, page 48
OeNB begins operation of clearing platform for regional interbank payments, page 78	JULY	
Deadline for exchanging ATS 500 banknotes featuring a portrait of Josef Ressel expires, page 86	AUGUST	ECB starts conducting several additional liquidity-providing tender operations as a result of the financial turmoil, page 23
OeNB negotiates the sale of an 85% share of Austria Card on January 1, 2008, to the Greek group P. Lykos S.A., page 80	SEPTEMBER	
	OCTOBER	
Austrian financial supervision reform bill is passed, page 56 Successful launch of TARGET2 by OeNB and Austrian banks, page 79 OeNB holds Conference on European Economic Integration on the topic "Currency and Competitiveness," page 89 "Gold Bars" special exhibition is opened at the OeNB's Money Museum, page 89	NOVEMBER	TARGET2 payment system goes into operation in a first group of eight European countries, page 79 European Commission presents progress reports on the EU candidate countries, page 48
Favorable IMF assessment of Austria's financial market in the IMF's Financial Sector Assessment Program (FSAP) update, page 55 OeNB, Statistics Austria and Austrian Federal Economic Chamber conclude statistics cooperation agreement, page 71	DECEMBER	Treaty of Lisbon is signed, page 43 European Commission reviews EU Member States' national reform programs, page 40 Fed, ECB and other central banks provide U.S. dollar funding in a concerted operation in December 2007 and …
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In the Article IV consultations, the IMF calls for structural adjustments of fiscal expenditures in Austria in 2008 to enable Austria to achieve a balanced budget by 2010, page 42	MARCH	Gold price passes the USD 1,000 per ounce mark, page 67 Fed, ECB and other central banks provide U.S. dollar funding in a concerted operation, page 24

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Editorial close: April 29, 2008

Ownership Structure and Decision-Making Bodies of the OeNB

Owners, General Council, State Commissioner

The OeNB's Owners

The OeNB is a stock corporation. Its nominal capital totals EUR 12 million; the majority of this sum is held by the Austrian federal government, the remainder by employer and employee organizations as well as banks and insurance corporations. Only Austrian citizens or legal persons or partnerships under commercial law which are based and have their head office in Austria and which are neither directly nor indirectly majority owned by foreigners may be shareholders. The transfer of OeNB shares requires the express approval of the General Meeting (stockholders' meeting). Since May 2006, the Republic of Austria has held 70.3% of the OeNB's capital stock.

Functions of the General Council

The General Council is charged with the supervision of all business not falling within the remit of the European System of Central Banks (ESCB). The General Council is convened by the President, as a rule once a month. Pursuant to Article 20 paragraph 2 of the Federal Act on the Oesterreichische Nationalbank 1984 (Nationalbank Act), the General Council shall advise the Governing Board in the conduct of the OeNB's business and in matters of monetary policy. The joint meetings of the General Council and the Governing Board must take place at least once every quarter. General Council approval is required for a number of management decisions, e. g. for starting and discontinuing business lines, establishing and closing down branch offices, as well as acquiring and selling holdings and real property. Also, the General Council must approve appointments of members of supervisory boards and executive bodies of companies in which the OeNB is a shareholder. Appointments of the second executive tier of the OeNB itself must likewise be confirmed by the General Council. Finally, the General Council has the exclusive right of decision on issues detailed in Article 21 paragraph 2 Nationalbank Act, e. g. on drawing up nonbinding tripartite proposals to the Austrian federal government for appointments to the OeNB's Governing Board by the Federal President, on defining general operational principles for all matters not covering the remit of the ESCB, on approving the financial statements for submission to the General Meeting, and on approving the cost estimates for the next financial year.

Composition of the General Council

The General Council consists of the President, one Vice President and twelve other members. Only persons holding Austrian citizenship may be members of the General Council. The President, the Vice President and six other members of the General Council are appointed by the federal government for a term of five years and may be reappointed.
The remaining six members are elected by the General Meeting for a term of five years, and may be reelected. Articles 20 through 30 of the Nationalbank Act govern issues pertaining to the General Council.

The General Council of the OeNB comprised the following members on December 31, 2007.

Herbert Schimetschek
President
Chairman of the Board of Management of Austria Versicherungsverein auf Gegenseitigkeit Privatstifung

Manfred Frey
Vice President
retired President of the regional finance authority of Vienna, Lower Austria and Burgenland

August Astl
Secretary General of the Austrian Chamber of Agriculture

Bernhard Felderer
Director of the Institute for Advanced Studies (IHS)

Philip Göth
Certified public accountant/tax consultant
Partner of Deloitte Zurich

Elisabeth Gürtler-Mauthner
Managing Director of Sacher Hotels Betriebsges.m.b.H. and Vice President of the Österreichische Hoteliersvereinigung (ÖHV)

Alfred Hannes Heinzel
President and CEO of Heinzel Holding GmbH

Manfred Hofmann
Director
Head of the Austrian Federal Economic Chamber's Department of Finance and Accounting
CEO of Wirtschafts-kammern Pensionskasse AG
Director of the Austrian Federal Economic Chamber's pension fund

Max Kothbauer
Chairperson of the Board of the University of Vienna

Johann Marihart
Chief Executive Director of Agrana Beteiligungs-AG

Werner Muhm
Chief of the Chamber of Labor of Vienna

Ewald Nowotny
CEO and Chairman of the Managing Board of BAWAG P.S.K. Bank für Arbeit und Wirtschaft und Österreichische Postsparkasse AG

Gerhard Randa
Chairman of the Board of Supervisory Directors of the Oesterreichische Kontrollbank AG

Walter Rothensteiner
Chief Executive Director of Raiffeisen Zentralbank Österreich AG

Representatives delegated by the Staff Council to attend proceedings that deal with personnel matters pursuant to Article 22 paragraph 5 of the Oesterreichische Nationalbank Act:

Martina Gerharter
Staff Council Chair

Gerhard Kaltenbeck
Staff Council Deputy Chair

State Commissioner
Thomas Wieser
Director General at the Federal Ministry of Finance

Deputy State Commissioner
Alfred Lejsek
Head of the Financial Markets Directorate
Federal Ministry of Finance

Personnel Changes

There were no personnel changes from April 24, 2007, to April 29, 2008.

President's Report

In 2007, following a period of solid global growth, the U.S. subprime crisis caused strong turbulence in the international financial markets, thus adversely affecting the macroeconomic environment.

Notwithstanding these circumstances, total net income generated by the Oesterreichische Nationalbank (OeNB) in 2007 was considerably higher than in 2006. While the strong appreciation of the euro against the U.S. dollar and other major currencies created a difficult operational environment for the Eurosystem central banks, the higher level of short-term interest rates had a positive impact on operating results. Even though almost two-thirds of the OeNB's operating profit had to be allocated to the risk provisions, which serve to cover financial risk, the 2007 operating profit (after risk provisioning) is about one-quarter higher than a year earlier. However, from a longer-term perspective on profitability, the OeNB's capital has been more than halved, above all owing to legal changes implemented since the end-1990s – a fact that has been pointed out repeatedly over the past years. Therefore, looking ahead, framework conditions will have to be modified to strengthen the OeNB's capital base and risk-bearing capacity. It is worth noting in this context that the liability base of the Eurosystem central banks has increased markedly, given the successful establishment of the euro. In view of their task to ensure financial stability, central banks' capital ratio should reflect the growth in the liability base according to internationally recommended standards. After all, national central banks need to have a sound capital base – this is a cornerstone of Eurosystem credibility.

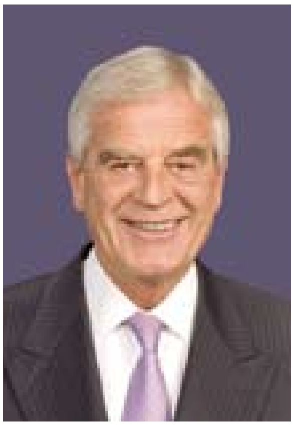
On the basis of its core functions, the OeNB pursues medium-term corporate goals in priority areas of competence – stability policy, risk management, means of payment and the analysis of Central, Eastern and Southeastern European countries. In 2007, work has progressed in all these areas. Optimizing resource allocation has been a guiding principle for several years, with a focus on lowering expenditure sustainably and on reducing staff.

In addition to its ongoing participation in the European System of Central Banks, the OeNB accomplished important work in all business areas in 2007, notably implementing its investment strategy successfully, taking significant steps toward the implementation of the Single Euro Payments Area (SEPA) and, with the smooth launch of TARGET2, contributing to the integration of payments in Europe. In external communications, the OeNB continued to provide both clear information on monetary policy and high-quality financial statistics. Furthermore, the OeNB's mandate in the field of banking supervision was extended significantly as of 2008, following the financial supervision reform in Austria, and the OeNB has risen to the challenge. In accordance with the principle of optimal resource allocation, the OeNB will implement this reform in cooperation with the Financial Market Authority (FMA). The OeNB has also made further progress in restructuring its holdings, taking advantage of synergies. A strategic partner – Lykos Group – was found for Austria Card, which produces smart cards and identity systems. This strategic partnership is meant to strengthen Austria Card's market position in the field of bank cards, thus also benefiting the Austrian economy.

President
Herbert Schimetschek

Governing Board

Governor's Report



The global economy initially continued to grow dynamically in the first half of 2007. But since August 2007, macroeconomic events have been shaped by a development termed the subprime crisis. Radiating from the relatively small and contained subprime market in the U.S.A., defaults spread into the global financial system through complex credit risk transfer instruments. The turbulences dealt a direct blow to the U.S. economy, which – despite a substantial relaxation of monetary policy and an economic stimulus package – cooled down markedly, dampening global economic growth, too.

The euro area economy remained robust in 2007, with economic activity beginning to slow somewhat only toward the end of the year. Real output growth in 2007 came to 2.6%, just marginally lower than in 2006. The structural reforms initiated under the Lisbon Strategy for Growth and Jobs and their subsequent implementation in line with the national reform programs contributed substantially to economic growth. The unemployment rate in the euro area accordingly declined to 7.4%, a level not seen in 25 years. The spillover effects of the U.S. subprime crisis will not leave the euro area completely unscathed, but the euro area economy's sound fundamentals and enhanced structures will support moderate economic growth also in 2008.

The boom in oil prices continued unabated in the period under review. Commodity and food prices likewise rose markedly; the relatively low rates of inflation prevailing in recent years came under pressure globally. Inflation in the euro area, like in Austria, shot up to more than 3% toward end-2007 and so exceeded the Eurosystem's target inflation rate of below, but close to, 2% over the medium term.

Responding to the clear increase in risks to price stability, the Governing Council of the ECB raised key interest rates in the first half of 2007. In implementing its monetary policy, the Eurosystem will continue to do all that is necessary to avoid the emergence of second-round effects and to anchor inflationary expectations at a level consistent with price stability. The maintenance of price stability in the medium term is the legal mandate of the ESCB and remains the primary monetary policy objective in the euro area.

The Eurosystem also faced major financial stability challenges: In order to contain the crisis of confidence in the financial sector and the financial market turmoil in the wake of the subprime crisis, the Eurosystem – partly in lockstep with other central banks – provided extra liquidity as from early August 2007. Extreme care was taken to ensure that the monetary policy stance continued to focus on maintaining price stability. While banks received temporary access to additional central bank money, the key interest rates remained geared to price stability.

A precise analysis of the causes and effects of the financial market turbulence is essential. Although it is too early to draw final conclusions, the need to improve the transparency of structured financial products with a view to enabling faster and simpler identification of risks is becoming apparent. Another issue is the transparency of major international banks' writedowns and their liquidity and risk management. In addition, external rating agencies and their role and importance in the market for structured financial products are moving into the spotlight of financial analysis.

Austria's economy grew robustly in 2007. At 3.4%, output growth was slightly higher year on year and was the highest recorded since 2000. The Austrian economy thus continued to outpace the euro area economy, as it has for several years. Brisk goods and services exports formed the key growth engine, as reflected in a further increase in the current account surplus. The Austrian labor market was in excellent shape, with employment climbing while the unemployment rate fell considerably. Propelled by both international and domestic developments, Austrian inflation measured by the HICP picked up to an annual average of 2.2% in 2007, rising well above the 3% mark toward year-end. Monetary, wage, structural and fiscal policies should now be geared to bringing inflation back to a level compatible with price stability in the medium term. Rapid budget consolidation – at the central, regional and local level – is also essential, both from a fiscal and structural policy perspective and in view of the agreements under the Stability and Growth Pact.

Austrian banks were only marginally affected by the subprime crisis in the U.S.A. This can be attributed to domestic banks' business approach that results in a fairly low dependence on money markets, a high share of interest income in total income and a concentration of business activities in Austria and Central, Eastern and Southeastern Europe. Austrian banks' increasing activities in this region prompted the OeNB to further enhance its contacts with the local national central banks and to step up analysis activities. The OeNB's subsequent financial stability assessment was recently confirmed by the IMF, which issued a favorable judgment on Austrian financial stability in the course of its Article IV consultations with Austria.

The reform of financial supervision in Austria enacted in late 2007 retained the dual system with the Financial Market Authority and the OeNB sharing tasks and responsibilities, but strengthened the OeNB's role in banking supervision, thus ensuring a new, optimized type of cooperation. Tasks entrusted to the OeNB include the responsibility for all on-site examinations of Austrian banks and individual bank analysis, further reinforcing the OeNB's role in maintaining financial stability.

In line with changes to the OeNB's tasks arising from its Eurosystem membership on the one hand and its role in financial supervision on the other, fundamental adjustments have also been made to the OeNB's governance structures over the past decade. A corporate strategy for the medium term, strong customer orientation, significant efficiency gains, sound cost management, corporate governance, knowledge management as well as distinct and integrated corporate communications have become key guidelines for the OeNB.

Governor
Klaus Liebscher

Governing Board

Peter Zöllner, Klaus Liebscher, Wolfgang Duchatczek, Josef Christl (left to right)

The Governing Board of the OeNB comprised the following members on December 31, 2007:

Klaus Liebscher
Governor

Wolfgang Duchatczek
Vice Governor

Peter Zöllner
Member of the Governing Board

Josef Christl
Member of the Governing Board

For additional information about the Governing Board of the OeNB, see *www.oenb.at*.

The Year 2007 at a Glance

Economic and Financial Developments

Global Economy Slows Down

In the course of 2007, the U.S. subprime crisis led to financial market turbulence and put a damper on the hitherto robust economy. While particularly the U.S. economy cooled down toward the end of the reporting year, growth remained fairly robust in Japan and Europe. Asia's emerging economies also continued to expand at a solid pace. The same holds true for the Central, Eastern and Southeastern EU Member States, which recorded high growth rates. According to the IMF, the global economy expanded by 4.9% in 2007, which is only slightly less than in 2006. The cooling of the U.S. economy and the Federal Reserve's substantial cuts in interest rates were at the root of the U.S. dollar's slide against the euro, which stood at USD 1.47 at end-December 2007 (January 2007: 1.33 USD/EUR). The strong rise in commodity prices accelerated inflation rates all over the world.

Euro Area: Robust Growth, Improved Labor Market Conditions, Increasing Inflation

In 2007, real economic growth amounted to 2.6% and was therefore 0.2 percentage points lower than in 2006. Particularly in the first half of 2007, strong euro area growth together with risks to price stability prompted interest rate increases of 0.25 percentage points in March and June 2007, respectively. In the second half of 2007, monetary policymakers not only had to cope with inflation topping 3% (annual average 2007: +2.1%), but also with financial market turbulence. In view of the heightened uncertainty, the Governing Council of the ECB decided to leave the key interest rates unchanged. Unemployment in the euro area decreased to 7.4%, thus reaching the lowest level since 1982.

Austria Posts Strongest Growth since 2000, Inflation at 2.2%

Austria's economic performance was highly dynamic in 2007. At 3.4%, real GDP growth in 2007 even eked out a slight increase over 2006 (+3.3%) and reached its highest level since 2000. The Austrian economy has thus again grown significantly more strongly than that of the euro area, with the booming export sector remaining the engine of growth. Austria's real exports of goods and services advanced by about 8%. The number of new jobs augmented by 114,000 between 2005 and 2007. With a jobless rate of 4.4%, Austria posted the fifth-lowest unemployment rate in the EU in 2007. The increase in HICP inflation from 1.7% in 2006 to 3.5% in December 2007 (annual average 2007: 2.2%) was mainly determined by international but partly also by domestic factors. In the same period, Austria's general government budget deficit decreased from 1.5% to 0.5%.

A Successful Year for the Austrian Banking Sector

Compared with banks in other countries, Austrian banks have been only marginally affected by the U.S. subprime crisis. Austrian banks' unconsolidated total assets augmented by about 13% to almost EUR 900 billion in 2007, mainly on the back of banks' foreign activities. Subsidiaries in Central, Eastern and Southeastern Europe contributed substantially to Austrian banks' business and profit growth. In 2007, unconsolidated operating profit advanced by 14.4% to EUR 6.7 billion. As operating income increased more than operating expenses, the cost-to-income ratio dropped significantly, reaching a record low of 62%.

Chart 1

Real GDP

Annual change in %

Source: Statistics Austria, Eurostat.

Chart 2

HICP Inflation

Annual change in %

Source: Statistics Austria, Eurostat.

Chart 3

Euro Area: Monetary Aggregate M3

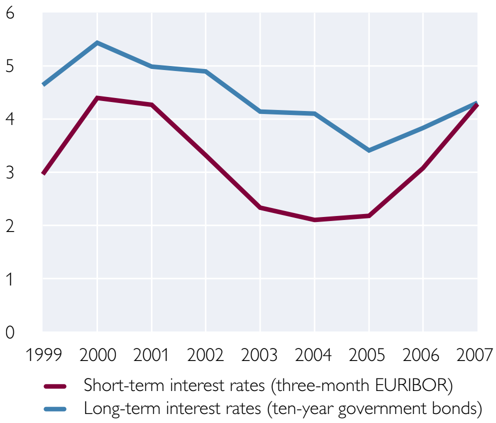
Annual change in %

Source: ECB.

Chart 4

Euro Area: Interest Rates

%

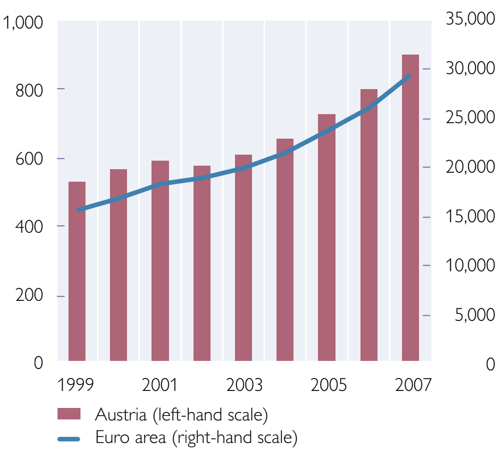


Source: Thomson Financial.

Chart 5

Banks' Total Assets

EUR billion *EUR billion*

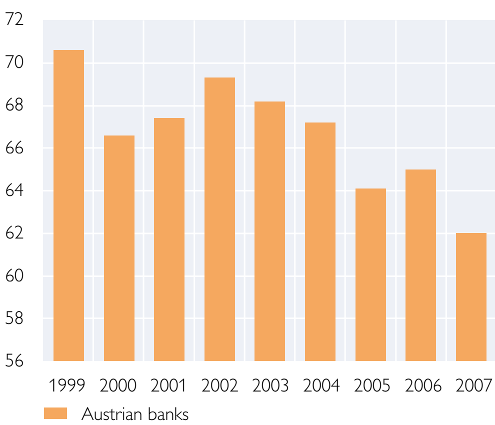


Source: OeNB, ECB.

Chart 6

Banks' Cost-to-Income Ratio

%



Source: OeNB.

The Year 2007 for the OeNB

Marked Increase in Operating Profit

Despite the allocation of risk provisions of EUR 407 million, the OeNB's operating profit increased by EUR 54 million or 28% to a total of EUR 247 million in 2007 compared with the previous year. The 90% profit share of the central government came to EUR 150 million (2006: EUR 130 million), while corporate income tax amounted to EUR 62 million (2006: EUR 48 million). The OeNB's profit for the year 2007 of EUR 17 million will be appropriated according to the General Meeting's decision.

Net Income Raised to EUR 491 Million, Expenses Remain Unchanged

Net income came to EUR 491 million (2006: EUR 437 million) as a result of allocations to risk provisions of EUR 407 million (2006: EUR 235 million). Net interest income amounted to EUR 738 million (2006: EUR 568 million), the net result of financial operations, writedowns and risk provisions equaled –EUR 290 million (2006: –EUR 175 million), and income from equity shares and participating interests constituted EUR 23 million (2006: EUR 25 million). Compared with 2006, total expenses were practically unchanged at EUR 244 million. EUR 108 million (2006: EUR 115 million) of this amount were attributable to staff cost, administrative expenses ran to EUR 78 million (2006: EUR 77 million), the cost of banknote production services to EUR 25 million (2006: EUR 25 million), and the depreciation of tangible fixed assets and other expenses made up EUR 33 million (2006: EUR 27 million).

Net Currency Position Down to EUR 12.1 Billion

The OeNB's total net currency position as at December 31, 2007, was EUR 12.1 billion, with gold holdings accounting for EUR 5.1 billion and foreign currency holdings for EUR 7.0 billion. The decrease by EUR 0.8 billion against December 31, 2006, is mainly attributable to valuation effects as well as transaction-related losses.

TARGET2 Launched in November 2007

Up to the launch of TARGET2 on November 19, 2007, European payment transactions were handled successfully by TARGET, with the number of payments rising steadily. TARGET2 falls under the responsibility of the Governing Council of the ECB and is used by banks for the settlement of large-value payments in euro. TARGET participants were scheduled to connect to the second-generation payment system in country groups, with the first eight countries, including Austria, migrating their operations on November 19, 2007. In December 2007, the system processed a total of 1,764,987 payments worth EUR 17,488.4 billion. In Austria, 15 banks are direct and 53 banks indirect participants of TARGET2. Around 90% of all Austrian banks may thus be accessed via TARGET2 worldwide.

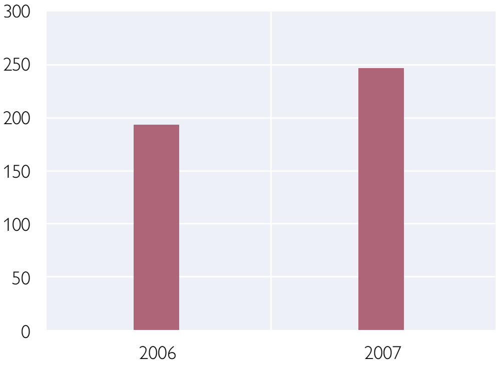
Cash Processing Volume Remains at a High Level

In 2007, some 1.2 billion banknotes and 1.8 billion coins were processed and checked for their circulation fitness and authenticity, which is about the same volume as in 2006. This high volume attests to the OeNB's commitment and significant contribution to ensuring cash security in Austria. Consequently, counterfeit euro banknotes and coins are quickly and efficiently withdrawn from circulation and are made available to the police for further investigation. At 7,800, the quantity of counterfeit banknotes recovered from circulation in Austria has remained small. Thus, only slightly more than six in one million banknotes processed in Austria were counterfeits.

Chart 7

OeNB: Operating Profit

EUR million



Source: OeNB.

Chart 8

OeNB: Income and Expenditure

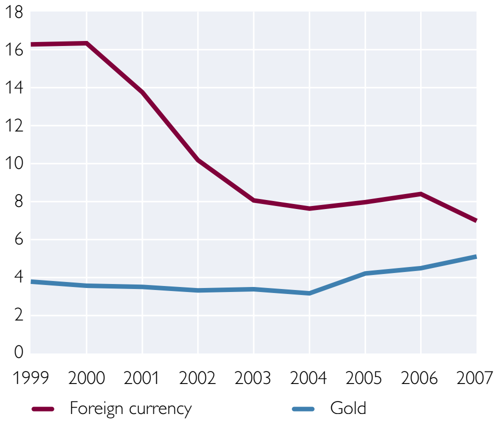
EUR million

Source: OeNB.

Chart 9

OeNB: Net Currency Position

EUR billion



Source: OeNB.

Chart 10

Number of TARGET Transactions

Million

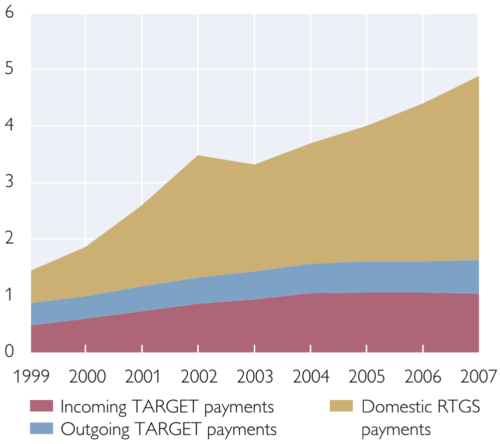


Chart 11

OeNB: Number of Processed Euro Banknotes

Million

Source: OeNB.


Avocado
1,50

Report of the Governing Board on the Financial Year 2007

Rising Inflation and Financial Market Turbulence Pose Monetary Policy Challenges

Global Economy Almost Sustaining Growth Pace – Downside Risks Increasing

Prolonged expansion in emerging economies cushions slowdown in industrialized countries

The IMF put real global economic growth in 2007 at 4.9%, only marginally slower than a year earlier, despite the international financial market turbulence that broke out in the second half of the year (see box 1). The forecasts for 2008 were revised sharply downward in view of the turmoil, however, with this year's IMF spring forecast expecting expansion to fall just short of 4%. The downturn in global growth will stem mainly from developments in the industrialized countries. Growth in the U.S.A., but also in the euro area and Japan, will in part be considerably weaker in 2008 relative to 2007. However, the long-running strong performance of the emerging economies (notably China, India and Russia) will somewhat soften the global downturn. Having already evolved into the main growth engine in 2007, this region will continue to gain in importance in 2008 because of the weaker economic development in the industrialized countries. The forecast risks are largely skewed to the downside and arise from financial market volatility, a sharper-than-expected downturn in the U.S.A. and an ongoing rise in commodity prices.

Subprime crisis in the U.S.A.

After a weak start in the first quarter of 2007, the U.S. economy recovered slightly in the second and third quarters. The brisker expansion was driven mainly by a substantial growth contribution from net exports. But the outbreak of the subprime crisis in July/August 2007 clearly retarded fourth-quarter economic growth with some lag. Real growth in 2007 as a whole came to 2.2%, 0.7 percentage points lower than in 2006. The contraction in residential construction, visible from as far back as mid-2006, was particularly pronounced. Fixed investment softened too. The existing economic uncertainty also caused a large-scale drawdown of inventories. As in 2006, consumer spending was by far the main growth engine. But toward end-2007, momentum was flagging in this area too, probably as a direct result of negative wealth effects, high energy prices and reduced consumer confidence in view of the subprime crisis. Owing mainly to a falloff in import growth, the external sector delivered its first positive growth contribution since 1995. All of the main institutions revised down their 2008 forecasts for the U.S. economy, in some cases sharply, and expect growth to continue to decline. The persistent uncertainties regarding the impact of the financial market turmoil on the real economy pose particular risks.

Weaker growth in Japan

Real economic growth in Japan amounted to 2.1% in 2007, down slightly on the previous year. The growth was spurred mainly by robust exports, in turn lifted by strong demand from the booming markets of the Asian emerging economies. Corporate investment activities also gained momentum in the second half of 2007, whereas construction activities slowed drastically owing to tighter building regulations. Growth in consumer spending was below average.

Emerging economies are becoming growth engine

The prudent economic policies pursued in many emerging economies are increasingly bearing fruit. In 2007, the countries described collectively as emerging economies developed into the main growth engine of the global economy. Weighted by GDP valued at purchasing power parities, the so-termed BRIC countries, i.e. Brazil, Russia, India and China, accounted for almost half of global economic growth. Since the

Box 1

U.S. Subprime Crisis Has Been Dominating Global Financial Market and Economic Developments since Mid-2007

The term "U.S. subprime crisis" encapsulates the disruption in the U.S. and international financial markets that was unleashed by the slump in the U.S. housing market. The crisis has made manifest how turbulence in a relatively small and contained market can spill over into the global financial system through complex credit risk transfer instruments.

How Did the U.S. Subprime Crisis Arise?

The background to the latest turmoil lies in the rising real estate prices in the U.S. in recent years. Lenders increasingly issued mortgage loans to less creditworthy (subprime) borrowers. The real estate boom was fueled by a particularly optimistic estimate of future house price movements and a related relaxation of credit standards as well as innovations in financial instruments. Mortgage loans were generally offered at very low, i.e. teaser, interest rates for the first few years, but subsequently reset at the prevailing market rate. Because of this adjustment and the rising interest rate level in the U.S.A., interest payments soared. In many cases, repayment of the principal also started at that time – after a few "interest-only" years. In addition, real estate prices had been stagnating for close to two years and had recently even been falling, making refinancing more difficult.

The reason why the problems of subprime borrowers in the U.S.A. disrupted global financial markets was securitization: U.S. subprime mortgage loans were repackaged and sold to investors in the form of asset-backed securities. The respective investors received payment flows related to the securitized loans (interest and principal payments) in line with the credit rating of the individual security tranches. Such securities were mainly bought by investment companies, insurance companies, pension funds and banks worldwide. In addition, special purpose vehicles, such as conduits or structured investment vehicles (SIV), were set up; these used asset-backed commercial papers (ABCP) for short-term refinancing and bought securities with long maturities that were likewise backed by U.S. subprime mortgage loans. Lest the demand for ABCP was too low to safeguard the liquidity of these entities, banks issued guarantees to mitigate the refinancing risk.

When the rise in defaults in this credit segment prompted rating agencies to downgrade many of these tranches in spring 2007, extremely so in some cases, uncertainty in this market soared. In the summer months of 2007, the liquidation of several hedge funds, the suspended redemption of shares in some quasi money market investment funds, and precarious situations at individual European banks resulted in a crisis of confidence in the financial market. This crisis was fueled by uncertainty about the distribution and concentration of credit risks and about as yet unrealized losses and hidden accounting losses on these financial instruments. Moreover, there was general uncertainty about the extent of banks' financing obligations to special purpose vehicles.

In this environment, banks became cautious about extending credit to each other. Liquidity in the unsecured interbank markets hence evaporated quickly, as reflected in rising money market rates in the main currencies. Responding to these developments, central banks around the world began to take measures.

Rapid Decisive Action by Central Banks

On August 9, 2007, the ECB took the first step, providing unlimited liquidity to the interbank market through a fine-tuning operation with overnight maturity in the form of a fixed rate tender at an interest rate of 4.00% against adequate collateral. At EUR 94.8 billion, the tender result clearly exceeded the previous record volumes of September 11, 2001, by around EUR 27 billion. On the following three business days, the ECB conducted additional liquidity-providing fine-tuning operations with overnight maturity, but this time as variable rate tenders.

The ECB allotted less liquidity from one operation to the next (EUR 61.1 billion on August 10, 2007, EUR 47.7 billion on August 13, 2007, and EUR 7.7 billion on August 14, 2007).[1] *Likewise as of August 9, 2007, the U.S. central bank, the Federal Reserve System (Fed), initially pro-vided USD 24 billion through open market operations. It raised money market liquidity the next day by – contrary to normal practice – allotting funds totaling USD 38 billion in as many as three tender procedures with overnight maturity. All of these measures initially eased tensions in the respective money markets.*

On August 17, 2007, the Fed lowered its discount rate by 50 basis points, thereby narrowing the interest rate differential between this facility and the actual policy (federal funds) rate, to 50 basis points. The Fed also announced that it would extend the lending period under this facility from overnight to 30 days and would accept a wider range of assets as collateral. The banks were generally very hesitant to take up this offer, fearing serious damage to their creditworthiness if their recourse to the facility became known. The Fed subsequently lowered its policy rate in six steps from 5.25% to 2.25% (as at March 18, 2008), i.e. by 3 percentage points in all. With these measures, the Fed aimed at making a timely response to the downside risks to economic growth stemming from the crisis in the mortgage markets.

In December 2007 – a phase in which liquidity conditions in the money markets had once more become critical – the shortcoming in the existing discount facility became evident again (banks once again avoided this facility for fear of negative publicity). This triggered the Fed's launch, in cooperation with other important central banks, of a new type of monetary policy instrument. By means of the Term Auction Facility (TAF) – a tender procedure with a maturity of one month – the Fed would provide liquidity to the banks on a broader basis and in a more discrete fashion. The Fed also agreed on temporary reciprocal currency arrangements (swap lines) with the ECB and the Swiss National Bank, also aimed at funneling U.S. dollar liquidity to the European banks. These operations have not had any effect on liquidity provision in euro.

On March 11, 2008, the Fed announced both an expansion of the TAF (by USD 40 billion more than in February 2008 to USD 100 billion) and another new type of facility to support financial market liquidity. Under the new Term Securities Lending Facility (TSLF), the Fed would lend up to USD 200 billion of Treasury securities to primary dealers (securities broker-dealers authorized to participate in the Fed's open market operations), beginning in late March. A wide range of securities would be allowed as collateral, including some from the mortgage sector. The loans would have a maturity of one month. Moreover, the reciprocal currency arrangements (swap lines) with other prominent central banks (notably the ECB and the Swiss National Bank), which first took effect in December 2007, was extended within the TAF, in terms of both volume and time period.

On March 16, 2008, the Fed announced another new facility (Primary Dealer Credit Facility – PDCF), through which it provides overnight loans to the primary dealers against collateral. This facility fits in with the other central bank measures to restore the smooth functioning of the financial markets. The interest rate for this credit facility was set at 25 basis points above the policy rate.

Impact of the Financial Market Turbulence

Other financial market segments besides the money market were hit by the turbulence too. Driven by hefty losses on shares in financial institutions, global stock indices plunged. In addition, the growing risk aversion among investors resulted in increased demand for safer assets, pushing down rates on government securities. In contrast to earlier episodes of global financial market turmoil, the emerging economies were affected only moderately this time.

[1] *All in all, the operations conducted by the ECB to ease money market conditions did not change average liquidity conditions. The ECB provided more liquidity at the beginning of the respective reserve maintenance periods and limited it toward the end. The technical term for this advance provision of liquidity is frontloading. Moreover, the maturity structure of the outstanding monetary policy operations has clearly changed. Main refinancing operations with a maturity of one week have been partly replaced by longer-term refinancing operations with a maturity of three months.*

The financial market turbulence notably impacted on the results of numerous banks in Europe and the U.S.A. Relative to other banks, Austrian banks have been only marginally affected by the subprime crisis in the U.S.A. (see the chapter "The OeNB as the Key Player in Securing Financial Stability in Austria"). Major international banks have thus far been able to absorb the – in some cases – large writedowns, having sound capital buffers thanks to their in part excellent performance over the past few years. Capital was also partly mobilized through Asian and Arab sovereign wealth funds, while some of the stricken financial institutions were taken over by competitors. The valuation of complex financial instruments posed a particular difficulty when the financial statements for 2007 were prepared because there was no market value reference. Some valuation practices were subsequently called into question, and new loss-bearing investments were identified.

As a result of the U.S. subprime crisis, growth forecasts for 2008 were revised downward, some even sharply. But it is still difficult to comprehensively quantify the impact of the financial market turmoil on the real economy. A general reappraisal of risk, higher money market rates and the partial drying-up of the securitization markets have led to a tightening of credit standards and rising lending rates. The ensuing increase in the costs of corporate and household debt servicing will reduce both the propensity to borrow and the capacity to repay existing loans. In addition, negative wealth effects are dampening consumer spending. The general decline in economic sentiment could influence both corporate willingness to invest and household propensity to spend.

What Lessons Can Be Learned?

The persistence of the U.S. subprime crisis and consequent heightened uncertainty in the financial markets allow the following provisional lessons and conclusions:

- *It is essential to improve (liquidity) risk management practices at banks. In an environment of ample liquidity and greater investor risk appetite, the development of liquidity risk management took a back seat, particularly at banks with the "originate and distribute" business model of issuing and securitizing loans. The crisis also confirms the need for stress tests with dramatic but plausible scenarios.*
- *The transparency of banks' structured products and special purpose vehicles must be enhanced. This would enable investors to more readily identify the risks attached to these constructions, alleviating uncertainty and boosting confidence in financial institutions.*
- *Both the role of external rating agencies and their incentive structures should be examined more closely. The New Basel Capital Accord (Basel II) is heavily geared to banks' internal ratings. The latest developments illustrate the importance and appropriateness of the idea of greater risk sensitivity embodied in Basel II.*
- *International cooperation between central banks and their involvement in banking supervision to safeguard financial stability are essential. This way, central banks have access to relevant data on banks and other financial intermediaries and are able to conduct targeted analyses that help rapidly identify potentially risky developments. The vital importance of close international cooperation between central banks was notably reconfirmed by the coordinated actions in December 2007 and March 2008.*
- *Regulatory measures to reinforce transparency, improve liquidity and risk management and to enhance and improve valuation approaches as well as the role of rating agencies are currently under intense discussion at the international and EU level. At the beginning of April 2008, the Financial Stability Forum, which has been set up at the BIS, presented to the G7 Finance Ministers and central bank governors a report with recommendations for enhancing the resilience of markets and financial institutions. But on top of regulatory measures, investors themselves must conduct more detailed risk assessments.*

Slight reduction in global current account imbalances

Inflationary pressure mounting worldwide

Output growth past its cyclical peak

improvement in macroeconomic fundamentals in recent years has boosted crisis resilience in many emerging economies, this group of countries suffered relatively few ill effects from the recent financial market turbulence. Growth forecasts for 2008 are hence rather good, even though, given existing trade relations, weaker economic growth in the industrialized nations will also dampen growth in these regions.

The stability-oriented monetary policy of many central banks and the inflation-reducing effects of globalization helped stabilize prices in recent years. Inflation rates remained moderate. But inflation began to pick up again, especially toward the end of 2007, on the back of international price increases in food, oil and other commodities. The strong demand for food and the generally higher demand for animal products in some emerging economies pushed up world market prices of food and beverages. Weather-related crop failures in some regions of the world formed another contributory factor.

Oil prices increased markedly throughout 2007, reaching a historical peak of over USD 100 per barrel of Brent crude at the start of 2008. This rise is attributable to stagnating production in tandem with expanding demand. The price pressure was intensified by speculative activities, risk premiums based on geopolitical developments and an increasing flight to investments in commodities owing to the turmoil in the international financial markets. However, thanks to the simultaneous U.S. dollar depreciation, the increase in the euro-denominated oil price was far less pronounced. In contrast to the U.S. dollar price, the average euro price for oil in 2007 was even slightly lower than a year earlier.

The shift in global demand growth from the industrialized countries to the emerging economies (particularly from the U.S.A. to China) outlined above and the depreciation of the U.S. dollar resulted in some reduction in global current account imbalances, although they have remained sizeable. The U.S. current account deficit narrowed slightly from 6.1% of GDP (2006) to 5.3% of GDP (2007), while the surpluses run by the oil-exporting countries edged down due to higher government spending. Despite a modest currency appreciation, China's current account surplus expanded.

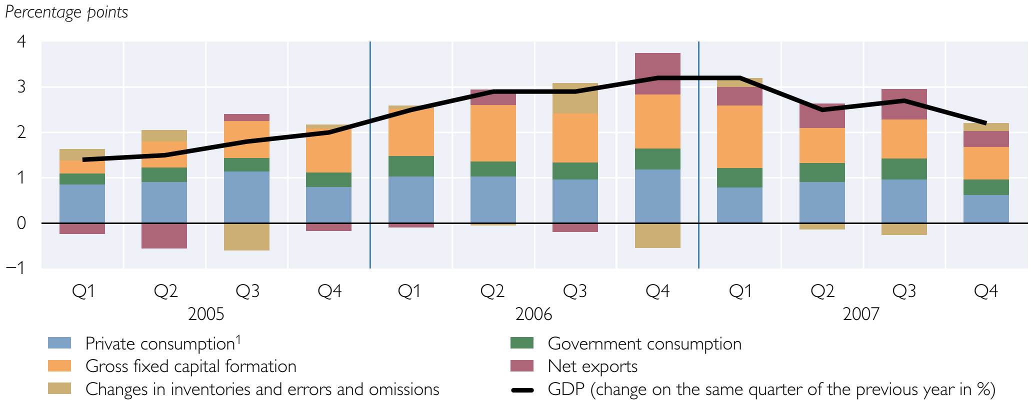
Slowdown in Euro Area Economic Activity

Following brisk growth in 2006, economic activity in the euro area cooled marginally in 2007. Real economic growth came to 2.6%, down 0.2 percentage points on the previous year. After a strong start to the year thanks to a mild winter, which bolstered construction activity, growth weakened in the second half of 2007. Output growth in the euro area is probably past its cyclical peak.

Domestic demand delivered the main growth contribution, in both the first and second half of 2007. Both consumer spending and corporate investment activity were relatively robust, though falling short of the growth rates recorded a year earlier. Consumer spending benefited from favorable labor market conditions and increasing disposable income, but growth was weaker than the positive business environment had led to expect. This can be explained by the rise in the savings rate stemming from waning consumer confidence. The downturn in confidence indicators accelerated in the summer of 2007, reflecting the growing general economic uncertainty. Coinciding with the outbreak of international financial market turbulence, the rise in consumer

Chart 12

Euro Area Real GDP Growth and Its Components



Source: Eurostat.

[1] *Households and nonprofit institutions serving households.*

prices gathered speed, sparking concerns about future real purchasing power. Consumer confidence nonetheless remained above its long-term average in the second half of 2007.

Investment activity was exuberant especially in the first half of 2007, owing in part to favorable weather conditions. Construction activity slowed to some extent as of mid-2007, however, as major advance indicators had already signaled at the start of the year. Corporate investment activity remained lively in the second half of 2007, though. Capacity utilization in the manufacturing sector was high, clearly exceeding its long-term average. Corporate profitability likewise continued to improve. Corporate lending was still largely unaffected by the financial market turbulence, although credit standards began to tighten toward the end of 2007. Interest rates on both new and existing loans climbed gradually. As in the household sector, confidence indicators for industry began to slide in mid-2007, but generally remained at a high level at year-end.

The euro showed a marked appreciation in 2007 of around 3% in real effective terms. With a gain of over 9%, the euro's average appreciation against the U.S. dollar stood out among the bilateral exchange rates. The euro rally was driven mainly by the difference in growth prospects for the euro area and the U.S.A. as well as several interest rate cuts by the Fed in connection with the subprime crisis.

Despite these exchange rate developments, the external sector was a major pillar for euro area economic activity in 2007. The falloff in demand from the U.S.A. was offset by increased exports to the emerging economies.

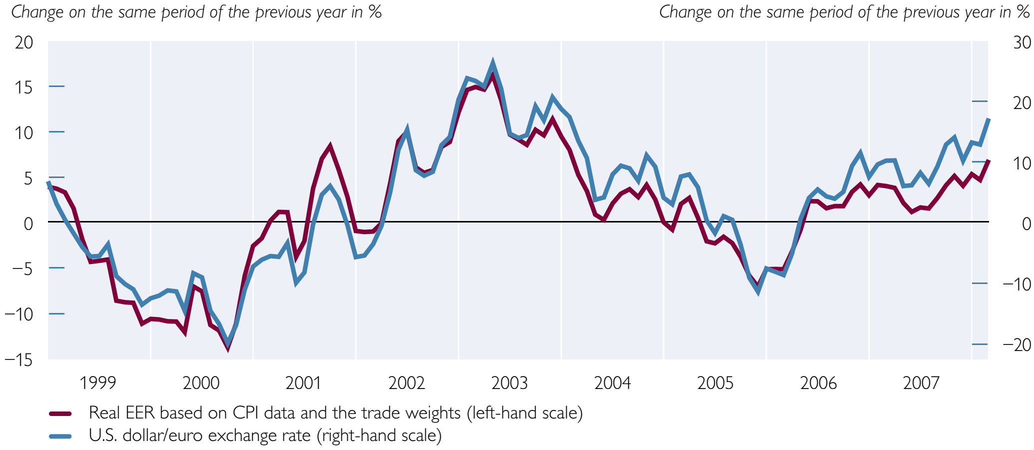
The U.S. dollar continued to depreciate against the euro in the first months of 2008, with the exchange rate topping USD/EUR 1.50 on February 27, 2008, and reaching a high of USD/EUR 1.59 on April 23, 2008.

The improvement in the labor markets seen since mid-2005 continued in 2007. In the reporting year as a whole, the unemployment rate in the euro area dropped to 7.4%, hitting its lowest level since 1982 (7.1%). At the same time, employment was on a strong path. Some 2.7 million jobs were created in 2007, corresponding to a growth rate of 2.0% relative to 2006. The

Unemployment drops to lowest level since 1982

Chart 13

Euro Exchange Rate



Source: Thomson Financial.

Governing Council of the ECB raises key interest rates by a total of 50 basis points in two steps in the first half of 2007

number of employees in the euro area has thus increased by around 15.6 million since 1999. Employment growth was broadly based across all sectors and forms of employment (full-time, part-time, permanent and temporary employment). Although strong economic activity was key to this development, a decline in structural unemployment was recorded, allowing the conclusion that the functioning of the labor markets has generally improved.

Monetary Policy in the Euro Area: Risks to Price Stability Remain despite Two Interest Rate Increases in First Half of 2007

Financial market turmoil poses challenge to monetary policymakers

The economic conditions facing monetary policy in the euro area changed fundamentally in the course of 2007. Economic developments in the euro area in the first half of 2007 were marked by strong growth and moderate inflation, but also by increasing risks to price stability. Following thorough economic and monetary analysis, the Governing Council of the ECB decided on two 25 basis point interest rate hikes in March and June 2007. This was mainly a response to increased inflationary risks arising from robust growth, stronger monetary expansion, capacity bottlenecks and rising oil prices. The two interest rate steps were the seventh and eighth since December 2005 when interest rates were at their lowest level so far. The Governing Council of the ECB left interest rates unchanged throughout the rest of 2007. As of June 2007, the minimum bid rate on the main refinancing operations has thus stood at 4.0%, the interest rate on the marginal lending facility at 5.0% and that on the deposit facility at 3.0%.

In the wake of the U.S. subprime crisis, the picture changed drastically in the second half of the reporting year. Great uncertainty and tensions in the financial sector shaped economic events as of August 2007. As financial market volatility mounted, a major reappraisal of risks took place. Stock prices dropped sharply, long-term interest rates fell, and the yield curve became inverted (in the euro area the three-month EURIBOR overtook the interest rate on ten-year government bonds).

Like the Fed, the Bank of England and the Swiss National Bank, the euro area central banks provided the interbank market with adequate liquidity in coordinated actions in December 2007, January 2008 and March 2008. These played a key role in alleviating financial market tensions (see box 1).

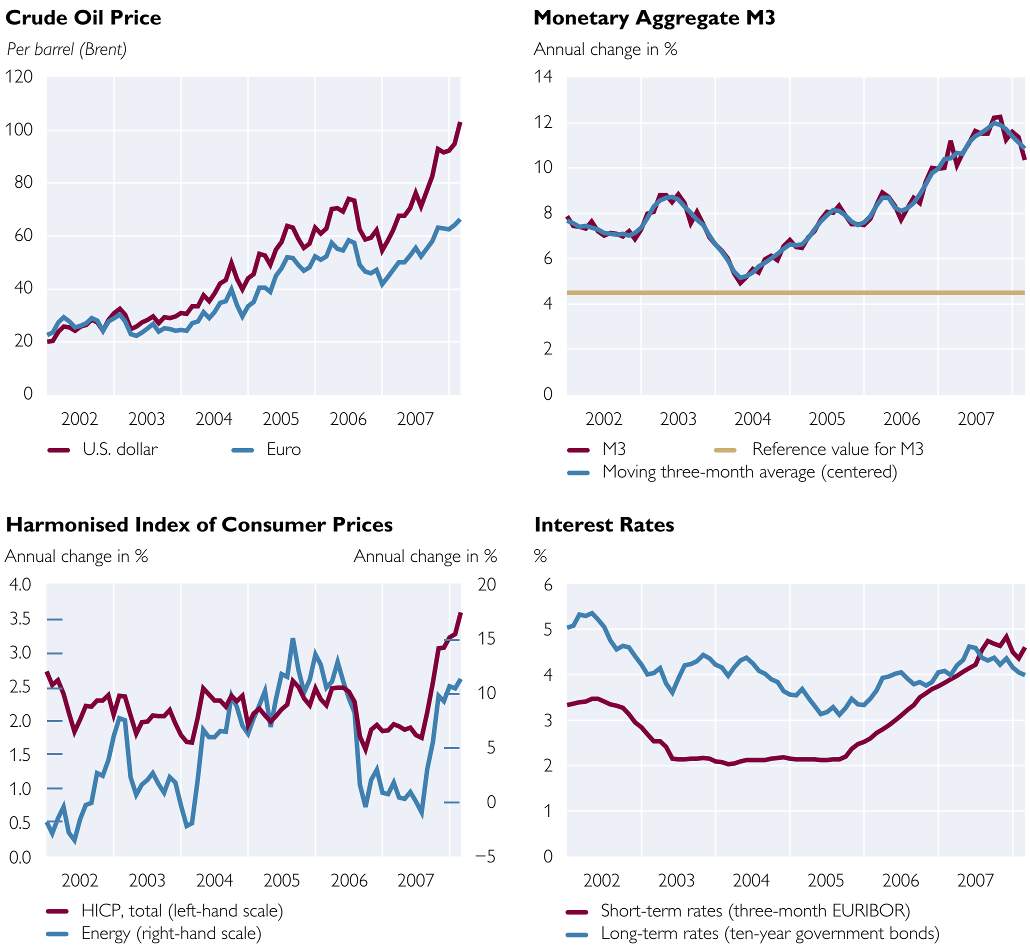
Inflation, which had been relatively subdued up to August 2007, picked up sharply in the fall. The HICP inflation rate in the euro area increased from less than 2% in August 2007 to 3.1% in November and December 2007. On average over 2007, euro area inflation amounted to 2.1% (2006: 2.2%). Propelled by the surge in commodity prices, pronounced price hikes occurred in food, motor fuels and other energy products.

Inflation rises above 3%

Both monetary and credit growth remained vigorous in 2007. The annual growth rate of M3 reached 12% toward end-2007, its highest level since the beginning of Stage Three of EMU. The healthy demand for savings vehicles included in M3 that has persisted since the third quarter of 2004 can probably be attributed to the relatively flat yield curve as well as to the greater uncertainty in the venture capital markets.

Chart 14

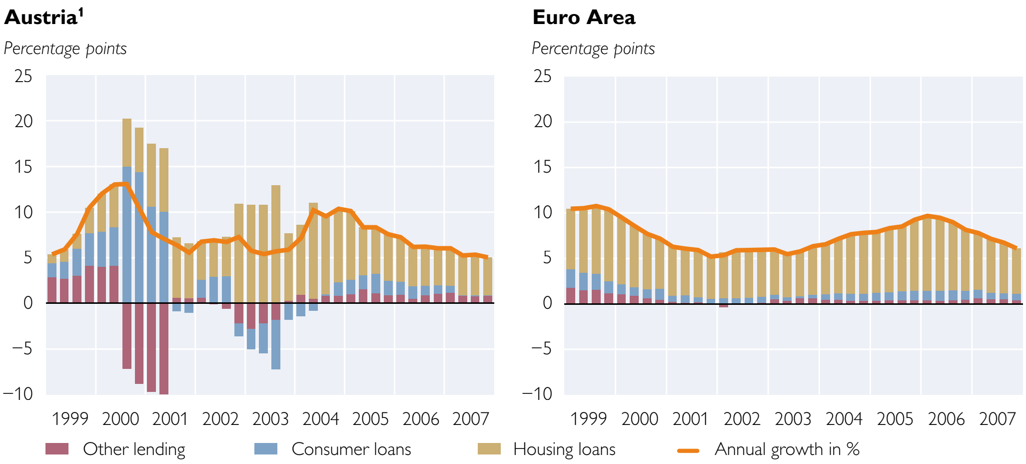
Development of Selected Economic Indicators in the Euro Area



Source: Thomson Financial, ECB, Eurostat.

Chart 15

MFI Loans to Households



Source: ECB, OeNB.

[1] Loans to households, excluding nonprofit organizations serving households.

The downward trend in credit growth seen in the first quarter of 2007 came to a halt in May 2007, with the growth rate climbing to 11% per annum in December 2007. Whereas lending to nonfinancial corporations accelerated, annual household lending growth continued to slow. These diverging trends reflect the less favorable outlook for housing markets in some euro area countries.

Outlook for 2008

Macroeconomic data for the first months of 2008 indicate softening but persistent growth in real GDP in the euro area. In step with this development, the latest euro area growth forecasts have been revised downward. A case in point is the European Commission's forecast of April 2008, which revises euro area growth in 2008 down by roughly ½ percentage point to 1.7%; growth in 2009 is expected to amount to 1.5%. According to the ECB staff projections of March 2008, real growth in 2008 will range between 1.3% and 2.1%. A rate of between 1.3% and 2.3% is expected for 2009. The uncertainty surrounding this outlook for economic growth is exceptionally high, and downside risks definitely prevail in the medium term, relating mainly to a potentially wider spillover of financial market developments. Further downside risks arise from latent additional oil and other commodity price rises, various protectionist pressures and the possibility of disorderly developments owing to global imbalances.

Inflation remains above the 3% mark at the beginning of 2008

The persistently high rates of inflation recorded in early 2008 (3.2% in January, 3.3% in February and 3.6% in March 2008) are likely to carry forward throughout much of 2008. The effects of higher oil and food prices are likely to abate – assuming no further exogenous price rises – only toward end-2008, which should allow inflation to ease back to around 2%. The ECB staff macroeconomic projections of March 2008 were accordingly revised markedly upward relative to December 2007, and expect HICP inflation of between 2.6% and 3.2% in 2008 and between 1.5% and 2.7% in 2009. In its April 2008 forecast, the European Commission foresees euro area HICP inflation at 3.2% in 2008 and at

2.2% in 2009. Upside risks are clearly present too, including wage rises, further price hikes in food, oil and commodities and sharper increases in administered prices and indirect taxes than currently factored into the projections.

At its meeting of April 2008, the Governing Council of the ECB noted that the latest information confirmed the existence of strong short-term upward pressure on inflation as well as upside risks to price stability over the medium term owing to vigorous monetary and credit growth. The economic fundamentals of the euro area are sound. Yet the level of uncertainty resulting from the turmoil in financial markets remains high. In line with the ECB's and the Eurosystem's mandate, maintaining price stability in the medium term remains the primary monetary policy objective for the euro area. The anchoring of medium to longer-term inflation expectations to a level consistent with price stability is thus of the highest priority for the Governing Council of the ECB. This should also prevent second-round effects and the materialization of upside risks to price stability.

Economic Activity Still Animated in EU Member States in Central, Eastern and Southeastern Europe

Economic growth in the EU Member States in Central, Eastern and Southeastern Europe (CESEE) remained brisk in 2007, amounting to a weighted average of 6.2%. The Baltic countries Latvia and Lithuania as well as Slovakia posted particularly high growth rates. Economic activity in the region was driven mainly by domestic demand, consumer spending being the primary growth contributor. Hungary and Slovakia were the only countries in which the external sector made a significant contribution to growth. In contrast, the growth contribution from that sector in, notably, the Baltic States and the EU Member States in Southeastern Europe was markedly negative. Following vigorous growth in 2007, a slight economic weakening is expected for CESEE in 2008 – basically in sync with the euro area.

HICP inflation in 2007 amounted to a weighted average of 3.7%, representing a rise of 0.5 percentage points on the previous year. The impact of elevated food and energy prices on inflation was far more visible in the Eastern European EU Member States than in the euro area. On the one hand, this is attributable to the larger weight of these product groups in the HICP of the countries in that region but, on the other, the price hikes in both components were much higher than in the euro area in most countries because of failed harvests and adjustments to regulated prices. The price pressure prevailing in some countries was intensified further by rising unit labor costs and the first signs of overheating.

Some of the CESEE Member States ran large, and in some cases expanding, current account deficits owing in part to the rapid economic catching-up process and the related strong need for investments. But vibrant growth in consumer spending, often fueled by brisk lending, also exacerbated external imbalances. Current account deficits were considerably offset by FDI inflows in some countries, but also by more volatile capital flows in others. Against the backdrop of heightened risk aversion and greater volatility in international financial markets, the financial capacity to sustain external imbalances will depend more heavily on the quality and solidity of the relevant countries' macroeconomic performance and their national structural policies.

Table 1

Selected Economic Indicators for the Central, Eastern and Southeastern EU Member States

	Real economic growth		HICP inflation		Current account balance	
	2006	2007	2006	2007	2006	2007
	Annual change in %		*% per annum*		*% of GDP*	
Poland	6.1	6.5	1.3	2.6	−3.2	−3.7
Slovakia	8.5	10.3	4.3	1.9	−7.0	−5.4
Slovenia	5.7	6.1	2.5	3.8	−2.8	−4.8
Czech Republic	6.4	6.5	2.1	3.0	−3.1	−3.0
Hungary	3.9	1.3	4.0	7.9	−6.1	−5.0
Estonia	11.2	7.1	4.4	6.7	−15.5	−17.4
Latvia	11.9	10.2	6.6	10.1	−22.3	−23.3
Lithuania	7.7	8.8	3.8	5.8	−10.8	−13.7
Bulgaria	6.1	6.2	7.4	7.6	−17.8	−21.5
Romania	7.7	6.0	6.6	4.9	−10.4	−13.9

Source: Eurostat.

Robust Economic Growth in Austria of 3.4% in 2007 – Expected to Slow to Around 2% in 2008

Austria's economic performance was exceptionally dynamic in 2007. At 3.4%, real GDP growth in 2007 even edged up on 2006 (+3.3%) and reached its highest level since 2000. The Austrian economy thus significantly outpaced that of the euro area, with the booming export sector remaining the engine of growth. Austria's real exports of goods and services advanced by some 8%. This robust growth was bolstered by the continued eastward shift in the concentration of export activities. There was pronounced momentum in the establishment and expansion of export relations with the Eastern European countries, Russia and China. Fired by the export boom, manufacturing grew apace. Thanks to the thriving economy, employment in industry notched up its first noticeable increase in 2007 after several years of contraction. Construction accelerated too, likewise generating a sizeable number of extra jobs.

Besides exports, investments were the second main pillar of economic activity, with both equipment and construction investment expanding vigorously. Tourism also supported growth: Both summer and winter tourism chalked up increases in overnight stays and sales.

Consumer spending remained the weak spot in the economy. Despite higher employment, real disposable household income only inched up. Moreover, households upped their saving rates. These factors depressed growth in consumer spending in 2007 to 1.4%, a marginal rate considering the benign economic climate. At generally over 3%, the wage settlements negotiated in fall 2007 were higher than in the previous year.

Given global economic conditions, Austrian growth will soften in 2008. Factors tempering growth include the global economic slowdown and high oil prices, along with uncertainty as to the extent of the spillover of financial market turbulence into the real economy. Despite these effects, the outlook for the Austrian economy in the first half of 2008 is favorable. Although the OeNB economic indicator of March 2008 predicts that real GDP growth in 2008 will fall well below that in 2006 and 2007, there are no signs that Austria is heading for a slump. Real GDP growth is expected to come to +0.6% in the first and +0.5% in the second quarter of 2008 (seasonally and working day adjusted, relative to the previous quarter). In its forecast of March 2008, WIFO (the Austrian Institute of Economic Research) predicts that the Austrian economy will grow by 2.1% in 2008, and 1.7% in 2009. And in its Article IV consultations for Austria, the IMF also expects growth to slow in 2008 and 2009 to around 2%, which is close to potential. In April 2008, the European Commission forecast 2.2% economic growth for 2008 and 1.8% for 2009.

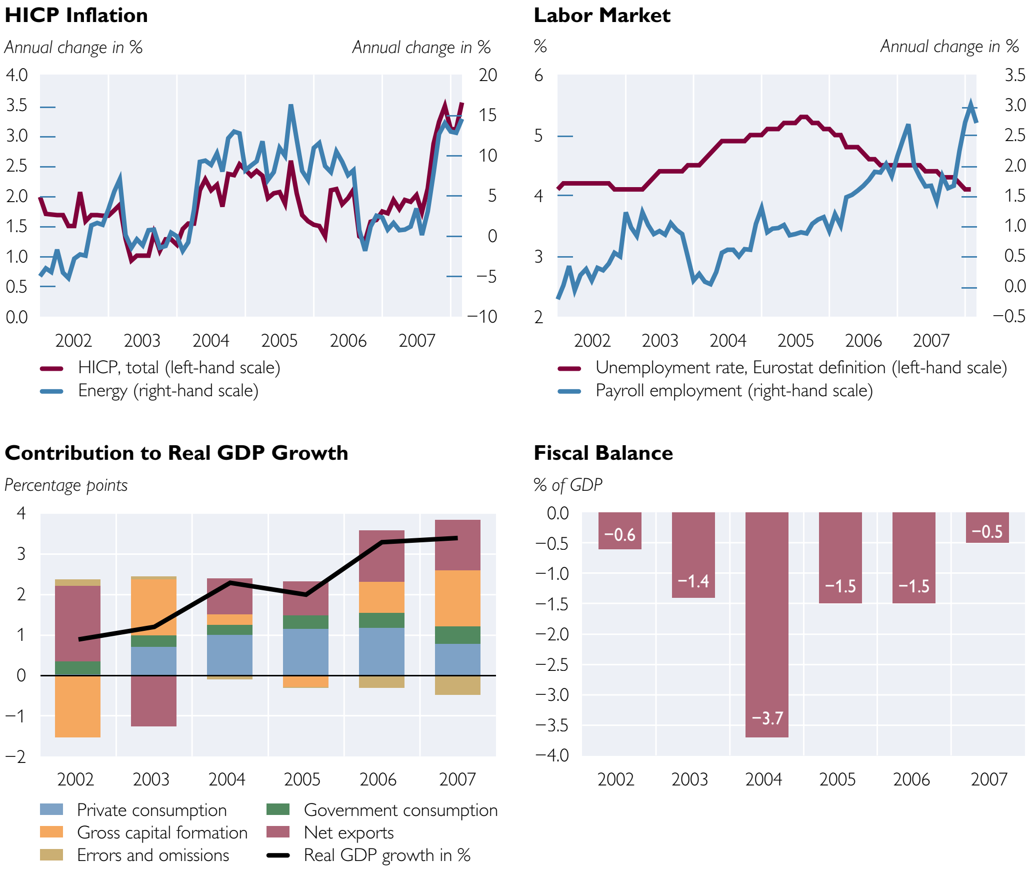
Climbing food and energy prices pushed up inflation to over 3% in fourth quarter of 2007 after subdued first half

HICP inflation amounted to 2.2% in 2007, gaining half a percentage point on 2006. On an intrayear basis, the inflation rate in the first half of 2007 hovered between 1.7% and 1.9%, rose marginally to 2.0% in the third quarter and accelerated during the last three months to reach 3.5% in December, the highest HICP inflation rate recorded in Austria since January 1993.

Though inflation eased slightly in the first two months of 2008, it remained at 3.1% in both cases, and mounted to 3.5% in March following

Chart 16

Development of Selected Economic Indicators in Austria



Source: Statistics Austria, Eurostat, Federal Ministry of Finance.

renewed price pressures in the energy and food sectors, which confirmed the OeNB's expectations that inflation will remain elevated at more than 3% in the first half of the year. However, in the second half of 2008, inflation should abate considerably because of the expected dissipation of the food price shock and of the base effect of past energy price increases, dropping to about slightly over 2% by year-end. Drawing on data up to March 2008, the OeNB expects average annual inflation in 2008 at 3.0%, which corresponds to a rise of 0.8 percentage points on 2007. Inflation should continue to slow in 2009, falling back to slightly more than 2%.

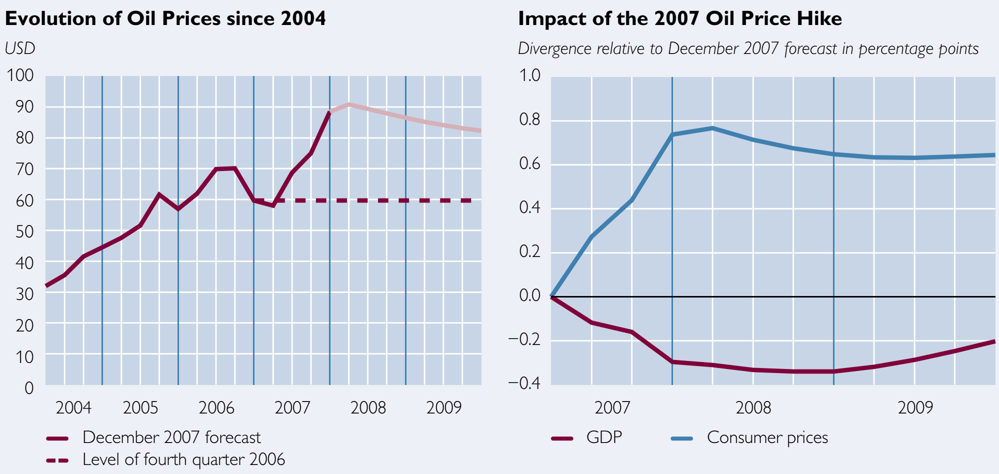
The Austrian labor market was in excellent shape in 2007. The brisk economic activity over the last two years generated 114,000 extra jobs relative to

Box 2

Impact of the Surge in Oil and Commodity Prices on the Austrian Economy

Between December 2006 and December 2007, the price of Brent crude climbed from USD 62.3 per barrel to USD 91.1 per barrel, which corresponds to an average increase in 2007 of USD 7.2 to USD 72.7. This price rise mainly reflects the surge in demand from the fast-growing economies in Asia, compounded by supply shortages and a series of geopolitical risk factors. In December 2007, the price of Brent crude hovered just under the USD 100 per barrel mark (topping it for the first time in late February 2008). In order to estimate the impact of the oil price increases on the Austrian economy, the OeNB carried out a simulation with its macroeconomic model. Taking as baseline the level of oil prices in the fourth quarter of 2006 (USD 59.7 per barrel Brent crude), the OeNB simulated the effects on the Austrian economy of the path of oil prices anticipated in its December 2007 economic outlook (2008: USD 88.6, 2009: USD 83.7). The simulation results show that the hike in oil prices would quickly feed through to consumer prices. For early 2008, the overall CPI price level is close to 0.8 percentage points above what it would have been if oil prices had remained steady at USD 59.7. Consumer prices subsequently decline again because of the assumed fall in oil prices. This translates into an extra stimulus to inflation of 0.35 percentage points in both 2007 and 2008. GDP growth reacts with a longer lag than prices, with the maximum effect setting in after around 1½ years. Real GDP growth in 2007 falls by 0.14 percentage points, and in 2008 by another 0.19 percentage points.

Impact of the 2007 Oil Price Hike on the Austrian Economy



Source: OeNB.

Box 3

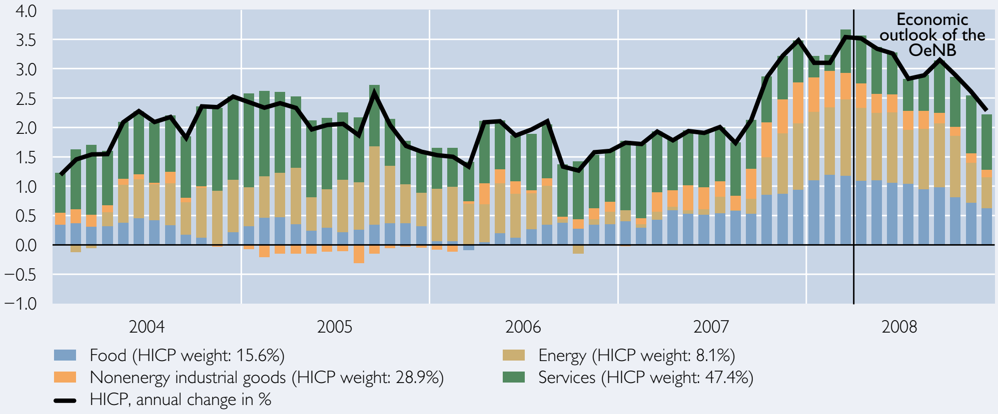
Accelerating Inflation in Austria since Fall 2007: Review by Consumer Categories and Measures to Combat Inflation

Food and energy prices mainly accounted for the rise in inflation in Austria in the last quarter of 2007. The price hikes in Austria in both areas followed above all from the elevated commodity prices in the international markets, for milk and wheat in the case of food, and for crude oil in the case of energy. Within food, mainly the prices for bread and cereal products (+4.5%), milk, cheese and eggs (+8.3%) and fruit (+4.4%) and vegetables (+5.7%) moved up sharply year on year. As for energy, the significant price increase can be attributed to the price hikes in electricity (+9.2%) and gas (+8.3%) that utilities generally implement early in the year, whereas the annual inflation in motor fuels in 2007 (+1.4%) was more subdued, having already surged in 2006. Looking at the evolution of motor fuel prices on an intrayear basis, however, illustrates that declines in prices in the first half of 2007 were offset by a steep advance in prices in the last three months of that year. The increase in the petroleum tax on diesel and gasoline in July 2007 pushed up inflation by 0.2 percentage points, according to the OeNB's calculations.

Although the inflation rate for nonenergy industrial goods in 2007 was below average at +1.3%, it was higher than in 2006 (+0.4%). This product group thus significantly drove up overall inflation. The pickup in industrial goods inflation was fueled mainly by prices for clothing and footwear, which shot up by 2.2% in 2007 after edging down by 0.2% in 2006. Services inflation amounted to 1.9% in 2007, and so was just slightly below the average rate. Having plunged by 24.7% year on year, airfares considerably tempered inflation in services. This mainly traces back to the expanding supply offered by discounters in the domestic airfare market.

HICP Inflation and Contributions to Inflation by Selected Consumer Categories in Austria

Percentage points | *Final observations: March 2008*



Source: Statistics Austria, OeNB.

If inflation in Austria is to be brought back to a level consistent with price stability according to the Eurosystem's definition of below, but close to, 2% over the medium term, various economic policies will have to take effect. The monetary policy of the Eurosystem must remain clearly and credibly committed to its primary goal of safeguarding price stability in the medium term. It is also imperative that second-round effects on prices and wages are avoided and that unions observe restraint in their wage demands, as should businesses in their pricing. Structural policies are vital too. Measures to intensify competition help contain prices. In the longer run, energy-saving innovations geared at i.e. tapping alternative domestic energy sources would boost Austria's resilience to international energy price shocks.

Finally, fiscal policy should be mobilized too. The Austrian economy has grown robustly for the last two years and capacities are being fully utilized. In this economic climate, additional aggregate demand generated by a budget deficit could push up inflation. The existing deficit should hence be reduced without delay. The public sector should refrain from further increases in taxes, fees and rates.

Sharp drop in unemployment

2005, including 63,000 in 2006 alone. Though the services sector provided most of the new jobs, employment picked up in industry and construction too, i.e. in sectors with a large proportion of full-time jobs offering above-average earning potential. The labor shortage in many sectors resulted in a partial opening of the labor market for lathe operators, welders and cutters from CESEE Member States. Another partial opening of the labor market is planned for 2008. Unemployment (Eurostat definition) fell from 5.2% (2005) to 4.4% in 2007, giving Austria the fifth-lowest jobless rate in the EU. The labor market lost some momentum toward end-2007 but picked up steam again in the first months of 2008. Employment growth was extremely vigorous at almost 3%, the drop in unemployment accelerated considerably in comparison with the last months of 2007, and activity in the vacancies market expanded as well.

Current account surplus hits record high

Austria's external sector ran a record surplus of EUR 8.8 billion in the current account of 2007, equivalent to 3.2% of GDP. Trade in goods and services was pivotal in widening the surplus by EUR 2½ billion. Despite the euro's appreciation, the traditionally negative balance on goods showed a surplus of EUR 1.3 billion. The largest contribution to the current account surplus, namely EUR 12.3 billion, came from services, with tourism posting a historic surplus of over EUR 6 billion. For the first time ever, the surplus generated by other services was higher (EUR 6.2 billion) than that achieved by tourism and travel. These service exports not only grew at a considerably faster pace than did revenues from travel and tourism, at 11% per annum over the past ten years, they have also been expanding much faster than goods exports. The technical services segment within business services (computer, architectural, engineering, research and development services and royalties and licenses) is particularly dynamic. In line with Austria's negative net investment position, the investment income balance was in deficit. According to provisional estimates, the Austrian economy's external liabilities exceed external ssets by some EUR 50 billion. The expanding surpluses on its current account enhance Austria's investment position in the international capital markets. Austria's net foreign investments in 2007 totaled EUR 6.3 billion.

Vigorous Economic Activity Shores up EU Member States' Budget Balances – Structural Reform Bolsters Economic Growth

The EU Member States design their economic policies in the common European interest, with the aim of promoting growth, employment and price stability in the EU. Consequently, the heads of state or government have subjected their national economic and fiscal policies to a joint fiscal discipline framework and to economic policy coordination mechanisms. Fiscal policies are subject to the rules of the Stability and Growth Pact (SGP), and economic policies are determined by the Lisbon strategy, an economic policy instrument that supports EU-wide structural change. Apart from the general objectives of the EU, these two frameworks contribute to greater flexibility, greater resilience to economic shocks and to cyclical smoothing.

Euro Area General Government Deficit Declines Markedly to 0.6% of GDP

Euro area government deficit shrinks to 0.6% of GDP in 2007

Budget consolidation made progress in 2007, with general government deficits contracting both in the euro area and in the EU, just like in 2006. Within the

Table 2

General Government Budget Balances

	2003	2004	2005	2006	2007	2008[1]
	% of GDP					
Belgium	0.0	0.0	–2.3	0.3	–0.2	–0.4
Germany	–4.0	–3.8	–3.4	–1.6	0.0	–0.5
Ireland	0.4	1.4	1.6	3.0	0.3	–1.4
Greece	–5.6	–7.4	–5.1	–2.6	–2.8	–2.0
Spain	–0.2	–0.3	1.0	1.8	2.2	0.6
France	–4.1	–3.6	–2.9	–2.4	–2.7	–2.9
Italy	–3.5	–3.5	–4.2	–3.4	–1.9	–2.3
Luxembourg	0.5	–1.2	–0.1	1.3	2.9	2.4
Netherlands	–3.1	–1.7	–0.3	0.5	0.4	1.4
Austria	–1.6	–3.7	–1.5	–1.5	–0.5	–0.7
Portugal	–2.9	–3.4	–6.1	–3.9	–2.6	–2.2
Finland	2.5	2.4	2.9	4.1	5.3	4.9
Slovenia	–2.7	–2.3	–1.5	–1.2	–0.1	–0.6
Euro area	**–3.1**	**–2.9**	**–2.5**	**–1.3**	**–0.6**	**–1.0**
Denmark	–0.1	1.9	5.0	4.8	4.4	3.9
Sweden	–0.9	0.8	2.2	2.3	3.5	2.7
United Kingdom	–3.3	–3.4	–3.4	–2.6	–2.9	–3.3
Bulgaria	0.0	1.4	1.8	3.0	3.4	3.2
Czech Republic	–6.6	–3.0	–3.6	–2.7	–1.6	–1.4
Estonia	1.8	1.6	1.8	3.4	2.8	0.4
Cyprus	–6.5	–4.1	–2.4	–1.2	3.3	1.7
Latvia	–1.6	–1.0	–0.4	–0.2	0.0	–1.1
Lithuania	–1.3	–1.5	–0.5	–0.5	–1.2	–1.7
Hungary	–7.2	–6.5	–7.8	–9.2	–5.5	–4.0
Malta	–9.9	–4.6	–3.0	–2.6	–1.8	–1.6
Poland	–6.3	–5.7	–4.3	–3.8	–2.0	–2.5
Romania	–1.5	–1.2	–1.2	–2.2	–2.5	–2.9
Slovakia	–2.7	–2.4	–2.8	–3.6	–2.2	–2.0
EU-27	**–3.1**	**–2.8**	**–2.5**	**–1.4**	**–0.9**	**–1.2**

Source: Eurostat.

[1] *Forecast of the European Commission (spring 2008).*

group of Member States whose currency is the euro the aggregate fiscal deficit dropped substantially from 1.3% of GDP in 2006 to 0.6% in 2007. The decline in the EU as a whole from 1.4% of GDP in 2006 to 0.9% in 2007 was less pronounced, but still significant. Six euro area countries closed 2007 with a budget surplus or a balanced budget, seven with a budget deficit, with Greece topping the list with a budget gap of 2.8% of GDP. In the EU as a whole, 12 Member States had a budget surplus or a balanced budget; only one country featured a deficit in excess of 3% of GDP, the limit relevant to fulfillment of the Maastricht fiscal convergence criterion.

Above all robust economic activity and the resulting higher-than-average tax revenue growth fostered the general deficit reduction. However, as the development of cyclically adjusted budgets shows, windfall tax revenues were used not for structural budget consolidation – as specified in the SGP – but rather for additional spending. Thus, the cyclically adjusted budget figures show less of an improvement than the nominal figures do, both in the EU and in the euro area. The euro area fulfilled another requirement of the SGP – annual improvements in the structural budget balance of 0.5 percentage points until the medium-term objectives have been reached – whereas the EU as a whole fell just short of this target.

According to European Commission forecasts, further improvements in the budget balances will come to a halt both in the euro area and in the EU as a whole in 2009, for one thing because of the expected cooling of business activity, and also because most countries' allocated budgets for 2008 do not provide for material consolidation. Under these circumstances, sound fiscal policymaking remains a key economic policy requirement, also with a view to achieving medium-term budget objectives – e.g. a medium-term position close to balance or in surplus – by 2010.

Austrian general government deficit contracts to 0.5% in 2007

The Austrian general government budget also benefited from robust economic activity: The general government deficit fell from 1.5% of GDP in 2006 to 0.5% of GDP in 2007. According to the provisional outturn of the central government budget for 2007, the estimated government deficit was some EUR 1 billion lower than expected because revenues developed so well. Central government expenditures, though, were higher than projected. Revenues were chiefly bolstered by substantial tax revenues in the wake of dynamic cyclical developments. In 2007, gross tax revenues (i.e. revenues before transfers to regional and local authorities and to the EU) went up by 7.1% from 2006. This rise was attributable especially to the powerful growth of income and wealth tax revenues, above all from wage and salary taxes, investment income taxes on dividends, interest income taxes and corporate income taxes.

The structural balance shrank from –1.4% of GDP in 2006 to –1.0% in 2007, which evidences that Austria did not fully reach the consolidation path called for in the SGP. According to the forecast of the European Commission of April 2008, the deficit will deteriorate somewhat in 2008. Higher social, education, family, pension, environment and research spending, along with the ongoing dynamic development of expenditure, especially health care expenditure, will make it harder to reach medium-term budget targets.

The update of the Austrian stability program for the years 2007 to 2010 specifies a general government surplus target of 0.4% of GDP by the year 2010. Moreover, under the program, the Austrian government is to report a structurally balanced budget in 2010. Substantial consolidation efforts are scheduled above all toward the end of the period covered by the stability program. Therefore, the adjustments to the medium-term objective envisaged for the years from 2007 to 2009 are gradual and not in line with the specifications of the SGP; in other words, the annual improvements in the structural deficit will fall short of 0.5% of GDP. Additionally, calculations in the program were based on the assumption that the entire period would consist of "good times" as defined in the SGP. Considering this premise, Austrian budget consolidation efforts must be stepped up.[1]

A reduction of the expenditure ratio is the method of choice for attaining the budget target. Government has adopted a stringent human resources policy and will manage discretionary expenditure that it can control extremely restrictively to secure the planned expenditure cuts. Revenues are set to remain fairly constant during the stability program period. Further reforms in public administration and in the health and education sectors should be envisaged to support the sustainable attainment of the targets in the stability program.

In October 2007, central, state and local governments agreed on a new revenue sharing schedule for the 2008 to 2013 period. This agreement is basically a continuation of the previous revenue sharing arrangements and covers neither substantial structural reforms nor a new division of responsibilities between the central, state and local government authorities. The October 2007 fiscal sharing arrangement includes the following important changes: the duration of the agreement was extended to six years; additional hospital funding was agreed for the provinces; and an agreement was concluded on the payment of the cost of 24-hour medical care and on the introduction of means-tested benefits to ensure a minimum income. In 2007, budgets performed below expectations: rather than achieving a surplus of 0.4% of GDP as provided for in the Austrian stability program, provincial and local government budgets posted a surplus of just 0.2% according to preliminary data. Therefore, not just the central government, but also state and local government should contribute to consolidation as agreed and as stipulated.

Government debt ratios decline in the euro area and in Austria

The decrease in government debt ratios in the euro area and in the EU as a whole observed since 2005 continued in 2007. The euro area ratio dropped to 66.4% of GDP; nearly all countries chalked up a debt ratio reduction. Nevertheless, at 58.7% of GDP, the debt ratio of the EU as a whole remained considerably lower.

Austria, too, made progress in slashing its debt ratio, which fell to 59.1% of GDP thanks to high nominal GDP growth in 2007. This outcome is the first to have fallen below the mark of 60% of GDP since 1992 and is some 6½ percentage points lower than the euro area average. European Commission forecasts see a further decline to slightly below 57% of GDP by 2009, and according to the Austrian stability program, the debt ratio is supposed to come to 55.4% in 2010.

[1] *See also box 4 for the assessment of budget developments in Austria by the IMF in the course of its Article IV consultations with Austria.*

Structural Reform Stimulates Economic Growth in the EU

Sustainable growth in all EU Member States is contingent on structural reform. This applies especially to euro area countries, as reform has a positive impact on their economic integration and resilience. Progressively stronger economic ties and the favorable effects of the single currency promote competition and trade on the Single Market, foster innovation and consequently create the prerequisites for supplying EU citizens with high-quality goods and services.

To this end, the EU Member States agreed on a European growth strategy, the Lisbon strategy, in the year 2000. This strategy was targeted at making the EU the world's most dynamic and competitive economy by 2010. According to the European Commission, the structural reforms for jobs and growth initiated within this framework have begun to bear fruit, having helped boost the pace of economic growth and potential output in recent quarters. The European Commission concluded in its December 2007 review of the national reform programs (NRPs) that the euro area countries have engaged in substantial structural reforms to tackle their economic, social and ecological challenges. The Commission welcomed the budgetary adjustment in 2007, the implementation of legislation to foster financial market integration, and the use of wage bargaining systems more conducive to wage flexibility in some Member States. However, policy areas remained in which challenges now need to be tackled with the highest priority, notably enhancing competition in product markets; increasing labor mobility in Europe; and improving the sustainability of public finances in view of demographic aging. Here, the European Commission recommended stepping up measures to reach medium-term budget targets and generally advancing the quality of public finances. Moreover, effective measures needed to be taken to reinforce competition above all in the services sector. Finally, labor markets have to be adjusted toward more flexicurity to become perceptibly more efficient.

Box 4

Structural Reform in Austria and Its Assessment by International Organizations

Austria has implemented structural reforms in numerous areas in recent years. Tax reform, pension reform, administrative reform, labor market reform and a substantial increase in R&D expenditure has made the economy more flexible and has enhanced Austria's business location quality.

- *The dominant theme of the labor market reforms implemented in Austria in 2007 was flexicurity, i.e. greater flexibility combined with employment security. Collectively agreed working time regulations were eased; maximum working hour limits were raised to 60 hours a week and 12 hours a day (up from 10 hours a day) and the higher limits apply to up to 24 weeks (up from 12 weeks). In exchange, part-timers have become eligible for bonus pay for additional working hours. The* ***new severance pay scheme*** *was extended to include self-employed workers, business owners, those working on a "contract for work" basis (also referred to as the new self-employed), independent professionals, and farm managers and foresters. Moreover, self-employed workers were included in the unemployment and health insurance scheme. The reform has made it easier for employers to serve notice to apprentices; in exchange, guaranteed training up to the age of 18 has been established explicitly as a target. Means-tested benefits (around EUR 750 a month) and a* *minimum wage (EUR 1,000 a month) are scheduled for implementation by the year 2009. The reform provides for an opening of the labor market for foreign labor in those professions in which fewer than 1.5 job seekers are registered unemployed per vacancy. To counteract illegal employment in the construction sector, employees must be reported before the start of construction; general contractors are liable for subcontractors. Funding for child-care facilities was increased and the payment of child-care benefits made more flexible to help improve peoples' work-life balance. Many measures have resulted from social partner initiatives or agreements.*

- *In the product markets, shop hours were extended from 66 to 72 hours a week. The EU Services Directive is to be implemented in Austria by the year 2009.*
- *Reforms to improve the quality of public finances and public administration are currently underway: the **Better Regulation** project envisaging administrative cost savings of 25% is to be implemented by 2010. Additionally, government reform is still being discussed; an expert panel is now elaborating proposals.*
- *International institutions' assessments of Austria particularly commend the effectiveness of strategies to enhance innovation and boost R&D expenditure. These efforts have lifted R&D expenditure; it rose from 1.88% of GDP in 1999 to 2.55% in 2007 and will climb further to 2.63% in 2008 according to Statistics Austria. Further improvements have taken effect only recently: on January 1, 2008, the labor market was opened to researchers from the Member States that have joined the EU since 2004 and from third countries. Specifically, researchers may work in Austria not just at research institutions but in all types of businesses without restriction. At the same time, family members (spouses and children) are no longer subject to the Foreign Labor Act, enabling researchers and their families to work in Austria without restriction. This amendment addressed a key criticism in the OECD's 2007 country report on Austria. Structural reform currently underway in the area of R&D consists in an evaluation of public subsidies and of the entire Austrian innovation promotion system. The evaluation is expected to produce results by the end of 2008. The Austrian Research Dialogue (an initiative of the Austrian Federal Ministry of Science and Research) and the innovation dialogue (Federal Chancellery) are charged with developing proposals before the technology talks in Alpbach, Austria, in late summer 2008. Additionally, a guide on encouraging innovation in public procurement was drawn up.*
- *In the field of education, efforts went into reducing the number of students per classroom to a maximum of 25. Austria will introduce a new type of secondary school system, the **new middle school (Neue Mittelschule)**, on a trial basis in the 2008–2009 school year. Five-year-olds' German proficiency will be assessed, and children whose skills are found to be deficient will be obligated to attend kindergarten. The **new study leave** model is designed to promote lifelong learning. The new system entitles employees to apply for study leave after one year of employment; the monthly study leave benefit of EUR 436 a month will be increased to equate the corresponding unemployment benefit (increase by an average of 70%).*
- *Environmental and energy sector reforms include the establishment of the Austrian Climate and Energy Fund and the provision of EUR 500 million to the fund for the development and implementation of innovative energy technologies. Moreover, Austria raised the mineral oil tax in July 2007.*

In its December 2007 review of the national reform programs initiated by the EU, the European Commission noted that Austria had made significant progress in implementing its national reform program. The European Commission particularly emphasized the effectiveness of the strategies to increase innovation and higher R&D expenditure as well as further reforms of the Austrian labor market. However, the Commission also remarked that only partial progress had been achieved in strengthening the business climate, promoting older and younger workers, increasing competition in services and identifying further emission reduction policies. Furthermore, the general policy recommendations issued to the euro area were also applicable to Austria.

The OECD's Economic Survey of Austria in 2007 and the Article IV consultations of the IMF with Austria in March 2008 only partially take account of the reforms implemented in 2007. Both reports recognize Austria's comparatively favorable economic performance, but also take note of two weaknesses: the development of service sector productivity, and the development of certain labor market segments, namely younger and older workers, and women. The following economic policy measures should be taken to counteract these weaknesses: increasing competition in services, e.g. by strengthening competition in the liberal professions; promoting human capital by introducing a mandatory preschool year, by introducing the new middle school, thus ending the early separation of students in the 10–14 age bracket, by introducing autonomy and standards in secondary schooling and by increasing participation in tertiary schooling; discouraging early retirement by reforming eligibility for disability pensions and by increasing penalties.

In its Article IV consultation with Austria in March 2008, the IMF strongly supported the government's objective of targeting a balanced budget over the cycle. As there was no need for discretionary fiscal stimulus, the IMF considered it important to press ahead with structural adjustments of fiscal expenditures. Otherwise, reaching the objective of a structurally balanced budget by the year 2010 might be jeopardized. IMF staff identified savings potential in the accelerated implementation of administrative reform, health reform and pension reform at the provincial level, and above all in the reform of fiscal federal relations, including clarifying the expenditure responsibilities of the different levels of government. Revenue sharing reform efforts should be focused on boosting the efficiency of subnational government spending. The IMF welcomed the adoption of the medium-term fiscal budgetary framework and urged the authorities to incorporate subnational governments into the framework as soon as possible. To prevent the structural budget balance from deteriorating, the IMF recommended that the tax reform announced in the Austrian Stability Program for 2010 not be implemented unfunded. Considering that labor cost is high, reducing nonwage labor cost should be envisaged. The IMF also recommended that Austria simplify its tax system.

The European Union – A Success Story

The OeNB in Europe

The OeNB is represented in numerous European and international bodies. Its international activities center on committee and working group meetings of the European System of Central Banks (ESCB) and, most importantly, the input of the OeNB's governor to monetary policy and other decision-making within the Governing Council of the ECB and within the Eurosystem. The governor also attends the informal Ecofin (meetings of EU finance ministers and central bank governors), the annual meetings of the International Monetary Fund (IMF) and the regular meetings of central bank governors at the Bank for International Settlements (BIS). Last but not least, the OeNB also cooperates internationally under the aegis of the Organisation for Economic Co-operation and Development (OECD).

Apart from its statutory memberships, the OeNB seeks to maintain good relations with other central banks and international organizations, economic policymakers as well as representatives of academia and research, with a view to fostering the exchange of expert knowledge, promoting Austria's interests in national and international bodies, and shaping monetary and economic policies in Austria and Europe.

In this respect, the OeNB is committed particularly to advancing the integration of the national central banks (NCBs) of the Central, Eastern and Southeastern European (CESEE) countries into the Eurosystem. The OeNB is developing long-term partnerships with the countries in the area to secure Austria's economic interests and to strengthen its own position as a competence center for integration issues within the Eurosystem. Building and sharing expertise in monitoring economic developments and financial markets as well as in compiling and assessing statistics is instrumental in achieving this goal.

Against the backdrop of its broad international commitments and its strategic interests, the OeNB observes developments at the European level particularly closely. Reflecting institutional, economic and political developments in 2007, the framework for European cooperation was enhanced considerably in the reporting year.

New Statutory Foundation Created for the EU Institutions

The year 2007 saw the 50th anniversary of the signing of the Treaty of Rome, i.e. of the birth of the European Community. The year of celebrations was marked, above all, by efforts to deepen European integration further. The EU was given a new statutory foundation with the signing of the Treaty of Lisbon[1] on December 13, 2007. The new Treaty has been designed to allow an enlarged Union of 27 Member States to work more efficiently than possible under the Treaty of Nice, which remains in force until the Treaty of Lisbon has been ratified.

Treaty of Lisbon signed

The amendment of the EU Treaties is paving the way for a future widening and deepening of European integration. Reforming the EU's statutory framework was a must, given the most recent and potential new enlargement rounds as well as the increasing cooperation among EU Member States in the context of globalization. The new Treaty

[1] *Formally, the Treaty of Lisbon amending the Treaty on European Union and the Treaty establishing the European Community; see the Official Journal of the European Union 2007/C 306/01 and http://europa.eu/lisbon_treaty/index_en.htm.*

will improve the ability to act and the democratic legitimation of the EU institutions, enhance the coherence of external policies and, to some extent, replace the draft Constitutional Treaty rejected in referendums in France and the Netherlands.

Once the Treaty of Lisbon was signed, it was sent to the governments of the EU Member States for ratification. The Treaty of Lisbon would need to take effect in June 2009 to make sure that the next elections to the European Parliament and the formation of the new European Commission will be carried out already in accordance with the new framework. The Treaty may be ratified by the national parliaments in most EU Member States, except in Ireland, where it must be put to a referendum in line with constitutional provisions. A few other countries are also considering referendums, which may prove to be a stumbling block of sorts on the road to putting the new framework into effect. By the end of February 2008, the Treaty of Lisbon had been ratified by five Member States, namely Hungary, Slovenia, Malta, Romania and France. In Austria the Treaty was ratified on April 9, 2008.

Box 5

What is New under the Treaty of Lisbon?

First and foremost, the Treaty of Lisbon provides for a clearer delimitation of competences, introduces more majority voting and changes the institutional framework for the EU institutions.

In the new Treaty, the European Council is listed as an EU institution; moreover, the Treaty created the function of a President of the European Council, who is elected for two-and-a-half years. In addition, it created the position of the High Representative for the Union in Foreign Affairs and Security Policy, which combines the tasks of today's EU Representative for Foreign Policy and those of the EU Commissioner for Foreign Affairs. The High Representative will be the Vice-President of the European Commission. Starting on November 1, 2014, the number of EU Commissioners will be reduced to two-thirds of the current number, and a rotation principle will be introduced.

The role of the European Parliament will be strengthened with the extension of the codecision procedure. Moreover, the President of the European Commission will henceforth be elected directly by the European Parliament, which also serves to raise the democratic legitimation of this institution. With regard to the vote allocation within the Council of Ministers, the "double majority" principle will be introduced, with a transitional period, on November 1, 2014. This means that decisions taken by the Council of Ministers will require a double majority of 55% of the Member States representing at least 65% of the Union's population. The principle of qualified majority voting will also be applied more extensively in the decision-making processes of the European Council. At the same time, the principle of unanimity will be retained for sensitive areas such as foreign, tax and social policies, matters of EU enlargement and changes to EU Treaties. Finally, through the Treaty of Lisbon, the European Charter of Fundamental Rights becomes binding, i.e. the fundamental rights can be asserted before the European Court of Justice.

By and large, clauses related to the establishment of the European Economic and Monetary Union (EMU) remained broadly unchanged by the new Treaty. Other than the general institutional changes, elements of the new Treaty relevant to EMU include, above all, the listing of price stability among the EU's objectives, the institutional status of the ECB as well as the protection of its independence and the strengthening of the Eurogroup. Moreover, the framework conditions for monetary union as embodied in the Treaty on European Union have been reaffirmed.

The Euro Has Arrived in a Few More New EU Member States

Following Slovenia on January 1, 2007, Malta and Cyprus were the next EU members from among the group that joined in 2004 to introduce the euro (on January 1, 2008). Thus, the euro area has grown to encompass 15 of today's 27 EU Member States, with approximately 320 million EU citizens now using the euro as their currency.

Beyond the euro area, the single European currency has come to play a significant role in many CESEE economies even today. A number of countries orient their monetary and exchange rate policies on the single currency. Five Member States were participating in the exchange rate mechanism II (ERM II) at the reporting date, limiting fluctuations of their currencies' external value to a multilaterally agreed fluctuation band of ±15% to the euro – with some countries having unilaterally adopted a smaller fluctuation band. Of the ERM II participants, Estonia and Lithuania have pegged their currencies to the euro through currency board systems; as have – beyond ERM II – Bulgaria as well as Bosnia and Herzegovina. In addition, Montenegro and Kosovo have already introduced the euro as legal tender.[2] The euro is also playing an important and growing role in trade invoicing and in capital market transactions in the area. Moreover, euro use among the CESEE population has become quite widespread, without a legal basis and irrespective of the exchange rate regime in place. It is not unusual for residents of the region to hold cash or deposits or to take out loans in euro these days (see also the chapter "The OeNB as the Key Player in Securing Financial Stability in Austria").[3]

As the European Commission noted in a communication adopted in May 2007, the changeover to the euro in Slovenia was "a swift and smooth affair." The "Big Bang" approach – i.e. the irrevocable locking of the exchange rate and simultaneous introduction of euro banknotes and coins – worked fine and may therefore be the method of choice also in future enlargement rounds of the euro area. Moreover, a two-week dual circulation period for the euro and the Slovenian tolar was found to be sufficient, given that the changeover was prepared well and timely by the institutions involved. The OeNB provided substantial support for the introduction of the euro in Slovenia (see the chapter "The OeNB Ensures the Security and Efficiency of the Cash Cycle").

Euro introduced successfully in Slovenia

Inflation remained fairly low in Slovenia the first few months following its accession to the euro area. Based on data available up to March 2007, Eurostat put the total impact of the euro on consumer price inflation during and after the changeover period at 0.3 percentage points. Toward the end of 2007 and in early 2008, however, inflation rose considerably (to 6.6% in March 2008). To some extent, this increase reflected the global increase in food and energy prices. Given the comparatively low level of competition in

[2] *Montenegro and Kosovo are special cases that need to be seen against the backdrop of the disintegration of former Yugoslavia.*

[3] *See Backé, P., D. Ritzberger-Grünwald and H. Stix. 2007. The Euro on the Road East: Cash, Savings and Loans. In: Monetary Policy & the Economy Q1/07. Vienna: OeNB. 114–127. Another OeNB paper on this issue is: Ritzberger-Grünwald, D. and H. Stix. 2007. Are Euro Cash Holdings in Central and Eastern Europe Driven by Experience or Anticipation? Results from an OeNB Survey. In: Focus on European Economic Integration 1/07. Vienna: OeNB. 77–100.*

Malta and Cyprus joined the euro area in 2008

trade in Slovenia, retailers were able to pass on price increases more readily to end consumers than would have been possible in a more competitive environment. Price increases became more widespread above all after the end of dual pricing in June 2007, especially for seasonal products coming onto the market for the first time after the changeover to the euro. The robust pace of the economy is likely to have added to inflationary pressures as well.

The convergence process of Malta and Cyprus was given a positive assessment in the convergence reports published by the European Commission and by the ECB in May 2007. Both countries were found to have met the required criteria on a sustained basis, and were consequently given the green light to join the euro area and to introduce the euro on January 1, 2008. Being particularly open economies, the two islands stand to benefit more than other countries from membership in the euro area. Apart from the benefits that the euro brought for trade, the euro is going to make the two countries even more attractive for tourists from the euro area and will thus stimulate the tourist industry.

During the changeover period, prices were monitored systematically by the public authorities and consumer organizations of both Cyprus and Malta. In many instances, this very strict monitoring led to the retainment of the pre-changeover prices. This notwithstanding, price pressures mounted slightly in early 2008 in both countries.

Later in 2008, the European Commission and the ECB stand to publish their regular two-yearly convergence reports, assessing the progress of the countries not yet participating in the third stage of EMU on their road to introducing the euro. The convergence assessment will be provided for Bulgaria, Estonia, Latvia, Lithuania, Poland, Romania, Sweden, Slovakia, the Czech Republic and Hungary.[4] Of those countries, Slovakia is the only country targeting euro area entry already in 2009.

The EU Has Grown to 27 Member States

Bulgaria and Romania joined the EU in 2007, thus concluding the fifth enlargement round, which had begun in 2004 with the accession of ten Central, Eastern and Southern European countries to the European community. The entry of Bulgaria and Romania to the EU marked the high point so far of the impressive transformation process the two countries have undergone. They managed to turn their planned economies into functioning market economies and to fulfill the legal requirements for joining the EU in a fairly short period.

Notwithstanding this achievement, the European Commission identified a number of areas in the preaccession process that require further work even after accession to the EU, notably the fight against corruption, judicial reform, the proper management of EU agricultural funds and direct payments as well as food safety. The two countries' accession was hence accompanied by a series of measures. Among other things, the EU set up a mechanism for cooperation and the verification of progress in the areas judicial reform and the fight against corruption. To better protect the EU's financial inter-

[4] *Two Member States – Denmark and the United Kingdom – are not covered by the ECB's or the European Commission's respective convergence reports because they have negotiated opt-out arrangements and are not participating in Stage Three of EMU.*

Box 6

Malta and Cyprus – Two New Euro Area Members as of January 1, 2008

With the introduction of the euro by Cyprus and Malta on January 1, 2008, the euro area now comprises 15 EU Member States. Both Malta and Cyprus now benefit from the advantages of the single currency, such as price stability, the elimination of foreign exchange risks, full price and cost transparency, lower transaction and information costs as well as a higher resilience to economic and financial shocks. In order to keep reaping those benefits to the full extent, it will take a continued commitment to stability-oriented economic policies with a view to securing fiscal discipline, keeping up the structural reform momentum and enhancing competitiveness further.

Following the positive assessment of the two countries' economic convergence in the ECB's and the European Commission's convergence reports of May 16 and the July 2007 European Council conclusion to welcome their entry into the euro area, the Ecofin Council adopted a decision allowing Malta and Cyprus to join the euro area on July 10, 2007. On that day, the Ecofin Council also irrevocably fixed the conversion rate of the Maltese lira (MTL) and of the Cyprus pound (CYP) at their central parity within the exchange rate mechanism II (ERM II), that is at MTL 0.429300 per euro and at CYP 0.585274 per euro.

The parallel circulation period, with both the old and the new currency being legal tender, ended on January 31, 2008, in both Malta and Cyprus. Commercial banks exchanged the legacy currencies free of charge until March 31, 2008, in Malta, and will continue to do so until June 30, 2008, in Cyprus. The central banks of the two countries will exchange the legacy currencies for considerably longer periods (Malta: coins until February 1, 2010; banknotes until January 31, 2018; Cyprus: coins until December 31, 2009; banknotes until December 31, 2017). In Malta, dual pricing is obligatory from July 1, 2007, until the end of June 2008. In Cyprus, dual pricing became mandatory on September 1, 2007, and will be required until September 20, 2008. The underlying purpose is to keep price increases down with the dual display of prices.

Both Malta and Cyprus owe their accession to the euro area to their stability-oriented economic policies, which were supported by structural reforms. The nominal convergence achieved with the euro area in 2006 manifested itself in low inflation rates (2.6% in Malta; 2.2% in Cyprus), low or decreasing budget deficits (2.6% of GDP in Malta; 1.2% of GDP in Cyprus), declining public debt ratios (64.2% of GDP in Malta; 64.8% of GDP in Cyprus), the convergence of long-term and short-term interest rates as well as a high degree of exchange rate stability during ERM II participation since May 2005.

Indicators for Malta and Cyprus Compared with the Euro Area

	Malta		Cyprus		Euro Area (EA-13)	
	1999	2007	1999	2007	1999	2007
Population, million	0.4	0.4	0.7	0.8	305.7	319.3
Population, % of total euro area population	0.1	0.1	0.2	0.2	×	×
GDP, % of euro area	0.1	0.1	0.1	0.2	×	×
GDP per capita at PPP, % of euro area	70.9	70.5	76.8	84.5	×	×
GDP per employed person, % of euro area	84.9	82.3	72.3	78.0	×	×
Employment rate[1]	54.5	55.7	65.4	71.0	61.3	64.7
Unemployment rate[1]	6.4	6.5	5.1	4.0	9.4	7.4

Source: Eurostat.

[1] *Data for 2000 instead of 1999.*

ests, a separate regulation specifying a mechanism for the proper use of agricultural funding was adopted. EU legislation also provides for comprehensive measures to deal with possible dangers in areas like food safety.

In June 2007 the European Commission submitted the first reports on the cooperation and verification mechanism, reviewing the state of play on the accompanying measures put in place by Bulgaria and Romania with regard to judicial reform, the fight against corruption and organized crime. The purpose of these reports is to review in how far the accompanying measures following accession have been implemented and/or whether they need to be adjusted. For example, the Commission examined whether the transparency and efficiency of the judicial process has been improved, and it assessed the need for further measures to prevent and fight corruption.

The European Commission concluded that, in varying degrees, Bulgaria and Romania had continued to make progress in remedying weaknesses that could prevent an effective application of EU laws, policies and programs, at the same time identifying the need to step up efforts in the fight against corruption. Given the short time for which Bulgaria and Romania have been EU members, the European Commission will retain the cooperation and verification mechanism and submit the next detailed reports in mid-2008. In interim reports released in February 2008, the European Commission reiterated its call for increased anti-corruption efforts and, in the case of Bulgaria, for further efforts to combat organized crime.

Continued Negotiations on Further EU Enlargement

EU enlargement has contributed to peace, security, freedom, democracy and the prevention of conflicts, has improved welfare and been a catalyst for growth across Europe. Enlargement has thus come to be one of the most important and most successful policy instruments of the EU.

The renewed consensus on enlargement, defined by the European Council in December 2006, is based on the principles of consolidation of commitments, fair and rigorous conditionality and better communication with the public, combined with the EU's capacity to integrate new members. At the time of writing, Croatia, the former Yugoslav Republic of Macedonia (FYR Macedonia) and Turkey are candidates for accession to the EU.

In November 2007, the European Commission adopted its annual Enlargement Strategy and Progress reports, assessing the progress made by the candidate countries over the past 12 months. It concluded that Croatia and the FYR Macedonia had made gradual progress, yet with varying degrees in individual chapters. Furthermore, the European Commission noted that the accession negotiations had reached a decisive stage in Croatia. With regard to Turkey, the European Commission continued to find substantial need for reform, identifying a need for immediate action for granting freedom of expression and religion, solving the social problems in the Southeast, and lifting the restrictions on direct travel links with Cyprus.

As regards Croatia, 18 out of 33 negotiation chapters have been opened so far; 2 chapters (science and research, education and culture) have been provisionally closed. As regards Turkey, 6 out of 33 have been opened, one of which (science and education) has been provisionally closed as well. As Turkey does not, as yet, meet all of its statutory obligations – specifically with regard to the extension of the existing customs union with the EU to the Member States that have joined since 2004, in

Box 7

Following the Accession of Bulgaria and Romania, the EU Has Grown to 27 Member States

As a result of the EU entry of Bulgaria and Romania, the number of EU citizens grew by approximately 30 million people, or around 6% of the EU-27 population. Based on GDP, Bulgaria and Romania added an extra EUR 101 billion, or roughly 1.1%, to the GDP of the EU-27. These figures indicate that both countries continue to be at a fairly early stage of economic convergence. Measured in purchasing power parities, their GDP per capita reached a mere 40% of the EU average in 2007. This notwithstanding, both Bulgaria and Romania have staged an impressive catching-up process in recent years. Given a solid growth performance, they managed to considerably narrow the per capita income gap with the EU registered in 1999. The key driving force behind this process was a rise in labor productivity. The unemployment rates are roughly on a par with the EU average. Unemployment has dropped markedly in Bulgaria in recent years, whereas it has risen somewhat in Romania.

With regard to the sectoral structure, the two newest EU members continue to differ significantly from the rest of the EU. The agricultural sector as well as the manufacturing and the construction industry continue to have a bigger share in value added as well as in overall employment than is the case on average across the EU-27, whereas the services sector is considerably smaller. In recent years, however, there has been some degree of harmonization of the sectoral structure. At the same time, the agricultural sector remains noticeably overrepresented in terms of both output and employment figures.

Indicators for Bulgaria and Romania Compared with the EU

	Bulgaria		Romania		EU-27	
	1999	2007	1999	2007	1999	2007
Population, million	8.2	7.6	22.5	21.5	482.2	496.2
Population, % of EU population	1.7	1.5	4.7	4.3	×	×
GDP, % of EU	0.1	0.2	0.4	1.0	×	×
GDP per capita at PPP, % of EU	27.0	38.3	25.8	41.5	×	×
GDP per employed person, % of EU[1]	30.7	35.7	24.9	41.8	×	×
Employment rate[2]	51.5	61.7	64.2	58.8	62.1	65.4
Unemployment rate[2]	16.4	6.9	7.7	6.8	9.4	7.2
Sectoral contribution to GDP, % of GDP						
Agriculture	16.3	6.2	14.9	8.8	2.5	1.9
Industry and construction	28.8	32.3	33.3	35.9	28.0	26.5
Services	54.8	61.5	51.8	55.2	69.4	71.7
Sectoral distribution of employment, % of total employment[2]						
Agriculture	13.1	8.1	45.2	30.6	8.0	5.9
Industry and construction	32.7	34.5	25.8	30.7	29.3	27.5
Services	53.7	57.4	29.0	38.7	62.4	66.4

Source: Eurostat.

[1] Data for Romania for 2001 instead of 1999.
[2] Data for 2000 instead of 1999.

particular Cyprus – it has not been possible to open the chapters relevant to those restrictions. Moreover, the EU will not close any other chapter provisionally unless Turkey has met all of its statutory obligations. The negotiations with the FYR Macedonia have yet to be opened.

The potential integration of the countries of the Western Balkans into the EU was advanced in 2007, among other things with the signing of a Stabilisation and Association Agreement (SAA) with Montenegro. The intention of SAAs is, among other things, to promote economic and trade relations and to pave the way, following a transition period, for free-trade rules compliant with the rules of the World Trade Organization (WTO).

The OeNB as the Key Player in Securing Financial Stability in Austria

Financial Stability in Austria Remains High

Unlike banks in other countries, Austrian banks have been only marginally affected by the U.S. subprime crisis. The OeNB monitors market developments very closely and – in cooperation with the Austrian Financial Market Authority (FMA) – has maintained close contacts with Austrian banks since the beginning of the financial turmoil in August 2007. The financial turbulence had relatively modest effects on Austrian banks, in particular because Austrian banks have a broad deposit base and focus their business activities on Central, Eastern and Southeastern European (CESEE) markets and on retail banking, which is fairly independent of cyclical developments.

Despite the financial turmoil, Austrian banks continued to boost their business performance and profitability throughout 2007. Not least because of the continued growth dynamics in CESEE, developments in the Austrian banking sector were favorable in 2007. In the course of the year, total banking sector assets on an unconsolidated basis[1] climbed by 12.8% to EUR 900 billion, with foreign business accounting for no less than 39% of assets. Total assets on a consolidated basis posted comparably strong growth. Banks' improved profit situation, which is above all attributable to their CESEE business activities, and sound capital ratios help increase banks' risk-bearing capacity. The stress tests the OeNB carries out at regular intervals confirm this development.

U.S. subprime crisis barely affects Austrian banks

In the reporting year, Austrian banks' earnings rose at a faster rate than their business volume – a development that clearly helped improve banks' profitability. Unconsolidated operating profit climbed by 14.4% against the year 2006 to EUR 6.7 billion, with unconsolidated operating income (+5.4%) expanding considerably faster than unconsolidated operating expenses (+0.5%). These differing growth rates led to a further improvement of banks' cost-to-income ratio[2], which serves as a measure of banking efficiency. Banks' cost-to-income ratio came to 62.0% in 2007. Although the net interest margin[3] contracted to below 1% and net interest income growth was relatively modest at +3.2%, net interest income (at a share of 42%) remained by far the most important source of unconsolidated operating income in 2007. Fee-based income (+9.5%) continued to be the prime driver of operating income growth, with its share climbing by 1.1 percentage points to 27%. Given the moderate rise in administrative expenses (+5.3%) and nearly unchanged personnel expenses (+0.3%), operating expenses remained largely stable. Overall, the unconsolidated total return on assets (ROA) for the reporting year came to 0.53% against 0.5% in 2006.

Ongoing improvement of Austrian banks' profitability

Consolidated profits also saw remarkably dynamic growth, which was largely based on banks' CESEE business. Interest and fee-based income grew by around 25% compared with the previous year. With expenditures (both administrative expenses and staff

[1] *Total assets on an unconsolidated basis are used, in particular, to analyze developments in Austria. These data do not include foreign business conducted via subsidiaries abroad.*

[2] *Operating expenses as a percentage of operating income.*

[3] *Net interest income as a percentage of total assets.*

costs) growing at a slower pace, the consolidated cost-to-income ratio also improved.

Austrian banks' capital ratios remained sound. On a consolidated basis, the overall solvency ratio stood at 12.1% at the end of 2007 and was thus substantially above the 8% threshold defined in the regulatory capital requirements.

Banks continue to expand CESEE activities

The large Austrian banks' CESEE business continued to drive their dynamic expansion. Given that 2007 saw no major acquisitions in the banking sector, the sector's rapid development is mainly attributable to organic growth. By mid-year, the consolidated business segment reports of the six large Austrian banks active in the region had already grown to 24.5% of the consolidated total assets of all Austrian banks (+5.9 percentage points year on year). The same six banks accounted for as much as 41.7% of the consolidated pretax profit of all Austrian banks (+6.2 percentage points). This development mirrors the generally high demand for loans fostered by favorable economic developments in CESEE; demand differs among countries, however. Thus, the aggregated sum of loans granted by Austrian banks' subsidiaries operating in CESEE had surpassed the EUR 120 billion threshold by end-June 2007. While rapid credit growth reflects the catching-up process in these countries, it also entails potential risks, which is why the OeNB closely monitors developments in the CESEE banking sector.

The pronounced expansion of large Austrian banks in Southeastern Europe and the Commonwealth of Independent States (CIS) is particularly remarkable. As a consequence of the latest EU enlargement by Bulgaria and Romania and thanks to the favorable development of business activities in these countries, Austrian banks continue to hold just over two-thirds of their subsidiaries' aggregated total assets within the EU. This helps limit institutional and legal risks, in particular. From a macroprudential point of view, however, the macroeconomic imbalances in some countries (both inside and outside the EU) and the additional risks that arise from developing new markets in Eastern and Southeastern Europe must be taken into account. Chart 17 gives an overview of the business activities in the region, showing the size of the respective banking sectors and the market share held by Austrian banks in the individual countries. Large Austrian banks' expansion activities are subject to adequate risk management and risk provisions.

Austrian banks' ever-increasing presence in CESEE countries has also made the region a more pronounced focus of the OeNB's financial stability analysis. To provide for a more comprehensive account of Austrian banking activities in this area, the OeNB has been enhancing its contacts to CESEE central banks on the one hand while continuously improving its analytical tools on the other. The new reporting system for banks' subsidiaries abroad, which was introduced at the beginning of 2008, will help the OeNB to closely monitor the local business activities of Austrian banks' subsidiaries abroad and to more efficiently analyze their risk-bearing capacities.

Importance of foreign currency loans in Austria declines slightly

Although the share of foreign currency loans in private sector borrowing in Austria has declined, the level of foreign currency lending remains high. Foreign currency loans to both nonfinancial corporations and households[4]

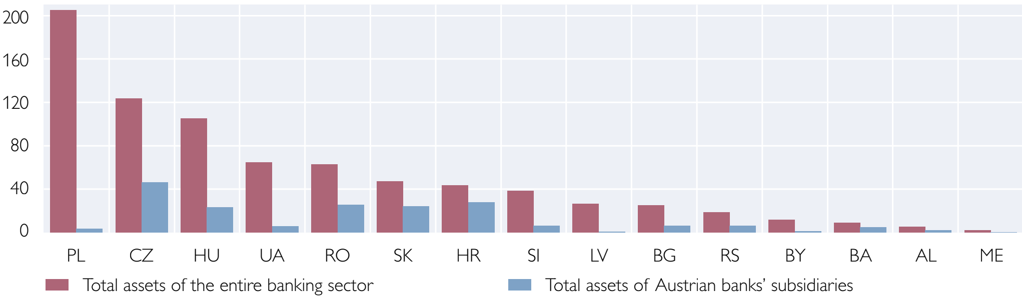
[4] *In this context, the household sector also comprises nonprofit institutions serving households.*

Chart 17

Exposure of Austrian Banks' Subsidiaries in Central, Eastern and Southeastern Europe

As at June 30, 2007

EUR billion



Source: OeNB, NCBs.

Note: *The Russian banking sector (total assets: around EUR 500 billion) is disproportionately large compared to the other countries covered; therefore, this chart does not include Russia. List of countries included: Albania (AL), Bosnia and Herzegovina (BA), Bulgaria (BG), Belarus (BY), Czech Republic (CZ), Croatia (HR), Hungary (HU), Latvia (LV), Montenegro (ME), Poland (PL), Romania (RO), Serbia (RS), Slovakia (SK), Slovenia (SI) and Ukraine (UA).*

decreased from their all-time highs. At end-December 2007, 8.1% of all loans taken out by nonfinancial corporations and 27.5% of those taken out by households were denominated in a foreign currency. Nonfinancial corporations had posted an all-time high in foreign currency-denominated borrowing in the third quarter of 2000 (18.7% of total loans), while foreign currency lending to households peaked in the second quarter of 2006 (31.5%). The decline in foreign currency loans is attributable, among other things, to borrowers' heightened risk awareness. To further support this development, in 2007 the OeNB – in cooperation with the FMA and the Austrian Federal Economic Chamber (WKO) – updated and reissued their joint information folder on the risks involved in foreign currency loans. The OeNB will continue to closely monitor the development of foreign currency lending.

The total volume of Austrian banks' foreign currency lending to domestic borrowers went down by 10.3% to EUR 46.7 billion in 2007, with loans to nonfinancial corporations accounting for around EUR 10 billion and loans to households for around EUR 32 billion. The currency composition of foreign currency loans remained almost unchanged: the Swiss franc remained the dominant currency with a share of around 89%, followed by the U.S. dollar at about 5% and the Japanese yen at around 3.5%.

From the financial stability perspective, monitoring the development of the foreign currency loan segment is also important because borrowers often face the risk of volatile returns of repayment vehicles in addition to the exchange rate risk. OeNB analyses have shown that around 79% of all foreign currency-denominated claims on domestic nonfinancial corporations and households are bullet loans and that 77% of these bullet loans are, in turn, backed by repayment vehicles.

Foreign currency loans also gained importance in CESEE, with Austrian banks' subsidiaries actively contributing to this development. According to a joint survey conducted by the OeNB and the FMA, the outstanding foreign currency loan volume of these credit institutions came to about EUR 57 billion in June 2007. More than half of these loans were taken out in Croatia, Hungary, Romania and Russia. All in all, around 60% of all foreign currency loans were denominated in euro, approximately 20% in Swiss francs and the remainder in U.S. dollars; the breakdown of currencies varied considerably from country to country, however.

Slowdown observed for other financial intermediaries and in the Austrian stock market

Overall developments in the Austrian insurance sector were positive in 2007. Booming unit-linked life insurance plans and subsidized personal pension schemes continued to play a substantial role in sustaining demand in the life insurance sector. Insurance companies' claims payments were influenced in particular by maturing life insurance policies. While in the first half of 2007, insurance companies' favorable investment results improved further owing to positive stock market developments, second-half results reflected the first effects of the financial turmoil. As a consequence, insurance companies' overall investment performance weakened against previous years. A survey conducted by the FMA showed that Austrian insurance companies' investment in U.S. subprime securities were negligible. Some insurance companies continued to profit from their expansion to CESEE countries.

The development of Austrian mutual funds was subdued in 2007. While assets under management increased slightly in the first half of the reporting year owing to valuation gains, they posted a decline in the second half because of higher outflows and lower valuation gains in the wake of the financial market turbulence. At end-2007, assets under management by Austrian mutual funds came to EUR 165.6 billion, down 1.9% year on year. With a 40% share of equities in their asset portfolios, Austrian pension funds also felt the impact of the stock market turmoil. In the first three quarters of 2007, the 13 Austrian occupational pension funds and the 6 industry-wide pension funds generated a capital-weighted return of 3%, against an average of 7.3% per annum in the comparable periods from 2004 to 2006.

After recording new all-time highs repeatedly until mid-July 2007, the Austrian stock market suffered considerable setbacks in the second half of the year. Still, the ATX[5] of Wiener Börse AG closed the year with a slight rise by 1.1%, standing at 4,513 points at year-end. In July 2007, shortly before the impact of the U.S. subprime crisis started to spill over to the Austrian stock market, the ATX had, for the first time, surpassed the 5,000 point threshold. In the first months of 2008, the decline in Austrian stock prices continued in lockstep with developments in international stock markets. Despite recent price losses, the longer-term development of the Austrian stock market proves to be clearly positive. From end-2002 to end-2007, the ATX went up by close to 300%. The market capitalization of domestic stocks amounted to more than 58% of GDP at end-2007 – up 44 percentage points compared with the previous five years. Listed companies took advantage of the favorable financing conditions particularly in the first half of the reporting year, issuing stock worth more than EUR 12 billion by way of capital increases and new issues in 2007.

[5] *The Austrian Traded Index (ATX) comprises the 20 most liquid and most highly capitalized stocks of the prime market segment at Wiener Börse.*

Favorable IMF Assessment of Austrian Financial Market

Under the Financial Sector Assessment Program (FSAP), which the IMF applies to member countries around the globe, the regular review of the Austrian financial market took place at the end of 2007. This exercise was an update of the initial assessment program the IMF had carried out in Austria in 2003; based on an analysis of strengths and weaknesses, it mainly serves to illustrate the priorities to be set for the further development of the financial system. In the run-up to the on-site mission performed by the team of IMF examiners from the end of November to the beginning of December 2007, the Austrian Federal Ministry of Finance, the FMA and the OeNB had prepared comprehensive data sets, answered detailed questionnaires, performed self-assessments according to international standards and compiled information on the Austrian financial market. Moreover, the IMF assessment also relied on a number of stress tests based on complex scenarios; for the first time, large Austrian banks participated in these stress tests.

The IMF's preliminary FSAP results signal a renewed positive assessment of the Austrian financial system. In particular, the IMF pointed to the continued further strengthening of the Austrian financial system and acknowledged its shock resilience. Moreover, the IMF stated that Austria had been agile in seizing the opportunities resulting from the opening-up of CESEE markets, which are now paying off in terms of earnings and an improved risk diversification. Given their sound holdings of deposits and their "originate and hold" strategy[6], Austrian banks had been relatively less affected by the recent financial turmoil. At the same time, the IMF pointed out that the risks arising from CESEE business needed to be monitored closely. In this respect, the IMF once again highlighted the importance of international cooperation among supervisory authorities, stressing that cooperation should be further strengthened.

Austrian financial system further strengthened

While the IMF recognized further improvements in the regulatory and supervisory framework, which had already conformed to a high standard, it pointed out that, nevertheless, there was still room for improvement in some areas. Thus, the IMF recommended that Austria further strengthen corporate governance principles, limit its extensive official liability provisions, and that it clearly define the responsibilities of external auditors and further promote their independence. In general, the IMF also demanded higher staffing levels in supervision, the further extension of on-site inspections of financial institutions, the performance of cross-border simulation exercises and of intensive stress tests also with insurance companies and pension funds. As the last few years have seen the implementation of extremely complex new regulatory provisions such as Basel II or the Markets in Financial Instruments Directive (MiFID) by the 2007 Austrian Securities Supervision Act[7] and a reform of financial market supervision, the IMF also deemed appropriate a longer period of consolidation of the supervisory and regulatory framework. The final results of the FSAP are likely

[6] *This strategy implies that after originating a loan, banks continue to hold it in their balance sheets. Banks applying this strategy usually focus on retail business. By contrast, banks applying the "originate to distribute" business model sell loans after they have been originated.*

[7] *Federal Law Gazette I No. 60/2007.*

to be available in the second quarter of 2008.

In March 2008, the IMF carried out its annual Article IV consultation in Austria. The Article IV consultation took into account the preliminary results of the FSAP update as well as current developments since the beginning of 2008 and reconfirmed the robustness of the Austrian financial system. With regard to the regulatory and supervisory framework, the IMF again pointed out the need for close cooperation between the FMA and the OeNB. Moreover, the IMF stressed that while Austrian financial institutions' expansion to CESEE had brought higher profits, it also entailed potential risks.

Reform of Austrian Financial Market Supervision

From an organizational point of view, the reform of the Austrian financial market supervisory system enacted in 2007 retained the dual system, with the FMA and the OeNB sharing tasks and responsibilities; the reform did, however, strengthen the OeNB's role in banking supervision, thus entailing a new type of cooperation.

Formally, the reform process was initiated by the new government program presented at the beginning of 2007. The new program announced an evaluation of financial market supervision and its subsequent reorganization to make it more effective and efficient and to eliminate areas in which responsibilities are ambiguous, overlapping or duplicative. The government bill presented at the beginning of November 2007 took into account the suggestions put forward in the report[8] by the Austrian Court of Audit, published in mid-2007, on the audit of the FMA and the supervisory functions of the OeNB and the Federal Ministry of Finance as well as the findings of the parliamentary inquiry commission regarding financial market supervision. The bill was adopted by the legislative authorities in December 2007 and entered into force on January 1, 2008.[9]

Joint OeNB and FMA project ensures smooth implementation of institutional reforms

Together with the FMA, the OeNB initiated a comprehensive project aimed at the best possible implementation of the institutional reform. This initiative ensured, in particular, that – despite the short run-up period – the two institutions have been able to perform their tasks and responsibilities under the new regime since January 1, 2008.

Altogether, the reform yielded positive results for the OeNB, but above all for the Austrian financial market, as it solved a number of interface issues, eliminated ambiguities, overlaps and duplications and as it allows for a combination of micro- and macroprudential analysis that is in line with international best practice. Consequently, the new organizational setup should ensure that, based on the FMA's and the OeNB's joint responsibility, the supervisory process is effective and efficient.

Moreover, in addition to the changes implemented in the field of banking supervision and considering first lessons from the U.S. subprime crisis, it is crucial for the success of the reform that it is underpinned by the explicit establishment of the OeNB's financial stability mandate in Article 44b of the Federal Act on the Oesterreichische Nationalbank (Nationalbank Act). Accordingly, the OeNB shall, in the public

8 *Austrian Court of Audit. 2007. Finanzmarktaufsichtsbehörde und Aufsichtsagenden der Oesterreichischen Nationalbank und des BMF. In: Reihe Bund 2007/10. 57–134.*

9 *Federal Law Gazette I No. 108/2007.*

Box 8

Allocation of Banking Supervisory Responsibilities between the FMA and the OeNB

- *The FMA retains its status as an independent and autonomous integrated financial supervisor and remains the supervisory authority in the field of banking supervision.*
- *The OeNB is responsible for all on-site inspections. As a basis for these inspections, the FMA and the OeNB define an inspection program stating the priorities of the on-site inspections for each institution and the respective starting dates. In principle, the FMA continues to issue inspection mandates to the OeNB; the OeNB, however, is entitled or even obliged to request the FMA to extend ongoing inspections or initiate inspections not envisaged in the inspection program if necessary. The FMA must decide upon such requests by the OeNB without delay, at the latest, however, within a week. Moreover, the OeNB may now carry out on-site inspections on its own initiative, i.e. without an inspection mandate of the FMA, if "macroeconomic reasons" warrant such inspection (e.g. the inspection of systemically relevant institutions).*
- *The OeNB is responsible for all off-site analyses of banks. In line with this responsibility, the OeNB is obliged to make all analysis results and any relevant information available to the FMA and to inform the FMA without delay if there is a substantial change in the risk situation or if there is reason to suspect a breach of supervisory regulations; moreover, the OeNB must carry out specific off-site analyses or produce further explanations of analysis results on request by the FMA.*
- *The OeNB operates a joint database with the FMA, which is intended to form the basis for off-site examinations. Various reporting data, relevant information resulting from the FMA's supervisory activities as well as data and results of OeNB examinations must be entered into this database. Aside from raising efficiency, the joint database is supposed to ensure, in particular, a common level of up-to-date information, which is indispensable for the smooth functioning of the interface between surveillance and analysis on the one hand and official decisions on the other.*
- *The FMA must, to the greatest possible extent, rely on the OeNB's surveillance, opinions and analyses and on the data available from the joint database. Unless it has reasons for justified doubts, the FMA may rely on the correctness or completeness of these data.*
- *The OeNB will also act as an expert authority in approval procedures for the advanced approach to operational risk measurement and is now in charge of approval procedures for all supervisory models. Moreover, the OeNB has been given additional rights to be heard before credit institutions are granted approval to merge or split.*
- *Finally, the new allocation of responsibilities also applies to the relationship with third parties: The adoption of memorandums of understanding – which under Austrian constitutional law is the responsibility of the Federal Minister of Finance – will be based on a joint proposal by the FMA and the OeNB.*

interest, monitor all circumstances that may affect the maintenance of financial stability in Austria. To be able to perform this task, the OeNB's data access rights have been extended. In the future, the OeNB will not only be able to produce macroeconomic analyses of the supervisory data entered in the joint OeNB/FMA database, but will have the right to access analytically relevant data on other financial intermediaries (in particular insurance companies and pension funds). These enhanced competences entail the obligation that the OeNB inform the Federal Ministry of Finance and the FMA of any findings of a principal nature or of particular importance to financial stability. Upon request, the OeNB must produce the necessary technical explanations, make documents available and deliver opinions.

Basel II Increases OeNB Examination Activities and Triggers Changes in Reporting

The new regulatory capital requirements for credit institutions (Basel II) entered into force on January 1, 2007. By monitoring the implementation of Basel II, the OeNB made an important contribution to ensuring the stability of the Austrian financial market in 2007. The Basel II framework leaves it up to banks whether they wish to base their credit risk assessment on simple procedures or advanced procedures, such as the internal ratings-based (IRB) approach. Credit institutions that opt for the advanced IRB approach to calculate capital requirements must prove that

Box 9

Organization of Banking Supervision in Europe

Across EU Member States, a number of different models are in place for banking and prudential supervision. Basically, these supervisory models can be categorized as sectoral (i.e. individual supervisory authorities exist for each financial services sector), functional (i.e. one authority is in charge of prudential supervision and a second authority is responsible for so-called conduct-of-business supervision) or integrated (i.e. a single supervisory authority is in place). Despite the generally acknowledged principle that there is no "one-size-fits-all" supervisory system and that every country must define the supervisory structure that best reflects its legal framework, traditions and national characteristics, certain common tendencies appeared at the EU level during the reforms of the past few years,[1] namely

- *a trend toward reducing (consolidating) the number of national supervisory authorities;*
- *the close – and recently further intensified – integration of central banks into prudential oversight even in cases where central banks are not directly responsible for supervision; and*
- *the increasing tendency to formalize the cooperation between central banks and supervisory authorities.*

In 24 of the 27 current EU Member States, the respective NCB is involved in banking supervision in one way or the other. In as many as 14 Member States, the NCB is the authority in charge of banking supervision or is entrusted, by law, with performing supervisory tasks. The following table provides an overview of models of banking supervision across the EU:

Models of Banking Supervision in the EU

Sectoral model[1]	Functional model[2]	Integrated model[3]	Central bank is in charge of banking supervision/assumes supervisory tasks[4]
BG, GR, ES, FR[5], CY, LT, LU, PT[5], RO, SI, FI	FR, IT, NL, PT	BE, CZ, DK, DE, EE, IE, LV, HU, MT, AT, PL, SK, SE, UK	BG, CZ, DE, GR, ES, IT, CY, LT, NL, AT, PT, RO, SI, SK

Source: ECB.

[1] An individual supervisory authority exists for each financial services sector (typically banks, insurance companies, securities sector).
[2] The regulation of supervisory responsibilities is based on the supervisory objectives for individual sectors (Twin Peaks model), i.e. different agencies are in charge of prudential supervision on the one hand and conduct-of-business supervision (e.g. compliance with transparency regulations and disclosure requirements, good conduct of business etc.) on the other.
[3] A single supervisory agency is in charge of supervising the entire financial sector.
[4] Like Austria, Germany has an independent single supervisory agency (Bundesanstalt für Finanzdienstleistungsaufsicht), which is the authority in charge of banking supervision, while the Deutsche Bundesbank has been assigned the task of regular prudential supervision. In Estonia, Ireland and Finland, banking supervision is in the hands of independent institutions that form an organizational unit with the respective central bank.
[5] The French and Portuguese systems combine the sectoral and functional models.

[1] See ECB, Recent developments in supervisory structures in EU and acceding countries, October 2006.

the models they apply to assess borrowers' creditworthiness meet comprehensive quality and quantity requirements.

On behalf of the FMA, the OeNB assesses the fulfillment of these requirements. Based on the OeNB's assessment, the FMA decides whether the respective bank meets the legal requirements and may apply the IRB approach. In cooperation with the FMA and often also with foreign supervisory authorities, the OeNB has – for several years – supported Austrian banks in the implementation of the IRB approach. While initial consultations were nonbinding, since mid-2006 the OeNB has been preparing opinions on the development and application of the respective models on a regular basis. These opinions sometimes require extensive on-site inspections.

In connection with Basel II, a risk-oriented reporting system was introduced on January 1, 2007, marking the most profound change in Austrian supervisory reporting since the reporting system was first introduced. The new system has been designed to account, above all, for the new framework conditions in place for the domestic banking industry. This implies that now there is a stronger focus on the compilation of data from banking groups and foreign subsidiaries as well as of detailed risk information. In line with the new reporting structure, reporting agents started to submit reports of condition and income and later reports on compliance with regulatory standards in 2007. Reports of condition and income are prepared according to the scope of consolidation; preliminary balance sheets, income statements as well as information on credit, equity, interest rate, country and exchange rate risk are compiled at quarterly intervals. The report on compliance with regulatory standards serves to monitor whether credit institutions fulfill the regulatory standards laid down in the Austrian Banking Act. It contains data on compliance with Basel II minimum capital requirements, on own funds, liquidity, large exposures and participating interests in nonfinancial institutions. Data are collected at monthly and quarterly intervals both at the individual bank level and at the consolidated level for groups of credit institutions according to Article 30 Banking Act. The additional data made available by the new reporting system allow for the further development of off-site analysis.

Risk-oriented reporting by banks allows for fine-tuning of analyses

Basel II also triggered the redesign of reports to the Central Credit Register. Following extensive negotiations with the reporting credit and financial institutions and insurance corporations, different sets of requirements were defined for different groups of reporting agents. This endeavor aimed at making reporting less burdensome by taking full advantage of electronic technologies while at the same time extending data availability in the course of reporting loan data to the OeNB. Another objective was to find a way of providing supervisors with the best possible access to the wealth of data on the risk situation of credit exposures that has become available since the beginning of 2008. In 2007, the OeNB chaired a European expert group on credit registers and was thus able to set the course for the further development of data exchanges at a European level.

OeNB Closely Involved in International and EU-Wide Supervisory Activities

Cooperation with other European central banks and with banking supervisory authorities continued to be a key element of OeNB activities in 2007. On the one hand, the OeNB's bilateral contacts are gaining importance against the backdrop of Austrian banks' expanding cross-border business activities. Upon the OeNB's initiative, therefore, the cooperation with the NCBs of the neighbor countries east of Austria has recently been further strengthened.

International cooperation further enhanced

On the other hand, the multilateral cooperation of central banks and banking supervisory authorities at the international and at the European level has been firmly established and enhanced over the last few years. At the ESCB level, a prominent forum of cooperation is the Banking Supervision Committee (BSC), which provides a regular platform for the discussion of current financial stability issues of European relevance. The OeNB is actively involved in the activities of the BSC and its working groups. Until end-2007, for example, the OeNB chaired the BSC Working Group on Developments in Banking, and recently it assumed the chair of the newly established Task Force on Liquidity Stress Testing and Contingency Funding Plans. Moreover, the OeNB played a leading role in the joint workshop of the IMF and the BSC Working Group on Macro-Prudential Analysis, which was held in Vienna at the end of January 2008 to discuss the rapid credit growth in Central and Eastern Europe.

In addition, the OeNB also actively contributed to the work of the Committee of European Banking Supervisors (CEBS), which advises the European Commission on banking supervisory issues and aims, in particular, at promoting the convergence of supervisory practices as well as the close cooperation of EU supervisory agencies. While over the last few years, activities concentrated above all on drawing up guidelines on various Basel II-related topics, practical issues of Basel II implementation were the major focus in 2007. Selected banks involved in cross-border activities served as a basis for identifying relevant issues that were then discussed within so-called Operational Networks to find common solutions. Together with supplementary measures, such as joint training courses and exchange programs for the staff of the national authorities involved, these efforts should help develop a common European supervisory structure. To further enhance the regulatory framework, CEBS also initiated a public consultation procedure on hybrid capital[10] and large exposures, the results of which are likely to be taken into account in the amendment to the Capital Requirements Directive scheduled for the fall of 2008.

The general functioning of CEBS and of the Lamfalussy regulatory process, respectively, underwent a comprehensive review in 2007, with review results being incorporated in the provisional version of the results of the Ecofin Council of December 2007. In their conclusions, the EU economic and finance ministers stated that overall, experience to date with the Lamfalussy framework had been positive, as the Lamfalussy framework had significantly increased the efficiency and effectiveness of the European regulatory and supervisory framework as well as the quality of the legislative process in accordance with the "better regulation" goals. Improvements were made in particular regarding consultation, transparency and impact analysis. At the same time, the Ecofin Council identified a number of areas at all four Lamfalussy Levels that showed potential for

[10] *Hybrid capital exhibits characteristics of both debt and equity.*

improvement and laid down a detailed schedule for the implementation of these improvements. Not least against the background of the experience of implementing Basel II and the MiFID, legislators should, for example, set realistic transposition and implementation deadlines and limit the number of options and discretions. Moreover, Member States were invited to "timely implement all remaining FSAP and related measures." In general, conclusions focused on supervisory cooperation stating, for instance, that the role of Level 3 committees[11] should be further clarified, their working should be further strengthened and that qualified majority voting should be introduced. Other measures include, inter alia, the removal of existing barriers to the exchange of information, the extension of possibilities for the voluntary delegation of tasks and the enhancement of cross-border supervisory cooperation. Additionally, the Ecofin Council agreed that its informal meeting scheduled for April 2008 should deal with these issues from a longer-term perspective.

In October 2007, moreover, the Ecofin Council adopted specific conclusions on the topic of financial stability. These conclusions comprised concrete measures to enhance safeguarding mechanisms for cross-border financial stability within the EU, such as e.g. the use of a common analytical framework developed within the ESCB to assess the systemic implications of potential crises.

The OeNB's Activities to Maintain Financial Stability

Under its stability mandate, the OeNB continually monitors all developments that are of importance for maintaining financial stability in Austria. These monitoring activities comprise the regular analysis of financial sector changes and developments as well as of potential, particularly systemic, risks which may arise e.g. from macroeconomic shocks. The regular observation of changes and developments in international financial markets focuses, inter alia, on the growing complexity of financial products and on new risk transfer mechanisms. To obtain a comprehensive picture, the OeNB needs to closely monitor especially the activities of Austrian financial intermediaries in CESEE. The aim of the OeNB's analyses is to identify unfavorable developments at the earliest possible stage so as to correct them in a timely fashion and to take preventive measures if necessary.

Stepped-up information exchange with Austrian banks

In exercising its mandate, in 2007 the OeNB's cooperation with the FMA included conducting surveys on Austrian banks' foreign currency loan volume in CESEE as well as on their exposure to hedge funds. Since the beginning of the financial turmoil in August 2007, the OeNB has enhanced its exchange of information with Austrian banks to be able to adequately analyze relevant market developments and banks' risks in the face of these developments. The results of the OeNB's analyses are discussed on a regular basis with supervisory authorities and financial intermediaries and are published semiannually in the OeNB's Financial Stability Report.

With the publication of the Guidelines on Managing Interest Rate Risk in the Banking Book, the OeNB and FMA added to their series of guidelines on Basel II. Given the changes in their overall environment, all banks need to

[11] *In the area of banking, CEBS is the relevant Level 3 committee.*

introduce effective systems to contain and manage interest rate risk to operate efficiently. The Guidelines on Managing Interest Rate Risk in the Banking Book are to assist banks in designing the strategies and procedures required to identify, manage and monitor interest rate risk.

Because there are so many banks in Austria, off-site analysis plays a particularly important role in banking supervision. Analytical tools have been completely revised and modernized over the last few years and continue to reflect state-of-the-art research. New analytical methods are regularly taken on board wherever feasible. In 2007, for example, the analytical model for the new supervisory reporting system was adapted; moreover, an improved methodology was put in place with regard to the aggregation of a wide variety of analytical results to arrive at an overall assessment of banks under examination. The ongoing improvement of the analytical framework aims at the early and reliable identification of potential problems in banking in order to be able to address such problems in an adequate and timely manner.

Stress tests constitute an important analytical tool

During the last few years, stress tests have become increasingly important in assessing the banking and financial system's resilience to shocks. Stress tests aim to capture, in a quantitative manner, the impact of hypothetical crisis scenarios on the banking system. Typical crisis scenarios observed in a stress test situation are sudden drops in stock market prices, massive interest rate fluctuations or exchange rate shocks on the one hand and macroeconomic crisis scenarios, such as recessions, with negative consequences for the borrowers' creditworthiness on the other.

Since the year 2000, the OeNB has designed a number of stress tests for credit, market and liquidity risk as well as for contagion risk in the interbank market; these tests were further enhanced during the first FSAP the IMF performed in Austria in 2003. The results of these stress tests have since been published on a regular basis in the OeNB's Financial Stability Report. Over the last few years, the OeNB developed a number of stress tests specifically for Austrian banks' activities in the CESEE countries.

In the course of the most recent update of the Austrian FSAP at the end of 2007, the existing models were substantially enhanced. Two macroeconomic crisis scenarios were developed on the basis of macroeconomic models. One scenario assumed a confidence shock hitting markets in CESEE and aimed to assess the impact on the exposure of Austrian banks in this region, while the other assumed a global economic downturn and focused on the domestic credit portfolio. For the first time, stress tests were carried out in cooperation with the six largest Austrian banks. The idea behind this joint exercise was to assess, on the basis of their internal risk management systems, the impact of these crisis scenarios. The results confirmed those of earlier stress tests according to which Austria's large banks have a high resilience to shocks.

Thanks to its wide range of research activities in the field of stress testing, the OeNB enjoys a high reputation among central banks, as reflected by numerous invitations to relevant international conferences, information visits from other central banks and cooperation activities in this area (e.g. with the Bank of England). On several occasions, the OeNB has received requests from the IMF to make available its stress testing expertise for FSAPs in other countries as well as for related technical support for other central banks.

Payment systems oversight evolves further

In 2007, the OeNB continued to fulfill its mandate for payment systems oversight, laid down in Article 44a of the Nationalbank Act, by continually monitoring the systemic safety of multilateral payment systems operating in Austria as well as the secure participation of Austrian banks in international payment systems. Overall, the degree of systemic stability was high in 2007, as confirmed by regular analyses of payment systems statistics and a number of individual examinations based on the OeNB's oversight principles. The latter contain the OeNB's requirements for ensuring systemic safety, which were extended in 2007 with regard to organizational and technical system security in the area of e-money schemes to include the requirements laid down in the Report on Electronic Money System Security Objectives According to the Common Criteria Methodology (EMSSO) and integrated in ongoing oversight processes. Moreover, the OeNB carried out a stock-taking exercise of the structural and operational issues of the relevant Austrian securities clearing and settlement systems. In its examination activities, in 2007 the OeNB continued to rely on the support of A-SIT (Zentrum für sichere Informationstechnologie – Austria), which has been accredited as an oversight office.

Most Austrian payment systems again reported a substantial increase in transaction numbers and volumes in 2007. As in previous years, the bulk of transactions was settled via direct debit payment systems, while the OeNB-operated large value payment system ARTIS/TARGET (and the next system generation, HOAM.AT/TARGET2) led the field in terms of transaction volumes. All in all, developments in this market were very dynamic, as reflected in the inclusion of six new reporting entities in payment systems statistics (see chapter entitled "Major Operational Role for the OeNB in the Creation of the Single Euro Payments Area").

In view of its financial stability mandate and of current EU and Eurosystem initiatives, the OeNB placed increasing emphasis on ensuring business continuity. With the aim of safeguarding the stability of the Austrian financial system in the best possible way even if critical infrastructures and/or market participants fail, the OeNB initiated a stock-taking exercise on existing business continuity arrangements in 2007, which is to serve as the basis for further activities in this area.

Together with A-SIT, the OeNB took steps to enhance security in electronic banking in 2007. Secure procedures for end-users (digital signature or special TAN[12] generators) are designed to link authorization and transaction data; they should be based on two independent security factors – "knowledge" (e.g. of a PIN[13]) and "possession" (e.g. of a signature card). To ensure that public confidence in these systems and in electronic payment media in general remains high, banks have to continuously keep the security procedures they use in their e-banking systems at a state-of-the-art level, and customers have to increasingly use these updated procedures in their payment transactions.

The OeNB also contributed to completing the development of a uniform Eurosystem-wide oversight regime for card payment schemes, which is espe-

[12] *TAN: Transaction number.*

[13] *PIN: Personal identification number.*

cially important considering the high significance of card payments and of the future role assigned to them within the Single Euro Payments Area (SEPA). Since the beginning of 2008, the "Oversight Framework for Card Payment Schemes" report – which was adopted by the Governing Council of the ECB in the fall of 2007 following a public consultation with market participants running for several months – has provided the basis for the cooperative oversight of card payment schemes that operate in a cross-border environment.

OeNB Reserve Management Performs Well despite Adverse Market Conditions

Volatile Markets as a Challenge for the OeNB's Treasury

World financial markets were plunged into turmoil in 2007. Following a succession of boom years, with the robust expansion continuing into the first half of 2007 apart from smaller corrections, spillovers from the *subprime crisis* in the United States built up to a full-fledged confidence and liquidity crisis in the summer and then affected the entire international financial system (see box 1). The crisis sent investors scrambling for safe havens in the hope of protecting their assets against losses and with a view to shifting their assets into liquid holdings. Taking swift and resolved action, the major central banks worldwide were, however, able to safeguard the stability of the financial system.

U.S. subprime crisis spills over to international financial markets – central banks highly active in managing the crisis

Among other things, the financial turmoil seriously affected foreign exchange markets. Throughout 2007, the U.S. dollar weakened further against other major currencies, a trend that had been observed since the spring of 2002 with a short interruption in 2005. The exchange rate of the U.S. dollar against the euro worsened from USD 1.32 per euro to USD 1.47 per euro until the end of December 2007, which corresponds to a loss in value of about 10%. Much of this slippage occurred after the emergence of the U.S. subprime crisis in August 2007. While the U.S. dollar remains by far the most important international currency in terms of trade volumes, its significance would appear to have declined considerably in the course of 2007, mirroring developments in recent years.[1]

Prolonged depreciation of U.S. dollar continues

In the first few months of 2008, the U.S. dollar continued to depreciate against the euro. The exchange rate passed the threshold of USD 1.50 per euro on February 27, 2008, and reached a historic peak of somewhat over USD 1.59 per euro on April 23, 2008.

Unlike the U.S. dollar, the Japanese yen deviated from its path of previous years in 2007. In relation to the euro, the yen departed from the downtrend observed since early 2000 and started to move sideways amid high volatility. The exchange rate fluctuated between JPY 168.80 and JPY 151.23 per euro, i.e. within a fluctuation margin of up to ±10% at times. The break in the previous trend is likely to reflect the fact that market agents were unwinding *carry trades* (see glossary) more readily against the backdrop of the changed market conditions, i.e. the considerably higher volatility in financial and foreign exchange markets. The rising risk aversion and volatility in financial markets is likely to have prevented carry traders increasingly from speculating that the interest rate differential between the low-yield yen (i.e. the financing currency) and other high-yield currencies (i.e. the investment currencies, such as the Australian dollar or the New Zealand dollar) would *not* be compensated by exchange rate movements. Consequently, demand for refinancing in Japanese yen was much lower than in previous years.

Higher risk aversion causes investors to unwind yen-based carry trades

One of the most significant consequences of the U.S. subprime crisis in the summer of 2007 was the flight of

[1] *See the Triennial Central Bank Survey "Foreign exchange and derivatives market activity in 2007" of the Bank for International Settlements of December 2007 (above all the table on page 11).*

Investors turn to government bonds as a safe haven

investors out of risk-laden asset categories. *Government bonds* were the biggest winners of this sudden urge for safe havens. While the yields of long-term government bonds had trended strongly upward up to June 13, 2007, amid the as yet rosier economic outlook for the U.S.A. (with ten-year U.S. government bonds rising by 65 basis points to 5.30% since the beginning of the year, and corresponding euro area bonds by 70 basis points to 4.70%), a massive trend reversal materialized in the summer and affected virtually all big government bond markets. Until year-end, the yields of ten-year U.S. government bonds dropped to 4.07%, and the yields of corresponding euro area bonds to 4.34%. Given a broad-based revaluation of corporate bonds from the summer of 2007 onward, the yield spread vis-à-vis government bonds widened considerably in some cases during that period.

Yield gap between corporate bonds and government bonds widens considerably in some cases

The yield decline continued into the first months of 2008, interrupted only briefly by a few weeks of consolidation. The yields of ten-year U.S. government bonds temporarily dropped below the threshold of 3.30%, with those of corresponding euro area bonds declining below 3.70%. From mid-March 2008 onward, we have seen a rebound of yields, reflecting above all higher inflation expectations. Until the end of April, 2008, the yields of ten-year government bonds rose to 3.87%, and the yields of ten-year euro area bonds to 4.18%.

Massive stock price setbacks, above all in the banking sector

Stock markets reacted very differently to the market for government bonds. As the turmoil on money and credit markets was rising, the withdrawal of investors from risky assets hit stock markets particularly hard. Measured in terms of the MSCI World Index,[2] global stock market prices dropped by a total of 6% in two stages from June 2007 until year-end, thus in fact only partly reversing the price gains by about 23% per annum earned since March 2003. Broken down by sectors, the pressure became especially high for bank shares, given the need for substantial writedowns: The MSCI World Finance Index dropped by approximately 18% from the summer of 2007 until the end of the year.

In the first months of 2008 the massive stock price setbacks accelerated further: The MSCI World Index dropped by another 16% until mid-March 2008, the MSCI World Finance Index even by about 19%. Thereafter, stock prices newly recovered somewhat, with the MSCI World Index rising by 11% until the end of April 2008 and the MSCI World Finance Index climbing by 18%.

The *stock markets of the emerging Asian economies*, which rallied much more strongly than the stock markets of industrialized countries – with the MSCI Asia Index jumping by 58% annually on average since 2003 (or even 147% per annum in the case of China) – were hit by the financial turbulences of summer 2007 with a time lag. Having soared by another 40% (80% in the case of China) from August 17 to October 29, 2007, the MSCI Asia Index dropped by about 8% (China: –18%) from November 2007 until year-end, and by another 18% (China: –32%) in the first few months of 2008. From mid-March to the end of April, 2008,

[2] *The MSCI World Index is calculated by Morgan Stanley Capital International (U.S.A.) and is one of the most important stock market indices worldwide. It contains stock prices from 24 countries and has been calculated since December 31, 1969 (base value: 100 points).*

the stock markets of emerging Asian economies rallied once more (Asia: +18%; of which China: +29%).

Volatility in international stock markets extraordinarily high

On balance, global stock market prices were subject to much higher *volatility* after the recent financial turmoil than in boom years preceding that period. These developments are particularly well reflected in the CBOE Volatility Index (VIX)[3] computed on the Standard & Poor's 500 index: While the VIX had been down to an average of around 14 in the period from early 2004 to the end of May 2007, it averaged around 21 from early June until the end of 2007. In August and in November 2007 as well as most recently in January and March 2008, the VIX reached peak values exceeding 30, dropping to slightly below 20 shortly before the time of writing.

Longer-term surge in gold prices accelerates …

The *gold price in U.S. dollars per ounce* has been on a pronounced upward trend for years. In September 1999, immediately after the first Central Bank Gold Agreement (see box 10) took effect and following a fairly long period of low prices, the price of gold jumped by around 25% in the course of just a few days. This surge may be seen as the first signal that the gold market was firming after a decade-long weakness. Since then, the price of gold in U.S. dollars per ounce has, on average, increased by more than 30% year by year. This development probably reflects the confluence of a number of factors, including central banks' deliberate limitation of sales of gold holdings, stagnating production, a general surge in commodity prices, the depreciation of the U.S. dollar and geopolitical risks. Last but not least, gold was particularly in demand above all in the past few months as a safe investment instrument, given that it is the only investment vehicle that comes without credit risks.

… with gold prices passing USD 1,000 threshold for the first time

In 2007, the price of gold trended sideward within a range of USD 610 and USD 690 per ounce until the end of August. During the growing financial turmoil, it jumped by around 24% to USD 836.50 per ounce from the beginning of September 2007 until the end of the year. Measured in euro, i.e. reflecting the depreciation of the U.S. dollar against the euro, the gold price increase was less pronounced with an annual increase of 16% to USD 568.24 EUR. The surge in gold prices continued in early 2008 up to March 17, 2008, exceeding the historical high of USD 840 observed in 1980 and even reaching levels considerably beyond the USD 1,000 threshold on March 17. In the subsequent days, however, heavy profit-taking sent the gold price plunging, and in the early days of April gold was again traded at levels of below USD 900 per ounce.

OeNB Portfolio Managers Highly Successful despite Adverse Market Conditions

Priority sequence for all OeNB investment subportfolios: (1) security, (2) liquidity and (3) returns

At the end of 2007, the OeNB's Treasury Department managed reserve assets and other assets worth around EUR 24 billion. The assets are invested in gold, foreign currency and euro portfolios – which form the monetary policy segment of investment – and a number of other subportfolios relating to the investment of own funds, pension reserve assets and reserve funds endowed for the National Foundation for Research, Technology and Development (National Foundation). Investment

[3] *CBOE: Chicago Board Options Exchange.*

Box 10

The Central Bank Gold Agreement

For historical reasons – particularly as a result of the gold standard, which prevailed until the first few decades of the 20th century, and also as a result of the Bretton Woods system, which was abandoned only at the beginning of the 1970s – central banks are among the major holders of gold worldwide even today. At the end of 2007 the IMF put central banks' official gold holdings at 29,873 tons – corresponding to 19% of global gold holdings and considerably exceeding the amount of gold mined worldwide in the course of ten years. The bulk of central banks' official gold holdings is in fact concentrated on just a few countries plus the IMF: ten central banks hold around 70% and the IMF another 10% of aggregate official gold reserves.

Unlike in the decades before the 1970s, when gold represented the central monetary anchor within the international monetary framework, gold has come to be only one of several assets in which central banks may invest. Since the de facto collapse of the Bretton Woods system, as a result of which central banks were much freer in managing their gold holdings, official gold sales thus draw particular attention among market participants. Given the marked share of official gold holdings in global gold holdings, the sale even of smaller shares of those holdings will have a considerable impact on the gold price.

Taking account of this fact, a number of (European) central banks – including the OeNB – have signed two Central Bank Gold Agreements since September 1999, committing themselves to selling no more than an agreed sum of gold each year and to making the supply side of the gold market more transparent; these measures have been designed to contribute to a stabilization of the gold market. The agreements introduced a joint annual sales limit of 400 tons for the period from 1999 to 2004, and of 500 tons for the period from 2005 to 2009. At the same time, the signatories decided not to expand other gold transactions, such as gold leasing. The number of signatory central banks has since risen from 14 to 17. On December 22, 2006, Banka Slovenije, Slovenia's central bank, adopted the Central Bank Gold Agreement. On January 25, 2008, the Central Bank of Cyprus and the Central Bank of Malta joined the agreement.

The Ten Countries Whose Central Banks Hold the Most Gold Worldwide

End-2007 levels

	tons
U.S.A.	8,134
Germany	3,417
France	2,603
Italy	2,452
Switzerland	1,145
Japan	765
Netherlands	621
China	600
Russia	450
Taiwan	423
IMF	*3,217*
ECB	*563*
Austria	*280*

Source: IMF, Gold Fields Mineral Services Ltd.

in the various subportfolios is subject to different objectives and rules. In a separate portfolio and in accordance with the decentralized reserve management approach of the ECB, the OeNB also manages its share of foreign reserve assets transferred to the ECB, whose euro equivalent is roughly EUR 1 billion.

Gold as key asset for portfolio diversification

In the OeNB's reserve management activities, gold plays a special role. At the end of 2007, the OeNB was holding around 280 tons of gold. The surge in gold prices and the concomitant depreciation of the U.S. dollar over the past few years have shown clearly how important gold is as an instrument for portfolio diversification for a central bank. Also in times of higher geopolitical tensions within and beyond Europe, investors must pay special attention to the special role of gold. In the third year of the current Central Bank Gold Agreement (effective from September 26, 2004, to September 26, 2009) the OeNB sold 8.75 tons of gold, compared with 13.75 tons in 2006 (see box 10).

Gold sales in the third year of the Second Central Bank Gold Agreement

The priority sequence governing the investment activities of the OeNB's Treasury Department – security, liquidity and returns – requires risk and portfolio managers to keep introducing innovations. Consequently, the two-level investment benchmark established a few years ago, which allows strategic and tactical investment decisions to be implemented efficiently and swiftly in line with hierarchical structures, was adjusted further in 2007.

OeNB portfolio managers apply sophisticated risk management methods

Apart from risk calculations, the OeNB's portfolio management is also guided by an integrated performance measurement system. This system provides for a timely tracking of the direct impact of individual portfolio decisions on the overall performance of the portfolio. A disciplined communication strategy helps to correct deviations from targets more rapidly, and to communicate investment ideas more easily. Weekly investment committee meetings of all parties involved in the investment process serve to analyze market and portfolio developments and risks. These analyses have helped achieve good results and contain risks even under adverse market conditions of heightened volatility and turbulences. The risk measurement methods applied at the OeNB were assessed in a comprehensive review in 2007 (see the Risk Management section in the chapter "Notes to the Financial Statements 2007").

OeNB acts highly professionally in investing reserve assets on behalf of the ECB

As in previous years, the OeNB was particularly successful in managing its share of the foreign reserve assets transferred to the ECB, which the OeNB invests on behalf and for the account of the ECB in accordance with rules established by the latter. Together with the central banks of Germany, France, the Netherlands, Finland and Portugal, the OeNB manages the ECB's yen portfolio, parts of which were assigned to the OeNB when the ECB adopted a currency specialization framework two years ago. A performance comparison of the respective portfolios for 2007 shows that the OeNB's investment activities were again conducted with exceptionally high professionalism.

The OeNB's Statistics – A Reliable Guide in Today's Globalized Economy

2007 Was an Eventful Year for the Statistics Providers of the OeNB

Providing financial statistics is a core competency of the OeNB

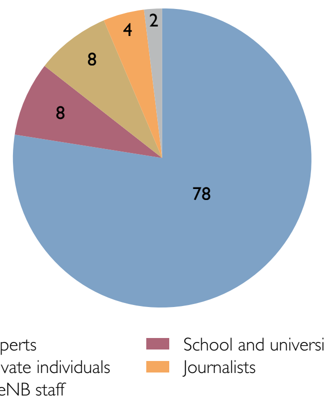
In 2007, the OeNB further expanded its position as Austria's key provider of financial statistics. The OeNB continued to enlarge and enhance its wide range of statistical products, which cover especially MFI balance sheet and interest rate statistics, supervisory and external statistics as well as financial accounts statistics. The OeNB's contributions to the new harmonized euro area statistics, which allow for a more comprehensive analysis of major economic trends in the single currency area, are a case in point. In addition to the above-mentioned data, the OeNB offers numerous other statistics, for instance statistics on consumer prices, interest rates, GDP, public finances and corporate balance sheets. The aim of the OeNB's online data set is to provide users with comprehensive, high-quality, thoroughly documented data as well as user-friendly interfaces. In 2007, Austrian and international users accessed this online data set, which comprises about 240 tables, more than three million times. Flexible search tools enable users to retrieve customized statistics for selected indicators and periods, which they can easily export into standard file formats. Moreover, users may direct statistics-related inquiries to the OeNB's statistics hotline at (+43-1) 40 420-5555 from 9 a.m. to 4 p.m. on all business days.

Diverse users groups – including commercial banks, insurance companies, other financial service providers, nonfinancial corporations, public institutions, students from schools and universities as well as interested individuals – call for customized products. The OeNB answers this demand by publishing detailed analyses, brief topical reports and special issues focusing on particular themes. Moreover, it organizes special events; in 2007, for instance, journalists had a chance to directly address the OeNB's statistics experts at five press conferences.

Chart 18

Customers of the OeNB's Statistics Hotline in 2007

Share of inquiries in %



Source: OeNB.

The OeNB cooperates with national and international statistical offices

Against the background of an increasingly globalized and constantly changing economic environment, the production of high-quality, timely statistical information requires efficient data collection systems and cooperation among domestic and international statistics offices. The OeNB's intensive cooperation with other central banks fosters a constant exchange of knowledge and thus also the development and advancement of internationally applicable statistical conventions and methodologies. At the national level, the OeNB cooperates above all with Statistics Austria to provide cost-efficiently produced data of a consistently high quality while at the same time keeping the reporting burden of respondents at a minimum. Since the existing statistics cooperation agreement concluded between the two institutions in 2002 worked out well, it was prolonged for another five years in 2007. Synergy effects arise notably for coproduced statistics such as the Austrian balance of payments and the financial accounts – with the key benefit that each institution focuses on its respective field of expertise, i.e. the OeNB on the financial sector and Statistics Austria on the real economy. In 2007, the OeNB also concluded a cooperation agreement with the Austrian Federal Economic Chamber formalizing the good cooperation of the past several years. Finally, the OeNB continuously seeks to keep in touch with economic research institutes, universities and other academic institutions so as to transfer its knowledge while at the same time benefiting from the state-of-the-art expertise of these institutions.

European Securities Database Takes Shape

Increasing demand for securities data

In response to the growing importance and diversity of investment in securities, analysts and policymakers have greatly stepped up their demand for high-quality and detailed securities data in recent years. To understand and appropriately react to economic processes, economic decision makers and individuals alike must make every effort to keep abreast of the current developments in the securities markets. Detailed and timely securities data provide important information about the development of corporate and household wealth. Such data play an essential role in banking supervision and help identify financial market turbulence in the making. Therefore, the further development of existing securities statistics will remain a top priority.

Against this background, as of 2009, the ECB will require all euro area countries to collect their cross-border portfolio investment data (as included in the balance of payments and in the international investment position) on a security-by-security (sec-by-sec) basis rather than in the current highly aggregated form. The ECB recommends sec-by-sec reporting also for the compilation of investment funds assets.

Centralized securities database offers decisive advantages

In a sec-by-sec reporting system, entities have to report the amount of the investment or liability as well as the securities identification number (usually the ISIN – International Securities Identification Number), whereas the central bank carries out the necessary classification and performs the additional calculations. Such systems are aimed at alleviating the reporting burden while at the same time improving quality and the central bank's flexibility in reacting to new demands. The OeNB successfully established such a reporting and data processing system already at the beginning of the 1990s and has been using an updated version since 2005. This system is used to produce or at least facilitate the production of almost all statistical data on securities. Consequently, the OeNB has also become an international pioneer in this field.

If a central bank is to carry out the required classifications (for example according to type of security, maturity, economic or business sector of the issuer, type of interest rate, etc.) and calculations, it needs to have a securities database which provides for the classification of incoming securities according to these requirements. To this end, the ESCB initiated the Centralised Securities Database (CSDB) project several years ago in order to

– avoid the establishment of a separate securities database by each central bank implementing such a reporting system, and

– achieve the greatest possible level of symmetry and consistency for the classification through a common securities database.

The CSDB is a centralized securities database which contains comprehensive information on all corporate securities issued in the EU and on all securities held by EU investors. CSDB data have been available to central banks since 2005. In 2009, when the second project phase is completed, both data quality and data exchanges should comply with advanced standards.

OeNB tests CSDB online access

By reason of its long-standing expertise, the OeNB, together with some other central banks, was asked in December 2007 to participate in the CSDB's pilot phase to test the online access functions (such as online modification features and a data quality management tool). This project phase is to terminate in mid-2008. From then on, central banks will be able to correct data directly in the CSDB, thus further improving data quality. Once this milestone has been reached, the automation of data exchanges will be the next step required to extend flexibility and consequently enhance both data quality and the convenience of the system.

The CSDB plays a pivotal role within the Directorate General Statistics of the ECB. In the medium term, the CSDB is likely to revolutionize the production of central banks' securities statistics. The ECB has already called upon the OeNB's expertise in this field on various occasions and welcomes the OeNB's engagement in the next project phase.

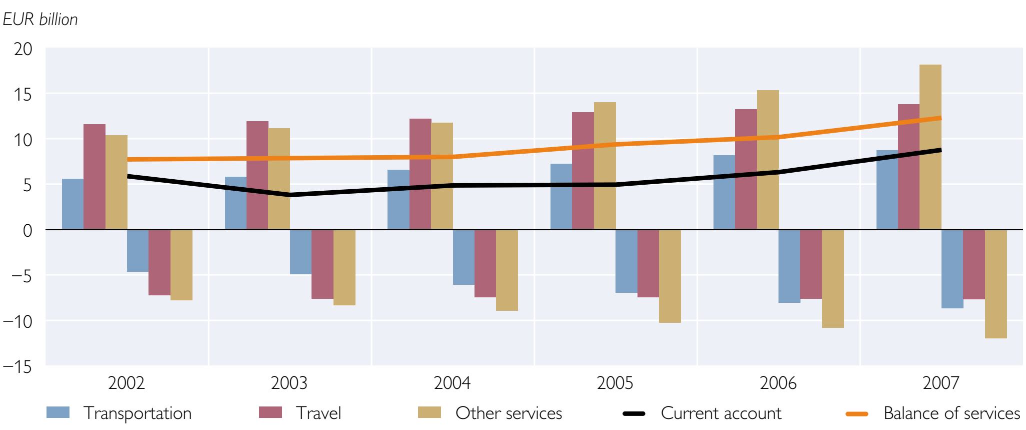
New Reporting System Enhances Services Statistics

Highly detailed services statistics for Austria

In 2006, the introduction of a direct reporting system for the Austrian balance of payments (for more details, see the OeNB's Annual Report 2006) constituted another important step toward enhancing the quality of Austria's external statistics. As a result, it is now possible to assign exports and imports of services much more precisely to the different service categories. Moreover, directly asking economic agents engaged in external transactions rather than relying on payment transactions data provides much more detailed information. On switching to the new system, the OeNB also implemented the Extended Balance of Payments Services classification (EBOPS), which

Chart 19

Austria's Services Exports (Positive) and Imports (Negative)



Source: OeNB.

was defined by the IMF and the OECD and contains some 50 standard components. Accordingly, the component "unclassified transactions" was removed from the Austrian balance of payments. Moreover, when it comes to specific questions, the new system facilitates a distinction between various economic service providers and users.

Yet, this change in the external statistics, which entailed the use of new methodologies, also led to a break in the data series. Therefore, the OeNB and Statistics Austria – with which the OeNB cooperates to compile the Austrian current account – have backcast the data series for the period from 1995 to 2006 based on the new statistical framework and in line with the system of national accounts. This enables interested users to access a consistent time series of Austria's external statistics classified according to individual countries and components.

The enhanced information on external transactions obtained through the direct reporting system led to retroactive adjustments of the annual results that boosted the surplus on services and consequently the current account surplus and that signaled a decline in trading volumes. Those readjustments basically reflect the elimination of the component "unclassified transactions" and the redesign of travel statistics. Other changes include a new concept for adjusting goods imports for service components (cif/fob adjustment[1]), a new concept for calculating insurance services based on the national accounts and the stricter classification of items such as financial services and lease financing to the current account or the financial account.

New structural information on cross-border services

Once the new system has been fully implemented, the OeNB and Statistics Austria envisage further measures to extend the information on Austrian trade in services. The direct reporting system, for example, allows for the connection of services exports and imports with business structure data. Combining the information from these statistics in Austria will provide insights into the export potential of Austrian service providers and the import intensity of the Austrian economy based on business indicators such as the number of employees, the industry, turnover and the business location. The results of such analyses will enable companies, policymakers and interest groups to design efficient export promotion strategies. Moreover, as the merging of these statistics closes the existing information gap regarding the analysis of the Austrian external sector, it is also significant for economists, universities and international organizations such as Eurostat, the ECB, the IMF, the OECD, the UN and WTO.

New data series for Austrian current account available

Statistics on Financial Assets and Liabilities of Households Markedly Enhanced[2]

In 2007, the scope of the OeNB's data series on financial assets and liabilities of households was significantly improved and changes were backcast until 1980. Therefore, it is now possible to contrast private consumption and savings with the financial behavior of households over several business cycles. In the period from 1980 to 2007, the financial assets of the household sector increased from 120% to 250% of the nominally disposable net income, while household liabilities rose from 61% to 87%. Hence,

Household sector data now available from 1980 onward

[1] *Cif: cost, insurance, freight; fob: free on board.*

[2] *For details on the calculation of the data, please refer to the special issue of Statistiken "Austrian Financial Accounts 2006. Analyses of Current Financial Accounts Data." Vienna: OeNB. 2007.*

the Austrian household sector's financial assets and liabilities were both below the euro area average in 2007 (325% and 109%, respectively).

Portfolio investment gains importance in the long run

What is striking – apart from the substantial increase in volume – is the fact that the structure of household investment has changed dramatically over the past 27 years: While at end-1980, short-term investment, such as bank deposits and cash holdings, predominated at 75% of financial assets, these categories made up less than 50% at end-2007. Conversely, long-term-oriented forms of investment have considerably gained in importance in this period. Debt securities, shares, limited liability company shares and notably mutual fund shares increased from 10% to almost one-third of total financial assets. Claims against insurance companies and, at a later stage, claims against both single-employer and multi-employer pension funds rose from 13% – a relatively high share in 1980 – to one-fifth of total financial assets.

Households tend to invest savings in financial assets

In line with cyclical developments, the saving ratio hovered between 7.3% and 13.7% in the period from 1980 to 2007. The high correlation between savings and financial asset accumulation during the entire observation period shows clearly that households have primarily invested in financial rather than nonfinancial assets. Thus, financial assets were far more volatile than new loans.[3] Despite the fact that both increased in boom periods, financial assets proved much more dynamic. The balancing item of financial investment minus loan financing averaged 7.5% of disposable income and 4.8% of gross value added from 1980 to 2007.

During the cyclical upswings in the early 1980s and around 1990, higher savings boosted financial investment. Yet, given the low supply and a succession of financial crises from 1987 until the mid-1990s, private investor demand focused on bank deposits and bank bonds at the time. The first substantial change in financial asset allocation took place in the second half of the 1990s. For the first time, financial flows reflected a substitution effect in portfolio decisions, thus highlighting the growing importance of capital market investment. The development of bank deposits and securities[4] turned out to be negatively correlated, which was also in line with the respective financial market trends. Following a period of stagnation between 2001 and 2003, the share of tradable securities in total financial investment rose to more than one-third between 2004 and 2006 as stock prices rallied. Moreover, the range of securities in which the household sector invested broadened.

Bank deposits benefit from recent setback in stock markets

In 2006 and 2007 respectively, financial investment as a share of disposable income was higher than the long-term average, which was partly due to increased private savings. Setbacks in stock markets together with the slowdown in bond markets in those years incited private investors to cut securities holdings and to return to bank deposits, a trend which was also spurred by rising interest rates. In 2007, investment in securities amounted to only 16% of total financial investment (2006: 32%). This development in Austria mirrors the trend in the euro area.

What is also new is the fact that financial assets and liabilities of house-

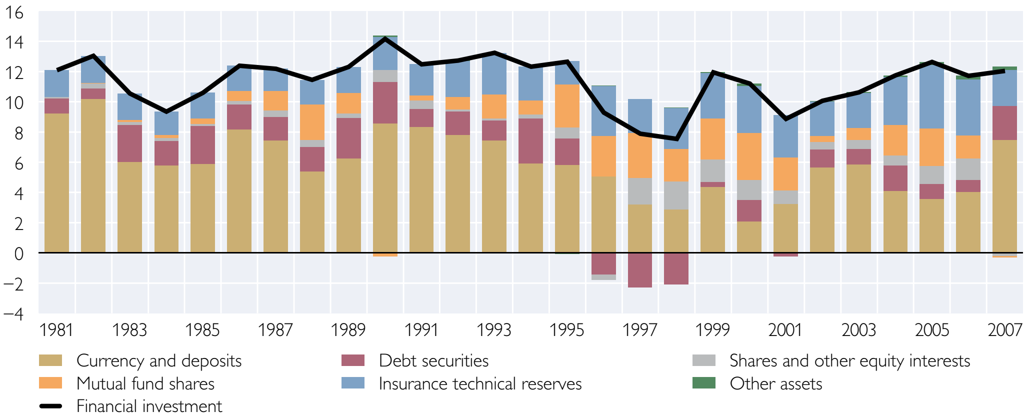
[3] *As a percentage of net disposable income, financial investment averaged 11.4%. The fluctuation band (standard deviation) was 1.6 percentage points. This compares with a debt ratio of 3.9% of disposable income and a fluctuation band of 0.8 percentage points.*

[4] *Debt securities, quoted shares and mutual fund shares.*

Chart 20

Financial Investment of the Household Sector

% of disposable income; share of individual financing instruments in percentage points



Source: OeNB, OeKB, Government Debt Committee, Statistics Austria, Wiener Börse AG.

holds and nonprofit institutions serving households (NPISH), which had both been subsumed under the aggregate "household sector," will be displayed separately from now on. The availability of data on households' financial wealth will make the connection between micro and macro data clearer. Aggregated financial accounts data, which are available quarterly with a lag of three months, can be used as a trend indicator for the financial behavior of households. Stock data, which are available for the reporting period starting with the first quarter 2006, show that households make up more than 90% of the household sector. The financial structure and behavior of households differ markedly from that of NPISH including private foundations, which is mainly attributable to the financial investments of private foundations. The most substantial differences relate to the investment in securities.

Household sector data further itemized

Major Operational Role for the OeNB in the Creation of the Single Euro Payments Area

In 2007, the creation of the Single Euro Payments Area (SEPA) was the key item on the OeNB's payment systems agenda. SEPA aims at providing secure, cost-efficient and swift payment processing in euro. In contributing to the realization of SEPA, the OeNB has performed an important operational function for several years, not only in the Austrian financial market but also at the international level.

SEPA Launched in January 2008

Since 1992, European citizens and enterprises have benefited from the single European market. The successful introduction of euro bank money in 1999 and of euro cash in 2002 marked the next milestones of European integration. The market for cashless retail payments remained fragmented across Europe, though – until SEPA went live in the 27 EU Member States, Iceland, Liechtenstein, Norway, and Switzerland on January 28, 2008. That day marked the beginning of a new era for credit transfers and card payments, following intensive preparations by all stakeholders. The launch of the third SEPA service – SEPA direct debits – was postponed until 2009, as the SEPA-wide use of this instrument is not possible before the implementation of a harmonized legal foundation in Europe, which was postponed owing to a delay in the adoption of the Payment Services Directive (see box 11).

SEPA Credit Transfer

SEPA Credit Transfer (SCT) is a payment instrument for the fully automated processing of domestic and cross-border transactions in euro without value limits. Since January 28, 2008, SCT has been available in the SEPA in addition to existing national solutions. Making transfers has thus become quicker and simpler, and there is no longer any distinction between domestic and cross-border euro transactions. SCT payment instructions are processed within a maximum of three banking days across SEPA. Within just the first few days after its introduction, the instrument was used to process, via the OeNB's STEP2 infrastructure, a daily average of up to 7,300 SEPA transfers with a total value of more than EUR 60 million.

SEPA Direct Debit

The new SEPA Direct Debit (SDD) is a harmonized service that is scheduled for SEPA-wide introduction in November 2009. Step by step, SDD will replace existing national solutions for direct debit and preauthorized transfer. All across Europe, customers will benefit from an eight-week refund period after the debit date (regardless of reason). At present, a six-week deadline applies to refund requests for preauthorized transfers in Austria. In the case of unauthorized collection or an invalid mandate, the refund period will be up to 13 months. Another new feature of SDD is that every direct debit must be provided with a due date, so that the payer is informed of the exact debit date.

Migration to SEPA card payments in Austria

In Austria, the migration to EMV-compliant[1] debit and credit cards was started as early as 2004 and has been completed for all card systems except Diners Club and American Express, which will make the required changes on time and in accordance with an international migration schedule. And steps have been taken to ensure that bank lobby ATMs will be SEPA com-

[1] *EMV stands for the three companies that developed the standard: Europay, MasterCard and VISA.*

pliant by 2010 as scheduled. POS terminals[2] have been replaced or will be upgraded with new software by 2010 at the latest.

SEPA standardization will increase competition in the card payment sector. In 2007, the Austrian card organizations Europay Austria Zahlungsverkehrssysteme GmbH and VISA-SERVICE Kreditkarten AG extended their product portfolios by VISA and MasterCard products, respectively, and changed their company names to PayLife Bank GmbH (PayLife) and card complete Service Bank AG (card complete). The ownership structures of PayLife and card complete are being reorganized after the European Commission had urged Austria to change them, maintaining that the current structures – several Austrian banks holding shares in both enterprises – might restrict competition.

The foundation of the Euro Alliance of Payment Schemes (EAPS) on November 7, 2007, was another result of the SEPA initiative in the field of card payments. This pan-European network, which is a Brussels-based alternative to VISA and MasterCard, currently consists of six national card schemes[3] offering more than 189,000 cash machines for some 222 million cards. Participation in EAPS is open to all payment schemes (in their capacity as issuers, acquirers, or both), provided that they comply with the relevant SEPA criteria and commit to the principle of mutual acceptance of all participating schemes.

The European System of Central Banks welcomes the creation of payment card systems[4] that serve as alternatives to international schemes such as VISA and MasterCard.

The OeNB's Key Contributions to the Smooth SEPA Launch

Since November 2003, the OeNB has provided banks with access to the pan-European clearing house STEP2, thus establishing itself early on as a competent and reliable partner for domestic banks in the increasingly integrated European payments market. The technical and economic benefits offered by OeNB's STEP2 access is evidenced by the broad range of its users – some 130 banks from 7 countries – for whom the OeNB processed an average of 26,000 transactions worth EUR 78.6 million a day in 2007.

The main reason for establishing the STEP2 service in 2003 in the first place was to facilitate the efficient and reliable processing of cross-border payments in euro as specified in Regulation (EC) 2560/2001.[5] Over the following years, the scope of the service was expanded to accommodate SEPA requirements. These developments led to the creation of the SCT, the first payment instrument that meets the relevant technical and business requirements. The OeNB enabled its STEP2 customers to use the SCT from its launch on January 25, 2008. The SCT marks a major milestone in achieving

[2] *POS: Point of Sale.*

[3] *Its members are CO.GE.BAN for PagoBANCOMAT and BANCOMAT (Italy), EPCS European Payment Card Solution GmbH for the electronic cash scheme and the German ATM scheme Deutsches Geldautomatensystem (Germany), the Brussels-based ATM scheme EUFISERV s.c.r.l. (Belgium), the card payment scheme EURO 6000 S.A. (Spain), the ATM network LINK Interchange Network Limited (U.K.), and SIBS – Sociedade Interbancária de Serviços S.A. for Multibanco (Portugal).*

[4] *A card payment scheme defines the technical, legal and commercial rules required for the settlement of transactions for a certain card brand (e.g. VISA, MasterCard etc.).*

[5] *Regulation (EC) No 2560/2001 of the European Parliament and of the Council of 19 December 2001 on cross-border payments in euro.*

Box 11

Directive on Payment Services in the Internal Market

Genesis of the Directive: *On December 1, 2005, the European Commission published the Proposal for a Directive on a New Legal Framework for Payments, which was later renamed the Payment Services Directive (PSD). This directive aims to establish a harmonized framework for an integrated payments market in the EU, thus removing legal barriers to the creation of the Single Euro Payments Area (SEPA) and replacing the different structures and rules on payments in each EU Member State. The final text of the directive was published in the Official Journal of the European Union on December 5, 2007,[1] after negotiations on the exact contents of the directive had been concluded. The Member States have committed to transposing the directive into national law by November 1, 2009, at the latest.*

Scope of the PSD: *The directive applies to payment services provided within the EU that are made in euro or in the currency of a Member State outside the euro area. The PSD introduces payment institutions as a new category of payment service providers, establishes a set of rules to ensure transparency of conditions and information requirements for payment services, specifies the rights and obligations of payment service providers and consumers, and lays down rules on the execution of payment transactions.*

Payment institutions – the ***new category of payment service providers*** *that has been introduced to stimulate competition – may offer services similar to those of credit institutions and are subject to separate prudential requirements[2] proportionate to the operational and financial risks involved in their business activities. The rules on* ***transparency of contractual conditions*** *and on* ***information requirements*** *for payment service providers will make it easier for customers to compare the services offered, among other things. The* ***rights and obligations*** *of payment service providers and users include e.g. new liability provisions which specify that users shall bear the losses relating to unauthorized payment transactions resulting from the use of a lost or stolen payment instrument up to a maximum of EUR 150.[3] The directive also specifies that as of 2012, the maximum* ***execution time*** *for payment orders shall be one banking day, after which the funds shall be made available to the payee. Until then, however, the amount of a payment transaction shall be credited to the payee's account after three banking days at the latest.*

Implementation of the PSD: *As the realization and smooth functioning of the single euro payments market hinge upon the swift and uniform implementation of the directive in all EU Member States, the European Commission has assisted the Member States in the process by regularly staging implementation workshops for representatives of the competent national ministries in Brussels since the beginning of 2008. These measures aim at fostering a common understanding of the directive text and at clarifying at an early stage issues that are open to interpretation.*

[1] Official Journal of the European Union, L 319/1 of 5 December 2007.

[2] For instance, with regard to initial capital and own funds requirements as well as safeguarding of funds received.

[3] Provided that users did not neglect their due diligence obligations.

the full integration of SEPA. To ensure the smooth functioning of interbank payment systems, the OeNB has also implemented quality assurance procedures by conducting comprehensive tests in cooperation with the participating banks and data centers.

Clearing platform STEP.AT launched

On July 2, 2007, the OeNB launched STEP.AT, a clearing platform for regional interbank payments that will familiarize market participants with the multilateral processing of payments via centralized hubs, which is common practice in Europe. In addition to the formats that have been used so far for domestic transactions, STEP.AT will also offer the new SEPA instruments, which round off the OeNB's portfolio of payment services. The SEPA-compliant settlement of domestic transactions is a major step toward replacing the proprietary formats.

With these two SEPA-compliant services (STEP2 access and STEP.AT), the OeNB makes it possible for Austria's credit industry to realize synergies in tackling emerging challenges. The OeNB thus fulfills its statutory mandate to ensure the smooth and secure functioning of payment systems in Austria.

TARGET2: Increasing the Security of Payment Transactions in Euro

TARGET2 is a real-time gross settlement system predominantly for settling large-value euro-denominated interbank payments. TARGET2 is run by the Eurosystem under the responsibility of the Governing Council of the ECB. Three Eurosystem central banks (the Banca d'Italia, the Banque de France and the Deutsche Bundesbank) provide the technical infrastructure for TARGET2 – the Single Shared Platform (SSP) – and run the system on behalf of the Eurosystem.

TARGET2 participants across the euro area will have equal access to the SSP and will benefit from improved liquidity management features. The legal framework for TARGET2 has been harmonized across Europe. The SSP provides a single price structure and a harmonized service level; identical conditions apply to direct participants settling transactions in the euro area.

TARGET2 went live on November 19, 2007, when the countries of the first migration group (Austria, Cyprus, Germany, Latvia, Lithuania, Luxembourg, Malta and Slovenia) were connected to the system. The OeNB and the Austrian banking community were thus among the pioneers of the system. Migrating to the SSP was a highly complex task in terms of the technical requirements and logistics involved. Thanks to the excellent cooperation in the run-up to the migration, especially among the members of the national migration team, the OeNB and the Austrian banking community completed the migration successfully.

The second migration group (Belgium, Finland, France, Ireland, the Netherlands, Portugal and Spain) connected to TARGET2 on February 18, 2008, and the migration of the third and last group (Denmark, Estonia, Greece, Italy, Poland and the ECB) is scheduled for May 19, 2008.

When all participating countries have joined the SSP, the transaction volume is expected to exceed EUR 2,300 billion a day. To ensure business continuity, TARGET2 will rely on two processing sites located in different EU countries, each backed up by an equivalent, separate standby site. This structure will guarantee a maximum of security and operational reliability.

The migration to TARGET2/SSP is one of the greatest innovations introduced by the OeNB and marks a major milestone in harmonizing euro payments at the European level. Austria was among the first group of countries to connect to TARGET2, enabling OeNB experts to play an active role in the development of the new system and allowing them to effectively advocate the interests of the Austrian market at the European level and to strengthen Austria's competitive position in the financial market.

TARGET2 goes live

During the TARGET2 migration phase, the OeNB had important tasks, and it will retain important responsibilities: For example, in its capacity as the national system operator, the OeNB will remain the key contact for Austrian banks' queries (help desk). The OeNB will also continue to perform functions in other business areas, e.g.

minimum reserves and cash supply as well as the administrative competence for domestic banks' settlement accounts. Developing TARGET2 further and promoting the Austrian market's interests will remain key OeNB tasks.

TARGET2-Securities – A New Technical Platform to Improve the Efficiency of Securities Settlement

With the TARGET2-Securities (T2S) initiative, the Eurosystem aims to harmonize securities settlement services in central bank money especially in the euro area. By processing securities and central bank money transactions via one technical platform, T2S will support central securities depositories (CSDs) in providing borderless and neutral core securities settlement services. In T2S, there will be no difference in the settlement of domestic and cross-border securities transactions, which will, in turn, promote the integration and harmonization of the post-trading sector.

T2S implementation: decision pending

In close cooperation with market participants, notably CSDs and their customers, the Eurosystem prepared a comprehensive draft of T2S user requirements in 2007, which was open to review during a public consultation period. Following modification of the draft based on market participants' feedback, the final user requirements are scheduled for review, together with an updated economic impact analysis, by the Governing Council of the ECB in the summer of 2008. The decision on whether to move to the specification phase – which hinges on market participants' support of the T2S initiative – will be taken at the same time.

The OeNB founded a National User Group (NUG) as a forum to keep Austrian market participants informed about the latest T2S developments and to coordinate the various positions on T2S. In addition, national characteristics and requirements regarding T2S are discussed at regular NUG meetings with the Austrian CSD (Oesterreichische Kontrollbank) and the Austrian credit institutions.

Information on T2S – including all documents that are subject to market consultation – is provided on the OeNB's dedicated T2S website (*www.t2s.at*), which went online in 2007.

Developments at the OeNB's Subsidiaries in the Field of Cashless Payments

On September 26, 2007, the OeNB reached an agreement with the Greek group Inform P. Lykos S.A. (Lykos) on the sale of an 85% share of the smart card and identity systems producer AUSTRIA CARD Plastikkarten und Ausweissysteme GmbH (Austria Card) to a Lykos subsidiary. This share transfer was completed on January 1, 2008. The OeNB continues to hold a 15% minority interest in Austria Card, which underscores the owners' commitment to strengthening and developing further Austria Card's position as a Vienna-based strategic supplier of Austrian banks and banking groups. In addition, the two owners agreed to consolidate Austria Card's leading position in Central and Eastern Europe, with the Vienna office being designated by Lykos as the headquarters for the bank card business in this region. Lykos group and Austria Card will make joint R&D efforts to ensure that Austria Card can continue to provide all its customers with state-of-the-art, top-quality products and services.

In 2005, the Austrian Payments Council (APC) was founded within the framework of the Austrian Society for Payment System Research and Cooperation (Studiengesellschaft für Zusammenarbeit im Zahlungsverkehr – STUZZA). The APC serves as a forum for coordinating the implementation of SEPA in Austria. Its members are representatives of the Austrian credit institutions, the OeNB, the Austrian Federal Economic Chamber's Banks and Insurance section and the Austrian Bankers' Association. In 2007, the APC continued to focus on integrating SEPA payment instruments smoothly into the Austrian payments infrastructure.

The OeNB Ensures the Security and Efficiency of the Cash Cycle

Value of Euro Cash in Circulation Continues to Rise

Currency in circulation in the euro area and in Austria

At end-2007, the number of euro banknotes in circulation in the euro area stood at 12.1 billion, their value at EUR 676.6 billion (+7.7% against 2006 in value terms). The volume of euro coins came to EUR 75.8 billion, their value to EUR 19.2 billion (+7.6% against 2006 in value terms). Together, the banknotes and coins in circulation were worth EUR 695.9 billion. In the period from end-2006 to early 2007, the value of euro banknotes in circulation even surpassed the value of circulating U.S. dollar banknotes (calculated in euro). One important reason for the ongoing increase in the demand for euro cash is its growing popularity as a transaction, investment and reserve currency outside the euro area.

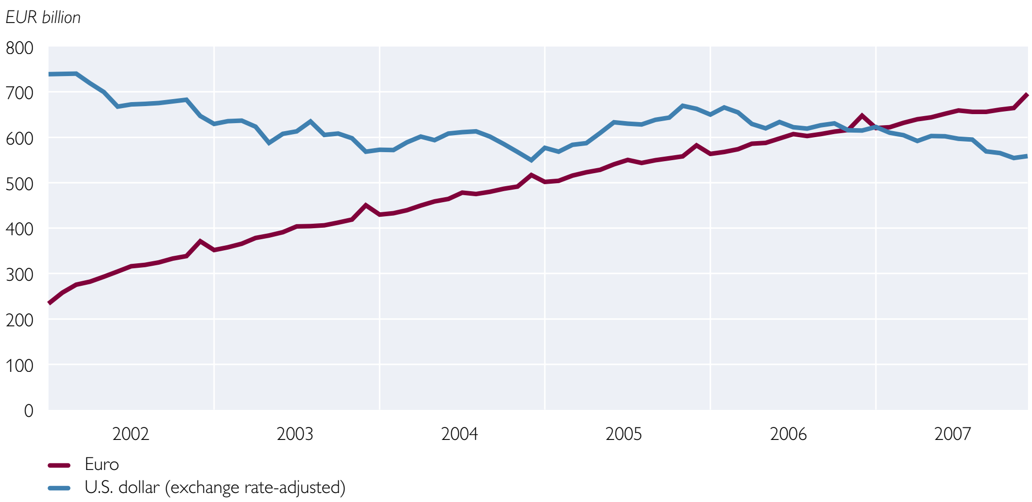
High Cash Security and Efficient Cash Supply in Austria

Because the euro is the sole legal tender in all euro area countries, the volume of currency in circulation within individual euro area countries can be estimated only on the basis of the countries' economic performance and of data on users' preferences for cash or cashless transactions. According to OeNB estimates, some 330 million to 350 million banknotes worth around EUR 16 billion to EUR 17 billion are currently in circulation in Austria.

Austria has been a banknote-importing country for several years, i.e. it receives more banknotes from abroad – especially EUR 20 and EUR 50 banknotes – than it exports to other euro area countries or the rest of the world. This trend reflects Austria's geographical position close to non-euro area countries as well as its strong banking presence in Central, Eastern and Southeastern Europe (CESEE) and its high tourism revenues, and it raises the stocks of banknotes in the OeNB's vaults. In a next step, the OeNB processes the banknotes and redistributes them within the euro area, thus con-

Chart 21

Value of Euro and U.S. Dollar Cash in Circulation



Source: ECB.

tributing to the efficiency of cash supply within the euro area.

In the area of cash supply, the OeNB has established itself as a competence center and logistics hub, which is confirmed by the fact that the OeNB's share in the Eurosystem Strategic Stock (built up to accommodate unexpected surges in demand) has been increased. The successful cooperation between Banka Slovenije and the OeNB has been continued since completion of the euro cash changeover in Slovenia. Moreover, the OeNB has also intensified the exchange of experience and information with Národná banka Slovenska in the run-up to the planned cash changeover in Slovakia on January 1, 2009, given the OeNB's cash logistics expertise and its cooperation with Banka Slovenije as well as Austria's geographical position.

Cash processing plays a key role in the OeNB's efforts to guarantee cash security. To ensure the high quality of banknotes in circulation, the Eurosystem has established common minimum sorting standards that provide for the application of numerous fitness criteria to check banknotes e.g. for soiling, tears, holes, crumples, limpness, creases and de-inking. Unfit banknotes – those that fail to meet the minimum standards – are destroyed. The better the quality of a banknote, the easier it is for a user to check its security features. In 2007, some 1.2 billion banknotes (i.e. roughly the same number as in 2006) were processed by the sorting machines of the OeNB and of the cash logistics company GELDSERVICE AUSTRIA Logistik für Wertgestionierung und Transportkoordination G.m.b.H. (GSA).

Slovakia plans to adopt the euro

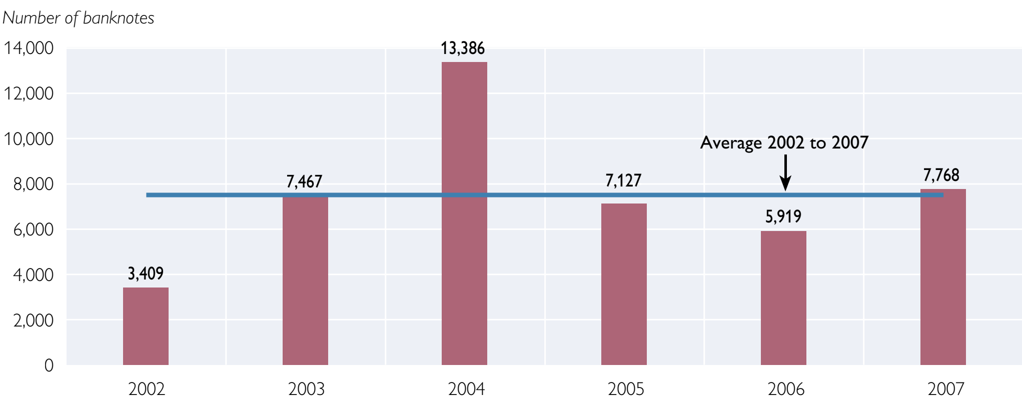
Number of counterfeits remains constant

Despite the rising volumes of banknotes in circulation in the euro area, the number of counterfeits discovered in 2007 dipped across Europe, dropping by 0.6% to 561,000 banknotes. The number of counterfeits detected in Austria totaled 7,768 and thus exceeded the 2006 figure, but remained within the long-term average of around 7,500 counterfeits a year. To put these figures into perspective: In 2007, just over 1 billion banknotes were put into circulation by the OeNB, and more than 1.2 billion banknotes were returned to the OeNB.

Judging from counterfeit banknotes removed from circulation in Austria, the EUR 100 banknote was most fre-

Chart 22

Euro Counterfeits Withdrawn from Circulation in Austria



Source: OeNB.

The OeNB Test Center – an institution of international standing

quently counterfeited (32%) in 2007, followed by the EUR 50 banknote (28.8%) and the EUR 200 banknote (26.4%). The loss incurred from counterfeits increased to EUR 881,655 owing to the sharp rise in high-denomination counterfeits.

Notwithstanding counterfeiters' use of cutting-edge reprographic techniques, it is still possible for everyone to identify counterfeits without technical aids by using the simple FEEL – LOOK – TILT test. This test should keep the risk of mistaking a counterfeit for a genuine banknote to a minimum.

Familiarizing the public with the euro's security features

To familiarize as many people as possible with the security features of the euro, the OeNB started an information campaign in cooperation with several Austrian radio stations in the fourth quarter of 2007. The success of this campaign can be directly gauged by the significant year-on-year decrease in the number of counterfeits detected during the pre-Christmas shopping season.

Alongside the special campaigns in the mass media, the OeNB continued to provide training courses free of charge for professional cash handlers (bank tellers, cashiers in retail trade, police officers, etc.) in Vienna and at the OeNB's branch offices. Many people were interested in attending the courses, and the service was expanded in 2007. Over the past four years, the OeNB has reached out to more than 30,000 people with these training courses.

OeNB Test Center Helps Ensure Cash Security

Banknotes and coins can be validated quickly and reliably with technical equipment such as banknote authentication devices, banknote counting and sorting machines, cash recycling systems as well as coin counters. To make sure that the equipment can identify all counterfeits, however, it must be tested and its software must be upgraded regularly. The OeNB Test Center in Vienna performs such tests free of charge for manufacturers, as required by the ECB. Test results are made available on the OeNB's and the ECB's websites. In the reporting year, the Test Center tested a total of 83 devices including eight prototypes. The OeNB Test Center has become an internationally renowned institution in the field of testing cash processing machines and testing and calibrating sensors. It offers its services to customers from Austria and many other countries, such as Italy, Sweden, Switzerland, the U.S.A., the People's Republic of China and Japan. In 2007, the Test Center for the first time tested coin processing machines in cooperation with Austria's mint, Münze Österreich Aktiengesellschaft.

NCBs as well as credit institutions and other professional cash handlers (such as bureaux de change) are authorized, as a rule, to reissue euro banknotes in the euro area. To ensure the integrity and fitness of reissued euro banknotes and to create harmonized standards throughout the euro area, the ECB established a framework for the detection of counterfeits and fitness sorting. This framework guarantees that banks and other professional cash handlers recycle euro banknotes to customers only if these banknotes have passed fitness and authenticity tests. Such checking may be done either by using banknote processing equipment that has been tested by an NCB or by appropriately trained experts.

Implementation of the framework for the detection of counterfeits and fitness sorting complete

Austria was one of the first euro area countries to implement the framework. The process was completed in 2007 when an agreement was signed between the OeNB and the Austrian banking associations. Implementation of the framework is not an easy task, which is why some euro area countries have applied for and have been granted an extension of the transition period. The agreement obligates Austrian credit institutions and other professional cash handlers that use banknote processing machines to recycle banknotes to regularly report data on cash recycling to the OeNB. Austria's central bank became one of the first Eurosystem NCBs to send data collected in line with the framework to the ECB.

The OeNB's Cash Service Subsidiaries

Banknote production in Austria

The *Oesterreichische Banknoten- und Sicherheitsdruck GmbH* (OeBS), a 100% OeNB subsidiary, is the company responsible for printing and producing banknotes in Austria and for developing security features. Within the Eurosystem, the OeBS produces the share of annual euro banknote production assigned to Austria on the basis of its share in the ECB's capital key.

In 2007, the OeBS produced 231.3 million EUR 10 banknotes (18% of the total volume of this denomination printed in the euro area that year). In 2008, the OeBS will again contribute to the production of EUR 10 banknotes.

GELDSERVICE AUSTRIA Logistik für Wertgestionierung und Transportkoordination G.m.b.H. (GSA) offers cash processing services and solutions for the entire cash supply chain and buys and sells foreign currency. The OeNB holds a majority share of currently 91.4% in GSA, and Austrian commercial banks hold most of the remaining shares. This cooperation between the central bank and commercial banks made it possible to achieve returns to scale, so that GSA – in its capacity as a service provider in the field of payment processing – contributes to enhancing the overall economic efficiency of cash supply in Austria. In the course of the euro introduction in Slovenia on January 1, 2007, the company expanded its business activities beyond Austria's borders and acquired corporate customers in Slovenia.

Coin production in Austria

The core purpose of Münze Österreich Aktiengesellschaft, a 100% OeNB subsidiary, is minting, distributing and

Chart 23

OeNB Cash Services Subsidiaries

Oesterreichische Banknoten- und Sicherheitsdruck GmbH (100%)	GELDSERVICE AUSTRIA Logistik für Wertgestionierung und Transportkoordination G.m.b.H. (91.4%)	Münze Österreich Aktiengesellschaft (100%)
• banknote and security printing • print product business • research and development services	• cash processing • cash supply chain solutions • logistics	• coin minting, distribution and withdrawal • production and sale of metal items • engineering and consulting services

withdrawing divisional and negotiable coins as well as producing and selling items made of precious and other metals. In 2007, Münze Österreich supplied the OeNB with 456 million euro coins (worth EUR 83.2 million) intended for circulation.

Exchange deadline for ATS 50 "Ferdinand Raimund" banknote expires in 2008

Exchange deadline for "Josef Ressel" schilling banknote

The exchange deadline for the ATS 500 banknote featuring a portrait of Josef Ressel expired on August 31, 2007. This banknote was first issued in 1966 and called in more than 20 years ago on August 31, 1987.

A total of 361,672 of these banknotes have not been returned to the OeNB. The corresponding balance – some EUR 13.1 million – was transferred to the Austrian Federal Ministry of Finance.

Over the next few years, the exchange deadline will expire for another four banknotes, which had all ceased to be legal tender before the introduction of the euro. No deadline is set for converting the schilling banknotes and coins of the last series; they may be exchanged free of charge into euro at the OeNB or at euro bus stops.

The next banknote to reach its exchange deadline is an ATS 50 banknote featuring a portrait of Ferdinand Raimund. This banknote was first issued in 1972 and called in in 1988. 2,650,641 of these banknotes with a value of around EUR 9.6 million were still outstanding as of December 31, 2007.

The Euro Bus Toured the Country for the Sixth Time in 2007

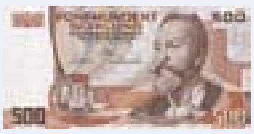
The euro bus toured Austria for the sixth time in 2007, providing Austrians with the opportunity to exchange their remaining schillings for euro free of charge and to obtain information on

Box 12

Called-In Banknotes and Exchange Deadlines

*Denomination: ATS **50** (3rd motif)*
*Portrait (front): **Ferdinand Raimund***
Date of issue: February 15, 1972
Exchange deadline: August 31, 2008

*Denomination: ATS **20** (4th motif)*
*Portrait (front): **Carl Ritter von Ghega***
Date of issue: November 4, 1968
Exchange deadline: September 30, 2009



*Denomination: ATS **500** (3rd motif)*
*Portrait (front): **Otto Wagner***
Date of issue: October 20, 1986
Exchange deadline: April 20, 2018

*Denomination: ATS **1,000** (4th motif)*
*Portrait (front): **Erwin Schrödinger***
Date of issue: November 14, 1983
Exchange deadline: April 20, 2018

No exchange deadlines have been set for the remaining schilling banknotes.

the euro and its security features. Between June 1 and August 31, 2007, the euro bus made 70 stops throughout Austria. This service, which is unique in Europe, was again well received.[1] By providing Austrian citizens with information on the security features of the euro, the euro bus initiative has made a simple yet effective contribution to ensuring cash security in Austria.

In 2007, 36,070 Austrians used this opportunity to exchange their remaining schilling stocks (just under ATS 54 million) for euro.

1 *See Mayerhofer, S. 2007. The 2007 Euro Bus Tour Proved a Success. In: Statistiken – Daten & Analysen Q4/07. Vienna: OeNB. 51–55. The full text is available in German only.*

The OeNB's Communications Activities Focus on Transparency and Knowledge Transfer

Information Campaign on the OeNB's Core Monetary Policy Tasks

"Ask – Know – Understand" – OeNB cooperation with radio stations

The OeNB's public relations activities aim at informing the Austrian public about the monetary policy objectives, strategies and measures of the Eurosystem as well as about the tasks the OeNB fulfills as an integral part of the Eurosystem.

In the first half of 2007, the OeNB carried on with information activities on its core monetary policy tasks, above all on the key areas of price stability and financial stability. In addition to informative advertising, communication measures included cooperation projects with print media and radio stations with a view to maximizing media reach.

"The OeNB makes sure that your money keeps its value."

The OeNB redesigned the five informative ads and the accompanying short teaser ads already used in 2006, also integrating information about the Eurosystem. All advertisements were placed in Austria's major regional newspapers, country-wide dailies as well as economic magazines.

To reinforce the impact of the teaser and informative ads, the OeNB placed a series of classic advertisements and advertorials in the economic sections of Austria's major dailies between May and June 2007, thereby increasing media reach to 76.7%.

From May to mid-June 2007, the OeNB resumed its media cooperation with radio stations, using the slogan "Ask – Know – Understand." To reinforce the impact of its past communication activities revolving around the slogan "I work hard for my money. Good that every euro is worth it." the OeNB built on existing advertising content in hopes of generating interest among listeners for the monetary policy objectives and tasks the OeNB fulfills as an integral part of the Eurosystem as well as for a number of other economic issues.

The OeNB appointed a new advertising and public relations agency from among the bidders under a periodic call for public tender in mid-2007. At the same time, the OeNB realigned its public relations and advertising activities. The slogan "I work hard for my money. Good that every euro is worth it." was replaced by "The OeNB makes

Box 13

The OeNB's New Logo

In 2007, the decision to relaunch the logo of the OeNB led to a substantial modernization of the OeNB's corporate design.

The graphic design of the new logo embodies the OeNB's guiding principles "stability and security." With its clear structure of stable vertical and secure horizontal lines, which are modeled on the basic geometric figures of rectangles and circles, the logo underpins this claim. Furthermore, the new logo also symbolizes the OeNB's close cooperation with the Eurosystem: The two horizontal lines within the circle allude to the euro symbol and the blue color echoes the European color code.

State-of-the-art communications of a modern central bank such as the OeNB is also about conveying its commitment to stability and security through an adequate and modern corporate design, which includes a cutting-edge logo. The OeNB adopted its new logo in January 2008, and the Annual Report 2007 is the first publication reflecting the new corporate design.

sure that your money keeps its value." Moreover, the graphic design was refashioned. Between October and December 2007, a broadly based print media campaign boosted media reach to 93%.

Stepping up the transfer of economic and financial knowledge

In a campaign to deepen people's knowledge and understanding of economic issues and monetary policy, the OeNB initiated an economic and financial education project. Harnessing an array of communication tools and information channels, the OeNB seeks to enhance the economic and financial literacy of the Austrian public, focusing particularly on money-related and monetary policy issues. Moreover, the OeNB will not only continue its close cooperation with schools by providing tools such as a special school information kit, but also plans further educational activities for both school and university students.

Press relations, 10th anniversary of the OeNB hotline

In 2007, the OeNB published 147 press releases and continued to provide information via its service hotline. In the past ten years, the call center has become an integral part of the OeNB's public relations activities. As a single point of contact, the call center channels the majority of all incoming (external) inquiries and handles them quickly and directly. In 2007, the hotline staff responded to more than a total of 36,700 queries with an increasing trend toward more complex e-mail inquiries.

The OeNB as a Platform for Dialogue and an International Exchange of Views

In the reporting year, the OeNB again facilitated exchanges among the Austrian public, economic players (especially from the financial sector), policymakers and researchers. All in all, the OeNB organized a total of 218 events attracting around 9,500 participants. The primary goal was to foster the exchange of views and theories on an international level.

In the first half of 2007, the highlights included the celebrations marking the 50th anniversary of the Treaties of Rome, hosted by the OeNB together with the Austrian social partners, and the 35th Economics Conference, which revolved around the relationship between human capital and economic growth. The fall 2007 Conference on European Economic Integration was dedicated to the topic "Currency and Competitiveness." October saw the highlight of the year, when the OeNB hosted the meeting of the Governing Council of the ECB, with Vienna and the OeNB turning into the center of Europe's financial community for a week.

Money Museum attracts a multitude of visitors

The Money Museum represents another communications platform of the OeNB. A variety of exhibitions and activities helped familiarize numerous visitors with money-related issues and monetary policy.

The two special exhibitions "Be embraced, ye millions! Beethoven and money" and "Gold bars" as well as the permanent exhibition "Austrian monetary history" attracted 12,522 visitors. In the Museum Night alone, the exhibition about Beethoven's financial situation drew 1,150 visitors to the museum. The Money Museum participated in the holiday activity program for young people organized by the City of Vienna three times during the reporting year ("Euro, pound and other currencies," "Beethoven and his money," which included a music quiz, and "The adventurous journey of the little gold nugget") as well as in the children's university offered by the University of Vienna ("How cotton changes into banknotes"). Both initiatives are geared at familiarizing young people in a playful manner with the concepts of money and central banking.

OeNB connects to Austrians at public fairs

In 2007, the OeNB ran stalls at public fairs in Salzburg, St. Pölten, Ried, Dornbirn, Klagenfurt, Graz, Innsbruck and Vienna, where it interacted directly with Austrian visitors. On a total of 51 days, OeNB representatives introduced the visiting public to money-related issues and monetary policy. Visitors of the OeNB's stall were challenged to test their knowledge about OeNB-related topics by playing the computer game "T€MPO." Information on banknote security and the accompanying cash authentication training sessions were particularly popular. According to the organizers, a total of one million visitors attended the above-mentioned fairs in 2007.

Efficient Management of OeNB Activities Guarantees Strong Performance

The OeNB's operations management has changed fundamentally since the bank joined the Eurosystem close to ten years ago. Eurosystem-wide cooperation, above all in various committees and working groups, has steadily intensified the exchange of information and has fueled competition for quality through the adoption of benchmarking and best practice techniques. In many instances, the joint coordination efforts have produced de facto standards.

In the field of operations management, the Eurosystem launched a comprehensive strategic planning process, which culminated in the implementation of measures related to the Eurosystem's mission statement as well as to its strategic intents and organizational principles (as outlined in the mission statement). Furthermore, the Eurosystem defined a harmonized structure of central banking functions, thus paving the way for numerous comparative analyses. Among other things, substantial effort went into harmonizing cost accounting within the Eurosystem. Furthermore, there are plans to coordinate, and thus considerably improve, supervisory risk management across the Eurosystem. Other strategically motivated innovations include the coordination and pooling of procurement across the ESCB as well as the centralized administration of ESCB-wide project portfolios. Last but not least, the work of the Budget Committee has contributed to the harmonization of planning, budgeting and monitoring practices at the national central banks (NCBs).

All these activities are aimed at enabling the Eurosystem as a whole, and each NCB, to fulfill its tasks with greater efficiency. In this respect, efforts have centered on establishing an effective division of labor within the Eurosystem. Having taken up this challenge, the OeNB seeks to meet the strategic objective of attaining excellence in central banking and strives to assert itself as a top European central bank. Numerous information visits to the OeNB by central bank colleagues from the ESCB and from all over the world confirm that the OeNB has succeeded in achieving this goal.

Excellence in central banking

Focus on Corporate Governance

The basic rules of corporate governance are instrumental in building credibility and trust. As a nonlisted corporation, the OeNB is not principally obligated to adhere to corporate governance rules, but it voluntarily implements recognized standards. At the same time, the OeNB has to comply with international provisions, the Federal Act on the Oesterreichische Nationalbank and other stipulations specifically applicable to central banks. Even though corporate governance rules have had a material influence on the OeNB's activities for years, the application of those rules is being refined continually. A dedicated corporate governance task force defines the required short- to medium-term measures. To this end, the accounting and internal control systems subcommittee of the General Council convened three times in 2007.

Continuous advances in corporate governance

In addition, the OeNB has set up a compliance unit which is responsible for taking measures to prevent insider transactions. As an added precaution, the relevant activities of the OeNB are subject to control by the Financial Market Authority (FMA).

Furthermore, the ECB is empowered to check the foreign currency positions that the OeNB holds for the ECB, or to order inspections to be carried out.

Box 14

The OeNB's Core Competences and Future Challenges

In defining its current strategy, the OeNB has taken its cue from the accelerating European integration process with clear specialization tendencies within the Eurosystem as well as from increasingly complex challenges arising on Austria's financial market. The OeNB has set itself ambitious goals for the period from 2007 to 2010, at the same time resolving to focus its activities on areas in which it has excelled in the past and which are set to remain significant in the future.

Maintaining Stability

The OeNB is committed to maintaining stability and security, as is reflected in the central role that it plays in safeguarding price stability and financial stability in line with its mandate. The OeNB is able to attain this goal by providing sound and accurate statistics, analyses and research results as well as by successfully implementing monetary and financial policies. In fulfilling this mandate, the OeNB acts in the Austrian interest and in the interest of promoting European integration.

Managing Risk

The OeNB will establish itself as the leading Austrian authority on risk management issues and will thus contribute to greater financial stability in Austria and Europe, above all Eastern Europe. To this effect, the OeNB will, among other things, intensify its analytical efforts and make the results of relevant analyses accessible to the general public.

Handling Money

With regard to the handling of cash and other means of payment, the OeNB focuses its activities on two areas: the creation of a Single Euro Payments Area (SEPA) for cashless payments, and the need to make cash logistics and cash production more efficient. The explicit aim of all efforts is to make the processing of payments, cash and noncash, as secure, cost-efficient and quick as possible.

"Going East"

The OeNB has refocused its perspective more strongly on the Central and Eastern European EU Member States as well as on Southeastern European countries and on selected Commonwealth of Independent States (CIS) and Asian countries. Implementing this strategy includes building and maintaining long-term partnerships and intensifying analytical efforts. Through this special commitment, which ties in with the OeNB's strategic intents, the bank promotes the integration of Europe by providing know-how, among other things, and by entering into specific cooperation projects. The intensified cooperation of the OeNB with Central, Eastern and Southeastern European countries supports Austrian companies (above all commercial banks) doing business in the area and thus promotes Austrian economic interests.

In defining its strategy, the OeNB paid particular attention to ensuring an efficient use of its resources. The strategy spotlights the following key areas:

- *Knowledge management*
- *Integrated corporate communication*
- *Strategic cooperation, especially within the ESCB*
- *Human resources management*
- *Cost management*
- *Corporate governance*
- *Environmental protection*

The correct conduct of operations and corresponding instructions for staff have been laid down in internal rules and regulations. Moreover, the OeNB's Code of Conduct establishes binding rules of conduct for all management and staff members. Line managers ensure compliance with those rules within their management responsibilities. Finally, numerous internal control layers, above all internal auditing, ensure compliance with external and internal rules (laws and staff regulations) as well as the effectiveness of the internal control system.

Future-Oriented Framework Conditions for Corporate Development

Enabling the OeNB to achieve excellence in central banking has been a special challenge for human resources management. After all, it takes an ever larger share of highly specialized experts to tackle the tasks the OeNB has to fulfill. Against this backdrop, the existing expert career path – which made it possible to promote staff for excellence to the rank of "Senior Experts" without giving them managerial responsibilities – has been redesigned. Recent innovations include all-inclusive contracts for Senior Experts as well as the introduction of two new ranks above Senior Experts, basically commensurate in pay and rank with management positions – "Advisors" and "Senior Advisors" – as well as the creation of a new broader "Expert" rank below the rank of Senior Experts. The new scheme is to be implemented gradually and with a long-term orientation in accordance with other significant factors, such as the evolution of the management career path.

Other projects launched in 2007 include the design of further measures aimed at anchoring gender equality as a dedicated quality benchmark of the OeNB's management and human resources policy. Gender equality aspects are meant to influence all strategies, objectives, annual planning processes and projects on a sustained and systematic basis.

Following the legal changes made to the framework of financial supervision in Austria in 2007, the OeNB has taken on new tasks also in this highly specialized area, which meant that additional experts had to be recruited. It has taken special efforts to gain highly qualified bank examiners and to integrate them into the existing team. Last but not least, establishing a tailor-made training program for those staff members will be a priority item in the agenda for 2008.

Enhancing human resources with a view to achieving excellence in central banking

In a continual optimization process, ongoing organization and process analyses have contributed significantly to honing the organizational structure of the OeNB. A case in point is the afore-mentioned integration of banking supervisory responsibilities into the structures of the OeNB, as outlined in more detail in the chapter "The OeNB as the Key Player in Securing Financial Stability in Austria." In the project at hand, processes and interfaces were redesigned both within the OeNB and between the OeNB and the FMA in line with the new legal framework conditions.

Optimizing processes and structures

A comprehensive organization analysis served to review the portfolio of tasks of the OeNB's statistical function and led to an optimization of organizational structures and operational procedures.

Moreover, the existing Intranet application was relaunched with a view to improving internal communication.

Within the framework of ESCB/Eurosystem cooperation and at an international level, strong advances were made in 2007 in enhancing the management of operational risk and business continuity. Based on preparations made in 2007, an integrated risk management project was launched to pool solutions existing in different business areas. Thus the tried and tested risk management systems established by the treasury, operational risk, financial market and banking analysis functions will be integrated into a comprehensive solution.

Successful IT solutions for the OeNB and the Eurosystem

Having been commissioned by the ECB to develop a Tender Operations system (TOP) to support the conduct of refinancing operations in the euro area, the OeNB's IT Development Division delivered TOP in March 2007. TOP is operated by the ECB and used by all euro area NCBs and the ECB itself. The system has been working smoothly and error-free since it went live; additional (new) functions were implemented in a follow-up project and have been available to users since the beginning of 2008.

With a view to ensuring effective cost management, the cost allocation of IT activities was refined in 2007 and integrated into the OeNB's annual planning process.

In December 2007, the OeNB's IT quality management system (QMS) was recertified to the ISO 9001:2000 standard. The main objective of the QMS, which was first introduced in 2001, is to implement and continuously optimize standardized IT processes in line with user needs. The IT quality management system thus contributes significantly to meeting the OeNB's high objectives of professionalism and quality as well as cost awareness and efficiency on a sustained basis.

OeNB Publishes Sustainability Report

Stability, security and trust are the key principles that guide the OeNB in taking action with a view to ensuring sustainability. Comprehensive knowledge management and investment in the development of human capital provide a solid basis for the OeNB to fulfill its tasks reliably and efficiently. The OeNB's commitment to sustainability is also reflected by an extensive array of environmental measures. Overall, the OeNB aims to achieve sustainability through the coordinated integration of economic efficiency, knowledge management and environmental protection. Given those interdependencies, the OeNB combines its Annual Report with an Intellectual Capital Report and an Environmental Statement to publish a full-fledged Sustainability Report; the Sustainability Report 2007 is the second report in this series.

The Intellectual Capital Report, which was first produced for the year 2003, outlines the OeNB's intellectual capital and provides a detailed overview of relevant projects, such as a knowledge management project that runs from 2007 to 2010. An Environmental Statement compliant with the EMAS[1] Council Regulation was first published in 1998. Protecting the environment in fulfilling its activities is a big concern for the OeNB, which is why the OeNB goes beyond the statutory requirements. Having already accomplished ten-year compliance with the EMAS Council Regulation, the OeNB has assumed a pioneering role in the ESCB in this field.

Business, Science and Culture Promotion

Sixty years ago, the European Recovery Program (ERP, commonly called the Marshall Plan), with which the United States helped rebuild European nations, laid the foundation for one of Austria's key financial assistance programs for businesses: ERP loans. The OeNB has supported the ERP loan program since the 1950s, and currently does so in cooperation with the public sector entity austria wirtschaftsservice (aws).

[1] *EMAS: Eco-management and audit scheme.*

Apart from specifically funding small and medium-sized enterprises as well as innovative projects in defined regions, current ERP programs promote the internationalization of Austrian companies and the readjustment of production factors toward future-oriented industries (such as aircraft component suppliers, power engineering and biotechnology). Funding projects pay particular attention to making the best possible use of EU cofinancing. All in all, outstanding ERP loans provided by the OeNB totaled EUR 956 million on December 31, 2007. Based on an average loan term of five to six years, the OeNB may extend a total of between EUR 150 million and EUR 200 million per year. The investment boom in 2007 generated a new record of 400 applications. 2007 was also a good year for the development of the Austrian export promotion framework, of which the OeNB forms an integral part. The OeNB contributes to the ongoing development of the export financing and guarantee system of the Oesterreichische Kontrollbank (OeKB). Innovations include the expansion of the OeKB's soft loan product portfolio by mixed credits (financing packages that involve official government credit as well as interest rate concessions), the establishment of corporate social responsibility rules as a recommendation for exporting companies, and preparations for the creation of the Austrian Development Bank, which took up its operations at the beginning of 2008. The OeNB has always considered it very important to contribute to safeguarding Austria's future. With this concern in mind, the OeNB founded the OeNB Anniversary Fund for the Promotion of Scientific Research and Teaching (Jubiläumsfonds – Anniversary Fund) in 1966 to mark the 150th anniversary of the OeNB's establishment, the Anniversary Fund has provided substantial funding for Austrian researchers for more than 40 years and has thus established itself as a stable and indispensable partner in Austrian research promotion. Funding of close to 8,800 projects totaled over EUR 694 million up to and including 2007, with grants provided for scientific projects in basic research and up to 2003 also in applied research.

In 2007, the OeNB made direct grants to the tune of some EUR 10.84 million for 164 research projects mainly in economics and medicine (clinical research) and to a lesser extent also in the social sciences and the humanities. Funds are granted for projects selected on the basis of sound criteria; stringent quality standards apply to the funding process.

The OeNB forms an integral part of Austria's research promotion framework

The OeNB Anniversary Fund provides a forum through which pertinent project results are regularly presented to an expert audience. In addition, the OeNB provided EUR 3.6 million of basic funding to three economic research institutes, the Institute for Advanced Studies (IHS), the Austrian Institute of Economic Research (WIFO) and The Vienna Institute for International Economic Studies (wiiw).

The National Foundation for Research, Technology and Development (National Foundation) provides a sound and reliable basis for the sustainable, strategic long-term financing of Austrian research initiatives independently of public finances. Its efforts are in particular targeted at financing interdisciplinary research projects which are likely to generate benefits in the long run. The provision of sustainable financing for such initiatives contributes to visibly positioning Austrian excellence in research and putting it on the global map. In the review year, the OeNB provided a total of EUR 50 million of support to the National Foundation.

Like many other Austrian businesses, the OeNB puts a particular emphasis on promoting cultural activities. Its collection of valuable old string instruments currently comprises 36 instruments, which are on loan to excellent young Austrian violin players and Austrian orchestras and chamber music ensembles. This collection now counts among the most important collections in Europe. The OeNB feels an obligation to make this collection accessible also to a broader public. On the occasion of the 40th anniversary of the Austrian radio channel Ö1, the OeNB co-sponsored a concert series in all provincial capitals. For those concerts it was possible to win both rising as well as established and internationally renowned musicians, who played instruments on loan from the OeNB.

Last but not least, the OeNB co-sponsored a project with the Viennese Leopold Museum in 2007. The exhibition "Between the Wars – Austrian Artists 1918–1938" offered an overview of Austrian artwork produced between the first and the second world wars. The exhibition featured paintings by Kokoschka, Boeckl, Wacker, Kolig, Faistauer and many other artists of the interwar period – mostly paintings collected by the Leopold Museum and the OeNB, but also loans from other museums and private collectors. With this exhibition, the OeNB made numerous paintings from its collection available for public viewing for the first time.

Financial Statements of the Oesterreichische Nationalbank for the Year 2007

Balance Sheet as at December 31, 2007

Assets

	December 31, 2007 EUR		December 31, 2006 EUR	
1 Gold and gold receivables		5,115,322,230.16		4,480,989,970.86
2 Claims on non-euro area residents denominated in foreign currency		7,192,263,013.84		5,204,492,549.03
2.1 Receivables from the IMF	298,404,783.57		286,102,786.08	
2.2 Balances with banks and security investments, external loans and other external assets	6,893,858,230.27		4,918,389,762.95	
3 Claims on euro area residents denominated in foreign currency		1,214,895,722.91		1,620,524,702.53
4 Claims on non-euro area residents denominated in euro		986,597,760.92		604,267,842.17
4.1 Balances with banks, security investments and loans	986,597,760.92		604,267,842.17	
4.2 Claims arising from the credit facility under ERM II	–		–	
5 Lending to euro area credit institutions related to monetary policy operations denominated in euro		12,694,666,927.00		12,150,942,571.00
5.1 Main refinancing operations	8,703,193,400.00		9,286,523,750.00	
5.2 Longer-term refinancing operations	3,991,473,527.00		2,864,418,821.00	
5.3 Fine-tuning reverse operations	–		–	
5.4 Structural reverse operations	–		–	
5.5 Marginal lending facility	–		–	
5.6 Credits related to margin calls	–		–	
6 Other claims on euro area credit institutions denominated in euro		127,137.61		114,785.55
7 Securities of euro area residents denominated in euro		4,633,276,301.15		3,276,539,398.54
8 General government debt denominated in euro		418,632,652.76		424,307,693.41
9 Intra-Eurosystem claims		19,964,089,383.19		16,950,770,703.24
9.1 Participating interest in the ECB	117,186,925.35		116,475,959.82	
9.2 Claims equivalent to the transfer of foreign reserves	1,161,289,917.84		1,157,451,203.42	
9.3 Claims related to promissory notes backing the issuance of ECB debt certificates[1]	×		×	
9.4 Net claims related to the allocation of euro banknotes within the Eurosystem	18,685,612,540.00		15,676,843,540.00	
9.5 Other claims within the Eurosystem (net)	–		–	
10 Items in course of settlement		100,875,792.70		103,011,656.71
11 Other assets		9,625,388,034.73		8,561,913,879.55
11.1 Coins of euro area	140,655,390.04		136,913,779.23	
11.2 Tangible and intangible fixed assets	147,686,002.65		153,843,810.70	
11.3 Other financial assets	7,719,123,572.90		6,795,448,294.21	
11.4 Off balance sheet instruments' revaluation differences	18,330,147.18		11,680,181.94	
11.5 Accruals and prepaid expenses	597,241,172.95		437,973,734.79	
11.6 Sundry	1,002,351,749.01		1,026,054,078.68	
		61,946,134,956.97		**53,377,875,752.59**

[1] *Only an ECB balance sheet item.*

Liabilities

	December 31, 2007 EUR		December 31, 2006 EUR	
1 Banknotes in circulation		18,052,675,160.00		16,814,843,600.00
2 Liabilities to euro area credit institutions related to monetary policy operations denominated in euro		6,548,091,077.64		4,473,529,774.79
2.1 Current accounts (covering the minimum reserve system)	6,153,091,077.64		4,429,029,774.79	
2.2 Deposit facility	395,000,000.00		44,500,000.00	
2.3 Fixed-term deposits	–		–	
2.4 Fine-tuning reverse operations	–		–	
2.5 Deposits related to margin calls	–		–	
3 Other liabilities to euro area credit institutions denominated in euro		–		–
4 Debt certificates issued [1]		×		×
5 Liabilities to other euro area residents denominated in euro		16,641,252.94		5,827,726.14
5.1 General government	10,799,291.39		4,719,190.85	
5.2 Other liabilities	5,841,961.55		1,108,535.29	
6 Liabilities to non-euro area residents denominated in euro		14,784,546.73		13,772,332.52
7 Liabilities to euro area residents denominated in foreign currency		75,297.04		62,630.43
8 Liabilities to non-euro area residents denominated in foreign currency		676,358,995.05		492,750,173.24
8.1 Deposits, balances and other liabilities	676,358,995.05		492,750,173.24	
8.2 Liabilities arising from the credit facility under ERM II	–		–	
9 Counterpart of Special Drawing Rights allocated by the IMF		192,294,330.00		204,397,772.00
10 Intra-Eurosystem liabilities		25,402,201,772.97		21,160,054,118.18
10.1 Liabilities equivalent to the transfer of foreign reserves [1]	×		×	
10.2 Liabilities related to promissory notes backing the issuance of ECB debt certificates	–		–	
10.3 Net liabilities related to the allocation of euro banknotes within the Eurosystem	–		–	
10.4 Other liabilities within the Eurosystem (net)	25,402,201,772.97		21,160,054,118.18	
11 Items in course of settlement		24,880,287.43		–
12 Other liabilities		472,953,360.84		435,414,186.92
12.1 Off balance sheet instruments' revaluation differences	127,028.25		182,225.40	
12.2 Accruals and income collected in advance	96,758,969.60		73,488,885.26	
12.3 Sundry	376,067,362.99		361,743,076.26	
13 Provisions		2,865,842,350.56		2,460,854,136.31
14 Revaluation accounts		3,529,439,663.09		3,176,112,287.25
15 Capital and reserves		4,133,247,130.46		4,125,785,417.62
15.1 Capital	12,000,000.00		12,000,000.00	
15.2 Reserves	4,121,247,130.46		4,113,785,417.62	
16 Profit for the year		16,649,732.22		14,471,597.19
		61,946,134,956.97		**53,377,875,752.59**

[1] *Only an ECB balance sheet item.*

Profit and Loss Account for the Year 2007

	Year ending December 31, 2007 *EUR*		Year ending December 31, 2006 *EUR*	
1.1 Interest income	1,965,217,752.45		1,365,051,482.13	
1.2 Interest expense	−1,226,902,981.38		−797,482,537.64	
1 Net interest income		738,314,771.07		567,568,944.49
2.1 Realized gains/losses arising from financial operations	209,043,369.30		144,581,213.16	
2.2 Writedowns on financial assets and positions	−358,375,378.68		−149,010,812.54	
2.3 Transfer to/from provisions for foreign exchange and price risks	−140,914,142.65		−170,211,391.03	
2 Net result of financial operations, writedowns and risk provisions		−290,246,152.03		−174,640,990.41
3.1 Fees and commissions income	6,046,573.75		4,748,359.05	
3.2 Fees and commissions expense	−2,660,943.08		−2,829,301.94	
3 Net income from fees and commissions		3,385,630.67		1,919,057.11
4 Income from equity shares and participating interests		22,587,331.09		25,201,625.35
5 Net result of pooling of monetary income		7,316,511.83		6,342,645.51
6 Other income		9,192,225.42		10,233,471.15
Total net income		490,550,318.05		436,624,753.20
7 Staff costs		−107,521,382.65		−115,315,844.89
8 Administrative expenses		−78,342,634.77		−76,996,623.04
9 Depreciation of tangible and intangible fixed assets		−13,325,311.38		−14,142,430.90
10 Banknote production services		−24,840,729.05		−24,573,567.19
11 Other expenses		−19,857,560.68		−12,641,658.01
Total expenses		−243,887,618.53		−243,670,124.03
		246,662,699.52		**192,954,629.17**
12 Corporate income tax		−61,665,674.88		−48,238,657.29
		184,997,024.64		144,715,971.88
13 Transfers to the pension reserve and central government's share of profit		−168,347,292.42		−130,244,374.69
14 Profit for the year		**16,649,732.22**		**14,471,597.19**

Notes to the Financial Statements 2007

General Notes to the Financial Statements

Legal Framework

The Oesterreichische Nationalbank (OeNB) is obligated (under Article 67 paragraph 2 of the Federal Act on the Oesterreichische Nationalbank 1984 as amended and as promulgated in Federal Law Gazette I No. 61/2006 – Nationalbank Act)[1] to prepare its balance sheet and its profit and loss account in conformity with the provisions established by the Governing Council of the ECB under Article 26.4 of the Statute of the European System of Central Banks (ESCB Statute) and of the European Central Bank. These rules are laid down in the Accounting Guideline adopted by the Governing Council on November 10, 2006.[2] The OeNB's financial statements for the year 2007 were prepared fully in line with the provisions set forth in this Guideline. In cases not covered by the Guideline, the generally accepted accounting principles referred to in Article 67 paragraph 2 second sentence Nationalbank Act were applied. The Nationalbank Act provisions that govern the OeNB's financial reporting (Articles 67 and 69 as well as Article 72 paragraph 1 Nationalbank Act) have remained unchanged from the previous year. Under Article 68 paragraph 3 Nationalbank Act, amended with the 2004 Financial Reporting Amendment Act, the OeNB continued to be exempt from Article 243 paragraph 2 last sentence as well as paragraph 3 items 2 and 5 Commercial Code.

In accordance with Article 67 paragraph 3 Nationalbank Act, the OeNB also continued to be exempt from preparing consolidated financial statements as required under Article 244 et seq. Commercial Code.

The financial statements for the year 2007 were prepared in the format laid down by the Governing Council of the ECB.

Accounting Policies

The OeNB's financial statements are prepared in conformity with the provisions governing the Eurosystem's accounting and reporting operations, which follow accounting principles harmonized by Community law and generally accepted international accounting standards. The key policy provisions are summarized below:

– economic reality and transparency
– prudence
– recognition of post-balance sheet events
– materiality
– going-concern basis
– accruals principle
– consistency and comparability

On the basis of the ECB's Accounting Guideline (ECB/2006/16), foreign exchange transactions, financial instruments denominated in foreign currency and related accruals must be recorded at trade date (economic approach) while securities transactions denominated in foreign currency may still be recorded according to the cash/settlement approach. Interest accrued in relation to foreign currency

[1] *The Nationalbank Act was amended with effect from January 1, 2008 (Federal Law Gazette I No. 108/2007) with a view to clarifying the OeNB's responsibility for ensuring financial stability.*

[2] *Guideline of the ECB of 17 December 2007 (ECB/2007/20) amending Guideline ECB/2006/16.*

transactions, including premiums or discounts, must be recorded on a daily basis from the spot settlement date. To record specific euro-denominated transactions, financial instruments and related accruals, the Eurosystem national central banks (NCBs) may use either the economic or the cash/settlement approach.

Foreign currency transactions whose exchange rate is not fixed against the accounting currency were recorded at the euro exchange rate prevailing on the day of the transaction.

At year-end, both financial assets and liabilities are revalued at current market prices/rates. This applies equally to on balance sheet and off balance sheet transactions. The arbitrage pricing principle is used to value gold interest rate swaps and gold forward interest rate swaps. To this end, the products are split into the components at which these products are traded on international exchanges (LIBOR curve, gold swap rates and gold forward rates). The revaluation took place on a currency-by-currency basis for foreign exchange positions and on a code-by-code basis for securities. The prices of master fund shares are calculated daily by the designated custodian bank using established market information systems on the basis of the assets held by the subfunds. The custodian bank's valuation of the subfund assets is crosschecked at least once a week with the respective master fund managers. In the case of illiquid assets or assets with low liquidity, price calculations are not based on established market information systems alone and, moreover, are cleared daily with the master fund managers. Securities held as permanent investment (financial fixed assets) and shown under *other financial assets* were valued at cost.

Premiums or discounts arising on securities are calculated and presented as part of interest income and are amortized over the remaining life of the securities.

In derogation from general accounting principles and standards, alternative valuation methods may be applied for synthetic instruments if the following conditions are met:

– The individual instruments are managed and their performance is evaluated as one combined instrument.
– On initial recognition, the individual instruments are structured and designated as a synthetic instrument.
– The application of the alternative treatment eliminates or significantly reduces a valuation inconsistency (valuation mismatch) that would arise from applying general rules at an individual instrument level.
– Formal documentation must be provided to allow fulfillment of the preconditions for using alternative valuation methods to be verified.

Unrealized gains and losses of the instruments combined to form a synthetic instrument are netted at year-end. In such a case, net unrealized gains are recorded in a revaluation account. Net unrealized revaluation losses are taken to the profit and loss account if they exceed previous net revaluation gains registered in the corresponding revaluation account.

Securities held as part of a synthetic instrument are not part of the overall holding on these securities but are part of a separate holding. Unrealized losses taken to the profit and loss account at year-end and the corresponding unrealized gains are separately amortized in subsequent years.

If one of the instruments combined expires, is sold, terminated or exercised, the reporting entity must prospectively discontinue the alternative treatment and any unamortized valuation gains credited in the profit and loss account in previous years must be immediately reversed.

The average acquisition cost and the value of each currency position are calculated on the basis of the sum total of the holdings in any one currency, including both asset and liability positions and both on balance sheet and off balance sheet items. On December 14, 2007, the share of the balances at the disposal of the IMF, so far expressed in euro, was redenominated in SDR (Special Drawing Rights) and added to the SDR position. Own funds invested in foreign exchange assets are treated as a separate currency item.

Gains and losses realized in the course of transactions are taken to the profit and loss account. The average cost method is used on a daily basis for gold, foreign currency instruments and securities, to compute the acquisition cost of items sold, having regard to the effect of exchange rate and/or price movements. As a rule, the realized gain or loss is calculated by juxtaposing the sales price of each transaction with the average acquisition cost of all purchases made during the day. In the case of net sales, the calculation of the realized gain or loss is based on the average cost of the respective holding for the preceding day.

Unrealized revaluation gains are not taken to the profit and loss account, but transferred to a revaluation account on the liabilities side of the balance sheet. Unrealized losses were recognized in the profit and loss account when they exceeded previous revaluation gains registered in the corresponding revaluation account; they may not be reversed against new unrealized gains in subsequent years. Furthermore, based on current legislation, the OeNB's management determined[3] that unrealized foreign currency losses that must be expensed were to be covered by the release of an offsetting amount from the *reserve fund for exchange rate risks* accumulated in the run-up to 1999 (recorded under liability item 14 *Revaluation accounts*). Unrealized losses in any one security, currency or in gold holdings are not netted with unrealized gains in other securities, currencies or gold, since netting is prohibited under the ECB's accounting guideline.

Participating interests are valued on the basis of the net asset value of the respective company.

Exchange rate risks have been calculated on the basis of the value-at-risk (VaR) method since 1997. In 2007, this method was reviewed with regard to its suitability for capturing current and possible future developments. Consequently, apart from technical adjustments, the confidence interval was increased from 97.725% to 99.0%, while leaving the one-year time horizon unchanged. The financial effects resulting from this adjustment, totaling EUR 220 million, were recognized accordingly in the financial statements for 2007. VaR is defined as the maximum loss of a gold or foreign currency portfolio with a given currency diversification at the given level of probability (99.0%) and for the given holding period (one year). The potential loss calculated under this approach is to be offset against the respective *revaluation accounts* (for which netting is prohibited), the *reserve for nondomestic and price risks*, and *risk provisions* in general (until December 31, 2006: *provisions for exchange rate risks*).

[3] *Decision of the Governing Board of November 10, 1999, and of the General Council of November 25, 1999.*

As a result of the harmonized accounting rules which have to be observed since January 1, 1999, future market developments, especially (volatile) interest and exchange rate movements, may entail considerable fluctuations of the income accruing to the OeNB, the other Eurosystem NCBs and the ECB.

Tangible and intangible fixed assets are valued at cost less depreciation. Depreciation is calculated on a straight-line basis from the quarter after acquisition throughout the expected economic lifetime of the assets (table 1):

Table 1

Asset	Depreciation period
Computers, related hardware and software, motor vehicles	4 years
Equipment, furniture and plant in building	10 years
Buildings	25 years
Fixed assets costing less than EUR 10,000	no capitalization

Realized Gains and Losses and Revaluation Differences and Their Treatment in the Financial Statements of December 31, 2007

Table 2

	Realized gains profit and loss account item 2.1 (posted to the profit and loss account)	Realized losses profit and loss account item 2.1 (posted to the profit and loss account)	Unrealized losses profit and loss account item 2.2 (posted to the profit and loss account)	Change in unrealized gains (posted to revaluation accounts)
	EUR million	*EUR million*	*EUR million*	*EUR million*
Gold	117.180	–	–	+703.636
Foreign currency				
Holdings for own account	41.429	22.548	292.582[1]	−24.726
Own funds	0.149	0	–	−0.272
Securities				
Holdings for own account	66.875	78.851	49.924	+43.783
Own funds	1.069	4.720	15.786	+3.635
IMF euro holdings	90.463	–	–	–
Balances at the disposal of the IMF redenominated from euro to Special Drawing Rights	33.014	35.017	–	–
Participating interests	–	–	0.083	+33.022
Off balance sheet instruments				
Holdings for own account	–	–	–	−2.045
Own funds	–	–	–	–
Total	**350.179**	**141.136**	**358.375**	**+757.033**

[1] *The losses resulting from holdings for own account had only a minor impact on profit because they were largely offset by the remaining provisions for foreign exchange rate and price risks, EUR 266.086 million.*

Banknotes in Circulation and Intra-Eurosystem Balances

Euro banknotes are issued by the ECB and the 13 NCBs, which together comprise the Eurosystem.[4] The total value of euro banknotes in circulation is allocated among the Eurosystem members on the last working day of each month in accordance with the banknote allocation key.[5]

The ECB has been allocated a share of 8% of the total value of euro *banknotes in circulation*, whereas the remaining 92% have been allocated to NCBs according to their weightings in the capital key of the ECB. The share of banknotes allocated to the OeNB is disclosed under the balance sheet liability item *banknotes in circulation*.

The difference between the value of the euro banknotes allocated to each NCB in accordance with the banknote allocation key and the value of the euro banknotes that it actually put into circulation, as reduced by the banknotes it withdrew from circulation, also gives rise to remunerated intra-Eurosystem balances. These claims or liabilities, which incur interest, are disclosed under the subitems *intra-Eurosystem claims/intra-Eurosystem liabilities: Net claims/liabilities related to the allocation of euro banknotes within the Eurosystem* (see Intra-Eurosystem balances in the notes on accounting policies).

In the first five years following the cash changeover year,[6] the intra-Eurosystem balances arising from the allocation of euro banknotes are adjusted in order to avoid significant changes in NCBs' relative income positions as compared to previous years. The adjustments are effected by taking into account the differences between the average value of banknotes in circulation of each NCB in the reference period and the average value of banknotes that would have been allocated to them during that period under the ECB's capital key. The adjustments are reduced in annual stages until the first day of the sixth year after the cash changeover year when income on banknotes are allocated fully in proportion to the NCBs' paid-up shares in the ECB's capital. For the OeNB and all other participating NCBs that together comprised the Eurosystem until December 31, 2006, the adjustment period ended on December 31, 2007.

The interest income and expense on these balances is cleared through the accounts of the ECB and is disclosed under item 1 *Net interest income* of the profit and loss account.

The Governing Council of the ECB has decided that the seigniorage income of the ECB arising from the 8% share of euro banknotes allocated to the ECB shall be due to the NCBs in the same financial year it accrues and distributed on the second working day of the following year in the form of an interim distribution of profit. It shall be so distributed in full unless the ECB's net profit for the year is less than its income earned on euro banknotes in circulation and subject to any decision by the Governing Council to reduce this income in respect of costs incurred by the ECB in connection with the issue and handling of euro banknotes. The Governing Council may also decide to transfer part or all of the ECB's seigniorage income to a provision for foreign exchange rate, interest rate and gold

[4] *Banka Slovenije joined the Eurosystem on January 1, 2007.*

[5] *Banknote allocation key means the percentages that result from taking into account the ECB's share in the total euro banknote issue and applying the subscribed capital key to the NCBs' share in such total.*

[6] *Slovenia adopted the euro in 2007; Cyprus and Malta followed in 2008.*

price risks. The amount distributed to the OeNB is recognized in the profit and loss account under item 4 *Income from equity shares and participating interests*.

With respect to 2007, the Governing Council decided at its meeting of December 20, 2007, that the full amount of such income should be retained by the ECB.

Intra-Eurosystem balances arising from the allocation of euro banknotes within the Eurosystem are included as a net single asset under *Claims related to the allocation of euro banknotes within the Eurosystem*.

Risk Management

Financial and operational risk incurred in connection with the OeNB's central banking activities have a crucial impact on its financial result and on its ability to continue as a going concern. The OeNB's risk management is based on binding rules; risk is determined by means of recognized procedures, and risk control is guaranteed through continuous monitoring. Moreover, regular reporting procedures have been put in place.

In line with international trends, the OeNB is developing an integral risk management structure[7] that will cover above all the impact and mutual influence of financial and reputational risks. The object of integral risk management is first, to control risk, second, to recognize opportunities for success through broader risk management strategies, and third, to implement the risk management strategies and structures allowing these objectives to be met.

Financial Risk

Financial risk covers a range of collateral-related risks, basically market, credit and liquidity risk. Reserve asset and risk management principles are laid down in a rule book adopted by the OeNB's Governing Board. The investment of reserve assets is governed by a benchmarking system and is subject to defined limits and durations. Moreover, the OeNB holds separately managed investment portfolios for different asset types and currencies. Regular reports are made to an investment committee and to the Governing Board of the OeNB. Strategies for broadening diversification must be authorized by the Governing Board.

Market Risk

Market risk is the risk of exposure arising from movements in markets, in particular exchange rate and interest rate change, as determined by generally recognized VaR calculation models. Exchange rate risk is controlled through a dual benchmarking system, namely strategic and tactical benchmarks. The strategic benchmarks – which the Governing Board of the OeNB adopts, as a rule, for one-year periods – also define the upper exposure limits. The strategic measures are complemented by tactical benchmarks, which are defined for shorter periods at the regular meetings of the responsible investment committee to reflect e.g. short-term market developments. Interest rate risk is managed on the basis of duration targets or limits. The risk involved in real estate holdings is calculated using the IATX (Immobilien ATX) for real estate stocks.

[7] *A dedicated project will be started in April 2008; it is scheduled to be completed in 2009.*

Credit Risk

Credit risk is the risk of incurring a loss due to the failure of a counterparty. Here, risk management relies on a credit risk limit system which documents current credit risk limits and actual exposure. Credit risk reports reflecting this information as well as information derived from monitoring developments in financial markets are discussed thoroughly at regular investment committee meetings and are reviewed at regular intervals by the Governing Board. Default rates used to calculate credit risk are taken from Standard & Poor's default matrices.

Liquidity Risk

Liquidity risk is the risk arising from a counterparty's inability to meet its financial obligations in time or in full, or the risk that a counterparty may not have sufficiently liquid funds to meet its obligations. To avoid this risk, the OeNB selects counterparties with the highest credit standing and strictly applies the established limits, with a particular emphasis on security and liquidity. These principles take precedence over profitability considerations.

Table 3 shows financial risk and financial provisions on December 31, 2006, and December 31, 2007.

Table 3

Year-End Comparison of Financial Risk and Financial Provisions

Risk	Risk assessment		Financial provisions		
	2007	2006	2007	2006	
	EUR million		EUR million		
Gold risk	1,249	877	1,249[1]	877[1]	Revaluation account
Exchange rate risk	1,344	1,436	–	349	Reserve fund for exchange risks
			37	61	Revaluation accounts
			621	743	Reserve for nondomestic and price risks
			686	283	Risk provisions[2]
	1,344	1,436	1,344	1,436	
Risk of interest rate changes and pro rata Eurosystem risk	1,337	1,230	1,337	1,230	Reserve for nondomestic and price risks
Credit risk	15	–	15	–	Reserve for nondomestic and price risks
Total	**3,945**	**3,543**	**3,945**	**3,543**	
Risk arising from real estate holdings	63	–	Covered by related hidden reserves		

[1] *Holdings on the revaluation accounts came to EUR 2,897 million on December 31, 2007 (EUR 2,194 million on December 31, 2006).*
[2] *Until December 31, 2006: provisions for exchange rate risks.*

Operational Risk

Operational risk is the risk of incurring losses due to defects, inadequate procedures or systems, human error or unforeseen events affecting operations. The OeNB has set up adequate risk controls for operational risk, as laid down in its risk management handbook *ORION – Handbuch Risiko- und Krisenmanagement* (ORION stands for Operationales Risikomanagement in der Oesterreichischen Nationalbank – operational risk management at the Oesterreichische Nationalbank). Risk valuation takes into account the impact of various risk scenarios on the OeNB's reputation, on costs, and any resulting losses. It is an ongoing process, and reports are submitted to management every half year.

IT Security Policy

IT security policy defines guidelines and provisions to guarantee a high level of security for the development, operation and use of IT systems at the OeNB. The following bodies and persons have key responsibilities in the IT security process:

- The IT Security Forum, a body which provides advice on, coordinates and controls IT security;
- The IT security manager, who is responsible for the technical accuracy of the measures submitted for approval as well as for initiating and implementing the IT security process; and
- The IT security experts, who are responsible for drafting and implementing IT security guidelines and IT specifications; and the technical experts in charge of the respective products.

Regular tests and reports are part of the framework of IT security policy.

Capital Movements

Table 4

Movements in Capital Accounts in 2007	December 31, 2006	Increase	Decrease	December 31, 2007
	EUR million	*EUR million*	*EUR million*	*EUR million*
I. Capital				
Capital (stock)	12.000	–	–	12.000
Profit-smoothing reserve	2.226	–	–	2.226
	14.226	–	–	**14.226**
II. Provisions for special business risks				
Reserve for nondomestic and price risks	1,973.263	–	–	1,973.263
	1,973.263	–	–	**1,973.263**
III. Capital including reserves and provisions (I. + II.)	**1,987.489**	–	–	**1,987.489**
IV. Supplementary capital (earmarked)				
OeNB Anniversary Fund for the Promotion of Scientific Research and Teaching				
Initial OeNB Anniversary Fund	31.500	–	–	31.500
OeNB Anniversary Fund National Foundation endowment	1,500.000	–	–	1,500.000
Earmarked capital funded with net interest income from ERP loans	606.796	+7.462	–	614.258
	2,138.296	**+7.462**	–	**2,145.758**
Total capital (III. + IV.)	**4,125.785**	**+7.462**	–	**4,133.247**

For details of the various changes, please refer to the notes to the respective balance sheet items.

Development of the OeNB's Currency Positions in the Financial Year 2007

Table 5

Net currency position (including gold)	December 31, 2007	December 31, 2006	Change	
	EUR million	*EUR million*	*EUR million*	*%*
Gold and gold receivables	5,115.322	4,480.990	+634.332	+14.2
Claims on non-euro area residents denominated in foreign currency[1]	7,192.263	7,207.987	−15.724	−0.2
Claims on euro area residents denominated in foreign currency	1,214.896	1,620.525	−405.629	−25.0
Other assets	158.776	165.514	−6.738	−4.1
less:				
Liabilities to euro area residents denominated in foreign currency	0.075	0.063	+0.012	+20.2
Liabilities to non-euro area residents denominated in foreign currency	676.359	492.750	+183.609	+37.3
Counterpart of SDRs allocated by the IMF	192.294	204.398	−12.104	−5.9
Off balance sheet instruments' revaluation differences	0.127	0.182	−0.055	−30.3
Other liabilities	2.508	3.193	−0.685	−21.5
Revaluation accounts[2]	61.977	23.223	+38.754	+166.9
	12,747.917	12,751.207	−3.290	−0.0
Off balance sheet assets/liabilities (net)	−664.119	110.076	−774.195	−703.3
Total	**12,083.798**	**12,861.283**	**−777.485**	**−6.0**

[1] *December 31, 2006: Excluding the balances at the disposal of the IMF (expressed in euro).*

[2] *Resulting from the change in net unrealized exchange rate gains on foreign currency-denominated securities on December 31, 2006, and December 31, 2007.*

Notes to the Balance Sheet

Assets

1 Gold and Gold Receivables

Closing balance	*EUR million*	
December 31, 2007	5,115.322	
December 31, 2006	4,480.990	
Change	+634.332	(+14.2%)

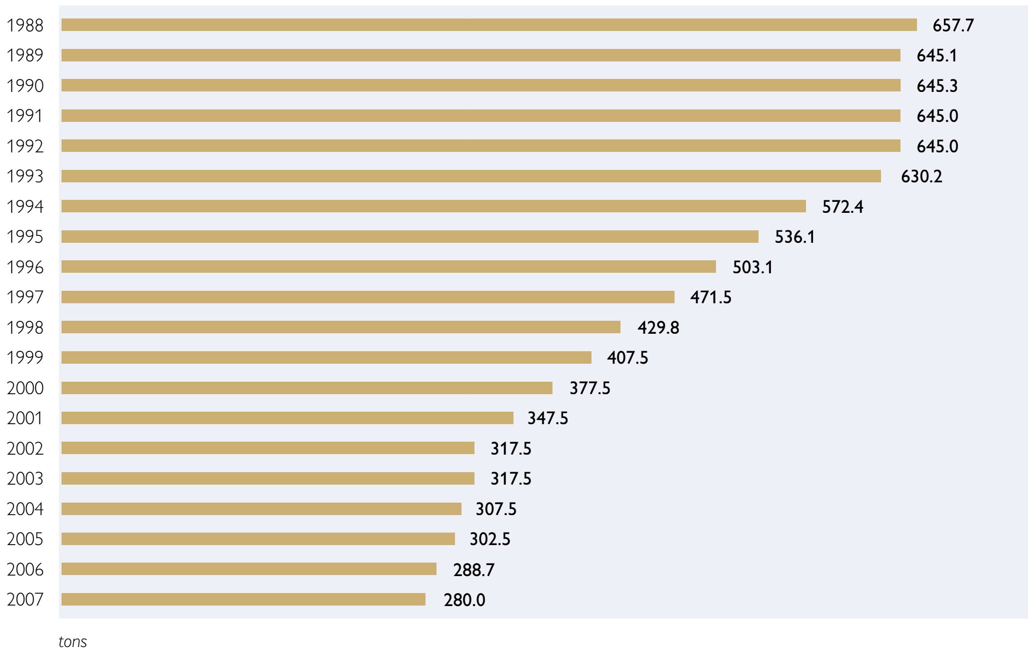
This item comprises the OeNB's holdings of physical and nonphysical gold, which amounted to 9,002,108.684 fine ounces or 279,996.91371 kg of fine gold on December 31, 2007. At a market value of EUR 568.236 per fine ounce (i.e. EUR 18,269.21 per kg of fine gold), the OeNB's gold holdings were worth EUR 5,115.322 million at the balance sheet date.

The valuation on December 31, 2007, resulted in unrealized valuation gains of EUR 2,897.491 million.

In 2007, 8.75 tons of gold were sold for EUR 137.220 million (2006: 13.75 tons for EUR 213.016 million). The sales were made within the framework of the Joint Statement on Gold, which was concluded by 14 central banks (including the OeNB) and the ECB in March 2004 and went into effect from September 27, 2004. The price gains of EUR 117.180 million realized on the sales were disclosed under item 2.1 *Realized gains/losses arising from financial operations* of the profit and loss account.

The Joint Statement on Gold provides for annual sales over a period of five years under a concerted program; annual sales are not to exceed 500 tons and total sales over the five-year period are limited to 2,500 tons. Moreover, gold leasings and the use of gold futures and options must not be increased over this period.

The OeNB's Gold Holdings



Source: OeNB.

Note: Includes the gold holdings transferred via swaps to the EMI and the ECB in 1995 (101.3 tons), 1996 (89.2 tons) and 1997 (71.1 tons).

2 Claims on Non-Euro Area Residents Denominated in Foreign Currency

Closing balance	*EUR million*	
December 31, 2007	7,192.263	
December 31, 2006	5,204.493	
Change	+1,987.770	(+38.2%)

These claims consist of *receivables from the IMF* and claims denominated in foreign currency against non-euro area countries, i.e. counterparties resident outside the euro area.

Table 6 shows the development of *receivables from the IMF.*

Table 6

	December 31, 2007	December 31, 2006	Change	
	EUR million	*EUR million*	*EUR million*	*%*
Total claims (Austrian quota) equivalent to SDR 1,872.3 million[1]	2,010.850	2,137.418	−126.568	−5.9
less:				
Balances at the disposal of the IMF	1,878.274	2,003.495	−125.221	−6.3
Receivables from the IMF	132.576	133.923	−1.347	−1.0
SDR holdings	158.311	144.189	+14.122	+9.8
Other claims against the IMF	7.518	7.991	−0.473	−5.9
Total	**298.405**	**286.103**	**+12.302**	**+4.3**

[1] Pursuant to federal law as promulgated in Federal Law Gazette No. 309/1971, the OeNB assumed the entire Austrian quota at the IMF on its own account on behalf of the Republic of Austria.

Drawings of SDRs on behalf of IMF members; the revaluation, by the IMF, of euro holdings under *balances at the disposal of the IMF*; as well as transfers by the IMF boosted *receivables from the IMF* by a total of EUR 91.863 million. Conversely, repayments by members reduced the *receivables from the IMF* by a total of EUR 47.592 million. Moreover, these claims were adjusted by revaluation losses (–EUR 126.568 million) as well as realized exchange rate gains and book value reconciliation (+EUR 80.950 million).

The IMF remunerates participations in the Fund at a rate of remuneration that is updated weekly. In 2007, this rate hovered between 3.38% and 4.38% per annum, mirroring the prevailing SDR rate.

The SDR holdings[8] were recognized in the balance sheet at EUR 158.311 million on December 31, 2007, which is equivalent to SDR 147.4 million. The net increase of holdings by EUR 14.122 million in 2007 resulted from interest credited, above all remunerations of the participation in the IMF (+EUR 3.424 million), net SDR purchases (+EUR 22.564 million) and revaluation differences (–EUR 9.908 million).

The net purchases referred to above do not reflect any purchases arising from designations by the IMF, under which title no purchases were made in 2007. Principally, the OeNB continues to be obliged under the IMF's statutes to provide currency on demand in exchange for SDRs. Members designated by the IMF may use SDRs up to the point at which the OeNB's SDR holdings are three times as high as the amount it has received gratuitously from the IMF, which totaled SDR 179.045 million on December 31, 2007.

Other claims against the IMF comprise the OeNB's other contributions to loans under special borrowing arrangements, most recently claims arising from contributions to Emergency Assistance for Natural Disasters (EAND).

Table 7 shows the development of *balances with banks and security investments, external loans and other external assets*.

Table 7

	December 31, 2007	December 31, 2006	Change	
	EUR million	*EUR million*	*EUR million*	*%*
Balances with banks	2,384.334	1,774.764	+609.570	+34.3
Securities	4,504.925	3,138.569	+1,366.356	+43.5
Other external assets	4.599	5.057	–0.458	–9.1
Total	**6,893.858**	**4,918.390**	**+1,975.468**	**+40.2**

Balances with banks outside the euro area include foreign currency deposits on correspondent accounts, deposits with agreed maturity, overnight funds and reverse repos. Securities relate to instruments issued by non-euro area residents.

3 Claims on Euro Area Residents Denominated in Foreign Currency

Table 8 shows the development of *claims on euro area residents denominated in foreign currency*.

Table 8

	December 31, 2007	December 31, 2006	Change	
	EUR million	*EUR million*	*EUR million*	*%*
Balances with banks	699.054	835.840	–136.786	–16.4
Securities	515.842	784.685	–268.843	–34.3
Total	**1,214.896**	**1,620.525**	**–405.629**	**–25.0**

[8] *Pursuant to federal law as promulgated in Federal Law Gazette No. 440/1969, the OeNB is entitled to participate in the SDR system on its own account, but on behalf of the Republic of Austria, and to enter the SDRs purchased or allocated gratuitously on the assets side of the balance sheet.*

Claims on euro area residents consist mainly of claims amounting to EUR 699.014 million that arose from reverse operations with Austrian banks totaling USD 1,029.019 million. This U.S. dollar funding was made available in connection with a EUR/USD swap that the ECB made with the Federal Reserve Bank of New York under the Federal Reserve's Term Auction Facility. Under the Term Auction Facility, the Federal Reserve Bank of New York provided the ECB with USD 20 billion by means of a temporary reciprocal currency arrangement (swap line). The ECB simultaneously entered into back-to-back swap transactions with NCBs that have adopted the euro, which used the resulting funds to conduct liquidity-providing operations with the Eurosystem counterparties. These back-to-back swap transactions of the ECB with the OeNB resulted in nonremunerated intra-Eurosystem balances between the ECB and the OeNB reported under liabilities item 10.4 *Other liabilities within the Eurosystem (net).*

4 Claims on Non-Euro Area Residents Denominated in Euro

Table 9 shows the development of *claims on non-euro area residents denominated in euro* on December 31, 2006, and December 31, 2007.

Table 9

	December 31, 2007	December 31, 2006	Change	
	EUR million	*EUR million*	*EUR million*	%
Securities investments	975.738	596.205	+379.533	+63.7
Other investments	10.860	8.063	+2.797	+34.7
Total	**986.598**	**604.268**	**+382.330**	**+63.3**

5 Lending to Euro Area Credit Institutions Related to Monetary Policy Operations Denominated in Euro

Table 10 shows the development of liquidity-providing transactions executed by the OeNB.

Table 10

	December 31, 2007	December 31, 2006	Change	
	EUR million	*EUR million*	*EUR million*	%
5.1 Main refinancing operations	8,703.193	9,286.524	−583.331	−6.3
5.2 Longer-term refinancing operations	3,991.474	2,864.419	+1,127.055	+39.3
5.3 Fine-tuning reverse operations	–	–	–	–
5.4 Structural reverse operations	–	–	–	–
5.5 Marginal lending facility	–	–	–	–
5.6 Credits related to margin calls	–	–	–	–
Total	**12,694.667**	**12,150.943**	**+543.724**	**+4.5**

5.1 Main Refinancing Operations

Main refinancing operations are regular liquidity-providing reverse transactions, carried out by the Eurosystem NCBs with a weekly frequency in the form of standard (variable or fixed rate) tender operations. Since March 8, 2004, the maturity of the standard tender has been one week. All counterparties which fulfill the general eligibility criteria may submit bids within a timeframe of 24 hours from the tender announcement.

Table 11 shows the increases in the minimum bid rate on the main refinancing operations of the Eurosystem in 2007 as decided by the Governing Council of the ECB.

Table 11

Decision of	With effect from	By (percentage point)	To (%)
March 8, 2007	March 14, 2007	+0.25	3.75
June 6, 2007	June 13, 2007	+0.25	4.00

5.2 Longer-Term Refinancing Operations

Longer-term refinancing operations are regular liquidity-providing reverse transactions, carried out in the form of variable rate tenders, with a monthly frequency and a maturity of three months. They are aimed at providing counterparties with additional longer-term refinancing and are executed through standard tenders by the NCBs.

5.3 Fine-Tuning Reverse Operations

Fine-tuning reverse operations are executed on an ad hoc basis with a view to managing the liquidity situation in the market and steering interest rates, in particular to smooth the effects on interest rates caused by unexpected liquidity fluctuations in the market. The choice of fine-tuning instruments and procedures depends on the type of transaction and its underlying objective. Fine-tuning operations are normally executed by the NCBs through quick tenders or through bilateral procedures. The Governing Council of the ECB may empower the ECB to conduct fine-tuning operations itself under exceptional circumstances.

In 2007, the OeNB conducted four such operations with volumes of between EUR 200.000 million and EUR 1,150.000 million.

5.4 Structural Reverse Operations

In 2007, no such operations were carried out.

5.5 Marginal Lending Facility

The financial sector may use the *marginal lending facility* to obtain overnight liquidity from NCBs at a prespecified interest rate against eligible assets. The facility is intended to satisfy counterparties' temporary liquidity needs. Under normal circumstances, the interest rate on the facility provides a ceiling for the overnight interest rate.

Recourse to the *marginal lending facility* averaged EUR 2.568 million in 2007.

Table 12 shows the increases in the interest rate on the *marginal lending facility* in 2007 as decided by the Governing Council of the ECB.

Table 12

Decision of	With effect from	By (percentage point)	To (%)
March 8, 2007	March 14, 2007	+0.25	4.75
June 6, 2007	June 13, 2007	+0.25	5.00

6 Other Claims on Euro Area Credit Institutions Denominated in Euro

Closing balance	EUR million	
December 31, 2007	0.127	
December 31, 2006	0.115	
Change	+0.012	(+10.8%)

This item comprises claims not related to monetary policy operations.

7 Securities of Euro Area Residents Denominated in Euro

Closing balance	EUR million	
December 31, 2007	4,633.276	
December 31, 2006	3,276.539	
Change	+1,356.737	(+41.4%)

This item covers all marketable securities that are not used in monetary policy operations and that are not part of investment portfolios earmarked for specific purposes.

The annual change is mainly attributable to net purchases.

8 General Government Debt Denominated in Euro

Closing balance	EUR million	
December 31, 2007	418.633	
December 31, 2006	424.308	
Change	−5.675	(−1.3%)

This balance sheet item exclusively subsumes the claim on the Austrian Federal Treasury from silver commemorative coins issued before 1989, based on the 1988 Coinage Act as promulgated in Federal Law Gazette No. 425/1996.

In theory, the maximum federal liability is the sum total of all silver commemorative coins issued before 1989, minus any coins returned to and paid for by the central government, minus any coins directly withdrawn by Münze Österreich AG and minus repayments, which are effected by annual installments of EUR 5.814 million out of the *central government's share* in the OeNB's profit. The proceeds from silver recovery, including the interest on the investment of these proceeds by Münze Österreich AG, are designated for repayment by the contractual deadline (every year on December 15). Any amount outstanding on December 31, 2040, will have to be repaid in the five following years (2041 to 2045) in five equal installments. The federal liability came to EUR 1,190.350 million on December 31, 2007.

The net increase in *general government debt* resulted from returns of silver commemorative coins to the central government in the course of 2006 with a total face value of EUR 8.119 million not offset by redemptions made out of the central government's share in the OeNB's profit for the year 2006 or the proceeds from metal recovery (which together totaled EUR 13.794 million).

9 Intra-Eurosystem Claims

Closing balance	EUR million	
December 31, 2007	19,964.089	
December 31, 2006	16,950.771	
Change	+3,013.318	(+17.8%)

This balance sheet item consists of the claims arising from the OeNB's share in the ECB's capital and the claims equivalent to the transfer of foreign reserves to the ECB. Furthermore, this item shows net claims related to the allocation of euro banknotes within the Eurosystem.

Table 13 shows the development of *intra-Eurosystem claims* on December 31, 2006, and December 31, 2007.

Table 13

	December 31, 2007	December 31, 2006	Change	
	EUR million	EUR million	EUR million	%
9.1 Participating interest in the ECB	117.187	116.476	+0.711	+0.6
9.2 Claims equivalent to the transfer of foreign reserves	1,161.290	1,157.451	+3.839	+0.3
9.3 Claims related to promissory notes backing the issuance of ECB debt certificates[1]	×	×	×	×
9.4 Net claims related to the allocation of euro banknotes within the Eurosystem	18,685.612	15,676.844	+3,008.768	+19.2
9.5 Other claims within the Eurosystem (net)	–	–	–	–
Total	**19,964.089**	**16,950.771**	**+3,013.318**	**+17.8**

[1] *Only an ECB balance sheet item.*

9.1 Participating Interest in the ECB

This subitem shows the share that the OeNB holds in the capital of the ECB. With the accession of Bulgaria and Romania to the EU and their NCBs' membership in the ESCB on January 1, 2007, the relative shares of the NCBs in the capital of the ECB (the ECB's "capital key," last changed on May 1, 2004) had to be adjusted. In this connection, the ECB's subscribed capital was automatically increased under Article 49.3 ESCB Statute. Since January 1, 2007, the OeNB's share of the ECB's subscribed capital has been 2.0159%, and its share of the ECB's fully paid-in capital (i.e., paid in by the central banks participating in the Eurosystem) has been 2.9002%. The increase of the *participating interest in the ECB* by a total of EUR 0.711 million represents the financial effect of the entry of the Bulgarian and Romanian NCBs into the ESCB.

See the *Notes on Off Balance Sheet Positions* for information about additional capital contributions transferred to the ECB.

9.2 Claims Equivalent to the Transfer of Foreign Reserves

This item represents the OeNB's claims arising from the transfer of foreign reserve assets to the ECB. The claims are denominated in euro at the original conversion rate. They are remunerated at the latest available marginal rate for the Eurosystem's main refinancing operations, adjusted to reflect a zero return on the gold component.

The adjustments to the ECB's capital key following the accession of Slovenia to the euro area on January 1, 2007, and the resulting changes in NCBs' capital shares entailed an adjustment of the NCBs' euro claims equivalent to the foreign reserve assets transferred to the ECB. As the OeNB's subscribed share of the ECB's capital rose in absolute terms, the OeNB's euro-denominated claims equivalent to the transfer of foreign reserves augmented by EUR 3.839 million to EUR 1,161.290 million.

See the *Notes on Off Balance Sheet Positions* for information about additional capital contributions transferred to the ECB.

9.4 Net Claims Related to the Allocation of Euro Banknotes within the Eurosystem

This item reflects the OeNB's claims vis-à-vis the Eurosystem relating to the allocation of euro banknotes within the Eurosystem (see also the section *Banknotes in Circulation and Intra-Eurosystem Balances*).

10 Items in Course of Settlement

This claim results from 2007 net float items settled at the beginning of January 2008.

11 Other Assets

Table 14 shows the development of *other assets*.

Table 14

	December 31, 2007	December 31, 2006	Change	
	EUR million	*EUR million*	*EUR million*	%
11.1 Coins of euro area	140.655	136.914	+3.741	+2.7
11.2 Tangible and intangible fixed assets	147.686	153.844	−6.158	−4.0
11.3 Other financial assets	7,719.124	6,795.448	+923.676	+13.6
11.4 Off balance sheet instruments' revaluation differences	18.330	11.680	+6.650	+56.9
11.5 Accruals and prepaid expenses	597.241	437.974	+159.267	+36.4
11.6 Sundry	1,002.352	1,026.054	−23.702	−2.3
Total	**9,625.388**	**8,561.914**	**+1,063.474**	**+12.4**

11.1 Coins of Euro Area

This item represents the OeNB's stock of fit euro coins issued by euro area countries.

11.2 Tangible and Intangible Fixed Assets

Tangible and intangible fixed assets comprise OeNB *premises* and *equipment* (including computers, related hardware and software, and motor vehicles), *tangible real assets* and *intangible fixed assets*.

Table 15 shows the development of *premises*.

Table 15

	EUR million
Cost incurred until December 31, 2006 [1]	116.887
Purchases in 2007	0.037
Sales (cost incurred) in 2007	0.033
Accumulated depreciation	30.802
Book value on December 31, 2007	86.090
Book value on December 31, 2006	90.439
Annual depreciation in 2007	4.386

[1] *Premises acquired prior to December 31, 1956, were booked at the cost recorded in the schilling opening balance sheet (Federal Law Gazette No. 190/1954).*

Table 16 shows the development of *equipment*.

Table 16

	EUR million
Cost incurred until December 31, 2006	83.868
Purchases in 2007	7.186
Sales (cost incurred) in 2007 [1]	8.207
Accumulated depreciation	60.291
Book value on December 31, 2007	22.556
Book value on December 31, 2006	24.353
Annual depreciation in 2007	8.924

[1] *The balance between the book value of the sales and the underlying historical costs less accumulated depreciation is EUR 0.060 million.*

Table 17 shows *tangible real assets* (the OeNB's collection of antique string instruments and the coins of the OeNB's Money Museum).

Table 17

	EUR million
Cost incurred until December 31, 2006	34.546
Purchases in 2007	0.003
Sales (cost incurred) in 2007	–
Accumulated depreciation	1.600
Revaluation	5.494
Book value on December 31, 2007	38.443
Book value on December 31, 2006	38.440
Annual depreciation in 2007	–

On December 31, 2007, the OeNB's collection of valuable instruments encompassed 28 violins, 5 violoncellos and 3 violas. The string instruments are on loan to renowned musicians under the OeNB's cultural promotion program.

Table 18 shows the development of *intangible fixed assets* (right of use).

Table 18

	EUR million
Cost incurred until December 31, 2006	0.720
Purchases in 2007	–
Sales in 2007	–
Accumulated depreciation[1]	0.123
Book value on December 31, 2007	0.597
Book value on December 31, 2006	0.612
Annual depreciation in 2007[1]	0.015

[1] *Depreciation is over a period of 46.75 years.*

11.3 Other Financial Assets

Table 19 shows the development of *other financial assets*.

Table 19

	December 31, 2007	December 31, 2006	Change	
	EUR million	EUR million	EUR million	%
Securities	6,181.359	5,533.925	+647.434	+11.7
Participating interests	880.786	849.731	+31.055	+3.7
Other investments	656.979	411.792	+245.187	+59.5
Total	**7,719.124**	**6,795.448**	**+923.676**	**+13.6**

Of the OeNB's securities portfolio, EUR 1,493.733 million represented investments of pension reserve assets, another EUR 1,523.160 million reflect investments of the *OeNB Anniversary Fund for the Promotion of Scientific Research and Teaching* (of which EUR 1,492.770 million were earmarked as an endowment for the National Foundation for Research, Technology and Development). Securities held as permanent investment (financial fixed assets) amounted to EUR 820.512 million, and the securities portfolio related to capital and reserves, i.e. the OeNB's own funds management, came to EUR 2,343.954 million.[9] Revaluations of the portfolios resulted in unrealized price gains of EUR 8.407 million and unrealized price losses totaling EUR 15.786 million as well as unrealized foreign currency gains of EUR 0.130 million.

Of the *participating interests*, EUR 566.257 million formed part of the own funds portfolio and EUR 314.529 million part of the investment portfolio relating to investments of the pension reserve.

Table 20 shows the development of *participating interests*.

Table 20

	EUR million
Net asset value on December 31, 2006	849.731
Purchases in 2007	–
Sales in 2007 (at book value)	0
Annual depreciation in 2007	0.083
Revaluation in 2007	31.138
Net asset value on December 31, 2007	880.786

Other investments include investments of the pension reserve (EUR 112.133 million), investments to promote the National Foundation (EUR 53.964 million), investments of the initial OeNB Anniversary Fund (i.e. exclusive of the National Foundation endowment; EUR 26.509 million) and the own funds portfolio (EUR 464.373 million) and consisted mainly of overnight and short-term funds.

11.4 Off Balance Sheet Instruments' Revaluation Differences

Closing balance	*EUR million*	
December 31, 2007	18.330	
December 31, 2006	11.680	
Change	+6.650	(+56.9%)

This item reflects revaluation gains arising on off balance sheet positions (for which an offsetting entry is made under liabilities item 14 *Revaluation accounts*. On December 31, 2007, these gains totaled EUR 18.330 million. EUR 4.559 million of this amount were attributable to valuation gains on gold interest rate swaps. The remainder, EUR 13.771 million, results from book value reconciliations and realized gains relating to off balance sheet transactions.

[9] *The OeNB's own funds shown under liabilities include its capital, the reserve for nondomestic and price risks, the profit-smoothing reserve, earmarked ERP capital, the reserve fund for exchange rate risks (fully drawn down on December 31, 2007) and the risk provisions.*

11.6 Sundry

Table 21 shows the development of *sundry* assets.

Table 21

	December 31, 2007	December 31, 2006	Change	
	EUR million	EUR million	EUR million	%
Claims arising from ERP loans to companies	880.569	917.411	−36.842	−4.0
Money market investment with the Oesterreichische Kontrollbank (OeKB) for ERP lending	75.644	31.341	+44.303	+141.4
ERP loan portfolio managed by the OeNB	956.213	948.752	+7.461	+0.8
Settlement account with the tax authorities	–	29.350	−29.350	−100.0
Schilling coins	14.144	8.346	+5.798	+69.5
Shareholder loans	4.032	4.928	−0.896	−18.2
Advances on salaries	7.676	6.935	+0.741	+10.7
Claims arising from real estate sales to subsidiaries	–	3.333	−3.333	−100.0
Other claims	20.287	24.410	−4.123	−16.9
Total	**1,002.352**	**1,026.054**	**−23.702**	**−2.3**

Pursuant to Article 3 paragraph 2 ERP Fund Act, the OeNB's maximum financing commitment corresponds to the sum by which the federal debt was written down initially (EUR 341.955 million) plus interest accrued on a reserve account (EUR 614.258 million on December 31, 2007). The ERP loan portfolio managed by the OeNB thus totaled EUR 956.213 million on December 31, 2007. The provisions governing the extension of loans from this portfolio are laid down in Article 83 Nationalbank Act.

The residual terms of advances on salaries generally exceed one year. All advance payments are secured by life insurance plans.

Other claims came to EUR 20.287 million at December 31, 2007, and mainly comprised advances, accounts receivable and claims arising from day-to-day business.

Liabilities

1 Banknotes in Circulation

Closing balance	EUR million	
December 31, 2007	18,052.675	
December 31, 2006	16,814.844	
Change	+1,237.831	(+7.4%)

This item reflects the value of euro *banknotes in circulation* allocated to the OeNB. Table 22 shows how this share is calculated and how it developed in 2007.

Table 22

	December 31, 2007	December 31, 2006	Change
	EUR million	*EUR million*	*EUR million*
Total value of euro banknotes actually put in circulation by the OeNB	−632.937	1,138.000	−1,770.937
Adjusted for:			
Liability resulting from the share of euro banknotes in circulation allocated to the ECB (8%)	−1,569.902	−1,462.274	−107.628
Claims related to the allocation of euro banknotes within the Eurosystem	+20,255.514	+17,139.118	+3,116.396
Net claims related to the allocation of euro banknotes within the Eurosystem	+18,685.612	+15,676.844	+3,008.768
Banknotes in circulation	**18,052.675**	**16,814.844**	**+1,237.831**

See the sections *Banknotes in Circulation and Intra-Eurosystem Balances* for further explanations on this item.

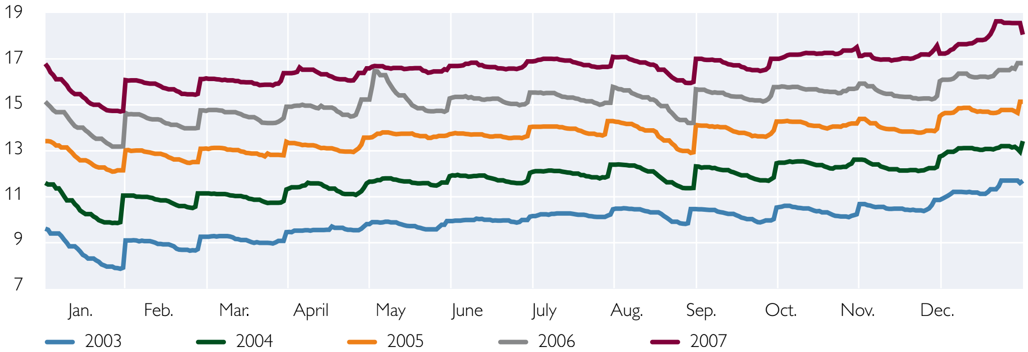
Table 23 shows the annual averages of *banknotes in circulation* during the past five years.

Table 23

	Banknotes in circulation, annual average	Change	
	EUR million	*EUR million*	%
2003	9,913	+1,026	+11.5
2004	11,751	+1,838	+18.5
2005	13,618	+1,867	+15.9
2006	15,128	+1,510	+11.1
2007	16,614	+1,486	+9.8

The OeNB's Banknotes in Circulation over the Past Five Years

Calendar-day volumes, EUR billion



Source: OeNB.

2 Liabilities to Euro Area Credit Institutions Related to Monetary Policy Operations Denominated in Euro

Table 24 shows the development of *liabilities to euro area credit institutions related to monetary policy operations denominated in euro.*

Table 24

	December 31, 2007	December 31, 2006	Change	
	EUR million	*EUR million*	*EUR million*	*%*
2.1 Current accounts (covering the minimum reserve system)	6,153.091	4,429.030	+1,724.061	+38.9
2.2 Deposit facility	395.000	44.500	+350.500	+787.6
2.3 Fixed-term deposits	–	–	–	–
2.4 Fine-tuning reverse operations	–	–	–	–
2.5 Deposits related to margin calls	–	–	–	–
Total	**6,548.091**	**4,473.530**	**+2,074.561**	**+46.4**

2.1 Current Accounts (Covering the Minimum Reserve System)

This subitem contains the transaction accounts of credit institutions which are required to hold minimum reserves.

Banks' minimum reserve balances have been remunerated since January 1, 1999, at the prevailing interest rate for the Eurosystem's main refinancing operations.

2.2 Deposit Facility

The *deposit facility* refers to overnight deposits placed with the OeNB by Austrian banks that access the Eurosystem's liquidity-absorbing standing facility at the pre-specified rate. In 2007, the volume of such transactions averaged EUR 44.402 million.

Table 25 shows the increases in the interest rate on the *deposit facility* as decided by the Governing Council of the ECB.

Table 25

Decision of	With effect from	By (percentage point)	To (%)
March 8, 2007	March 14, 2007	+0.25	2.75
June 6, 2007	June 13, 2007	+0.25	3.00

5 Liabilities to Other Euro Area Residents Denominated in Euro

Closing balance	EUR million	
December 31, 2007	16.641	
December 31, 2006	5.828	
Change	+10.813	(+185.6%)

This item comprises general government deposits of EUR 10.799 million and current account deposits of credit institutions that are not subject to minimum reserve requirements, and current account deposits of nonbanks.

6 Liabilities to Non-Euro Area Residents Denominated in Euro

Closing balance	EUR million	
December 31, 2007	14.785	
December 31, 2006	13.772	
Change	+1.013	(+7.3%)

This item comprises euro-denominated liabilities to non-Eurosystem central banks and monetary institutions.

8 Liabilities to Non-Euro Area Residents Denominated in Foreign Currency

Closing balance	EUR million	
December 31, 2007	676.359	
December 31, 2006	492.750	
Change	+183.609	(+37.3%)

This item shows liabilities resulting from repurchase agreements.

9 Counterpart of Special Drawing Rights Allocated by the IMF

Closing balance	EUR million	
December 31, 2007	192.294	
December 31, 2006	204.398	
Change	−12.104	(−5.9%)

This item represents the counterpart in euro of the SDR 179 million allocated gratuitously to the OeNB, measured at current market values at the reporting date. The OeNB was allocated SDRs from 1970 to 1972 and from 1979 to 1981, always on January 1.

10 Intra-Eurosystem Liabilities

Closing balance	EUR million	
December 31, 2007	25,402.202	
December 31, 2006	21,160.054	
Change	+4,242.148	(+20.0%)

This item shows the OeNB's net liabilities arising from transactions with the 12 other NCBs participating in the Eurosystem in 2007 as well as six ESCB central banks (the Bank of England, Danmarks Nationalbank, Latvijas Bank, Lietuvos bankas, the Central Bank of Cyprus and the Central Bank of Malta) and with the ECB (in particular balances arising in connection with the TARGET payment system). Moreover, this item covers net claims arising at year-end from the difference between monetary income to be pooled and distributed, and the balances arising from any redistribution of ECB seigniorage income.

The individual bilateral end-of-day balances of the OeNB with the other NCBs are netted by novating them to the respective bilateral account with the ECB. The ECB remunerates the net balance at the prevailing marginal interest rate for the Eurosystem's main refinancing operations.

11 Items in Course of Settlement

This claim results from 2007 net float items settled at the beginning of January 2008.

12 Other Liabilities

Table 26 shows the development of *other liabilities*.

Table 26

	December 31, 2007	December 31, 2006	Change	
	EUR million	*EUR million*	*EUR million*	*%*
12.1 Off balance sheet instruments' revaluation differences	0.127	0.182	−0.055	−30.3
12.2 Accruals and income collected in advance	96.759	73.489	+23.270	+31.7
12.3 Sundry	376.067	361.743	+14.324	+4.0
Total	**472.953**	**435.414**	**+37.539**	**+8.6**

12.1 Off Balance Sheet Instruments' Revaluation Differences

Off balance sheet instruments' revaluation differences subsumes the revaluation losses arising on off balance sheet positions, which are posted to the profit and loss account, and book value reconciliation.

12.3 Sundry

Table 27 shows the development of *sundry* liabilities.

Table 27

	December 31, 2007	December 31, 2006	Change	
	EUR million	*EUR million*	*EUR million*	*%*
Central government's share of profit (without dividends)	149.848	130.244	+19.604	+15.1
Liability from schilling banknotes in circulation with an exchange deadline	150.337	167.080	−16.743	−10.0
Earmarked funds of the OeNB Anniversary Fund				
Initial OeNB Anniversary Fund	25.607	23.793	+1.814	+7.6
OeNB Anniversary Fund National Foundation endowment	46.734	34.419	+12.315	+35.8
Other	3.541	6.207	−2.666	−43.0
Total	**376.067**	**361.743**	**+14.324**	**+4.0**

Pursuant to Article 69 paragraph 3 Nationalbank Act, the *central government's share of profit* corresponds to 90% of the profit for the year after tax.

The reduction of the subitem *liabilities from schilling banknotes in circulation with an exchange deadline* is attributable to exchanges of banknotes and closure of acceptance for the 500 schilling banknote with the portrait of Josef Ressel, the third banknote for which the exchange period has ended since the introduction of the euro.

According to the General Meeting's decision, EUR 8.741 million of the *profit for the year 2006* were apportioned to the *OeNB's Anniversary Fund for the Promotion of Scientific Research and Teaching*. Adjusted for the return on investment for 2007 and repayments made, the initial OeNB Anniversary Fund thus received funds totaling EUR 38.649 million. Of these funds, EUR 13.042 million were paid out in 2007; EUR 18.847 million of the remaining undisbursed funds of EUR 25.607 million have been pledged. In 2007, the General Council voted to allocate an additional EUR 10.840 million to fund 164 projects and EUR 3.580 million to fund three institutes. This means that since funds were first pledged as financial assistance in 1966, a total EUR 694.416 million have been paid out.

The EUR 46.734 million the OeNB Anniversary Fund provided for the National Foundation are earmarked pro rata income for 2007; payment to the National Foundation is made the day after the General Meeting.

13 Provisions

Table 28

	December 31, 2006	Transfer from	Transfer to	December 31, 2007
	EUR million	*EUR million*	*EUR million*	*EUR million*
Pension reserve	1,893.116	−100.876	+98.942	1,891.182
Personnel provisions				
Severance payments	52.864	−2.194	+5.455	56.125
Anniversary bonuses	10.963	−1.218	+1.228	10.973
Residual leave entitlements	9.534	−0.233	+0.556	9.857
Supplementary contributions to pension plans	2.509	−0.188	–	2.321
Other	0.932	−0.042	–	0.890
Statutory or contractual social charges	0.086	−0.086	+0.090	0.090
Salary cost revisions in 2006 and 2007	0.481	−0.481	+0.402	0.402
Provisions for				
Financial risk	283.000	−3.844	+407.000	686.156
Schilling banknotes without an exchange deadline	202.286	−9.436	–	192.850
Corporate income tax	–	–	+11.469	11.469
Accounts payable	0.700	−0.700	+2.016	2.016
Accounts payable to subsidiaries	3.735	−3.735	+0.883	0.883
Other	0.648	−0.379	+0.359	0.628
Total	**2,460.854**	**−123.412**	**+528.400**	**2,865.842**

Under its initial retirement plan, the OeNB assumed full liability to provide retirement benefits to all employees recruited up to April 30, 1998. To cover this liability, the OeNB is obligated by law to hold a *pension reserve* corresponding to the actuarial present value of its pension liabilities.

Following a change in the retirement plan, staff recruited after May 1, 1998, stands to receive a state pension supplemented by an occupational pension from an externally managed pension fund. For this supplementary pension, the OeNB took out a contract effective May 1, 1999, which also applies retroactively to employees taken on in the 12 months from May 1, 1998. With the OeNB's direct liability to pay retirement benefits now limited to staff recruited before May 1, 1998, the *pension reserve* set up to secure this liability has become a closed system. The OeNB taps this *pension reserve* to pay out retirement benefits.

Pension payments covered by the *pension reserve* augmented by EUR 4.006 million or 4.1% to EUR 100.876 million in 2007. This includes the remuneration of 14 retired board members or their dependents (totaling EUR 4.200 million; 2006: 15 persons at EUR 4.183 million).

In addition to transfers under the Nationalbank Act, the income on investment relating to the *pension reserve* was transferred to the *pension reserve* on December 31,

2007. Including gains in the value of assets credited to the *revaluation accounts*, these figures add up to EUR 1,891.182 million. According to actuarial calculations, this sum corresponds to 100.18% of the capital coverage needed to meet the pension of OeNB employees on December 31, 2007. The *pension reserve* is shown at its actuarial present value, based on a discount rate of 3.85% per annum (unchanged from 2006).[10]

Given the potential need for the OeNB to pay one-off supplementary contributions to staff pension plans, the OeNB's financial statements include dedicated provisions based on actuarial principles. The corresponding amounts are based on a discount rate of 3.50% per annum.

At its meeting on October 12, 2006, the General Council adopted Conditions of Service for staff employed by the OeNB after December 31, 2006. An important feature of the Conditions of Service applicable to such staff is a further modification of the defined contribution scheme introduced earlier.

Provisions for severance payments and anniversary bonuses are calculated according to actuarial principles; the discount rate of 3.50% per annum is the same as that applied in 2006.

The risk provisions serve to cover financial risks (see table 3).

The provision for *schilling banknotes without an exchange deadline* was drawn down for exchanges of schilling banknotes.

No provisions for pending lawsuits were made, as the latter are not expected to have a material impact.

14 Revaluation Accounts

The amounts on the *revaluation accounts* reflect the valuation gains established in the course of the valuation of assets as on December 31, 2007. Those gains are realizable only in the context of future transactions in the respective category or may be used to reverse revaluation losses that may arise in future years. The revaluation gains in each currency cover the risk associated with nondomestic assets (as established with the VaR method).

[10] *The discount rate is evaluated annually. It is calculated on the basis of the actual investment yield, taking into account general increases in salaries and expected yields. Marginal deviations in the future need not automatically entail an adjustment of the discount rate.*

Table 29 shows the development of *revaluation accounts*.

Table 29

	December 31, 2007	December 31, 2006	Change	
	EUR million	*EUR million*	*EUR million*	*%*
Revaluation accounts				
Gold	2,897.491	2,193.855	+703.636	+32.1
Foreign currency	36.570	61.568	−24.998	−40.6
Securities	69.602	73.532	−3.930	−5.3
Participating interests	242.411	211.273	+31.138	+14.7
Off balance sheet instruments	4.559	6.604	−2.045	−31.0
Total	3,250.633	2,546.832	+703.801	+27.6
Unrealized valuation gains from January 1, 1999 (initial valuation)				
Securities	–	1.423	−1.423	−100.0
Participating interests	278.807	278.807	–	–
Total	278.807	280.230	−1.423	−0.5
Reserve fund for exchange rate risks (funded up to the end of 1998)	–	349.050	−349.050	−100.0
Total	**3,529.440**	**3,176.112**	**+353.328**	**+11.1**

In line with requirements, the initial valuation gains recorded in the opening balance sheet of January 1, 1999, were partly realized during 2007 in the course of sales of underlying assets.

Article 69 paragraph 1 Nationalbank Act obliges the OeNB to maintain a *reserve fund for exchange rate risks* which may arise on nondomestic assets. In connection with exchange gains on sales of gold and foreign exchange and the coverage of unrealized exchange losses, this reserve was fully drawn down on December 31, 2007.

15 Capital and Reserves

According to Article 8 paragraph 1 Nationalbank Act, the *capital* of the OeNB (liability item 15.1) is EUR 12.000 million and is divided equally into 150,000 registered shares.

Table 30 shows the development of *capital and reserves*.

Table 30

	December 31, 2007	December 31, 2006	Change	
	EUR million	*EUR million*	*EUR million*	*%*
Profit-smoothing reserve	2.226	2.226	–	–
Reserve for nondomestic and price risks	1,973.263	1,973.263	–	–
OeNB Anniversary Fund for the Promotion of Scientific Research and Teaching	1,531.500	1,531.500	–	–
Earmarked capital funded with net interest income from ERP loans	614.258	606.796	+7.462	+1.2
Total	**4,121.247**	**4,113.785**	**+7.462**	**+0.2**

The *reserve for nondomestic and price risks* serves to cover the risks associated with foreign currency and security prices. The section *Risk Management* contains more information on the OeNB's risk management principles.

Since 2003, the capital of the OeNB's Anniversary Fund for the Promotion of Scientific Research and Teaching (EUR 1,531.500 million) has consisted of its initial funding (EUR 31.500 million) and of an endowment to support the National Foundation (EUR 1,500.000 million).

The initial funding of EUR 31.500 million of EUR 7.267 million apportioned from the *net income* for the year 1965 in April 1966 and EUR 24.233 million allocated from the *profit for the year* 2002 in May 2003.

The endowment of EUR 1,500.000 million for the National Foundation was established in 2003 by earmarking funds reappropriated from the *freely disposable reserve fund* (EUR 545.000 million) and from the *general reserve fund* (EUR 955.000 million).

Earmarked ERP capital funded with net interest income from loans represents the cumulative interest income accruing to the OeNB from lending out of the ERP loan portfolio managed by the OeNB. Appropriation of this ERP capital is subject to international law; it is earmarked exclusively for ERP loans.

Notes on Off Balance Sheet Positions

The following financial assets and liabilities of the OeNB were stated off the balance sheet on December 31, 2007:

– obligation under the IMF's statutes to provide currency on demand in exchange for SDRs up to the point at which the OeNB's SDR holdings are three times as high as the amount it has received gratuitously from the IMF, which was equivalent to EUR 418.573 million on December 31, 2007;
– contingent liabilities to the IMF under the *New Arrangements to Borrow*, equivalent to EUR 438.192 million;
– obligation to make a supplementary contribution of EUR 34.492 million to the OeNB's stake in the capital of the Bank for International Settlements (BIS) in Basel consisting of 8,564 shares of SDR 5,000 each;
– forward purchases (EUR 1,020.642 million) and sales (EUR 1,006.871 million) consisting of swaps and euro- as well as foreign currency-denominated forward transactions; the forward sales include the forward liabilities to the ECB outstanding as at December 31, 2007, which arose in connection with U.S. dollar funding established by the Federal Reserve under the Federal Reserve's Term Auction Facility;
– contingent liabilities arising from the coverage of gold investments (EUR 574.969 million);
– Liabilities of EUR 16.166 million from foreign currency investments effected in the OeNB's name for third account;
– repayment obligations to the amount of EUR 20.928 million arising from pension contributions paid by OeNB staff members payable on termination of employment contracts;
– a contingent liability of EUR 1,007.950 million, equivalent to the OeNB's share of the maximum of EUR 50 billion reserve assets that the ECB may require the euro area NCBs to transfer under Article 30.1 ESCB Statute (based on the OeNB's share of 2.0159% in the ECB's subscribed capital as on December 31, 2007);

– a contingent liability of EUR 100.795 million, equivalent to the OeNB's share of the ECB's capital of EUR 5 billion, should the ECB increase its capital by such amount under Article 28.1 ESCB Statute (based on the OeNB's share in the ECB's subscribed capital of 2.0159% at the balance sheet date);
– contingent liabilities of EUR 144.740 million arising from bank guarantees given and contingent assets of EUR 6.093 million arising from bank guarantees received.

At the current juncture, no substantiated figures about the possible material impact on the OeNB of lawsuits pending against the Republic of Austria in a bankruptcy case can be provided.

Table 31 shows *holdings of derivatives* on December 31, 2007.

Table 31

	Underlying value *EUR million*	Market value gains *EUR million*	Market value losses *EUR million*
Gold interest rate swaps			
Sales	145.468	4.432	–

The market values represent the valuation of December 31, 2007, with gains of EUR 4.559 million less a depreciation of EUR 0.127 million effected in previous years entered in the *revaluation accounts* (liability item 14).

Notes to the Profit and Loss Account

Table 32

	2007 *EUR million*	2006 *EUR million*	Change[1] *EUR million*	 *%*
1 Net interest income	738.315	567.569	+170.746	+30.1
2 Net result of financial operations, writedowns and risk provisions	−290.246	−174.641	+115.605	+66.2
3 Net income from fees and commissions	3.386	1.919	+1.467	+76.4
4 Income from equity shares and participating interests	22.587	25.202	−2.615	−10.4
5 Net result of pooling of monetary income	7.317	6.343	+0.974	+15.4
6 Other income	9.192	10.233	−1.041	−10.2
Total net income	**490.551**	**436.625**	**+53.926**	**+12.4**
7 Staff costs	−107.521	−115.316	−7.795	−6.8
8 Administrative expenses	−78.343	−76.997	+1.346	+1.7
9 Depreciation of tangible and intangible fixed assets	−13.325	−14.142	−0.817	−5.8
10 Banknote production services	−24.841	−24.574	+0.267	+1.1
11 Other expenses	−19.858	−12.641	+7.217	+57.1
Total expenses	**−243.888**	**−243.670**	**+0.218**	**+0.1**
Operating profit	**246.663**	**192.955**	**+53.708**	**+27.8**
12 Corporate income tax	−61.666	−48.239	+13.427	+27.8
	184.997	144.716	+40.281	+27.8
13 Transfers to the pension reserve and central government's share of profit	−168.347	−130.244	+38.103	+29.3
14 Profit for the year	**16.650**	**14.472**	**+2.178**	**+15.1**

[1] *Absolute increase (+) or decrease (–) in the respective item.*

Operating Profit over the Past Five Years

Source: OeNB.

1 Net Interest Income

Net interest income represents the balance of interest income and interest expense.

Net interest income from assets and liabilities denominated in foreign currency totaled EUR 332.969 million (+EUR 25.800 million), that from euro-denominated assets and liabilities came to EUR 304.304 million (+EUR 140.994 million). Monetary policy refinancing operations yielded EUR 451.462 million (+EUR 75.788 million), and the ECB remunerated the transfer of foreign reserves with EUR 39.343 million (+EUR 11.257 million). Income on intra-Eurosystem balances arising from the allocation of euro banknotes within the Eurosystem came to EUR 752.944 million (+EUR 367.643 million). Conversely, EUR 226.469 million (+EUR 82.435 million) were required to remunerate minimum reserves. Interest expenses of EUR 946.594 million (+EUR 373.793 million) resulted from TARGET liabilities.

2 Net Result of Financial Operations, Writedowns and Risk Provisions

Realized gains/losses arising from financial operations from day-to-day business result from receivable or payable differences between the acquisition cost and the market value of gold, foreign currency, securities or other transactions. Among other things, these gains include price gains from the sale of 8.75 tons of gold.

Net realized gains increased by EUR 64.462 million to EUR 209.043 million, basically consisting of EUR 224.670 million of net income on gold and foreign currency transactions (+EUR 5.555 million) and EUR 15.627 million of net expenses on securities transactions (–EUR 58.885 million).

Writedowns on financial assets and positions largely reflect the decline in market prices of balance sheet items as on December 31, 2007, below the average cost of the respective currencies or securities. Foreign currency writedowns came to EUR 292.582 million (+EUR 227.793 million), securities writedowns to EUR 65.710 million (–EUR 18.023 million) and writedowns on participating interests to EUR 0.083 million (–EUR 0.406 million).

Transfers to/from provisions for foreign exchange rate and price risks resulted from the full drawdown of the EUR 266.086 million remaining in the *reserve fund for exchange rate risks*, which the OeNB had funded up to the end of 1998 with a view to covering unrealized foreign currency losses. Thus, in compliance with Article 69 paragraph 1 Nationalbank Act, these losses did not have an impact on profit. However, in view of the assessment of risk associated with nondomestic assets, EUR 407.000 million were transferred to the *risk provisions* (until December 31, 2006: the *provisions for exchange rate risks).*

4 Income from Equity Shares and Participating Interests

Dividend payments of EUR 18.000 million made by Münze Österreich and of EUR 2.456 million made by the BIS for 2006 were disclosed under *income from equity shares and participating interests*.

Oesterreichische Banknoten- und Sicherheitsdruck GmbH paid dividends of EUR 2.100 million in 2007. The distribution of profit by STUZZA (Studiengesellschaft für Zusammenarbeit im Zahlungsverkehr G.m.b.H.) resulted in income of EUR 0.025 million. Moreover, this item shows the remaining liquidation proceeds of EUR 0.006 million from the liquidation of Realitäten-Verwertungs-Gesellschaft m.b.H.

On December 20, 2007, the Governing Council of the ECB decided not to distribute the ECB's 2007 income of EUR 2,004 million on euro banknotes in circulation (seigniorage income) to the NCBs but to transfer this amount to a provision for foreign exchange rate, interest rate and gold price risks. The OeNB's share of the ECB's seigniorage income, and hence its share of this provision, comes to EUR 58.130 million.

5 Net Result of Pooling of Monetary Income

The amount of the OeNB's monetary income is determined by measuring the actual annual income that it derives from the earmarkable assets held against its liability base. Any interest paid on liabilities included within the liability base is to be deducted from the monetary income to be pooled.

The liability base consists of the following items: banknotes in circulation; liabilities to credit institutions related to monetary policy operations denominated in euro; net intra-Eurosystem liabilities resulting from TARGET transactions; and net intra-Eurosystem liabilities related to the allocation of euro banknotes within the Eurosystem.

The earmarkable assets consist of the following items: lending to euro area credit institutions related to monetary policy operations denominated in euro; intra-Eurosystem claims equivalent to the transfer of foreign reserve assets to the ECB; net intra-Eurosystem claims resulting from TARGET transactions; net intra-Eurosystem claims related to the allocation of euro banknotes within the Eurosystem; and a limited amount of the OeNB's gold holdings in proportion to its capital key share (gold is considered to generate no income). Where the value of the OeNB's earmarkable assets exceeds or falls short of the value of its liability base, the difference is offset by applying to the value of the difference the average rate of return on the earmarkable assets of all NCBs taken together.

The monetary income pooled by the Eurosystem is allocated among NCBs according to the subscribed ECB capital key. The difference between the monetary income pooled by the OeNB in 2007 (amounting to EUR 671.687 million) and the monetary income reallocated to the OeNB (amounting to EUR 664.370 million) was the net result arising from the calculation of monetary income.

7 Staff Costs

Salaries, severance payments, and the employer's social security contributions and other statutory or contractual social charges fall under the heading *staff costs*. These costs are reduced by recoveries of salaries and employees' pension contributions.

As of January 1, 1997, the pension contributions of employees who had joined the OeNB after March 31, 1993, and who qualify for an OeNB pension were raised from 5% of their total basic pay to 10.25% of their basic salaries up to the earnings cap as defined in the General Social Security Act. A rate of 2% applies to income above the earnings cap.

Salaries net of pension contributions collected from staff members grew by EUR 0.866 million or 1.0% to EUR 86.721 million against the previous year. The OeNB's outlays were reduced by recoveries of salaries totaling EUR 6.689 million for staff members on secondment to subsidiaries and foreign institutions.

The four members of the Governing Board received emoluments totaling EUR 1.045 million (2006: EUR 1.024 million). Table 33 shows a breakdown of these items:

Table 33

	Emoluments
	EUR million
Governor Klaus Liebscher	0.279
Vice Governor Wolfgang Duchatczek	0.263
Executive Director Peter Zöllner	0.256
Executive Director Josef Christl	0.247

With regard to the remuneration of Governing Board members, the Federal Constitutional Act on the Limitation of Remunerations for Public Officials stipulates that the emoluments of the central bank governor must not exceed those of the Austrian Federal Chancellor. The emoluments of the other members of the Governing Board, in turn, must not exceed the emoluments of the Governor of the OeNB. Remuneration in kind (tax value of the private use of company cars, subsidies to health and accident insurance) totaled EUR 0.035 million in 2007.

The emoluments of the OeNB's President and Vice President amounted to EUR 0.111 million in 2007 (2006: EUR 0.109 million).

Table 34 shows the development of staff in full-time equivalents (FTEs).

Table 34

	December 31[1]			Annual average[1]		
	2007	2006	Change	2007	2006	Change
Staff employed at the OeNB[2]	917.5	931.7	−14.2	920.3	935.4	−15.1
Total	1,082.1	1,100.5	−18.4	1,087.1	1,104.8	−17.7

[1] *Including part-time employees on a pro rata basis.*
[2] *Excluding employees on secondment or leave (such as maternity and parental leave).*

Statutory or contractual social charges totaling EUR 13.305 million (+EUR 0.143 million) contain municipal tax payments of EUR 2.622 million, social security contributions of EUR 6.658 million and contributions of EUR 3.927 million to the Family Burden Equalization Fund.

8 Administrative Expenses

Administrative expenses include rent, operating expenses, maintenance and repair costs of EUR 26.084 million (+EUR 1.369 million) as well as banknote processing expenses of EUR 9.599 million (–EUR 0.211 million).

10 Banknote Production Services

Expenses for *banknote production services* result above all from the purchase of euro banknotes from the Oesterreichische Banknoten- und Sicherheitsdruck GmbH (OeBS).

12 Corporate Income Tax

A corporate income tax rate of 25% is to be applied to the taxable income under Article 72 Nationalbank Act, which qualifies as income under Article 22 paragraph 1 of the Corporate Income Tax Act.

13 Transfers to the Pension Reserve and Central Government's Share of Profit

Transfers to the pension reserve under Article 69 paragraph 2 Nationalbank Act came to EUR 18.500 million. Under Article 69 paragraph 3 Nationalbank Act, the *central government's share of profit* is 90% of the net income for the year after tax, as in previous years, and amounted to EUR 149.847 million (2006: EUR 130.244 million).

Post-Balance Sheet Events

Eurosystem Entry

From January 1, 2008, Cyprus and Malta fulfilled the conditions for euro adoption; the Central Bank of Cyprus and the Central Bank of Malta joined the Eurosystem on that day.

As a result of their membership in the Eurosystem pursuant to Article 49.1 ESCB Statute, the two central banks were required to fully pay up their shares in the ECB's subscribed capital (until then, they had paid up 7% of their shares) and, pursuant to Article 30.1 ESCB Statute, to transfer foreign reserve assets to the ECB in an amount corresponding to their subscribed capital shares. The contributions of the NCBs that had joined the Eurosystem earlier remained unaffected.

The OeNB's percentage share in the fully paid-up capital of the ECB (relative capital key) declined from 2.9002% to 2.8924% when the Central Bank of Cyprus and the Central Bank of Malta joined the Eurosystem.

The increase in the subscribed capital of the ECB under Article 49.2 ESCB Statute triggered by the expansion of the Eurosystem to 15 members was effected in March 2008 following the approval of the ECB's annual accounts by the Governing Board of the ECB.

Table 35

Key for subscription to the ECB's capital	From January 1, 2007 to December 31, 2007	From January 1, 2008
	%	%
Deutsche Bundesbank	20.5211	20.5211
Banque de France	14.3875	14.3875
Banca d'Italia	12.5297	12.5297
Banco de España	7.5498	7.5498
De Nederlandsche Bank	3.8937	3.8937
Nationale Bank van België / Banque Nationale de Belgique	2.4708	2.4708
Oesterreichische Nationalbank	2.0159	2.0159
Bank of Greece	1.8168	1.8168
Banco de Portugal	1.7137	1.7137
Suomen Pankki – Finlands Bank	1.2448	1.2448
Central Bank and Financial Services Authority of Ireland	0.8885	0.8885
Banka Slovenije	0.3194	0.3194
Banque centrale du Luxembourg	0.1575	0.1575
Central Bank of Cyprus[1]	–	0.1249
Central Bank of Malta / Bank Ċentrali ta' Malta[1]	–	0.0622
Total euro area NCBs	**69.5092**	**69.6963**
Bank of England	13.9337	13.9337
Narodowy Bank Polski	4.8748	4.8748
Banca Naţională a României	2.5188	2.5188
Sveriges Riksbank	2.3313	2.3313
Danmarks Nationalbank	1.5138	1.5138
Česká národní banka	1.3880	1.3880
Magyar Nemzeti Bank	1.3141	1.3141
Bulgarian National Bank	0.8833	0.8833
Národná banka Slovenska	0.6765	0.6765
Lietuvos bankas	0.4178	0.4178
Latvijas Banka	0.2813	0.2813
Eesti Pank	0.1703	0.1703
Central Bank of Cyprus[1]	0.1249	–
Central Bank of Malta / Bank Ċentrali ta' Malta[1]	0.0622	–
Total non-euro area NCBs	**30.4908**	**30.3037**
Total euro area and non-euro area NCBs	**100.0000**	**100.0000**

[1] *Euro area member from January 1, 2008.*

Sale of 85% of AUSTRIA CARD –
Plastikkarten und Ausweissysteme Gesellschaft m.b.H.

As endorsed by the OeNB's Governing Board and by the OeNB's executive committee on September 18, 2007, the OeNB concluded a purchase and assignment agreement for its 85% stake in AUSTRIA CARD – Plastikkarten und Ausweissysteme Gesellschaft m.b.H. with Salnea Beteiligungsverwaltungs GmbH on September 26, 2007. The deal was closed – i.e. the OeNB transferred its shares to the buyer and the buyer transferred the purchase price to the trustee – on January 1, 2008.

Sale of the OeNB-Owned Hotel Miramonte

On September 26, 2007, the Governing Board endorsed the sale of Hotel Miramonte following an auction and submitted a report on the sale to the General Council at the General Council meeting of October 11, 2007. Hotel Miramonte and hence the title to the property will be transferred after the sales contract is signed and after the appropriate entry in the land register has been made, which will be after the end of the 2007/08 winter season.

Governing Board (Direktorium)

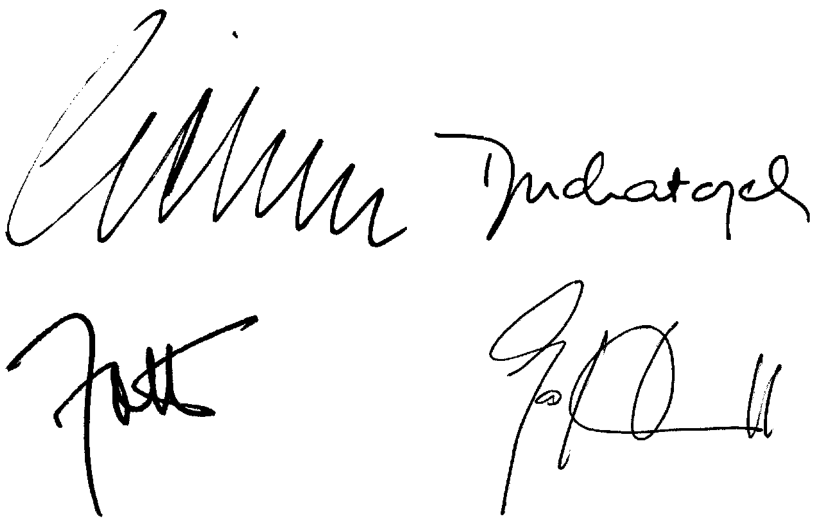
Governor Klaus Liebscher
Vice Governor Wolfgang Duchatczek
Executive Director Peter Zöllner
Executive Director Josef Christl

General Council (Generalrat)

President Herbert Schimetschek
Vice President Manfred Frey
August Astl
Bernhard Felderer
Philip Göth
Elisabeth Gürtler-Mauthner
Alfred Hannes Heinzel
Manfred Hofmann
Herbert Kofler (until April 22, 2007)
Max Kothbauer
Johann Marihart
Werner Muhm
Ewald Nowotny (from April 23, 2007)
Gerhard Randa
Walter Rothensteiner

In accordance with Article 22 paragraph 5 Nationalbank Act, the following representatives of the Central Staff Council participated in discussions on personnel, social and welfare matters: Martina Gerharter, Gerhard Kaltenbeck.

Vienna, March 12, 2008



Report of the Auditors

Bestätigungsvermerk der Abschlussprüfer

„Wir haben den um den Anhang erweiterten Jahresabschluss der Oesterreichischen Nationalbank, Wien, für das Geschäftsjahr vom 01. Jänner 2007 bis 31. Dezember 2007 mit einer Bilanzsumme von € 61.946.134.956,97 unter Einbeziehung der Buchführung und des Geschäftsberichts – soweit er sich auf den Jahresabschluss bezieht – geprüft.

Die Buchführung, die Aufstellung und der Inhalt dieses um den Anhang erweiterten Jahresabschlusses sowie des Geschäftsberichts liegen in der Verantwortung der gesetzlichen Vertreter der Gesellschaft.

Dieser um den Anhang erweiterte Jahresabschluss sowie dieser Geschäftsbericht wurden in Übereinstimmung mit den Vorschriften des Nationalbankgesetzes 1984 in der geltenden Fassung und den ergänzenden Bestimmungen der vom Rat der Europäischen Zentralbank gemäß Artikel 26 Abs. 4 des „Protokolls über die Satzung des Europäischen Systems der Zentralbanken und der Europäischen Zentralbank“ mittels der „Guideline of the European Central Bank of 10 November 2006 on the Legal Framework for Accounting and Financial Reporting in the European System of Central Banks (ECB/2006/16)“ erlassenen Vorschriften erstellt.

Der gemäß § 68 Abs. 1 NBG zu erstellende Geschäftsbericht ersetzt den Lagebericht gemäß § 243 UGB.

Unsere Verantwortung besteht in der Abgabe eines Prüfungsurteils zu diesem um den Anhang erweiterten Jahresabschluss auf der Grundlage unserer Prüfung und einer Aussage, ob der Geschäftsbericht – soweit er sich auf den Jahresabschluss bezieht – in Einklang mit dem Jahresabschluss steht.

Wir haben unsere Prüfung unter Beachtung der in Österreich geltenden gesetzlichen Vorschriften und Grundsätze ordnungsgemäßer Abschlussprüfung durchgeführt. Diese Grundsätze erfordern, die Prüfung so zu planen und durchzuführen, dass ein hinreichend sicheres Urteil darüber abgegeben werden kann, ob der um den Anhang erweiterte Jahresabschluss frei von wesentlichen Fehldarstellungen ist, und eine Aussage getroffen werden kann, ob der Geschäftsbericht – soweit er sich auf den Jahresabschluss bezieht – mit dem Jahresabschluss in Einklang steht. Bei der Festlegung der Prüfungshandlungen werden die Kenntnisse über die Geschäftstätigkeit und über das wirtschaftliche und rechtliche Umfeld der Oesterreichischen Nationalbank sowie die Erwartungen über mögliche Fehler berücksichtigt.

(Fortsetzung des Bestätigungsvermerkes auf der nachfolgenden Seite)

(Fortsetzung des Bestätigungsvermerkes)

Im Rahmen der Prüfung werden die Nachweise für Beträge und sonstige Angaben in der Buchführung und im Jahresabschluss überwiegend auf Basis von Stichproben beurteilt. Die Prüfung umfasst ferner die Beurteilung der angewandten Rechnungslegungsgrundsätze und der von den gesetzlichen Vertretern vorgenommenen, wesentlichen Schätzungen sowie eine Würdigung der Gesamtaussage des um den Anhang erweiterten Jahresabschlusses. Wir sind der Auffassung, dass unsere Prüfung eine hinreichend sichere Grundlage für unser Prüfungsurteil darstellt.

Unsere Prüfung hat zu **keinen Einwendungen** geführt.

Auf Grund der bei der Prüfung gewonnenen Erkenntnisse entspricht der um den Anhang erweiterte Jahresabschluss nach unserer Beurteilung den gesetzlichen Vorschriften des Nationalbankgesetzes 1984 in der geltenden Fassung und den ergänzenden Bestimmungen der vom Rat der Europäischen Zentralbank gemäß Artikel 26 Abs. 4 des „Protokolls über die Satzung des Europäischen Systems der Zentralbanken und der Europäischen Zentralbank“ mittels der „Guideline of the European Central Bank of 10 November 2006 on the Legal Framework for Accounting and Financial Reporting in the European System of Central Banks (ECB/2006/16)“ erlassenen Vorschriften und vermittelt ein möglichst getreues Bild der Vermögens- und Finanzlage des Unternehmens zum 31. Dezember 2007 sowie der Ertragslage des Unternehmens für das Geschäftsjahr vom 01. Jänner 2007 bis 31. Dezember 2007 in Übereinstimmung mit den österreichischen Grundsätzen ordnungsmäßiger Buchführung im Sinne des § 67 Abs. 2 NBG.

Der Geschäftsbericht steht – soweit er sich auf den Jahresabschluss bezieht – in Einklang mit dem Jahresabschluss.“

Wien, am 12. März 2008

TPA Horwath Wirtschaftsprüfung GmbH	MOORE STEPHENS AUSTRIA Wirtschaftsprüfungsgesellschaft mbH
Mag. Thomas Schaffer, CPA Wirtschaftsprüfer	Dr. Peter Wundsam Wirtschaftsprüfer

Die Veröffentlichung oder Weitergabe des Jahresabschlusses mit unserem Bestätigungsvermerk darf nur in der von uns bestätigten Fassung erfolgen. Für abweichende Fassungen (zB Verkürzungen) gelten die Bestimmungen des § 281 UGB.

OeNB translation of the external auditors' report from German into English for information purposes. In case of discrepancies, the German text signed by TPA Horwath Wirtschaftsprüfung GmbH and MOORE STEPHENS AUSTRIA Wirtschaftsprüfungsgesellschaft mbH shall prevail.

Report of the Auditors

We have audited the financial statements – comprising total assets of EUR 61,946,134,956.97 – including the Notes to the Financial Statements, of the Oesterreichische Nationalbank in Vienna for the year ending on December 31, 2007, and taking into account the accounting principles on which they are based as well as the Annual Report, insofar as it refers to the Financial Statements. Accounting and reporting operations, as reflected in these Financial Statements, including the Notes to the Financial Statements and the Annual Report, are the responsibility of the OeNB's management.

The Financial Statements, including the Notes to the Financial Statements, and the Annual Report were prepared in conformity with the provisions of the Nationalbank Act 1984 as amended and the supplementary provisions established by the Governing Council of the ECB under Article 26.4 of the Statute of the European System of Central Banks and of the European Central Bank, as set forth in the Guideline of the European Central Bank of 10 November 2006 on the legal framework for accounting and reporting in the European System of Central Banks (ECB/2006/16).

The Annual Report to be prepared under Article 68 paragraph 1 Nationalbank Act replaces the report of the Management Board to be drawn up pursuant to Article 243 Commercial Code.

Our responsibility is to express an opinion on these Financial Statements, including the Notes to the Financial Statements, based on our audit and to state whether the Annual Report, insofar as it refers to the Financial Statements, is in accordance with the Financial Statements.

We conducted our audit in accordance with laws and regulations applicable in Austria and with Austrian standards on auditing. Those standards require that we plan and perform the audit to obtain reasonable assurance whether the consolidated Financial Statements are free from material misstatement and whether we can state that the Annual Report, insofar as it refers to the Financial Statements, is in accordance with the Financial Statements. In determining the audit procedures, we considered our knowledge of the business, the economic and legal environment of the Oesterreichische Nationalbank as well as the expected occurrence of errors.

An audit involves procedures to obtain evidence about amounts and other disclosures in the accounting records and the Financial Statements on a sample basis. An audit also includes assessing the accounting principles used and significant estimates made by management as well as evaluating the overall presentation of the Financial Statements, including the Notes on the Financial Statements. We believe that our audit provides a reasonable basis for our opinion.
Our audit *did not give rise to any objections*.
In the course of our audit we have found that the Financial Statements, including the Notes to the Financial Statements, are in accordance with the provisions of the Nationalbank Act 1984 as amended and the supplementary provisions established by the Governing Council of the ECB under Article 26.4 of the Statute of the European System of Central Banks and of the European Central Bank, as set forth in the Guideline of the European Central Bank of 10 November 2006 on the legal framework for accounting and reporting in the European System of Central Banks (ECB/2006/16) and provide a true and fair picture of the OeNB's financial position on December 31, 2007, and the results of its operations from January 1, 2007, to December 31, 2007, in line with the principles of generally accepted accounting practice under Article 67 paragraph 2 Nationalbank Act.
Insofar as the Annual Report refers to the Financial Statements, it is in accordance with the Financial Statements.

Vienna, March 12, 2008

TPA Horwath Wirtschaftsprüfung GmbH	MOORE STEPHENS AUSTRIA Wirtschaftsprüfungsgesellschaft mbH
Thomas Schaffer, CPA external auditor	Peter Wundsam external auditor

The Financial Statements including our audit report may be published or distributed only as audited by us. Shorter versions or excerpts etc. are subject to Article 281 Commercial Code.

Profit for the Year and Proposed Profit Appropriation

With the statutory allocations of the OeNB's profit – including the central government's share of EUR 149.847 million (2006: EUR 130.244 million) – having been made in conformity with Article 69 paragraphs 2 and 3 Nationalbank Act (item 13 of the profit and loss account), the balance sheet and the profit and loss account show a profit for the year 2007 of EUR 16,649,732.22.

On March 26, 2008, the Governing Board endorsed the following profit appropriation proposal to the General Council:

		EUR
to pay a 10% dividend on the OeNB's capital stock of EUR 12 million		1,200,000.00
to allocate to the Leopold Museum Private Foundation		98,471.69
to allocate to the OeNB Anniversary Fund for the Promotion of Scientific Research and Teaching:		
funds earmarked for promotion by the OeNB	12,579,460.15	
funds earmarked for the National Foundation for Research, Technology and Development	2,771,800.38	15,351,260.53
		16,649,732.22

Report of the General Council on the Annual Report and the Financial Statements for 2007

The General Council (Generalrat) fulfilled the duties incumbent on it under the Nationalbank Act 1984 by holding regular meetings, by convening subcommittees to examine specific issues and by making informed decisions.

The Governing Board (Direktorium) periodically reported to the General Council on the Oesterreichische Nationalbank's operations and results, on the conditions on the money, capital and foreign exchange markets, on important day-to-day management issues, on all developments of significance for an appraisal of monetary and economic developments, on the arrangements made for auditing the OeNB's finances, and on any other significant dispositions and events affecting the OeNB's operations.

The Financial Statements for the year 2007 were given an unqualified auditor's opinion after examination by the auditors elected at the General Meeting of May 31, 2007, TPA Horwath Wirtschaftsprüfung GmbH and MOORE STEPHENS AUSTRIA Wirtschaftsprüfungsgesellschaft mbH, on the basis of the books and records of the Oesterreichische Nationalbank as well as the information and evidence provided by the Governing Board.

In its meeting of April 29, 2008, the General Council approved the Annual Report of the Governing Board and the Financial Statements for the business year 2007. The General Council submits the Annual Report and moves that the General Meeting approve the Financial Statements of the Oesterreichische Nationalbank for the year 2007 and discharge the General Council and the Governing Board of its responsibilities regarding the preceding business year. Moreover, the General Council requests that the General Meeting approve the allocation of the profit for the year in accordance with the proposal made in the notes to the Financial Statements 2007 (page 142).

Notes

Abbreviations, Legend

ABCP	asset-backed commercial paper
AG	Aktiengesellschaft (roughly: stock corporation)
APC	Austrian Payments Council
A-SIT	Secure Information Technology Center – Austria
ATM	automated teller machine
ATS	Austrian schilling
ATX	Austrian Traded Index
Basel II	New Basel Capital Accord
BIS	Bank for International Settlements
BMF	Austrian Federal Ministry of Finance
BSC	Banking Supervision Committee of the ESCB
CEBS	Committee of European Banking Supervisors (EU)
CESEE	Central, Eastern and Southeastern Europe
CIS	Commonwealth of Independent States
CPI	consumer price index
CSD	central securities depository
CSDB	Centralised Securities Database
CYP	Cyprus pound
EBA	Euro Banking Association
ECB	European Central Bank
Ecofin	Council of Economic and Finance Ministers (EU)
EER	effective exchange rate
EMAS	eco-management and audit scheme
EMU	Economic and Monetary Union
EMV	Europay, MasterCard and VISA
EPC	European Payments Council
EBOPS	Extended Balance of Payments Services classification
ERM II	Exchange Rate Mechanism II (EU)
ERP	European Recovery Program, commonly called Marshall Plan
ESCB	European System of Central Banks
EUR	euro
EURIBOR	Euro Interbank Offered Rate
Eurostat	Statistical Office of the European Communities
FDI	foreign direct investment
FMA	Financial Market Authority (Austria)
FSAP	Financial Sector Assessment Program (IMF)
FTE	full-time equivalent
FYR Macedonia	Former Yugoslav Republic of Macedonia
GRI	Global Reporting Initiative
GSA	GELDSERVICE AUSTRIA Logistik für Wertgestionierung und Transportkoordination G.m.b.H. (cash logistics company)
HICP	Harmonised Index of Consumer Prices
IHS	Institute for Advanced Studies
IMF	International Monetary Fund
IRB	internal ratings-based
ISIN	International Securities Identification Number
M3	broad monetary aggregate M3
MFI	monetary financial institution
MiFID	Markets in Financial Instruments Directive
MSCI	Morgan Stanley Capital International
MTL	Maltese lira
MWh	megawatt hours
NCB	national central bank
NPISH	nonprofit institutions serving households
NRP	national reform program (EU)
OeBS	Oesterreichische Banknoten- und Sicherheitsdruck GmbH
OeKB	Oesterreichische Kontrollbank
OECD	Organisation for Economic Co-operation and Development
OeNB	Oesterreichische Nationalbank
PDCF	Primary Dealer Credit Facility (credit facility in the U.S.A.)
POS	point of sale
ROA	return on assets
RTGS	Real-Time Gross Settlement
SCF	SEPA Cards Framework
SDR	Special Drawing Right (IMF)
SEPA	Single Euro Payments Area
SGP	Stability and Growth Pact
STEP.AT	Austrian clearing and settlement system that is operated by the OeNB and that conforms to SEPA standards
STEP2	Straight-Through Euro Processing (EBA)
STUZZA	Studiengesellschaft für Zusammenarbeit im Zahlungsverkehr (Austrian Research Association for Payment Cooperation)
T2S	TARGET2-Securities
TAF	Term Auction Facility (credit facility in the U.S.A.)
TARGET/ TARGET2	Trans-European Automated Real-time Gross settlement Express Transfer
TSLF	Term Securities Lending Facility (credit facility in the U.S.A.)
TOP	Tender Operations system
USD	U.S. dollar
VIX (CBOE)	Volatility Index (Chicago Board Options Exchange)
WIFO	Österreichisches Institut für Wirtschaftsforschung (Austrian Institute of Economic Research)
wiiw	Wiener Institut für internationale Wirtschaftsvergleiche (The Vienna Institute for International Economic Studies)
WTO	World Trade Organization

x	=	No data can be indicated for technical reasons
. .	=	Data not available at the reporting date
0	=	The numerical value is zero or smaller than half of the unit indicated
–	=	The numerical value is zero (legend entry in the Financial Statements only)
n. a.	=	Not applicable (legend entry in the Financial Statements only)

Discrepancies may arise from rounding.

Glossary

Acquirer: Service provider authorizing and clearing payment card transactions. It is licensed by card organizations to enlist as business partners merchants willing to accept electronic payment from cardholders who have signed up with the relevant organization and handles all relevant transactions for the merchants.

Basel II: Term commonly used to refer to the new capital adequacy framework for banks issued by the Basel Committee on Banking Supervision. As of January 1, 2008, all credit institutions in the EU are obliged to adopt this capital framework, which replaces the first Capital Accord of 1988 (Basel I). Basel II aims to enhance financial stability by establishing a more risk-sensitive regime that ensures the continuous development of credit institutions' risk management systems and accommodates new financial market developments.

Benchmark: Typically a benchmark index, which defines the market environment relevant for the investment of a portfolio and provides a yardstick for all investment decisions. The goal of investors is to outperform the benchmark on a sustainable basis and without incurring major additional risks.

Capital adequacy: The concept that banks must maintain sufficient and appropriate capital backing to cover their exposure to risks. The capital adequacy frameworks Basel I and Basel II established by the Basel Committee on Banking Supervision (BCBS) prescribe a capital ratio of 8% of risk-weighted assets.

Capital ratio: A key financial measure of banks' capital strength, expressed as the ratio of own funds to risk-weighted assets.

Carry trade: Refers to an investment strategy in the foreign exchange markets of buying a higher-yielding currency with the capital of a lower-yielding currency to gain an interest rate differential. The more market participants pursue such a strategy, the greater the likelihood is that the high-yield currency appreciates against the low-yield currency, as the supply of the funding currency exceeds the demand for the target currency under ceteris paribus conditions. This strategy bears the risk that should the target currency depreciate against the funding currency, the resulting loss is greater than the profit from the interest rate differential.

Centralised Securities Database (CSDB): ECB database containing extensive data on securities issued or held by EU residents.

Clearing: The process of reconciling claims or liabilities related to payment orders or security transfer instructions prior to settlement; may include the netting of instructions.

Convergence criteria: Four requirements that are laid down in the Maastricht Treaty and that an EU Member State must fulfill to qualify for participation in Stage Three of Economic and Monetary Union (EMU), i.e. for the introduction of the euro: (1) an inflation rate not more than 1.5 percentage points above that of the three best-performing Member States in terms of price stability, (2) a long-term interest rate not more than 2 percentage points above that of the three best-performing Member States in terms of price stability, (3) a government budgetary position without a deficit that is excessive, in particular if the government deficit does not exceed 3% of GDP and the ratio of public debt to GDP does not exceed 60%, unless the ratio is sufficiently diminishing and approaching the reference value at a satisfactory pace, and (4) currency variations within the normal fluctuation margins of the exchange rate mechanism II (ERM II) for at least two years without devaluation against the currency of any other Member State.

Credit risk: The risk of an impairment of a bank's assets or loss given default resulting from a deterioration of customers' creditworthiness.

Credit standards: Banks' internal lending criteria (written or unwritten), including special obligations agreed between the lender and the borrower.

Creditworthiness: A debtor's past and future ability and willingness to repay debts.

Currency board system: The strictest kind of exchange rate regime, which implies that a country opting for such a system, as a rule, forgoes the privilege of operating a central bank in its own right and thus the privilege of conducting an independent monetary policy. A currency board system institutionally guarantees the free convertibility of cash and deposits into an international anchor currency (also reserve currency) by holding adequate reserve assets. To this effect, a country must fix its exchange rate against the chosen anchor currency and commit itself to linking domestic currency in circulation to the stock of reserve assets. Furthermore, a currency board system is not allowed to buy domestic assets, which is why it cannot provide liquidity in the event of crisis. Unlike a central bank, a currency board may, thus, not act as a lender of last resort.

Discount rate: The interest rate at which the central bank is prepared to lend funds to commercial banks, which supply government debt, such as bills or securities with residual maturity, as collateral.

EMV standard: A universal specification for payment cards with processor chip technology and the respective POS terminals. EMV stands for the three companies that developed the standard: Europay, MasterCard and VISA.

ERM II (exchange rate mechanism II): Agreement which provides the framework for exchange rate policy cooperation between the euro area countries and the EU Member States seeking to adopt the euro. It specifies fluctuation bands for the exchange rates of participating currencies to the euro. The standard fluctuation band amounts to ±15% around the central rate, while narrower bands may be agreed on a case-by-case basis.

Euroization: A policy under which a country abandons its own currency to adopt the euro.

Facility: Monetary policy instrument for supplying counterparties with central bank liquidity or for absorbing, at the central bank, liquidity from counterparties.

Federal Reserve: The Federal Reserve System (frequently referred to as the Fed), the central banking system of the United States, comprises 12 Federal Reserve Banks controlling 12 districts under the Federal Reserve Board. The U.S. Congress established the Fed in 1913 to monitor and regulate the U.S. monetary and banking system. Its most important body is the Federal Open Market Committee (FOMC), which sets U.S. monetary policy.

Financial instrument: Defined by the International Accounting Standards (IAS) and International Financial Reporting Standards (IFRS) as any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

Fine-tuning operation: An open market operation executed by the Eurosystem to deal with unexpected liquidity fluctuations in the market. The frequency and maturity of fine-tuning operations are not standardized.

Fixed rate tender: A tender procedure in which a central bank provides liquidity to, or withdraws liquidity from, the market on the basis of bids submitted by competing counterparties (banks). Specifically, counterparties bid the amount of money they wish to transact at the rate specified by the central bank.

Foreign exchange swap: The simultaneous spot purchase/sale and forward sale/purchase of one currency against another. Under the Federal Reserve's temporary reciprocal currency swap facilities with the ECB, the latter conducted term dollar funding auctions in tandem with the Federal Reserve's Term Auction Facility auctions, i.e. U.S. dollars were sold to Eurosystem banks at the euro spot rate and repurchased term by term.

Harmonised Index of Consumer Prices (HICP): In line with Treaty provisions, price convergence among the EU Member States is measured in terms of a harmonized index of consumer prices. The HICP, which is computed by Eurostat, is the result of these standardization efforts and is the key inflation indicator for the monetary policy of the Eurosystem. As laid down by the Governing Council of the ECB, the Eurosystem targets a price stability objective of an annual HICP increase of below, but close to, 2%.

Hedge funds: Pooled investment vehicles which are much less restricted than other investment funds in choosing and changing investment strategies. Investment strategies, and hence setup, asset allocation and investment risk, differ strongly from hedge fund to hedge fund. Typically, hedge funds pursue an aggressive total return strategy, holding both long and short positions, frequently by taking highly leveraged bets on market movements that are not offset by a corresponding hedged position.

Implied volatility: A measure of expected volatility of future short-term and long-term interest rates and hence a measure of market risk. In addition to using historical time series to calculate the past standard deviation of interest rates *(historical volatility)* as an indicator for future fluctuations, it is also possible to determine volatility implicitly using an option pricing model. Given the price of the option and price-influencing factors such as the time to maturity, the price of the underlying security, the interest rate and the exercise price, no other input is required. Volatility is an essential measure for professional financial market participants and for the financial system in general.

International Financial Reporting Standards (IFRS): Under Regulation (EC) No. 1606/2002, listed companies governed by the law of an EU Member State have been obliged to prepare their consolidated financial statements according to IFRS since January 1, 2005. The International Accounting Standards Board (IASB) started to develop IFRS in 2003. All International Accounting Standards (IAS) remain applicable unless the IASB has amended or replaced them by new standards. The primary objective of IFRS financial reporting is to enable investors to compare financial information.

International Securities Identification Number (ISIN): A code defined in the standard ISO 6166 of the International Organization for Standardization that uniquely identifies a specific securities issue. The responsibility for assigning valid ISINs lies with National Numbering Agencies (NNAs); the Austrian NNA is the Oesterreichische Kontrollbank (OeKB). The validity of an ISIN depends on the database of the Association of NNAs (ANNA).

Issuer: An entity, such as a bank or a credit card company, that issues debit or credit cards.

Liquidity risk: The risk that a counterparty will not settle an obligation at its full value when due. It does not imply that the counterparty is insolvent, since it may be able to settle the required debt obligations at some unspecified time thereafter.

Lisbon strategy: The reform agenda introduced by the Lisbon European Council in March 2000 that aims at making the EU the most competitive and dynamic knowledge-based economy in the world by 2010.

Longer-term refinancing operation: A regular open market operation executed by the Eurosystem in the form of reverse transactions. Such operations are carried out through a monthly standard tender and normally have a maturity of three months.

M3: A broad monetary aggregate that comprises M1 (currency in circulation and overnight deposits), M2 (M1 plus short-term savings and time deposits) as well as marketable instruments, in particular repurchase agreements, money market fund shares/units and debt securities with a maturity of up to and including two years issued by monetary financial institutions (MFIs). M3 has been assigned a prominent role in the monetary policy strategy of the Eurosystem. M3 developments in the euro area are monitored against a reference value of 4.5%, which reflects the annual growth rate of M3 over the medium term that is deemed consistent with the maintenance of price stability.

Main refinancing operation: A regular open market operation executed by the Eurosystem in the form of reverse transactions, i.e. operations under a repurchase agreement. Such operations are carried out through a weekly standard tender and normally have a maturity of one week.

Market capitalization: The equity value of a listed company; equivalent to the product of the share price and the number of shares issued.

Market risk: The risk that financial market fluctuations (e.g. changes in interest rates, stock prices or exchange rates) will impact on an entity's assets and liabilities.

Memorandum of Understanding (MoU): Agreement reached between two authorities on cooperation principles and information-sharing procedures regarding issues of common interest.

Money market: Interbank trade in central bank deposits with a view to accommodating liquidity differences. In a broader sense, all trading activities in short-term financial instruments.

Mortgage: Long-term loan secured by registration of a lien on property. Mortgage loans are generally secured against property. Volumes, maturity and interest rates (fixed, variable) may range widely. In the event of debtor default, the lender initiates foreclosure on the mortgaged property.

On-site inspection: Thorough examination of individual banks, during which supervisors largely work on the premises of a given bank. By reviewing relevant business areas, supervisors cross-check the data reported by banks against first-hand information in as much detail as is required to assess the need for supervisory action.

Open market operation: An operation executed on the initiative of the central bank in the financial market for liquidity management purposes.

Operational risk (in banking): The risk of loss resulting from inadequate or failed internal processes, people and systems or from external events.

Payment card personalization: The process by which a cardholder's information is loaded onto a payment card, either optically or electronically. Optical personalization means printing customer information onto the card using one of a variety of methods – laser, raised print or thermosublimation. Information includes e.g. the customer's name, the bank identification code and the account or credit card number. Electronic personalization means the uploading of the respective programs and personal data onto the payment card's magnetic stripe and chip.

Primary dealer: A bank or securities broker-dealer authorized by the Federal Reserve that has the capacity and the obligation to participate directly in open market operations executed by the Fed. Primary dealers must fulfill certain quality criteria (in respect of e.g. liquidity or capital requirements) and submit competing bids in the Fed's securities auctions. They act as intermediaries in the U.S. government bond market, trading government bonds directly with the Fed, on the one hand, and, on the other, selling them to and buying them from their customers (including foreign banks and financial institutions).

Rating: Assessment of the creditworthiness of a debtor against standardized qualitative and quantitative criteria. Ratings are used to determine a borrower's probability of default.

Return on assets (ROA): A measure of a company's profitability, equal to net income divided by its total assets, expressed as a percentage.

Risk-Oriented Reporting System: Development and extension of coverage of the regulatory reporting scheme to better capture individual risk in different areas within banks. The Risk-Oriented Reporting System covers statistical aspects of equity risk and operational risk in addition to credit risk, interest rate risk and market risk. Other functions of the system include the compilation of detailed data from banking groups and banks' foreign subsidiaries.

Settlement: The process through which financial obligations are discharged – especially those incurred in forward transactions – in respect of funds or assets transfers. There are two types of settlement – cash settlement and actual delivery of the underlying asset.

Shift of liability: In the payments field, a contractual agreement that the party in the process chain that has failed to adopt the EMV standard is liable for any damage to another party resulting from this noncompliance with the EMV standard. To give some examples, a bank that has failed to equip its cards with chips or to set up EMV-ready cash machines is liable for any resulting damage, as is a retailer who has no EMV terminal and has to rely on a card's magnetic stripe even though the customer's card has a chip. If an acquirer has failed to supply a retailing partner with a suitable terminal, the liability reverts to the acquirer.

Special purpose vehicle (SPV): Legal person, established for the fulfillment of a specific task, whose sole corporate objective comprises the financing of a project. Conduits or structured investment vehicles (SIVs) – a form of SPV – buy e.g. long-term assets and refinance the purchase price by issuing asset-backed securities (ABS). Money market financial instruments are also referred to as asset-backed commercial paper (ABCP).

Stability programs: The euro area countries' annual medium-term government plans and assumptions for the development of key economic and, in particular, budget variables in line with the requirements of the Stability and Growth Pact. Countries not participating in the euro area must submit annual convergence programs according to the SGP.

Stability and Growth Pact (SGP): Framework annexed to the EU Treaty, adopted in 1997 and reformed in 2005, that is meant to help prevent excessive public deficits. The primary goal of the SGP is the achievement of balanced general government budgets over the medium term.

STEP2: The first pan-European clearing house (PEACH) for fully electronic standardized intra-EU credit transfers. According to Regulation (EC) No. 2560/2001, charges for cross-border transfers must not be higher than for national payments. The OeNB has been providing open and neutral access to STEP2 since 2003. More than 150 banks in Austria and abroad use this access.

Stress test: Analysis of the impact of drastic, yet plausible stress scenarios in terms of credit risk and market risk on the adequacy of a bank's capital.

Systemic risk: The risk that the inability of one institution to meet its obligations when due will cause other institutions to be unable to meet their obligations when due. Such a failure may trigger significant liquidity or credit problems and, as a result, could threaten the stability of or confidence in markets. The failure may be due to operational or financial reasons.

TARGET2: Second generation of the TARGET system that went into operation in November 2007. A Single Shared Platform (SSP) developed and operated by the Deutsche Bundesbank, the Banque de France and the Banca d'Italia on behalf of the Eurosystem is at the heart of TARGET2; it offers an extended harmonized service across Europe with a uniform pricing scheme.

TARGET2-Securities (T2S): The concept of TARGET2-Securities (T2S) envisages centralized processing of delivery-versus-payment (DVP) transactions by transferring central bank accounts and securities accounts to a single technical platform fully owned and operated by the Eurosystem. The T2S project aims at removing barriers between the systems and at harmonizing settlement of securities denominated in euro and at ensuring price transparency, open access and the unbundling of services and prices.

Terminal (payment systems): Device set up at points of sale for the entry and transfer of data needed to process payments made with payment cards.

Treaty: Refers to the Treaty establishing the European Community (Treaty of Rome) and subsequent amendments. The Treaty of Rome entered into force on January 1, 1958. It was amended by the Treaty on European Union (Maastricht Treaty, which entered into force on November 1, 1993). The Treaty of Amsterdam (May 1, 1999) and the Treaty of Nice (February 1, 2003) amended both the Treaty establishing the European Community and the Treaty on European Union. Furthermore, the Treaty of Lisbon, which was signed by the heads of state or government in Lisbon on December 13, 2007, also materially amends the Treaty, renaming it the Treaty on the Functioning of the European Union. Once the Treaty of Lisbon has been successfully ratified by the 27 Member States, the Treaty on the Functioning of the European Union and the Treaty on European Union will enter into force in their amended form with the same legal effect.

Value-at-risk method (VAR method): A quantitative assessment of a portfolio's risk of loss of value based on a probability calculation. Besides the aggregate risk, the individual risk sources (e.g. currency risk and interest rate risk) are closely examined.

Variable rate tender: A tender procedure whereby the counterparties (banks) bid both the amount of money they want to transact with the central bank and the interest rate at which they want to enter into the transaction. The central bank, which sets a minimum bid rate for these operations, thus provides or withdraws liquidity.

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Periodical Publications of the Oesterreichische Nationalbank

For further details see www.oenb.at

Monetary Policy & the Economy quarterly

This quarterly publication, issued both in German and English, offers analyses of current cyclical developments, medium-term macroeconomic forecasts and studies on central banking and economic policy topics. It also summarizes the findings of macroeconomic workshops and conferences organized by the OeNB.

Statistiken – Daten & Analysen quarterly

This publication contains brief reports and analyses focusing on Austrian financial institutions, cross-border transactions and positions as well as financial flows. The contributions are in German, with executive summaries of the analyses in English. The statistical part covers tables and explanatory notes on a wide range of macroeconomic, financial and monetary indicators. The tables and additional information and data are also available on the OeNB's website in both German and English. This series also includes special issues on selected statistics topics published at irregular intervals.

econ.newsletter quarterly

The quarterly English-language newsletter is published only on the Internet and informs an international readership about selected findings, research topics and activities of the OeNB's Economic Analysis and Research Department. This publication addresses colleagues from other central banks or international institutions, economic policy researchers, decision makers and anyone with an interest in macroeconomics. Furthermore, the newsletter offers information on publications, studies or working papers as well as events (conferences, lectures and workshops). For further details see *www.oenb.at/econ.newsletter.*

Financial Stability Report semiannual

Issued both in German and English, the Financial Stability Report contains first, a regular analysis of Austrian and international developments with an impact on financial stability and second, studies designed to provide in-depth insights into specific topics related to financial market stability.

Focus on European Economic Integration semiannual

The English-language publication Focus on European Economic Integration is the successor publication to Focus on Transition (published up to issue 2/2003). Reflecting a strategic regional research priority of the OeNB, this publication is a channel for communicating our ongoing research on Central, Eastern and Southeastern European (CESEE) countries ranging from economic country studies to studies on central banking issues and related topics. One of the purposes of publishing theoretical and empirical studies in the Focus on European Economic Integration, which are subject to an external refereeing process, is to stimulate comments and suggestions prior to possible publication in academic journals.

Workshops – Proceedings of OeNB Workshops

three to four issues a year

The Proceedings of OeNB Workshops were introduced in 2004 and typically comprise papers presented at OeNB workshops at which national and international experts, including economists, researchers, politicians and journalists, discuss monetary and economic policy issues. Workshop proceedings are generally available in English only.

Working Papers

about ten papers a year

The OeNB's Working Paper series is designed to disseminate, and provide a platform for discussing, findings of OeNB economists or outside contributors on topics which are of special interest to the OeNB. To ensure the high quality of their content, the contributions are subjected to an international refereeing process.

Economics Conference (Conference Proceedings)

annual

The Economics Conference hosted by the OeNB is an international platform for exchanging views and information on monetary and economic policy as well as financial market issues. It convenes central bank representatives, economic policymakers, financial market players, academics and researchers. The conference proceedings comprise all papers presented at the conference.

Conference on European Economic Integration (Conference Proceedings)

annual

This series, published in English by a renowned international publishing house, reflects presentations made at the OeNB's annual conference on Central, Eastern and Southeastern European issues and the ongoing EU enlargement process (formerly East-West Conference). For further details see *ceec.oenb.at*.

Annual Report

annual

The Annual Report of the OeNB provides a broad review of Austrian monetary policy, economic conditions, new developments in the financial markets in general and in financial market supervision in particular as well as of the OeNB's changing responsibilities and its role as an international partner in cooperation and dialogue. It also contains the OeNB's financial statements.

Intellectual Capital Report

annual

The Intellectual Capital Report is a review of the OeNB's intellectual capital and its use in the OeNB's business processes and services. The report highlights the interaction between human, relational, structural and innovation capital within the OeNB and reveals the influence of underlying factors. The integrated view of this stock-taking exercise serves to assess the consistency of the OeNB's intellectual capital with its knowledge-based strategic orientation.

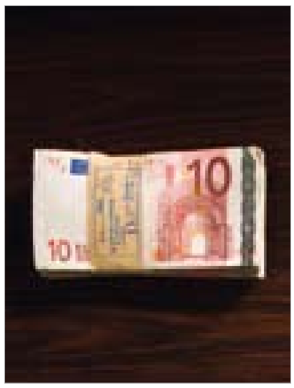

Photo Sequence

These photos document the story of a simple cash cycle as illustrated by a EUR 10 banknote. The banknote is distributed by the OeNB, withdrawn by an ATM customer, passed from one consumer to the other to pay for goods or services and, finally, returned for cash processing to the OeNB via a commercial bank.

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Rue Albéric-Magnard 3		(+33-1) 53 92 23-44	
75116 Paris, France		Fax: (+33-1) 45 24 42-49	

Our Mandate and Responsibilities

Mandate

The Oesterreichische Nationalbank (OeNB) is the central bank of the Republic of Austria and, as such, an integral part of the European System of Central Banks (ESCB). In this capacity, the OeNB acts on the basis of full personal, financial and institutional independence.
The OeNB's aims and actions are guided by the fundamental principles security, stability and trust. The primary objective of the Eurosystem, and hence of the OeNB, is to maintain price stability in the euro area and thus to safeguard the euro's purchasing power.

Responsibilities

Contribution to Monetary Policymaking within the Eurosystem

- Participation of the OeNB's Governor in decision-making within the Governing Council and General Council of the European Central Bank (ECB)
- Conduct of extensive economic analysis and research

Monetary Policy Operations – Reserve Management

- Conduct of monetary policy operations with Austrian banks
- Participation in Eurosystem foreign exchange interventions
- Management of the OeNB's own reserve assets and of the reserves transferred to the ECB
- Conduct of minimum reserve operations and monitoring of Austrian banks' minimum reserve holdings

Financial Stability and Banking Supervision

- Conduct of banking supervision in cooperation with the Financial Market Authority and of payment systems oversight with a view to securing financial stability
- Risk analysis of financial markets and banks

Provision of Statistics

- Compilation of conclusive, high-quality statistics, above all monetary, interest rate and prudential statistics as well as external trade statistics (e.g. balance of payments and financial accounts)

Cash Supply

- Provision of Austrian businesses and consumers with secure banknotes and coins and ensuring of smooth cash circulation

Payment Systems

- Provision and promotion of smoothly operating payment systems in Austria and their cross-border integration

National and International Cooperation

- Close cooperation with national bodies, e.g. Financial Market Authority, the Government Debt Committee and the Statistics Advisory Board (Statistikrat)
- Representation in a wide range of bodies of the Eurosystem, the ESCB and the EU
- International monetary policy cooperation and participation in international financial institutions (IMF, BIS)

Consultancy

- Drafting of laws and opinions

Selected Indicators for the OeNB

	2007	2006
Business indicators		
As on December 31	*EUR thousand*	
Net currency position	12,083,798	12,861,283
Banknotes in circulation	18,052,675	16,814,844
Total assets	61,946,135	53,377,876
Operating profit	246,663	192,955
Corporate income tax	61,666	48,239
Central government's share of the OeNB's profit	149,847	130,244
Profit for the year	16,650	14,472
	Absolute figures	
Full-time equivalent staff	917.5	931.7
Intellectual capital indicators		
	Number	
Inquiries to OeNB hotlines	38,516	38,153
Newsletter subscriptions	14,985	14,953
OeNB publications	63	64
Research cooperation projects with external partners	44	44
Working visits to national and international organizations	26	29
Environmental performance indicators		
Heat consumption, kWh/m²	45	62
Electricity consumption, MWh/employee	7.7	8.0
Paper use, kg/employee	85	136

Source: OeNB.

Our Mission Statement

In 2005, the national central banks of the independent Eurosystem (including the OeNB) published a joint mission statement that enshrines the following key objectives and values:

We in the Eurosystem have as our primary objective the maintenance of price stability for the common good. Acting also as a leading financial authority, we aim to safeguard financial stability and promote European financial integration.

In pursuing our objectives, we attach utmost importance to credibility, trust, transparency and accountability. We aim for effective communication with the citizens of Europe and the media. We are committed to conducting our relations with European and national authorities in full accordance with the Treaty provisions and with due regard to the principle of independence.

We jointly contribute, strategically and operationally, to attaining our common goals, with due respect to the principle of decentralisation. We are committed to good governance and to performing our tasks effectively and efficiently, in a spirit of cooperation and teamwork. Drawing on the breadth and depth of our experiences as well as on the exchange of know-how, we aim to strengthen our shared identity, speak with a single voice and exploit synergies, within a framework of clearly defined roles and responsibilities for all members of the Eurosystem.

The OeNB's mission statement complements the Eurosystem's mission statement and transposes it to Austrian requirements. The main messages are:

As the central bank of the Republic of Austria, the OeNB serves the Austrian and European public.

To build and maintain trust in the OeNB, we take pride in performing our tasks professionally, drawing on the high competence and motivation of our employees.

Our products and services are customer oriented to ensure their value to our customers and partners.

Ongoing market-oriented product and process innovation ensures the efficient and cost-effective provision of services in line with sustainability and in particular environmental protection.

We are cooperative, solution-oriented and reliable partners in our relations with customers and associates.

Our employees' commitment, motivation, creativity, willingness to learn, team spirit and mobility – the success factors of our work now and in the future – are the hallmarks of our working style.

Organization Chart

President
Herbert Schimetschek

Office of the General Council
Richard Mader

Vice President
Manfred Frey

Governing Board (Direktorium)

Central Bank Policy
Klaus Liebscher, Governor

Office of the Governor
Markus Arpa, Head

Internal Audit Division
Wolfgang Winter, Head

Communications Division
Günther Thonabauer, Head

Planning and Controlling Division
Gerhard Hohäuser, Head

Anniversary Fund
Wolfgang Höritsch, Head

Personnel Division
Axel Aspetsberger, Head

Future Unit
Peter Achleitner, Director

Money, Payment Systems, Accounting and IT
Wolfgang Duchatczek, Vice Governor

Legal Division
Hubert Mölzer, Head

Payment Systems and Information Technology Department
Wolfgang Pernkopf, Director

Information Technology and Payment Systems Strategy Division
Walter Hoffenberg, Head

IT Development Division
Reinhard Auer, Head

IT Operations Division
Erich Schütz, Head

Payment Systems Division
Andreas Dostal, Head

Cashier's Division and Branch Offices Department
Stefan Augustin, Director

Printing Office
Gerhard Habitzl, Head

Cashier's Division
Gerhard Schulz, Head

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Southern Austria Branch Office
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Organization and Internal Services Department
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Supervisory and Monetary Statistics Division
Gerhard Kaltenbeck, Head

External Statistics and Financial Accounts Division
Michael Pfeiffer, Head

[1] Environmental Officer Johann Jachs
As of April 29, 2008

In line with the Federal Act on the Oesterreichische Nationalbank, the Annual Report of the OeNB provides information about the monetary policy of the Eurosystem, economic developments, financial markets, payment services and cash services. Furthermore, it details the OeNB's national and international responsibilities and role. The OeNB's Financial Statements and the Notes to the Financial Statements are an integral part of the Annual Report.

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