



To the point!

Cross-Asset- and Strategy-Research

The Bundesbank is in the red

But profitability is of little importance to central banks

Two days ago, Bundesbank President Joachim Nagel presented the central bank's annual report. For once, the headlines did not revolve around Nagel's comments on monetary policy. Instead, the focus was on the loss incurred by the Bundesbank, which required the reversal of risk provisions of around €1 billion. But that's not all. Further and far greater losses are to be expected. In the coming years, the Bundesbank will record losses on a scale that will completely deplete the remaining risk buffer of €19.2 billion. The €2.5 billion capital stock is also expected to be washed away. The Bundesbank would then have negative equity.

Where the losses come from

The losses have been completely predictable. Similar effects will also occur at the other national central banks of the Eurosystem. Why?

The losses are the result of a combination of massive bond purchases by the Eurosystem on the one hand and the rapid turnaround in interest rates last year on the other. In the course of its bond purchases, the Bundesbank has accumulated securities worth more than €1 trillion. So over a thousand billions! And predominantly German government bonds. The Bundesbank took these onto the books at high prices. We remember: Bunds were characterized by negative interest rates.

Now interest rates have risen sharply since the summer of 2022. This means in reverse: The value of purchased bonds on the Bundesbank's balance sheet fell significantly. When the bonds mature, the Bundesbank realizes a loss. At the same time, the Bundesbank must pay commercial banks a positive interest rate



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The coming years will also bring losses for the Bundesbank

The losses are a direct result of the massive purchase of bonds at negative interest rates

on their deposits. The deposit rate is currently 2.5%, with an upward trend.

The central bank has negative "carry." The interest on their liabilities is higher than the interest on their assets. Losses are the inevitable consequence.

Why the losses should not worry us

The main sufferer is first and foremost the Ministry of Finance. For many years, no more Bundesbank profits will flow into the federal budget, since no profits will be generated that could be distributed.

More importantly: A central bank does not need capital. It is also not bound by regulatory capital requirements. It is not a commercial bank, but a central bank. That is, it has a monopoly on producing what everyone else is trying to get through hard work: Money.

As long as the credibility of monetary policy is intact, the capitalization and profitability of a central bank do not matter. There are examples of how negatively capitalized central banks have successfully conducted monetary policy over a long period of time, such as the central banks of Israel, Chile or the Czech Republic.

When the central bank makes losses and at the same time the credibility and independence of monetary policy are called into question, things get dicey. Therefore, the losses are a reminder: The rigorous anti-inflation course adopted must be maintained. A return of inflation to the 2% target will remove doubts about the credibility of the Eurosystem. Then the profitability of the central bank does not matter. Except for Minister of Finance Christian Lindner.

A central bank
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