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In Charts, the dots indicate the actual data, and the lines reflect the smoothing approximation of the data. The smoothing approximation of the daily data is more distinguished than the curve of the actual data.

Details may not add because of rounding-off.

– *no transactions or no outstanding amounts in the period.*
x *no data available or no computation of indicators possible.*
0 *the indicator is below 0.5 but over 0, or the result of the computation of the indicator is 0.*

Photos: Ieva Lūka and Andris Tenass

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ABBREVIATIONS

ABSPP	asset-backed securities purchase programme
BIS	Bank for International Settlements
BRIC countries	Brazil, Russia, India and China
CBPP3	third covered bond purchase programme
CPI	Consumer Price Index
CSB	Central Statistical Bureau of Latvia
EBA	European Banking Authority
EC	European Commission
ECB	European Central Bank
EEA	European Economic Area
EFC	Economic and Financial Committee
EKS	Electronic Clearing System of Latvijas Banka
EMU	Economic and Monetary Union
ERM II	exchange rate mechanism II
ESA 2010	European System of Accounts 2010
ESCB	European System of Central Banks
ESFS	European System of Financial Supervision
ESRB	European Systemic Risk Board
EU	European Union
EURIBOR	Euro Interbank Offered Rate
Eurostat	Statistical Bureau of the European Union
FCMC	Financial and Capital Market Commission
FRS	US Federal Reserve System
GDP	gross domestic product
HICP	Harmonised Index of Consumer Prices
IMF	International Monetary Fund
INTS	internet statistical database of Latvijas Banka
IP	Internet Protocol
IT	information technologies
JSC	joint stock company
LCD	Latvian Central Depository
Ltd.	limited liability company
LTRO	longer-term refinancing operations
M1	narrow monetary aggregate
M2	intermediate monetary aggregate
M3	broad monetary aggregate
MFI	monetary financial institution
Ministry of Finance	Ministry of Finance of the Republic of Latvia
NCB	national central bank
OECD	Organisation for Economic Co-operation and Development
OPEC	Organisation of Petroleum Exporting Countries
OTC	over-the-counter trading
SAMS	Interbank Automated Payment System of Latvijas Banka
SEPA	Single Euro Payments Area
SJSC	state joint stock company
SSM	Single Supervisory Mechanism
TLTRO	targeted longer-term refinancing operations
UK	United Kingdom
UN	United Nations
US	United States of America
VAT	Value Added Tax
WTO	World Trade Organisation

FOREWORD OF THE GOVERNOR

We now have had one year with the euro. We can enjoy a more convenient flow of money, reduce the servicing costs of public debt, save the costs of currency conversion, and live without worry about the possible devaluation of the national currency. Despite the uncertainty caused by the geopolitical situation, the euro has helped to keep the economic growth rate in the positive territory.

At the same time, we have found out that the euro is no magic wand or a panacea for the solution of all problems. Even though the monetary policy carried out by the Eurosystem is favourable to Latvia's economic development, it is up to us to continue decisive reconstruction and modernisation of the economy, also raising its competitiveness.

The economy of Latvia in 2014 was significantly impacted by the developments in external markets, including the complicated geopolitical situation in eastern neighbouring countries, the rapid drop in the exchange rates of currencies of CIS countries, and the slow recovery rate of the euro area economy. The influence of the developments in the euro area economy was decisive, for the EU countries are the most important trading partners of Latvia.

The euro area growth in 2014 was weaker than expected, giving rise to concerns about future growth prospects in the region. For that reason, large scale monetary policy measures were launched in the euro area in order to stimulate economic activity in Europe and prevent low inflation risks. The Governing Council of the European Central Bank took several important decisions and, in January 2015, announced the launch of an extended asset purchase programme.

Latvia has been an active participant in addressing significant euro area economic growth issues. Latvia's accomplishments in overcoming the economic crisis and organising its economy are important for the entire euro area, for tasks of similar complexity – putting the fiscal policy in order, regaining economic competitiveness, carrying out structural reforms – are on the agenda of all European countries. A stimulating monetary policy can achieve better results only if structural reforms are implemented in the entire euro area simultaneously, strengthening both the common economy and the economies of individual members of the monetary union.

The rate of economic growth slowed in Latvia in 2014, and Latvijas Banka therefore called for complex growth-stimulating measures in various areas. This call has been heard, as evidenced by the decisive actions taken by the Government and the Saeima of the

Republic of Latvia, in the Insolvency Law amending the provisions impeding creditors' activities. However, many other problems are to be addressed, including maintaining rational and sustainable budget policy amidst sluggish economic growth, carrying out reforms in education and healthcare, and establishing order in the legal environment.

In 2014, the growth of the gross domestic product in Latvia was stable albeit gradually losing momentum. This dynamics resulted from a weaker contribution by those sectors which had been the main engines of growth in previous years. At the same time, further growth was ensured by the sectors oriented towards domestic demand – trade, construction, and public services.

A cause for concern was the prolonged period of low investment activity, which was probably related to the decisions by entrepreneurs to postpone investment in view of the negative geopolitical situation.

Persisting uncertainty in the geopolitical situation may continue to dampen entrepreneurs' risk appetite and investments in business expansion as well as to prevent households from making bigger purchases, thus stimulating the formation of accruals. The resumed operation of JSC *KVV Liepājas metalurgs* in 2015 and low oil prices have a potential positive impact on the growth of the Latvian economy.

As for the work of Latvijas Banka in 2014, it must be emphasised that the year was a transition period in many areas. Active participation in the Eurosystem had the effect of significantly changing the discharge of some of Latvijas Banka's functions.

The duties of Latvijas Banka in the area of international cooperation increased significantly as it integrated into the Eurosystem. Latvijas Banka became a fully-fledged monetary policy implementer. That had a favourable effect on the ability of the Latvian financial system to make use of important financial resources under a series of targeted longer-term refinancing operations (TLTROs) launched by the Eurosystem in 2014 and the expanded asset purchase programme which started in 2015. Moreover, the euro base rates were set at their historically lowest levels, and that had a positive impact on borrowers and further reduced the costs of servicing the public debt.

The introduction of the euro brought about important changes in the payment systems maintained by Latvijas Banka. The careful preparations facilitated successful modification of the payment systems for settlements in euro and completion of their migration to SEPA. Interbank payments became faster and more convenient in Latvia. As of November 2014, the operations of Latvijas Banka's electronic clearing system (EKS) were ensured also on the working days transferred by the Cabinet of Ministers Decree that are TARGET2 holidays.

The introduction of the euro required the transformation of the Credit Register maintained by Latvijas Banka. Important amendments to the Law on the Credit Register came into effect, expanding the goals of the Credit Register, inter alia including the provision that Latvijas Banka has the right to provide the information included in the Credit Register also to the EU institutions.

In the area of statistics, Latvijas Banka was involved in the common euro area project in 2014, organising Latvia's participation in the survey of household finances and consumption, and collected statistical information for the preparation of Eurosystem's monetary statistics and euro area statistical data as well as for the discharge of Latvijas Banka's tasks.

Important work has been accomplished informing the public on such practical issues related to the euro changeover as the exchange of lats for euro, the adjustment of the payment system, the design and security features of the euro currency. One year after the changeover, Latvian businesses and general public are among the best informed in the euro area regarding the design and security features of the euro.

In the autumn of 2014, European and Latvian policy makers, economists, opinion leaders, entrepreneurs, academics and representatives of Latvian and world media gathered for Latvijas Banka's annual economic conference. On the agenda at this forum were the lessons of the economic crisis of 2008 both in individual countries and in the euro area at large and measures to be taken to ensure sustainable and stable economic growth.

People all over Europe now have an opportunity to appreciate Latvia's contribution to coin art. In 2014, Latvijas Banka continued the tradition of striking collector coins, now denominated in euro, and also issued the first commemorative 2 euro coin "Riga – European Capital of Culture 2014". These activities attracted the attention of local and foreign numismatists and other interested parties, since the Latvian euro coins are among the most beautiful in the euro area.

Thinking about the work of Latvijas Banka in 2014, the words of the outstanding Latvian poet and playwright Rainis "Only what changes will last" come to mind. Intensive work can be expected also in 2015, which will be a turning point in the economic development of the entire euro area. Latvia too must use the opportunities provided by the favourable monetary policy.

The euro introduction demonstrated that we are capable of undertaking the most complicated tasks, and our first year in the euro area proved that we are equal partners to the other euro area countries ready to make a contribution to addressing the common problem issues of the European economy.

The performance of the Council, Board and each and every employee of Latvijas Banka has been and will continue to be of crucial importance in everyday work and in finding new solutions. I would like to express my sincere gratitude to all of them for their selfless and enthusiastic work and wish them every success in their future activities.

Ilmārs Rimšēvičs
Governor of Latvijas Banka
Riga, 27 March 2015

STATEMENTS OF VISION, MISSION AND VALUES OF LATVIJAS BANKA

VISION OF LATVIJAS BANKA

Latvijas Banka is a participant of the Eurosystem and a full-fledged member of the European System of Central Banks and makes a significant contribution to stable and sustainable economic development of Latvia and the euro area. Latvijas Banka is an independent entity that carries out its tasks in the public interest and with a high sense of professional responsibility. Latvijas Banka is a reliable cooperation partner and the economic competence centre in Latvia.

MISSION OF LATVIJAS BANKA

The primary operational goal of Latvijas Banka as the central bank and a participant of the Eurosystem is price stability promoting long-term economic growth. The principal tasks of Latvijas Banka are as follows:
– participate in the formulation and implementation of the euro area's monetary policy;
– manage financial investment;
– ensure cash currency circulation in Latvia and participate in shaping the cash currency circulation in the euro area;
– participate in promoting smooth operation of payment systems in the Eurosystem;
– prepare and publish statistical information in compliance with the provisions of the European Union legislation.

Latvijas Banka performs the tasks entrusted to it in a professional and continuous manner, ensuring high-quality work and efficiency.

Latvijas Banka contributes to the general public's knowledge of economics and is an active participant of the Eurosystem.

VALUES

Our values reflect our attitude towards work, colleagues and society.

Competence:
– we have in-depth knowledge and excellent skills;
– we learn from the best practices of others and serve as a model for others;
– we find quality and effective solutions.

Credibility:
– we work in the public interest, and we are interested in public opinion;
– we act in a responsible and predictable manner;
– our operations and activities are transparent – we act openly and explain our action.

Cooperation:
– we work as a team;
– we are responsive and open to new ideas;
– we listen to recommendations and maintain good long-term partnerships;
– we are result-oriented.

ECONOMIC ENVIRONMENT

GLOBAL AND EURO AREA ECONOMIC ENVIRONMENT

CURRENCY AND FINANCIAL MARKETS

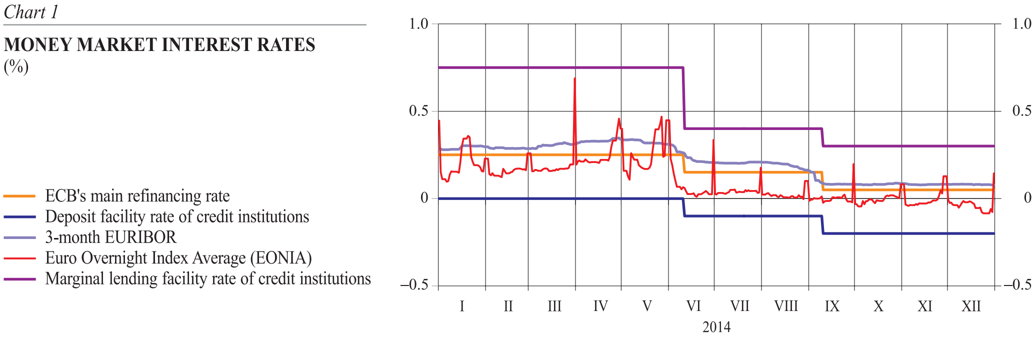
The trend of global economic growth observed in the previous years persisted, with the GDP growth rate gaining some momentum yet remaining subdued in advanced countries and falling in emerging market economies. Speaking about the advanced economies, GDP growth was more pronounced in the US and the UK, while the respective growth figures for Japan and the euro area were close to zero. Of major emerging economies, China and India succeeded in retaining growth at the previous year's level, but the economies of Brazil and Russia were stagnating in 2014. To aid their economies, central banks of advanced countries kept pursuing expansionary macroeconomic policies. By increasing money supply in the economy they supported the expansion of stock markets (except in the UK) and improvement of consumer sentiments, which in most cases facilitated strengthening of private consumption. Nevertheless, the overall inflation rate tended to decline even in the face of the expanded money supply implemented by central banks of advanced countries. Low-level inflation was driven by the sharp drop in oil prices in the second half of 2014. The falling demand for oil as well as the ample oil supply triggered not only some decline in consumer prices but also redistribution of incomes between oil producers and oil importers, with the incomes of former falling and of latter rising. Prices of many other commodities went down as well. Intensifying financial market risks and the conflict in Eastern Ukraine preconditioned a gold price hike; however, it was offset by the declining pace of inflation and stronger US dollar.

Oil price dynamics had the largest surprise in store for financial market participants in 2014. The price of *Brent* crude oil, which had been stable early in the year, demonstrated, starting with June, a dramatic fall from 115 US dollars per barrel and at the close of the year stood at 57 US dollars per barrel, recording a 48% annual contraction. This sharp oil price drop was triggered by incommensurate oil demand with oil supply: despite the volume of oil production rapidly expanding, the growth rate in the leading oil-consuming countries, including China, was losing momentum. The meeting in November of OPEC members was decisive: the pleas to cut production amidst reinforced overproduction concerns of some members of the group did not meet any support. Market participants predict low oil prices to persist also in 2015. It is expected to boost the economic activity and purchasing power of the population in the regions that heavily depend on oil imports (including those in the US and the euro area).

Financial market sentiments were determined by the world leading central banks being more and more split in their monetary policy stances. The FRS decided to conclude its asset buying programme and was on its way to raise the main refinancing rate, thus confirming the end of its accommodative monetary policy; the ECB, at the same time, lowered its main refinancing rate to a record low (see Chart 1) and, in order to boost the economy, launched several asset buying and long-term lending programmes. The central banks of Japan and China also engaged in implementing stimulus measures.

Chart 1

MONEY MARKET INTEREST RATES
(%)



The conflict between Russia and Ukraine undermined the fragile euro area recovery and alerted the investors.

The MSCI World index grew by 2.9% in 2014 (a notable downslide from 24.0% growth in 2013). It was on account of distinctive dynamics in major world economies, future perspectives and uncertainty due to geopolitical conflicts. The Japanese stock market index Nikkei 225, having recorded a record high hike in 2013, picked up a mere 7.1% in 2014. After the central bank of China had launched its stimulus measures, the Chinese Shanghai Composite stock index sharply rose in the concluding months of the year, with investors' earnings amounting to 53% over the year (the highest yield among leading stock indices of the world).

Of advanced countries, stock market growth was most dynamic in the US where the leading stock indices repeatedly reached their historical highs. S&P 500 rose by 11.4%, and Dow Jones Industrial Average grew by 7.5%. The US stock market showed some signs of volatility which in combination with market improvements for the fifth year in the run arouse investors' concerns about a potential overestimation of stock prices. However, along with the US announcements of positive growth indicators, these worries were softening. Across the euro area, new concerns about slipping into recession were emerging.

In the course of the year, Europe's Dow Jones EURO STOXX 50 picked up mere 1.2%, while Germany's DAX grew by 2.7%. Most volatile was the Greek stock market, which had entered the year as being the most profitable, but affected by the bank stress test results and political instability suffered a collapse in the second half of the year. The Greek ASE index plunged 28.9% over the year.

The euro area bond market sentiments were primarily underpinned by market participants' expectations regarding the ECB's stimulus measures, both already implemented and projected for the future, for the euro area economy. Late in the year, market participants became more assured that the ECB would take to additional stimulus measures, including also sovereign bond buying, in the near future. Together with the ECB decisions, among them the resolution to introduce a negative deposit facility interest rate in June, these expectations were the main triggers behind unprecedentedly low interest rate levels in money and capital markets. The yields on German government bonds, which are deemed to be the safest euro area securities, contracted to a historical low. In the meantime, yields on the German government bonds with agreed maturity of up to five years became negative, while the yield on the government 10-year bonds slipped from 1.93% at the beginning of the year to 0.54% at its close. The yields on government bonds of other developed euro area countries also contracted notably.

The low interest rates on safer investment urged investors to favour profit opportunities in riskier markets. As a result, the risk premium on government securities of other euro area countries decreased and the yields went down to historically lowest levels. The yields (in annual terms) on Portugal's government 10-year bonds contracted most (by 336 basis points; to 2.65%). Other euro area countries, particularly the sovereign crisis hardest-hit ones like Italy, Ireland and Spain, also saw the yields on government bonds contract markedly (to 1.87%, 1.24% and 1.60% respectively). The Greek government bonds were an exception, for their yields grew rapidly at the close of the year due to a stronger political risk and growing uncertainty about Greece's further participation in the international loan programme. The yield on the Greek government 10-year bonds rose from 8.27% to 9.42%.

In 2014, when the divergence of central bank monetary policy stances became more apparent, the spread between the yields on the US and German government bonds widened. As was expected, on 29 October the FRS decided to conclude its asset buying programme, seeing continued progress in the US economy towards attaining the employment and inflation targets, and anticipating increases in the target range for the federal funds rate as an upcoming decision. Despite the financial market participants' predictions of higher US interest rates already in 2015, the yields on US government 10-year bonds declined from 3.02% to 2.17% over the year.

In 2014, the euro to US dollar exchange rate declined by 12.0% (from 1.3743 at the close of 2013 to 1.2098 a year later), with its maximum (1.3993) on 8 May 2014 and minimum (1.2097) on 31 December 2014. A weaker euro was mainly driven by the sluggish economic growth in the euro area and the divergence of the ECB and FRS's monetary policies which facilitated the outflow of capital to financial markets that promised better profit earning opportunities.

A stronger US dollar occurred due to relatively higher interest rates in the US, lower commodity prices, security considerations amidst rising geopolitical threats and the anticipated acceleration in economic growth. The US dollar gained more in value in the second half of the year when the pace of economic development gathered speed and the labour market situation kept on improving, supporting market participants' expectations of interest rate hikes in the near future.

The US dollar to Japanese yen exchange rate rose from 105.31 at the end of 2013 to 119.78 at the end of 2014 (an increase of 13.7%), with its maximum (121.85) on 8 December 2014 and minimum (100.76) on 4 February 2014. A further decline in the value of Japanese yen was underpinned by the combination of expansionary monetary policy, aimed at avoiding the long-standing deflation, and much higher interest rates in the US. The exchange rate of the British pound sterling against the currencies (excluding the US dollar) of other developed countries appreciated and was supported by a better economic outlook, improvement of labour market situation and market expectations of Bank of England's higher interest rates in the near term. The British pound sterling to US dollar exchange rate lost 5.9% over the year (from 1.6557 at the end of 2013 to 1.5577 at the end of 2014), with its maximum (1.7192) on 15 July 2014 and minimum (1.5486) on 23 December 2014.

The conflict between Russia and Ukraine alerted the investors and shattered the financial markets in both countries. The financial market of Russia suffered a double shock from capital outflows associated with uncertain outlook of economic growth, political instability and falling oil prices, and also from the sanctions imposed by the US, the EU and other countries depriving Russian government-owned banks and enterprises of the access to capital markets in the US and Europe. The Russian ruble to euro exchange rate depreciated by 38% and to US dollar by 46% over the year. In order to curb the rapidly rising inflation and in support of the national currency, the Central Bank of the Russian Federation raised the base rate on four occasions in 2014 (from 5.5% early in the year to 17% at its close). Moreover, the central bank conducted interventions, worth 80 billion US dollars, in the foreign exchange market, while its foreign reserves contracted by 24% (to 388 billion US dollars).

REAL SECTOR

The global economy grew at a faster pace in 2014 than expected earlier, with the global GDP growth rate almost on a par with the previous year (3.3%). Markedly uneven growth rates across world's major economies were typical for the year. The development was quite successful in the US and the UK, while the euro area and Japan recorded sluggish economic activity in 2014 on account of the effects of the recent financial crisis and weaknesses related to unaddressed structural problems, e.g. high unemployment rate in many EU economies. Often driven by cyclical factors, tougher monetary and financial conditions, and political instability, the growth in emerging market economies was moderate overall in 2014. Major developing countries also showed pronounced differences in their growth rates, with that in China decelerating, economic activity gaining momentum in India, but Brazil and Russia displaying notable economic worsening.

Following a short break early in the year, the US economy posted certain acceleration from the second quarter onwards, reaching the steepest GDP growth in the last 10 years already in the third quarter. The US economic recovery was spurred by accommodative monetary policy, softer fiscal consolidation vis-à-vis 2013 and an improving US labour market situation, which positively impacted the purchasing power of the population. The improved US real estate market situation and falling global oil prices were positive incentives as well, and thus the private demand remained the main US growth engine.

The euro area activity, particularly in its major countries like Germany, France and Italy, also fell behind the projections in 2014. Due to stagnation in industry primarily because of falling producer confidence caused by complicated geopolitical conditions, Germany recorded a slow GDP growth rate in the first three quarters of the year. In 2014, the most important driver of growth in Germany was private consumption; towards the close of the year, producer sentiments improved and production output expanded; exports were likewise on an upward trend. However, in the year overall, the German GDP growth fell behind the expectations. As to France, its economy was stagnating for the third year in the row. In 2014, France's GDP picked up 0.4% due to somewhat improved activity in the fourth quarter when inventory adjustments and government consumption resulted in a positive GDP indicator. In 2014, the economy in Italy underwent a downslide for the third time since 2009. Both Italy and France face a serious problem of unemployment rate which affects negatively the population's confidence. In Spain and Ireland GDP trended upwards, as an effective post-crisis economic policy was implemented and supported the revival of population's confidence, thereby also strengthening the private demand.

Following a period of considerable fiscal consolidation which the euro countries had been going through since 2010, the overall fiscal situation continued to improve somewhat in 2014, and the euro area budget deficit slipped to 2.6% of GDP. Nevertheless, the level of sovereign debt in the euro area remained high in 2014 (94.4% of GDP).

Lower oil prices in global markets are likely to have a positive impact on the economic activity in oil-importing countries, while their effect on oil-exporting nations is negative. The Russian economy was subdued by the low oil prices, steep depreciation of the Russian ruble, imposed sanctions and weak economic diversification. Despite contracting investment and weakening private consumption, GDP in Russia continued to grow in the first three quarters of 2014, primarily driven by a positive net export contribution to GDP (caused by falling imports), richer-than-expected harvests and relatively good industrial performance. A fall in Russian imports was triggered by moderating domestic demand due to weaker purchasing power as well as the effects from the sanctions imposed on Russia and weaker Russian ruble. Purchasing power in Russia was negatively affected by climbing inflation, with consumer price inflation rising to 11.4% in December (from 6.1% in January). The fourth quarter saw a short-lived uplift in private consumption triggered by the steep depreciation of the Russian ruble at year's end, which made people purchase consumer durables. At the end of the year overall, the activity in the Russian economy weakened: manufacturing lost momentum, problems in financial and corporate sectors became more pronounced, and consumer and business confidence worsened.

The pace of GDP growth in Lithuania slowed somewhat mainly on account of reduced demand from Russia, Lithuania's main partner in foreign trade, and negative effects of the imposed sanctions. Consequently, private demand acted as the main growth engine in Lithuania in 2014. Estonia, in turn, demonstrated the least dynamic GDP growth of all Baltic States, which, notwithstanding the abating demand in Estonia's major trade partners (Russia, Finland and Sweden) and negative effects from the sanctions, still remained slightly above the 2013 level. Similar to Lithuania and Latvia's other trade partners, the economic growth in Estonia in 2014 depended on stronger domestic demand, while the complex external circumstances had a downward pressure on export expansion.

In Poland, Denmark, Sweden and the UK, the other major trade partners of Latvia, GDP growth was positive in 2014 primarily on account of private demand.

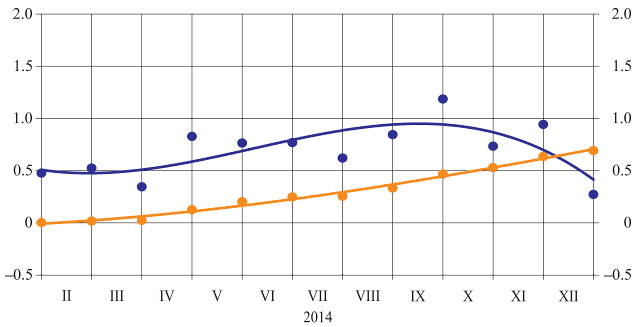
LATVIA'S ECONOMIC ENVIRONMENT

INFLATION AND PRICES

Untypical for Latvia's circumstances, inflation was lingering at a low level for the second year in a row in 2014 (average annual HICP at 0.7%; see Chart 2). A rise in inflation vis-à-vis 2013 was primarily on account of domestic factors. Despite the average price rise of 1.5% for the consumption basket without food and energy prices, the actual inflation level differed rather strongly from the projections at the beginning of 2014 due to a number of factors.

Chart 2

HICP DYNAMICS
(%)



HICP (year-on-year basis)
Last 12-month average HICP

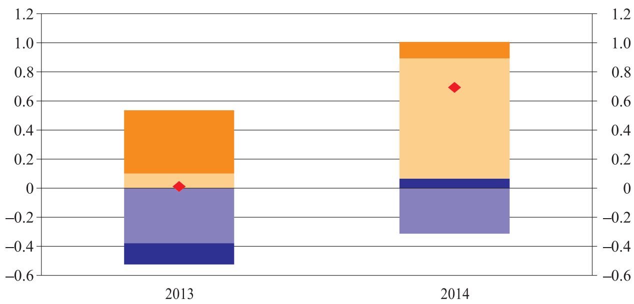
Source: CSB data.

The conflict between Russia and Ukraine broke out as early as February and soon became a drag on the external demand; as a result, the pace of economic growth was subdued both in Latvia's major trade partners and at home, without exerting demand-side pressure on prices and boosting import-driven inflation. Whereas in March it was resolved to postpone the electricity market liberalisation from April 2014 to January 2015, which made the actual inflation level differ from the projected one by around 0.5 percentage point.

Given the tightening competition in oil production during the year amidst a balanced demand for energy, the global oil prices kept falling at an accelerated pace, directly (via prices of fuel and other types of energy) driving inflation down and curbing price hikes in various goods and services sectors (see Chart 3).

Chart 3

CONTRIBUTION OF INDIVIDUAL GROUPS TO AVERAGE ANNUAL HICP
(percentage points)



Food, alcohol, tobacco
Services
Other tradable goods
Energy
Average annual HICP (%)

Sources: CSB and Eurostat data.

Energy price changes did not trigger a rise in global food prices, while more favourable weather conditions in major milk-exporting countries supported a downturn in prices. The good grain harvest pushed up the grain stock estimate, thus maintaining prices at a lower level.

Along with the effect from the global food price falls, a decline in food prices (mainly dairy and meat products) in Latvia was spurred by Russia's sanctions imposed on trade with the EU countries. Meanwhile, prices of some individual product groups were on a moderate upward trend. This trend was characteristic for food products of longer storage life (e.g. cheese).

A gradual economic growth and higher incomes, hikes in excise tax on tobacco and a weaker euro all exerted an upward pressure on average annual inflation. Rising real incomes and declining prices of some food products and energy maintained the purchasing power and demand for services. As a consequence, the rise in services prices was more pronounced than in 2013. The weakening of the euro held down a drop in the prices of tradable energy goods.

The average annual producer price increase in manufacturing was 0.4%, including 0.2% for domestically sold output. Most of this increase (around 3/4) was on account of higher water and sewage tariffs in Riga, simultaneously mirrored also in consumer price hikes. Producer prices in food industry and energy sector, in turn, were on a downward trend, with the largest negative contribution of domestically sold output to producer price dynamics. Food product price falls were more pronounced than the developments on the consumption side. On the one hand, production is showed as a stage of the consumer price formation process; on the other hand, it could figure also as a partial explanation for weaker elasticity of food product consumption vis-à-vis other goods. Due to regular purchases and constant consumption, food products are among those goods that make up the so-called FROOP (frequent out of pocket purchases) component, which, due to consumption inelasticity, is characterised by a steeper average price rise for a longer period of time than the rest of the consumer basket. As the average income level in Latvia is lower, its share in total consumption is larger than the EU average.

GROSS DOMESTIC PRODUCT

Latvia's GDP increased by 2.5% in 2014 (according to working day adjusted data), but its pace of growth vis-à-vis 2013 decelerated (4.8%). This deceleration was a phenomenon of the whole year, with the growth rate approaching 2% in the fourth quarter. A loss in growth momentum is projected for 2015 as well.

Being the key driver of growth dynamics in 2014, private consumption expanded by 2.6% and contributed 1.6 percentage points to the pickup in GDP. A rather steep rise in disposable income, particularly supported by an increase in average wages, brought about an upswing in population's purchasing power: the annual rate of growth in real net wages preserved high levels throughout the year. It can partly be associated with some reduction in the size of shadow economy.

Nevertheless, the contribution from consumption turned out to be smaller than predicted earlier, because spending was restricted by precautions about the economic perspective and thereby revived the intention to build savings. In early 2014, spending was subdued due to recovery of saving practices after the euro changeover. Since spring, in turn, the related precautionary attitudes and uncertainty about future incomes were heightened by the conflict between Russia and Ukraine, economic sanctions imposed by Russia and still sluggish economic development of the euro area countries.

Exports ranked second among most important GDP growth engines in 2014. Despite the falling demand from Russia and weak economic development of the EU countries, real exports of goods and services increased by 2.2%, contributing 1.3 percentage points to GDP growth. Deterioration in the demand from Russia and the weakness of Russian ruble adversely impacted the economic activity of several companies; nevertheless, their attempts to find new markets in combination with a weaker euro (the latter enabling

Latvia to compete more effectively when exporting outside the euro area) resulted in maintained production and export volumes.

Because of the geopolitical circumstances, investors also remained watchful. Their stances were reinforced even more by the amendments introduced to the Immigration Law and the Insolvency Law that reduced the activity in the construction and real estate sectors. As to gross fixed capital formation, it continued to intensify in 2014 overall, increasing by 2.2% and contributing 0.5 percentage point to GDP growth (on account of the increase in the first half of the year as the dynamics turned negative in the third quarter).

Investment in manufacturing continued on an upward trend. In 2014, the production capacity utilisation was at a high level and in the fourth quarter even reached a historic high of the last nine years (73.3%). Notwithstanding the still existing production capacity utilisation potential (as in the Latvian manufacturing sector production capacity utilisation has historically lagged behind the EU average), a further export expansion requires new investment. This drive, notably supported by financing from the EU funds, is likely to promote investment in manufacturing also in the future.

In 2014, government consumption grew by 3.2%, providing a 0.5 percentage point contribution to GDP growth. Contribution from inventories, on the other hand, was negative (0.5 percentage point) despite the fact that an increase could have been anticipated due to decelerating economic growth and the effects of Russian embargo. Vis-à-vis the previous year, inventories shrank in 2014. The opposite trend observed in 2013 was determined by several factors, among them merchant expectations of higher demand prior to the euro changeover, high-running stocks of raw materials and finished goods due to financial problems of JSC *Liepājas Metalurgs*, and exporting of several ships produced at the JSC *Rīgas kuģu būvētava* initially pushing up but afterwards reducing the level of inventories.

Real imports of goods and services expanded by 1.5% in 2014. This relatively moderate pickup can be explained by weak investment dynamics, decelerating export (including re-export) and consumption growth as well as the replacing of imports with domestic goods.

In 2014, total value added increased by 2.1%, which, albeit, was less than in the previous years. This increment depended primarily on the construction sector, which contributed 0.6 percentage point (10.4% rise at constant prices) to the annual growth in value added mainly on account of the construction of residential, educational, manufacturing and warehouse buildings. With the labour market situation gradually improving and disposable income of households rising, also wholesale and retail trade influenced the developments in value added positively (contribution of 0.3 percentage point and 2.1% at constant prices to its annual growth respectively). Positive contributions to total annual growth in value added came also from transport and storage (0.3 percentage point and 3.1%), public administration and defence (0.4 percentage point and 3.4%), and product tax hikes (0.6 percentage point and 4.6%). Meanwhile, the value added dynamics in economy was adversely affected by real estate activities (0.1 percentage point negative contribution to total annual growth in value added; 0.6% annual decrease) and mining and energy (0.1 percentage point and 2.5%).

At constant prices, the volume of manufacturing output remained almost unchanged (a fall of 0.1%; working day adjusted data), whereas at current prices, a reduction of 0.5% was recorded (not working day adjusted data). Even though no manufacturing output contractions had been recorded since the economic crisis, the situation in 2014 was deteriorating due to the Russian–Ukrainian conflict and problems associated with the respective markets, recovery of the euro area economy which was too slow, and discontinuation of JSC *Liepājas Metalurgs* operation in the middle of 2013 with a continuous adverse impact on industrial production. In 2014, manufacturing was supported by the domestic demand: amidst weak external demand, manufacturing exports contracted more than domestic sales. The turnover of domestically sold manufacturing output at current prices declined by 0.9% in 2014 (working day adjusted data), while that of manufacturing exports posted a 1.3% contraction.

Similar to the previous year, the largest negative contribution to annual changes in manufacturing came from the manufacture of base metals due to discontinued operation of the JSC *Liepājas Metalurgs* and problems of other sector companies. Likewise, negative contribution came from repair and installation of machinery and equipment, manufacture of beverages and of textile articles and wearing apparel (basically on account of Russian market problems). Meanwhile, the largest positive contributors to annual growth in manufacturing were the sectors of wood and articles of wood and cork, and computers, electronic equipment and optical products. Although the output of Russian-sanctions-hit food products grew in the year overall, the output index was on a downward trend over the year, primarily due to the shrinking output of dairy products.

Retail trade turnover expanded by 3.6% in 2014, with trade in food and non-food products growing at similar rates. The same growth rate was observed also for automobile sales. The breakdown of dynamics by month, e.g. in the euro changeover context and with expenditure rising during the then warm Easter Holiday season, showed sharply distinctive results.

Despite generally upward dynamics, precautionary attitudes of the population held trade back from growing at even a faster pace in the situation of apparently smaller tourist spending. The demand for luxury goods contracted as the weakening purchasing power of visitors from Russia notably reduced the sales of brand clothing, watches, jewellery, investment gold and electronic products. In other trade segments, falling numbers of visitors from Russia were offset by tourists from Germany, the UK, Estonia and Lithuania who arrived to enjoy the versatile programme of the European Capital of Culture.

In 2014, the transport and storage sector developed at a faster pace than in 2013. The volume of cargos loaded and unloaded at Latvian ports posted a 5.2% increase (to 74.2 million tons), with Riga and Liepāja ports recording growth and some decline observed at Ventspils port. Volumes of cargoes reloaded went up even despite the existing geopolitical uncertainty and news coming from Russia about their plans to redirect the cargo traffic from other Baltic ports to Russian ports. The amount of coal reloaded at Latvian ports shrank in 2014 (largest contraction at Ventspils port). It was, however, more than compensated by rising volumes of oil products reloaded at Riga port. Volumes of reloaded base metal cargoes, affected by discontinued operation of JSC *Liepājas Metalurgs*, contracted at Liepāja port, while good harvests reaped both in Latvia and Russia triggered a sharp boost in the volume of reloaded grain cargoes. As to transportation by rail, 57.0 million tons were hauled, i.e. 2.2% more than in 2013. The rise in cargo transportation was determined by expanding volumes of import and export freights. The volume of transit freight transported by rail contracted, meanwhile 62.2 million tons of freight (2.7% more than in 2013) was transported by road. The increase in the overall freight traffic was primarily on account of expanding international freight traffic (15.3%), while the volume of domestic freight transport, recording a slight 0.2% pickup, remained broadly unchanged.

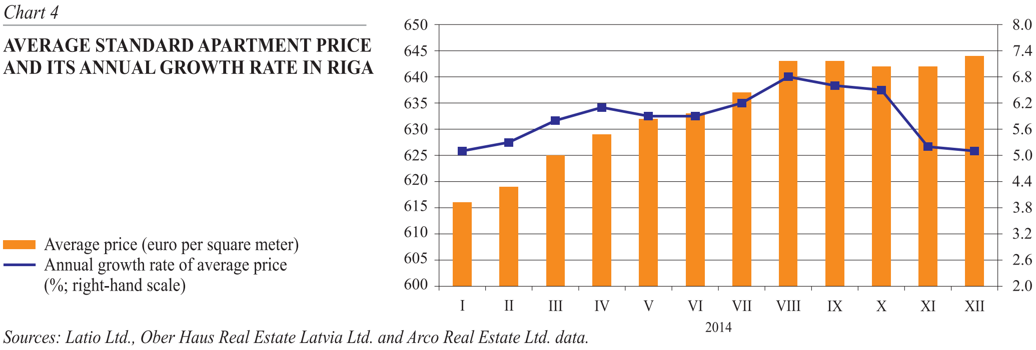
In 2014 vis-à-vis 2013, non-financial investment (at current prices) posted a 0.9% increase. Most of the positive contribution to non-financial investment growth was ensured by manufacturing (2.3 percentage points to total growth; 21.2% annual growth in non-financial investment). Stronger investment dynamics in manufacturing was mainly on account of financing from the EU funds in the concluding phase of the 2007–2013 programming period. The contribution coming from information and communication services was also positive (1.5 percentage points and 35.7%), mainly due to larger investment by major mobile telecommunication companies aimed at improving mobile network coverage. Investment, driven by the expanding retail trade turnover and demand for additional retail premises, grew also in wholesale and retail trade (1.5 percentage points and 29.7%). The largest negative contribution to the growth of total non-financial investment came from the sector of electricity, gas steam and air conditioning supply (2.6 percentage points and 19.4%); this sector recently received significant injections and a number of large sector projects were concluded therein. Investment in public administration and defence and mandatory social insurance also shrank, thereby accounting for a considerable negative contribution (1.1 percentage points and 5.0%).

Real estate market was bustling moderately in 2014. In comparison with 2013, the number of registered purchase agreements was 1.1% higher in the year overall (1.5% annual increase in the number of purchase agreements in Riga). The real estate market activity was intensifying until August, when, with the passing of amendments to the Immigration Law, which came into effect as with September and tightened the terms and conditions entitling to temporary residence permits for real estate investors, it decelerated markedly. Towards the end of the year, real estate transactions contracted notably both in the country as a whole and Riga.

Large demand for housing in new housing projects from non-residents was the primary driver of the related price hikes. Price changes in the standard apartment market, on the other hand, were not so pronounced, with the average price picking up 5.1% over the year. At the end of 2014, the average apartment sales price stood at 644 euro per square meter (see Chart 4).

Chart 4

AVERAGE STANDARD APARTMENT PRICE AND ITS ANNUAL GROWTH RATE IN RIGA



Sources: Latio Ltd., Ober Haus Real Estate Latvia Ltd. and Arco Real Estate Ltd. data.

The housing rental market was buoyant in 2014, as quality housing for rent was much in demand among students and employees of foreign corporations as well as residents with limited opportunities to purchase housing. As a result, the supply of adequate housing for rent in Riga decreased, and the rent continued to soar.

LABOUR MARKET

In 2014, unemployment continued on a downward trend while wages were increasing. The cyclical component of unemployment remained close to zero. A gradual decline in unemployment was on account of the structural component which was soaring vis-à-vis the EU average; its further decrease is likely to rely on the efficiency of the policy targeted at individual population groups and regions. Employment growth was delayed by negative demographic developments (shrinking numbers of population in general and of working-age population) and slowing economic dynamics. The purchasing power of average wages (for full-time employment) rebounded to pre-crisis levels in 2014, thereby supporting stronger private consumption amidst weak external demand. Wage growth slightly exceeded productivity growth. Yet, owing to Latvia's rather low labour income share in total value added in comparison with the EU average, resilient profitability indicators and positive export share dynamics in imports of other countries, the competitiveness issue has not come to the foreground.

In 2014, the average monthly wage in full-time employment equivalents was 765 euro (6.8% annual rise). Wages in the private sector grew somewhat faster than in the public sector. Labour productivity increased with respect to both hours worked and per employee. Thus unit labour costs rose moderately.

As methodology was changed, the number of employed in 2014 cannot be directly compared with the 2013 figure using the CSB's labour survey data and national accounts (both sources record a fall in employment). However, the CSB's business survey and the State Revenue Service data also suggest some deceleration in the employment growth.

Registered unemployment lost 1.0 percentage point over the year and amounted to 8.5% of economically active population towards the year's end. As previously, Latgale boasted the highest rate of registered unemployment (17.8%), while the figure for Riga was the lowest (5.2%). In 2014, the regional unemployment disparities decreased at a slower pace than before.

According to the CSB's labour survey data, job seekers accounted for 10.2% of economically active population at the end of 2014 (1.1 percentage point year-on-year decrease). Sharp differences in job seekers' rates by education level still persisted: it was more complicated for less educated to find employment. For instance, at the end of 2014, the share of job seekers among people with university education was several times smaller than among individuals with elementary education (5.3% and 22.1% respectively). Meanwhile, the relatively high youth unemployment (17.8%) can be partly explained by low economic activity among persons aged 15 to 24.

An increase in the number of vacancies was notably suspended; according to the EC survey data, employment expectations by businesses remained neutral, thus suggesting that no labour shortages are threatening the overall economy either currently or in the near future. The EC confidence survey data imply that the number of businesses referring to labour shortages as an essential obstacle to entrepreneurship is solidly moderate; hence a steep rise in unit labour costs should not be expected. As before, mostly construction businesses refer to labour shortages as such an obstacle (14.0%), whereas in manufacturing and services sector the respective figures for end-2014 were 10.2% and 4.4%.

FOREIGN TRADE, BALANCE OF PAYMENTS AND EXTERNAL DEBT

Latvia managed to preserve a positive growth rate of its foreign trade in goods even in the face of lasting geopolitical instability in its neighbouring countries and amidst weak external demand. In 2014, Latvia's balance of foreign trade in goods improved somewhat, with its deficit slipping down to 9.7% of GDP. Exports of goods, at the same time, picked up 2.1%, pointing to resilient competitiveness of Latvian producers also in rather unfavourable external circumstances.

In 2014 overall, the largest positive contributors to the annual export growth were manufacture of wood and articles of wood (1.5 percentage points), machinery and mechanical appliances, electrical equipment (1.2 percentage points), products of the chemical and allied industries (0.4 percentage point), food products (0.3 percentage point), and building materials, optical instruments, plastics and articles thereof. Business investment in the development of high-value-added products underpinned a sustained rise in Latvia's export share of high technology goods (from 7.7% of total exports in 2011 to 10.7% in 2014, according to Eurostat data).

According to the WTO data, Latvian export market shares in world imports continued to expand in 2014. Latvian businesses managed to boost them by diversifying both output and external markets as well as by placing new products in the market. Exports grew most primarily to countries outside the euro area, e.g. Lithuania, the UK, Sweden and

Hungary. The Russian embargo on many foods produced within the EU, which came into effect as of 7 August 2014, only slightly affected the overall dynamics of Latvian exports in goods, mainly impacting individual export groups, dairy product exports in particular. A stronger adverse effect on general export growth, also supported by slower economic development in the euro area countries, came from the falling demand and weaker ruble of Russia. Reacting to the Russian embargo, several exporters managed to diversify their export markets by late 2014. Via various polls and surveys they assured their intention to intensify exploration of foreign markets, projecting also volume expansion for exports of goods. As before, Latvia's major trade partners in 2014 were Lithuania (18.4%), Estonia (11.8%), Russia (10.7%), Germany (6.9%) and Poland (6.5%). As to the structure of Latvia's exports of goods, the share of the EU countries in it increased from 71.0% in 2013 to 72.4% in 2014, of which exports to the euro area countries declined to 30.4% (32.0% in 2013) of the total. Along with exports to the EU countries, Latvian exporters now more often focus on the emerging market economies as potentially large export markets. In 2014, Latvia added such exotic countries as Madagascar, Morocco, Liberia, Nigeria and Chad to its export market list.

For the second year in a row, the volume of goods imports declined only slightly in 2014, posting a 0.4% decrease in comparison with 2013. On the one hand, this contraction improved the balance of foreign trade in goods, suggesting that Latvia's dependence on imports had softened, because locally produced goods replaced imported products more often than before. Amidst the Russian sanctions, significantly, the population of Latvia more often opt for the locally produced goods. Import volume contractions, on the other hand, are associated with a weaker new investment activity. In 2014, the largest contraction in imports of goods was posted by mineral products (14.1%) and transport vehicles (5.3%). Latvia's major trade partners in imports of goods were Lithuania (17.7%), Germany (11.2%), Poland (11.2%), Russia (8.2%) and Estonia (7.7%).

In 2014, trade surplus was recorded for wood and products of wood, agricultural products and miscellaneous articles. Mineral products retained the largest deficit, while the trade gap in this group of goods was narrowing for the second year in a row. Of major trade partners, Latvia retained a positive foreign trade balance with Estonia, Russia, the UK, Sweden and Denmark.

The current account deficit rose to 749.1 million euro or 3.1% of GDP in 2014. In comparison with 2013, its increase depended on the falling value of transportation services exports, which, in turn, was primarily determined by lower transportation services prices under the impact of stiffening competition related to geopolitical situation in Russia. The inflow of financing from the EU funds also weakened slightly in 2014, while contributions to EU institutions rose. The current account deficit was covered by EU funding and long-term capital in the form of foreign direct investment. All in all in 2014, the inflows from the EU funds in Latvia's current account and capital account accounted for 1.0 billion euro or 4.4% of GDP.

The goods and services trade balance improved year-on-year, posting a deficit of 688.5 million euro or 2.9% of GDP in 2014. With exports growing faster than imports, the balance of foreign trade in goods got somewhat better. The annual increment in exports of goods was spurred by Latvian exporters' ability to compete in foreign markets and flexibly redirect their produce to other foreign markets, in such a way alleviating the effects of geopolitical tensions and Russian embargo on food products. The annual rise in exports of goods was accompanied by the expansion of commodity imports for manufacturing and investment activity related to imports of capital goods. In 2014, the services trade balance decreased, because profits from transportation services exports shrank due to lower prices of transportation services caused by the tight competition.

Against the previous year, the deficit of the overall primary income account increased (to 192.4 million euro or 0.8% of GDP), because the inflow of EU financing for agriculture contracted and income from various investment activities abroad shrank somewhat as well.

Some year-on-year surplus decrease was observed also for the secondary income account (to 131.7 million euro or 0.5% of GDP). It was determined by Latvia's contributions to EU cooperation institutions, including also the EU budget. In 2014, the secondary income account continued to enjoy a boost from the inflows of financing, albeit in smaller volumes in year-on-year terms, from the European Fisheries Fund and other funds. It was associated with changes in sector allocation of the total EU financing in 2014, with more financing going to the European Regional Development Fund, and the recording of these inflows in the capital account.

The surplus of capital account of Latvia's balance of payments posted a pickup to 718.5 million euro or 3.0% of GDP in 2014. This increase was on account of financing from the European Regional Development Fund for improving the public infrastructure and promoting entrepreneurial activities and also from the Cohesion Fund for financing large infrastructure development projects in environmental protection and transportation (totalling 720.9 million euro or 3.0% of GDP).

The financial account of Latvia's balance of payments posted a deficit of 958.4 million euro. The year-on-year rise in the deficit was driven by credit institutions increasing their assets in the form of debt securities and deposits as well as sales of Latvian government bonds in international financial markets, enabling the refinancing of the international loan at lower interest rates. Successfully issued bonds and lower-rate borrowing opportunities in international financial markets provided additional funding for meeting other needs of the economy.

Net inflow of foreign direct investment in Latvia amounted to 355.2 million euro or 1.5% of GDP in 2014. The rate of increase of the respective flows decelerated for the third consecutive year. In 2014, this dynamics was rooted in the geopolitical situation, which adversely affected business sentiments and reduced their risk appetite. The largest share of this investment went into financial and insurance activities, and real estate activities. Investment in manufacturing and trade was also significant. Investment flows primarily came from Sweden, the Netherlands, Cyprus, Russia, Germany and Norway.

Latvia's financial environment saw also such positive developments as the sovereign credit rating upgrades by several international credit rating agencies, which intensified investors' interest about Latvia and boosted their confidence. Standard & Poor's upgraded Latvia's credit rating late in May 2014, while Moody's Investors Service and Fitch Ratings did it in June. This indicates that risks are well balanced in Latvia's economy and a responsible economic policy should be pursued also in the future.

At the end of 2014, Latvia's net external debt stood at 7.5 billion euro or 31.1% of GDP, while net government debt was 7.4 billion euro (897.1 million euro or 13.9% in excess of the previous end-of-year figure). Eurobonds accounted for 52%, the EC loan for 21%, and the World Bank loan for 4% of the total debt. By currency, 73% of the total debt was denominated in euro, 25% in US dollars and 2% in other currencies.

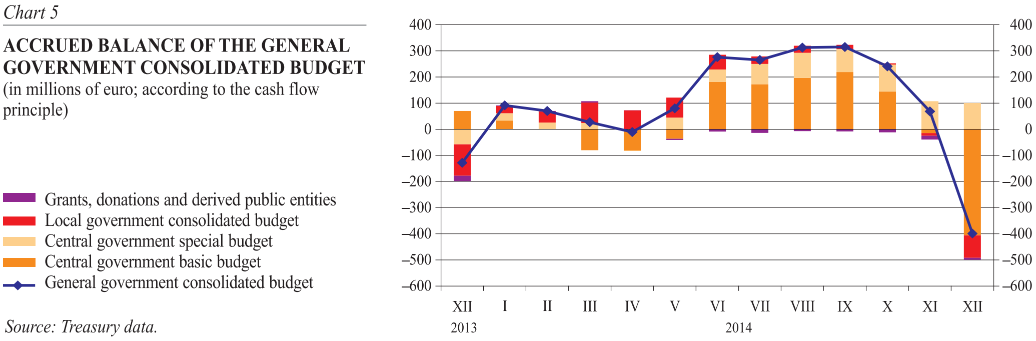
FISCAL DEVELOPMENTS

The general government consolidated budget posted a deficit of 399.0 million euro or 1.7% of GDP in 2014 on a cash flow basis (see Chart 5), whereas according to the accrual principle (ESA 2010) used to evaluate compliance with the Maastricht criteria, the estimated budget deficit was 347.0 million euro or 1.4% of GDP.

In 2014, the budget balance was negatively affected by a significant central government

Chart 5

ACCRUED BALANCE OF THE GENERAL GOVERNMENT CONSOLIDATED BUDGET
(in millions of euro; according to the cash flow principle)



Source: Treasury data.

basic budget deficit of 405.8 million euro as compared to a 70.2 million euro surplus in 2013. This was partly due to the fact that the social insurance budget expenditure (old age and disability pension supplements) was transferred to the central government basic budget, contributing to positive changes in the central government special budget balance: a deficit of 57.9 million euro in 2013 was followed by a 100.4 million euro surplus in 2014. The consolidated local government budget balance also improved year-on-year, posting a deficit of 86.0 million euro (119.9 million euro in 2013).

In 2014, the increase in the general government budget expenditure was steeper than that in revenue (5.0% and 1.9% respectively), thereby continuing the trend observed in 2013, when the annual rates of change for expenditure and revenue reached 4.5% and 2.6% respectively. Tax revenue grew by 3.9% indicating a positive trend in the context of decelerating economic growth.

Towards the end of 2014, the Fiscal Discipline Council published its first Fiscal Discipline Monitoring Report. The Report confirmed compliance of the Draft Law on Medium-Term Budget Framework for 2015, 2016 and 2017 and the Draft Law on State Budget 2015 with the fiscal conditions stipulated in the Fiscal Discipline Law. At the same time, the Fiscal Discipline Council urged to address the issue of increasing tax revenue.

In 2014, the general government consolidated budget revenue remained on a downward trend, amounting to 8.5 billion euro or 35.5% of GDP, after reaching 37.2% of GDP in 2012 – the highest level of revenue in five years.

The rate of increase in the general government consolidated budget revenue continued to moderate, growing by 155.4 million euro or 1.9% in 2014 as compared to a rise of 2.6% and 12.9% in 2013 and 2012 respectively. The increase in revenue continued to be fully based on tax revenue which picked up by 250.2 million euro; however, with the economic growth decelerating further, the rate of increase was lower in 2014 than that in 2013, i.e. 3.9% and 5.3% respectively. Some tax benefits notwithstanding, revenue from taxes on labour continued to demonstrate positive trends, mainly on account of an increase in the average monthly wages and salaries and the number of employed (6.8% and 0.7% respectively). The above developments supported a 3.2% and 3.0% rise in consumption and the overall retail trade turnover respectively (in nominal terms) which, in turn, provided for a VAT revenue increase of 136.9 million euro or 8.2%. In 2014, a 5.0% year-on-year decrease in refunds of the overpaid VAT also contributed to VAT revenue growth. Non-tax revenue contracted by 61.0 million euro year-on-year, mainly on account of lower revenue from the use of state or local government capital and a decrease in other non-tax revenue. In 2014, revenue from foreign financial assistance also declined by 42.5 million euro or 3.8% year-on-year.

Expenditure of the general government consolidated budget totalled 8.9 billion euro or 37.2% of GDP in 2014, posting annual growth of 426.0 million euro. The pick-up in expenditure exceeded revenue growth and also accelerated in annual terms by 5.0% and 4.5% respectively. Expenditure growth was mainly driven by an increase in expenditure on subsidies and grants (227.4 million euro or 13.3%), primarily due to a more extensive use of EU funds. Wage and salary expenditure also continued on an upward trend, growing by 74.5 million euro or 5.5% largely on account of higher minimum wages and raised salaries for the teaching staff. With local government interest payments on financial derivatives going up, interest expense grew by 21.5 million euro or 6.5% year-on-year.

At the end of 2014, the general government debt expanded by 924.0 million euro year-on-year, reaching 9.1 billion euro or 37.8% of GDP on a cash flow basis, whereas according to the ESA 2010 methodology it amounted to 9.6 billion euro or 40.0% of GDP. This increase can be explained by a successful issue of 10-year government bonds in the amount of 2 billion euro, with historically lowest yields on Latvia's securities in international markets. At the same time, in 2014 government debt in the amount of 1 billion euro was repaid to the EC and bonds in the amount of 400 million euro matured. In preparation for the loan repayment to the EC also in January 2015, additional funds were generated in 2014. Changes in the US dollar exchange rate vis-à-vis the euro also had an increasing effect on the amount of the government debt.

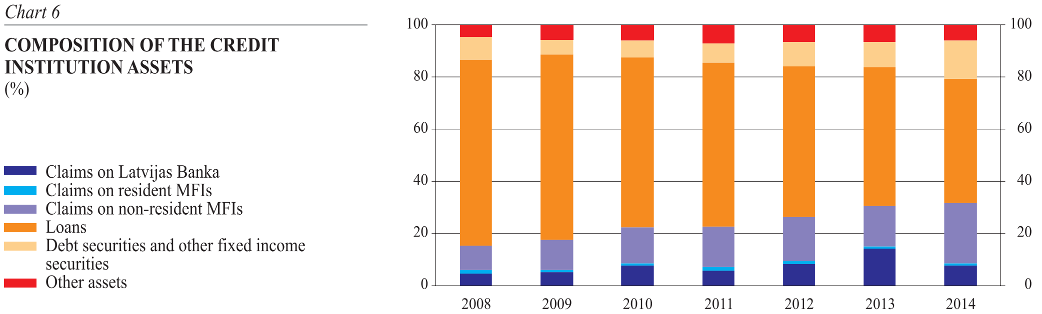
CREDIT INSTITUTION DEVELOPMENTS

At the end of 2014, 26 credit institutions, including nine[1] branches of foreign credit institutions, 32 credit unions (three ceased their operation during the year), and two money market funds were registered in the Republic of Latvia. Based on the applications submitted by the particular credit institutions, as of 1 January 2014 credit institution licences were cancelled for JSC *UniCredit Bank* which left the Baltic market as a result of changes in the group strategy and for SJSC *Latvijas Hipotēku un zemes banka* due to its planned transformation into *Latvijas Attīstības finanšu institūcija* (Latvian Development Financial Institution). The government's share in the paid-up share capital of credit institutions stood at 7.2% at the end of 2014.

Latvia's economy continued to develop in 2014, and the assets of credit institutions grew for the second consecutive year, representing an increase from 1.4% in 2013 to 5.6% in 2014 (see Chart 6 for the composition of the credit institution assets). Nevertheless, lending activity remained low; therefore, the credit institution loans to resident and non-resident non-MFIs continued to shrink, contracting by 6.1% in comparison with a 6.5% decline in 2013. With the credit portfolio shrinking, on the liability side, non-resident MFI financing contracted further, dropping from 24.7% in 2013 to 22.9% in 2014 and at the end of the year accounting for 10.5% of the credit institutions' total assets (including 10.2% financing from parent banks; see Chart 7). Conversely, resident and non-resident deposits went up by 4.3% and 24.3% respectively. Non-resident deposit growth was substantially supported by the US dollar appreciation, as the largest share of non-resident deposits was placed in US dollars.

Chart 6

COMPOSITION OF THE CREDIT INSTITUTION ASSETS
(%)



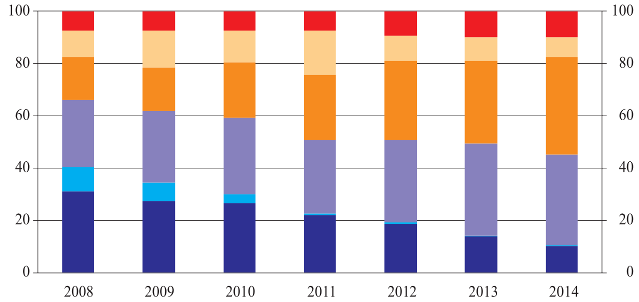
The banks' liquid assets-to-total assets ratio grew further to stand at 39.9% at the end of 2014, close to the historical maximum. With the economy developing further, the loan

[1] Formally, there were 10 branches of foreign credit institutions, since the Swedish Branch of Nordea Bank AB was registered in 2014 to represent Nordea Group in Latvia in the future; in the transition period, however, both the Finnish and the Swedish Branches of Nordea Group were registered in Latvia.

Chart 7

COMPOSITION OF THE CREDIT INSTITUTION LIABILITIES
(%)

- Liabilities to related non-resident MFIs
- Liabilities to other non-resident MFIs
- Resident deposits
- Non-resident deposits
- Other liabilities
- Capital and reserves



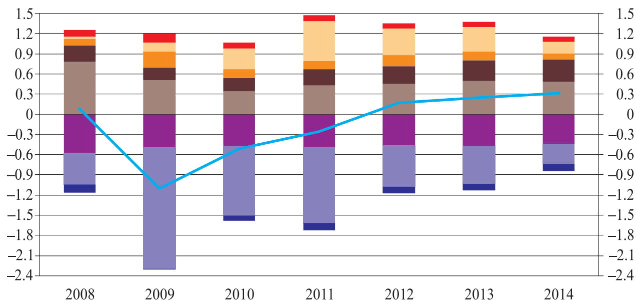
portfolio quality of credit institutions improved and the share of loans past due over 90 days in the aggregate loan portfolio of credit institutions contracted to 6.9% at the end of 2014. The quality of loans granted to non-financial corporations continued to improve.

Most Latvian credit institutions operated with profit in 2014, overall earning 311.4 million euro in comparison with 246.2 million euro profit earned in the previous year (see Chart 8). The operating income of credit institutions totalled 916.4 million euro in 2014, representing a year-on-year decrease of 3.1%. Despite its decline of 2.0% year-on-year, net interest income remained the most sizeable component of the operating income, accounting for slightly more than a half of it. Net commissions and fees, the second most important income component, continued to expand (by 8.3% as compared to 13.6% in 2013), still accounting for about 30% of the operating income. The operating costs of credit institutions posted a slight decrease of 6.8% year-on-year.

Chart 8

CREDIT INSTITUTION INCOME AND EXPENSE
(in billions of euro)

- Net interest income
- Net income from commissions and fees
- Income from trading in financial instruments and revaluation
- Income from reducing provisions
- Other income
- Administrative expense
- Expenditure on provisions
- Other expense
- Retained earnings/losses of the reporting year



The total capital ratio of credit institutions continued to improve, standing at 20.9% at the end of the year (the minimum requirement is 8%), whereas Tier I capital ratio amounted to 18.1%. Over the year, nine credit institutions increased Tier I capital by 140.0 million euro in total.

MONEY SUPPLY

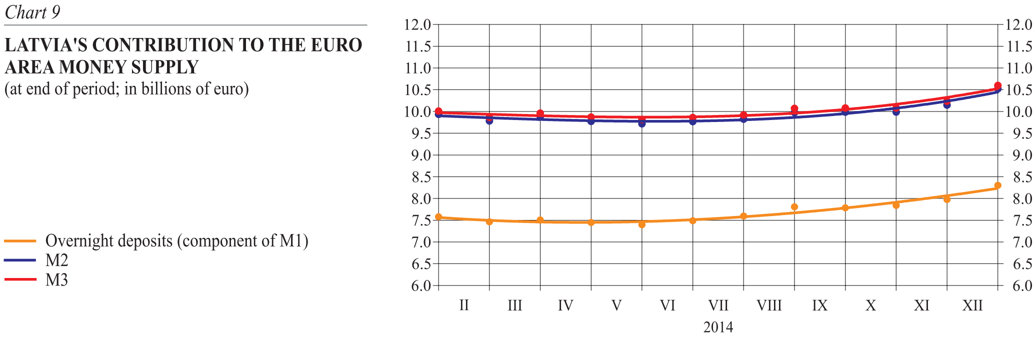
The development of the monetary aggregates in 2014 (see Appendix 1) reflected the structural changes related to Latvia joining the euro area, moderate economic growth as well as a sustained ample liquidity surplus accumulated by credit institutions.

Due to caution triggered by external risks and the desire to mitigate these risks, both credit institutions and borrowers refrained from more active lending and borrowing activities. Lending was also hampered by the expected changes in the legal framework for insolvency. With the minimum reserve ratio also going down, credit institutions deposited most of their excess funds with Latvijas Banka in the first months of the year; however, following a decision taken by the ECB in June on setting negative interest rates on deposits with central banks of the euro area, they were largely deposited with foreign credit institutions and invested in government and corporate debt securities. Thus, the composition of credit institution assets changed, while domestic loans continued on their downward trend. Over the year, the increase in deposits was fairly moderate, concentrating primarily in the household sector, where the high level of deposits reached in the context of the euro changeover at the end of 2013 was exceeded already in the second quarter. Meanwhile, deposits of non-financial corporations remained below the above level already from the beginning of the year. Overnight deposits, the most liquid money supply component, remained the most popular deposit segment reflecting the impact of the record low deposit rates discouraging economic agents from making longer-term savings. Demand for cash followed a gradual downward trend and picked up only in December due to seasonal factors. Thus, the euro changeover and the financial and economic stability supported the return of cash to credit institutions.

Following the euro changeover, the set of monetary aggregates in Latvia is viewed from two aspects. Firstly, it is viewed from the perspective of Latvia's contribution to the euro area monetary aggregates (see Chart 9). The respective calculation takes into account the euro area "residence principle", i.e. Latvia's contribution also includes deposits placed with Latvian MFIs by other euro area residents. Secondly, looking at the dynamics of domestic deposits and loans, only data on the corresponding transactions of Latvian residents is used.

Chart 9

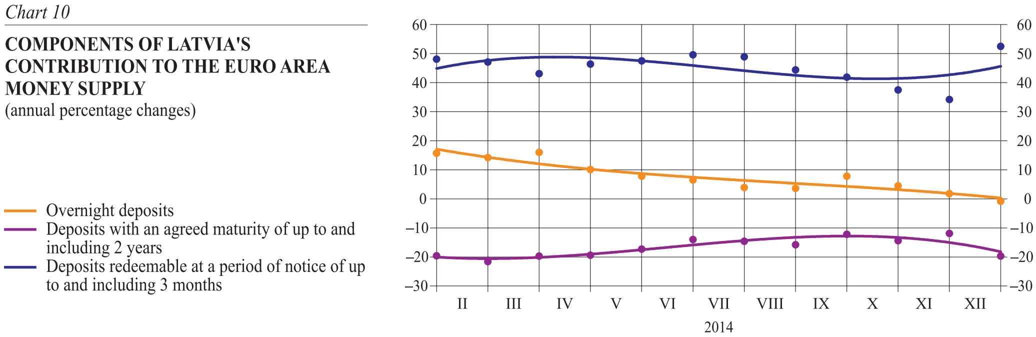
LATVIA'S CONTRIBUTION TO THE EURO AREA MONEY SUPPLY
(at end of period; in billions of euro)



In 2014, overnight deposits (Latvia's contribution to the euro area M1) shrank by 0.8%, largely on account of the high base level driven by the surge in demand deposits in December 2013 related to the euro changeover. Latvia's contribution to the euro area money supply aggregate M2 posted an even steeper decline (2.0%). This was due to a substantial 19.7% fall in deposits with an agreed maturity of up to 2 years, which could not be offset by a steep 52.5% rise in less sizeable deposits redeemable at notice of up to 3 months (see Chart 10). In 2014, euro area's overall overnight deposits and M2 grew by 8.1% and 3.5% respectively, deposits redeemable at notice remained unchanged during the year, whereas deposits with an agreed maturity shrank by 5.8%. Latvia's contribution to additional components comprised in the broad monetary aggregate M3 of the euro area was insignificant: at the end of 2014, debt securities with a maturity of up to and including 2 years issued by MFIs and money market fund shares and units amounted to 36.8 million euro and 40.6 million euro respectively.

Chart 10

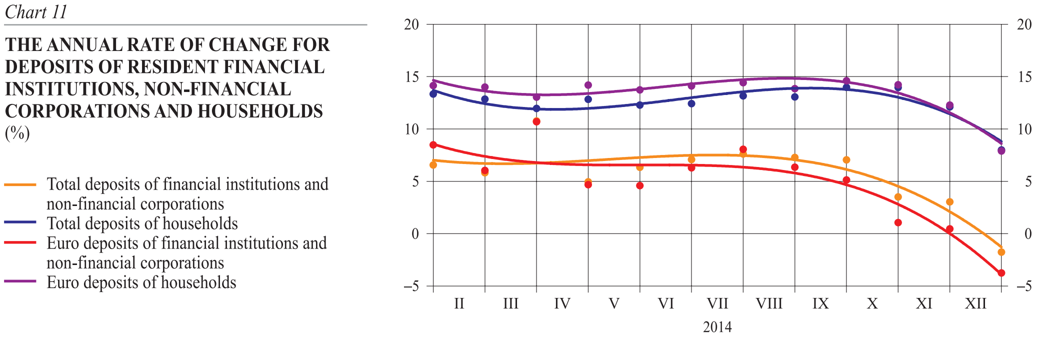
COMPONENTS OF LATVIA'S CONTRIBUTION TO THE EURO AREA MONEY SUPPLY
(annual percentage changes)



Deposits of resident financial institutions, non-financial corporations and households increased by 3.4% in 2014 as compared to 13.2% in 2013. For the most part of the year (in February and April and in the period from June to December), an increase in household deposits was observed, in some months also supported by growth in deposits of financial institutions and non-financial corporations. In 2014, household deposits with credit institutions grew by 8.0% (see Chart 11), while deposits of financial institutions and non-financial corporations shrank by 1.8%. The dynamics of household deposits reflected the cash substitution effect, income growth and caution in spending, whereas the developments in deposits of financial institutions and non-financial corporations mirrored the base effect of the euro changeover, the slowdown in economic growth and external market tensions. Thus, the share of household deposits rose to 54.9% of aggregate deposits in comparison with 52.6% at the end of 2013. Household deposits accounted for 68.1% of all time deposits and deposits redeemable at notice and 50.2% of overnight deposits, representing an increase from 62.7% and 48.6% respectively at the end of 2013.

Chart 11

THE ANNUAL RATE OF CHANGE FOR DEPOSITS OF RESIDENT FINANCIAL INSTITUTIONS, NON-FINANCIAL CORPORATIONS AND HOUSEHOLDS
(%)

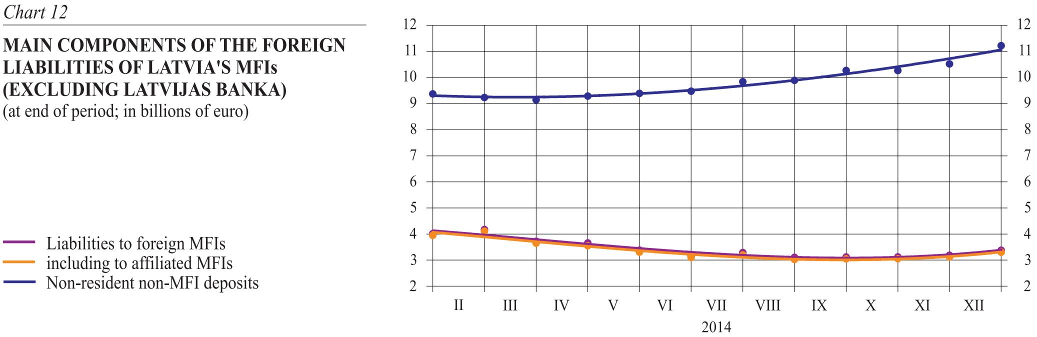


The currency composition of resident deposits remained broadly unchanged in 2014 and was dominated by euro deposits, with their share reaching approximately 90% of aggregate deposits; at the same time, 6% of deposits were placed in US dollars, while British pound sterling and Swiss franc deposits constituted less than one percent of aggregate deposits. In absolute terms, deposits made both in euro and other currencies expanded during the year.

As regards the inflows of non-resident funds, the tendency observed in previous years intensified in 2014: the increase in non-resident non-bank deposits with Latvian credit institutions was much more rapid than in the previous year, posting 24.3% growth in non-resident deposits in 2014 as compared to 10.4% in 2013. Although the US dollar appreciation vis-à-vis the euro partially accounted for the above, it was also a signal of confidence in the stability of Latvia's financial sector. Conversely, as a result of persistently low lending activity, the inflows from affiliated foreign MFIs fell by 20.9% in 2014 (by 21.0% in 2013); however, the decline was recorded only in the first half of the year, with the level of liabilities stabilising in the second half (see Chart 12).

Chart 12

MAIN COMPONENTS OF THE FOREIGN LIABILITIES OF LATVIA'S MFIs (EXCLUDING LATVIJAS BANKA)
(at end of period; in billions of euro)



Foreign assets of the balance sheet of MFIs (excluding Latvijas Banka) posted a particularly steep surge of 47.5%, largely on account of negative interest rates on deposits with national central banks and a reduction of the minimum reserve ratio. With credit institutions moving their excess funds abroad, claims on foreign MFIs grew by 56.8%, the portfolios of foreign government and non-MFI private sector securities expanded by 98.9% and 91.6% respectively, while loans to foreign non-MFIs increased by 3.8%. Thus, at the end of 2014 the negative net foreign assets of MFIs (excluding Latvijas Banka) recorded a fall of 2.7 billion euro year-on-year.

Of the counterparts, the decline in MFI loans to private sector retained its downward effect on the monetary aggregates, with loans to resident financial institutions, non-financial corporations and households shrinking by 7.1% (by 6.4% in 2013). The fall in household loans slowed down to 7.1% (8.2% in 2013), whereas loans to non-bank financial corporations posted an increase for the second consecutive year (32.1% in 2014; for changes in loans to financial institutions, non-financial corporations and households, see Chart 13). A sharper overall decline was caused by a 9.6% drop in loans to non-financial corporations (5.6% in 2013), to some extent on account of structural changes in the credit institution sector in January. With the loan portfolio contracting and GDP continuing to grow, the ratio of domestic loans to GDP decreased further from 65.6% in 2012 to 58.3% in 2013, and to 52.2% in 2014 (see Chart 14). The loan portfolio decreased partly as a result of write-offs of lost loans; however, no revival in lending activity was observed in the credit market on account of both supply and demand factors.

Chart 13

THE ANNUAL RATE OF CHANGE FOR LOANS TO RESIDENT FINANCIAL INSTITUTIONS, NON-FINANCIAL CORPORATIONS AND HOUSEHOLDS
(%)

- Loans to non-financial corporations
- Loans to households
- including loans for house purchase
- Total loans to financial institutions, non-financial corporations and households
- Loans to financial institutions (right-hand scale)

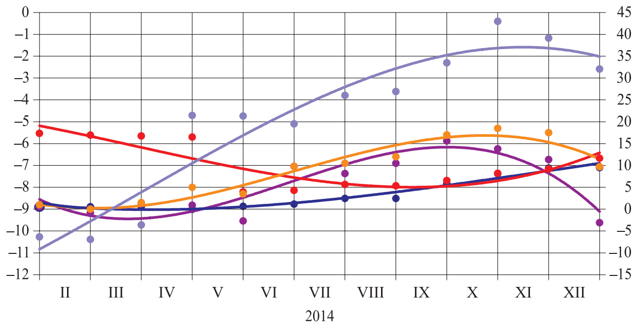
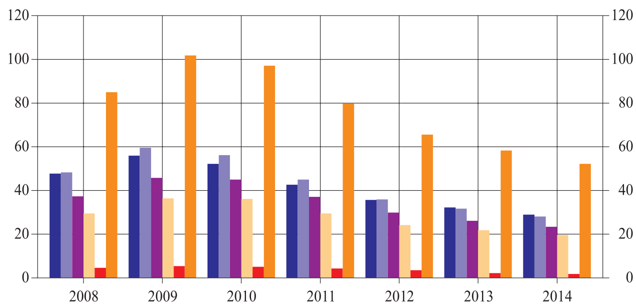


Chart 14

THE RATIO OF RESIDENT LOANS TO GDP
(%)

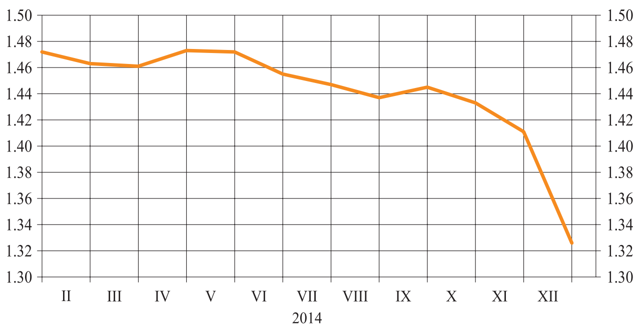
- Loans to financial institutions and non-financial corporations
- Mortgage loans
- Loans to households
- Loans for house purchase
- Consumer credit
- Total loans



With loans continuing on a downward trend, resident loans decreased to 40.7% of the aggregate balance sheet assets of MFIs (excluding Latvijas Banka) at the end of 2014, down from 46.3% at the end of 2013. The stability of the financial sector was supported by a reduction in the loan-to-deposit ratio: resident deposits covered 75.4% of loans at the end of 2014 in comparison with 67.7% reported at the end of 2013 (for the loan-to-deposit ratio, see Chart 15).

Chart 15

THE RATIO OF LOANS TO RESIDENTS AND RESIDENT DEPOSITS



The share of loans past due decreased further: loans past due over 90 days amounted to 6.9% of aggregate loans at the end of 2014 (8.3% at the end of 2013).

Lending decreased in most economic sectors in 2014, with loan investment growing only in some manufacturing sub-sectors, such as manufacture of fabricated metal products (by 19.6%), manufacture of chemicals and chemical products (by 5.7%) and manufacture of wearing apparel (by 2.3%) as well as in postal and courier activities (2.8 times), storage (by 14.8%) and in some sub-sectors of financial and insurance activities and other service activities. Meanwhile, a sharp decline in the loan portfolio was recorded for energy (22.2%), retail trade (21.7%), crop and animal production (17.7%), manufacture of wood and of products of wood (16.5%), land transport (16.1%), wholesale trade (15.9%), construction (8.2%) and real estate activities (6.4%). With loans posting a gradual decline in almost all major sectors of the economy, the composition of the loan portfolio by sector remained broadly unchanged in 2014. At the end of the year, the major share of overall corporate loans was still concentrated in real estate activities representing 31.2% (31.3% at the end of 2013), manufacturing (13.3%; 13.0% at the end of 2013), financial and insurance activities (9.9%; 7.5% at the end of 2013), trade (9.7%; 10.8% at the end of 2013), transportation and storage (8.0%; 7.0% at the end of 2013) as well as agriculture and forestry (6.1%; 6.6% at the end of 2013).

A substantial decrease in annual terms was reported for consumer loans to households – mostly on account of reclassification carried out by individual credit institutions – and corporate mortgage loans, posting a decline of 18.4% and 11.2% respectively. Commercial credit, loans to households for house purchase and industrial credit contracted more moderately (by 8.9%, 6.7% and 6.0% respectively). Loans for house purchase totalled 4.7 billion euro or 84.0% of all household loans at the end of December 2014, representing a year-on-year decrease of 0.3 billion euro. At the end of 2014, loans to households for house purchase, commercial credit and industrial credit accounted for 37.6%, 17.5% and 17.2% of aggregate loans respectively (37.4%, 17.9% and 16.9% respectively at the end of 2013).

Following the euro changeover, loans granted in euro continued to dominate in the aggregate loan portfolio. At the end of 2013, lats loans and euro loans accounted for 13.2% and 81.9% of aggregate loans respectively, whereas at the end of 2014 the share of euro loans constituted 95.2%. In 2014, foreign currency loans contracted somewhat (by 9.7%); however, these loans accounted for a mere 4.8% of aggregate loans (of them, 46.9% were granted in US dollars, 27.6% in Swedish krona, 14.7% in Swiss francs and 10.5% in British pounds sterling).

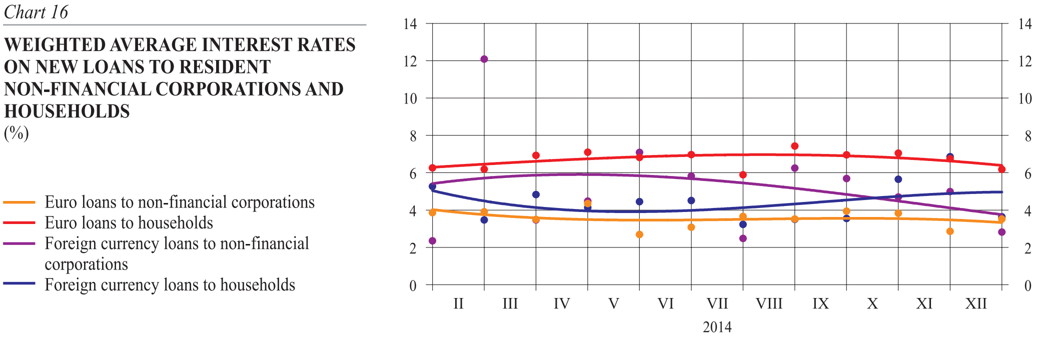
Due to seasonal factors, Latvia's contribution to the euro area monetary base reached a record high, totalling 6.4 billion euro at the end of the year. The proportionate share of Latvijas Banka in the total amount of banknotes issued by the Eurosystem (3.8 billion euro) and the credit institutions' current accounts including the minimum reserve system (2.1 billion euro) accounted for the largest share. Latvijas Banka's net foreign assets (non-euro area assets) expanded by 44.8 million euro or 1.6%, amounting to 2.8 billion euro at the end of 2014.

LENDING AND DEPOSIT RATES

MFI lending and deposit rates in Latvia remained broadly unchanged in 2014: the decline in the euro money market interest rates was moderate, the narrowing of the spread over the money market index was hampered by an increased credit risk in relation to the Russian–Ukrainian conflict, imposing sanctions, depreciation of the Russian ruble and the amendments to the Insolvency Law. In addition, the credit institutions' incentive to narrow the spread over the money market index was also reduced in some lending sectors due to a slight competition among credit institutions. By contrast, lending rates in lending segments where credit institutions felt more confident about their cooperation partners' creditworthiness, e.g. lending rates in the sector of large-size loans to non-financial corporations, shrank more rapidly, reaching even record-low values in some months (see Chart 16). With no difficulties in attracting funds for credit institutions, the decline in the money market interest rates found its reflection in the credit institutions' short-term time deposit rates relatively quickly. At the same time, in a low interest rate environment households used the opportunity to earn higher interest income more actively, directing more of their savings to longer-term deposits. Like before, during the most significant public holidays in 2014 credit institutions offered slightly more favourable terms and conditions for time deposits to households.

Chart 16

WEIGHTED AVERAGE INTEREST RATES ON NEW LOANS TO RESIDENT NON-FINANCIAL CORPORATIONS AND HOUSEHOLDS
(%)



Credit institutions granted new loans primarily to large non-financial corporations with a good credit history, and the decline in the euro money market index was reflected in lower interest rates on new euro loans to non-financial corporations over 1 million euro, declining from an average of 3.6% in 2013 to 3.3% in 2014. By contrast, those on new euro loans to non-financial corporations in the amount of up to 1 million euro, traditionally considered more risky loans, rose from an average of 4.3% in 2013 to 4.6% in 2014, despite declining euro money market interest rates. Credit risk for some sectors and non-financial corporations whose operation was more affected by the geopolitical situation in the eastern neighbouring countries increased, thus also having an upward effect on the spread offered over the money market index.

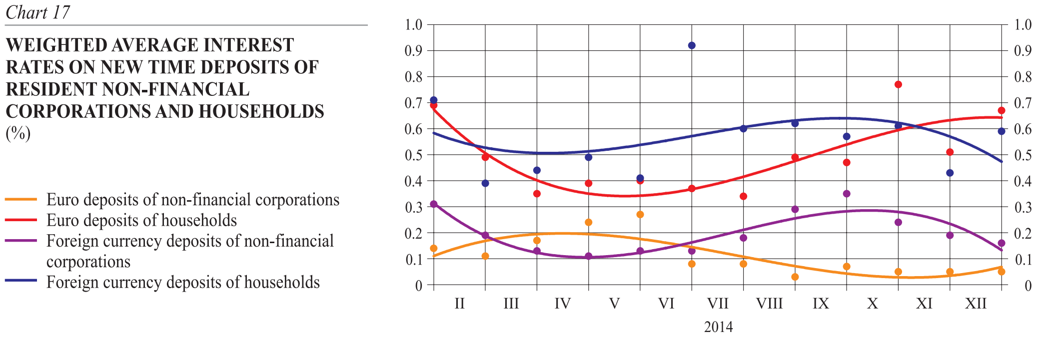
Against the background of persistently low demand for loans and tight lending conditions, the weighted average interest rate on new euro loans to households for house purchase also ranged from 3.1% to 3.5% in 2014. Granting of new loans to households for house purchase and a steeper decline in interest rates were hampered by credit institutions' concerns as to the introduction of the so-called jingle mail option, following the adoption of the amendments to the Insolvency Law by the Saeima (the Parliament) of the Republic of Latvia. In the last months of 2014, credit institutions tightened their credit standards for loans to households for house purchase, such as collateral requirements and the requirements for the loan-to-value ratio. The fall in the euro money market interest rates affected the floating interest rates and interest rates with the initial rate fixation period of up to 1 year on new euro loans to households; however, the trend represented a slight decrease from an average of 3.2% in 2013 to 3.1% in 2014. Despite the market participants' expectations of sustainably low euro money market rates, interest rates with an initial rate fixation period of over 1 year on new loans to households for house purchase grew significantly higher and more volatile than the floating interest rates. The differences in the levels and volatility of interest rates explain why households mostly preferred to take floating interest rate loans or loans with a short initial rate fixation period to finance their house purchases. In the case of new household loans for house purchase, the annual percentage rate of charge, comprising fees for considering loan applications, loan administration costs and similar costs, was close to the respective annualised agreed rate (an average of 3.5% in 2013; 3.4% in 2014), confirming that the above additional expenses remain quite small relative to the size of the loans to households for house purchase.

Interest rates on new consumer credit to households grew from 19.2% in 2013 to 19.6% in 2014, with high risk loans still representing a significant share in the total amount of new euro loans granted to households. The effective weighted average interest rate on consumer credit to households rose from 25.5% in 2013 to 26.9% in 2014, suggesting an increase in additional credit-related expenses, such as commissions, the fee for considering loan applications and the fee covering loan administration costs.

On account of a decline in the euro money market indices, the record-low interest rates on new time deposits received from resident non-financial corporations and households decreased further from an average of 0.3% in 2013 to 0.2% in 2014 (see Chart 17). There was a particularly rapid drop in interest rates on new time deposits received from resident non-financial corporations. The effect of the decline in the euro money market index on households was reduced by their efforts to increase interest income, directing more of their savings to longer-term deposits and placing deposits in periods when credit institutions offered more favourable terms and conditions (shortly before or after the most significant annual public holidays).

Chart 17

WEIGHTED AVERAGE INTEREST RATES ON NEW TIME DEPOSITS OF RESIDENT NON-FINANCIAL CORPORATIONS AND HOUSEHOLDS
(%)



In the context of the euro area, lending and deposit rates of Latvian credit institutions were relatively high, especially against the background of improved monetary policy provisions; following the adoption of new ECB monetary policy measures, including the introduction of the targeted longer-term refinancing operations, the situation in the euro area improved overall: the credit market fragmentation decreased, with lending rates going down particularly in the euro area countries affected by the sovereign debt crisis. Thus, it can be concluded that the relatively high interest rates observed in Latvia were primarily due to domestic factors.

FOREIGN EXCHANGE AND INTERBANK MARKET

FOREIGN EXCHANGE MARKET

The overall turnover of foreign exchange transactions in Latvian credit institutions fell sharply in 2014. According to the data of credit institution monthly reports on foreign currency purchase and sales transactions, the overall turnover of foreign exchange transactions stood at 816.7 billion euro, by almost one third less than in the previous year. The turnover of foreign exchange transactions was primarily affected by the euro changeover, since there was no further need to exchange lats for euro either for interbank market transactions, euro loan repayments or foreign trips.

The structure of the types of foreign exchange transactions remained broadly unchanged: swap transactions continued to be the most popular transaction type, accounting for 65.8% (66.3% in 2013) of the overall transaction turnover. Similarly to the previous year, spot transactions stood at 33.6% in the overall transaction turnover.

Non-resident MFIs remained the main counterparties of Latvian credit institutions in the foreign exchange market. In 2014, their transaction turnover accounted for 467.1 billion euro or 57.2% of the overall turnover. In addition, these counterparties made the most significant contribution to the overall foreign exchange turnover, both exchanging the euro for the US dollar and carrying out exchange transactions in other currency pairs. As a result of the euro changeover, the turnover of foreign exchange transactions with non-resident MFIs contracted by 35.4% in 2014. The decline in the turnover of foreign exchange transactions with other resident financial intermediaries was even steeper, representing a drop of 76.9% (to 1.0 billion euro), whereas the turnover of such transactions with other non-resident financial intermediaries surged by 77.5% (to 52.6 billion euro). The turnover of foreign exchange transactions with resident non-financial corporations, the government and households also shrank considerably. For example, the turnover of transactions with households decreased by 70.8%. This allows to make approximate estimates of the amount of cash converted by households from lats to a foreign currency (especially, the euro) every year. The turnover of foreign exchange transactions with resident non-financial corporations and the government decreased to almost the same extent (by 67.9%). Following the euro changeover, the least pronounced fall in the overall annual turnover of foreign exchange transactions was observed for transactions with resident MFIs (4.0%) and those with non-resident non-banks (4.5%).

After the introduction of the euro, in 2014 most non-cash transactions in Latvian credit institutions were made in the US dollar-euro currency pair, accounting for approximately 54% (445.8 billion euro) of the overall turnover. The second most significant currency pair was the British pound sterling vis-à-vis the US dollar, representing 14.6%. The turnover of all other foreign exchange transactions against the euro did not exceed 6.0% of the overall turnover of foreign exchange transactions. Overall, transactions of all other currencies against the US dollar were more popular than those against the euro: the turnover of transactions involving all other currencies excluding the euro accounted for 36.9% of the overall annual turnover of foreign exchange transactions in all currencies.

The turnover of foreign exchange transactions conducted in cash at credit institutions and currency exchange offices also decreased considerably, primarily due to the euro changeover; the respective turnover stood at 1 billion euro in 2014, representing an almost 60% fall year-on-year. The share of cash transactions at currency exchange offices also dropped from 69.5% in 2013 to 57.8% in 2014.

Following the euro changeover, the most popular euro exchange cash transactions at Latvian credit institutions and currency exchange offices were those vis-à-vis the US dollar, with their share in overall foreign exchange cash transactions hovering slightly above 50.0% in 2014. The British pound sterling was the second currency most often exchanged in cash for the euro in 2014, accounting for 20.0%. At the same time, despite a slight decrease at the end of 2014, the share of transactions with the Russian ruble even expanded, standing at 12.7% as compared to the cash transactions against the lats in the previous year. Hence, the declining amount of transactions notwithstanding, the US dollar, the British pound sterling and the Russian ruble remained, like in the previous years, the three most popular currencies used in foreign exchange cash transactions against Latvian currency, the euro.

THE INTERBANK MARKET

The introduction of the euro brought changes in the money market operations of Latvian credit institutions. Instead of the relatively closed and limited lats money market, Latvian credit institutions started operating in the sizeable euro money market with a large number of counterparties. In 2014, Latvian credit institutions retained an ample liquidity surplus, their currency risk was largely eliminated, also supporting a decline in interest rates, and the previous volumes of money market exchange transactions involving lats and euro disappeared. Against the background of atypically low interest rates, facilitated by the policy of the ECB and also the national central banks issuing foreign currency significant for Latvian market, interest rates on interbank transactions of Latvian credit institutions continued to decline.

Money market statistics also suggest that Latvian credit institutions gradually extended their interbank market operations to broader regions. In 2014, interbank transactions with domestic credit institutions dropped to an average of 4.8%, down from 6.9% in 2013, while transactions with non-resident credit institutions grew to 95.2%.

In 2014, the transaction turnover in euro shrank on the domestic interbank market as compared to that in lats in 2013. A particularly sharp decline in the turnover was recorded at the beginning of summer, around the time when the ECB resolved to lower the key ECB interest rates and introduce a new monetary policy instrument, TLTRO, as well as reported on its readiness to decide on other non-standard monetary policy instruments. As a result of these measures, the volume of transactions also continued to shrink in the second half of the year.

The volume of domestic interbank loans granted in the national currency on the domestic interbank market was 5.6 billion euro in 2014, down from 7.6 billion euro in 2013 (a fall of 26.3%). In 2014, the volume of interbank transactions carried out in a foreign currency declined to 20.7 million euro or by 10.1%.

Unsecured overnight transactions continued to account for the largest share in the volume of interbank loans both on the domestic interbank market and in transactions with foreign MFIs. However, in an environment of low interest rates, characteristic of the euro area market recently, the turnover of transactions with a maturity of up to 1 month rose considerably, although the interest rates applied in this market segment only slightly exceeded those on overnight transactions in 2014.

In the first half of 2014, the weighted average interest rate on unsecured overnight euro transactions on the domestic market stood at 0.08% (0.07% in 2014 overall, similar to that on the lats money market in 2013); yet it should be taken into account that in the second half of the year transactions with an interest rate of 0.00% were concluded in this market segment, albeit to a lesser extent. The weighted average interest rate on unsecured overnight interbank loans granted in foreign currencies on the domestic market declined from 0.13% in 2013 to 0.07% in 2014.

In 2014, developments on the interbank market were significantly affected – both in terms of volume and transaction rates – by the liquidity conditions in the euro area, developments in the credit institution sector and the decisions of the ECB.

Sufficient liquidity in the euro area banking system overall and in Latvia in particular allowed to retain money market interest rates at a low level already in early 2014. The decision taken by the Governing Council of the ECB in June on reducing the key ECB interest rates even further, inter alia setting a negative interest rate on deposit facility, facilitated a steeper decline in money market interest rates in the second half of the year. This was reflected both in the average interest rates of transactions and the dynamics of EURIBOR.

Interest rates on euro loans granted to non-MFIs are traditionally linked to EURIBOR. In 2014, EURIBOR followed an ongoing upward trend observed since the end of 2013, reaching the peak of the year in April, with 3-month EURIBOR and 6-month EURIBOR standing at 0.35% and 0.44% respectively; however, in early June EURIBOR dropped sharply and continued on a downward trend until the end of the year. Overall, 3-month EURIBOR decreased from 0.29% in early 2014 to 0.08% at the end of the year. EURIBOR for other maturities also declined, shrinking by approximately 0.20 percentage point. At the end of the year, 6-month EURIBOR and 12-month EURIBOR stood at 0.17% and 0.33% respectively. 1-month EURIBOR was already negative at the end of 2014. In 2014, 3-month EURIBOR and 6-month EURIBOR averaged 0.21% and 0.31% respectively, down from 0.22% and 0.34% respectively in 2013.

SECURITIES MARKET

In 2014, both the government and the corporate securities markets of Latvia continued their positive development, while the stock market grew more risky. At the same time, market participants' expectations as regards further expansionary monetary policy implemented by the Eurosystem had downward pressure on the yields on government securities in the euro area countries, including Latvia.

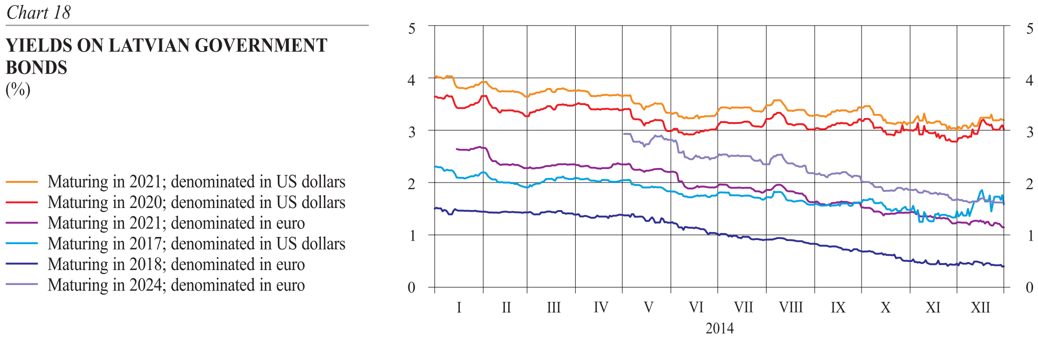
Thus, the yield on 12-month Treasury bills declined in primary auctions from 0.37% in December 2013 to 0.07% in November 2014, whereas that on government 5-year bonds fell from 1.96% in November 2013 to 1.10% in December 2014.

In the secondary market, the bid yield on Latvian government bonds maturing in October 2022 on NASDAQ OMX Riga also declined from 3.65% at the beginning of January to 1.80% at the end of December. The bid yield on the government securities with the time to maturity less than a month shrank from 0.30% to 0.10%.

The quoted bid yield of US-dollar-denominated Latvian government bonds issued on external markets and maturing in 2021 dropped from 4.03% to 3.23% in 2014. The spread between the above bid yield and that on US government bonds of the respective maturity shrank from 143 basis points to 129 basis points. Despite emerging signs of divergence between the monetary policy of the US and that of the euro area, easing in Latvia's risk perception also supported a narrowing of the spread between the yields (see Chart 18 for the yields on Latvian government bonds issued on external markets).

Chart 18

YIELDS ON LATVIAN GOVERNMENT BONDS
(%)



The outstanding amount of Treasury bills and government bonds grew by 8.3% to stand at 1 046.5 million euro, while that of government savings bonds rose from 1.8 million euro to 5.2 million euro. Government securities offered by the Treasury through government securities auctions in 2014 amounted to 370.0 million euro, down by 16.1% in comparison with 2013. The amount of government securities maturing posted a 32.3% decrease year-on-year. In 2014, the entire amount supplied was sold, with demand 3.8 times exceeding supply.

In 2014, Latvian government issued eurobonds in the external market on two occasions. 7-year government bonds worth 1 billion euro with the average yield of 2.815% were issued in January (the margin of 120 basis points above the average swap rates). 10-year government bonds worth 1 billion euro with the average yield of 2.875% were issued in April (the margin of 120 basis points above the average swap rates). Demand exceeded supply 3–4 times at both auctions.

Corporate debt securities in all currencies registered with the LCD grew by 279.6 million euro, reaching 922.7 million euro. Several issues were followed by additional issues, and 30 new issues of securities worth 254.8 million euro were launched. The major issuers were ABLV Bank JSC (184.0 million euro; five issues), JSC *Mogo* (19.1 million euro; 1 issue), JSC Baltic International Bank (16.5 million euro; 9 issues) and JSC TRASTA KOMERCBANKA (10.0 million euro; 1 issue). Corporate debt securities were dominated by US dollar-denominated debt securities worth 521.7 million euro, followed by euro-denominated debt securities worth 401.0 million euro. The shift from deposits to fixed income securities as well as the low interest rates and the expansion of quick credit providers resulted in fast development of corporate debt securities.

In 2014, the turnover of debt securities on NASDAQ OMX Riga was 143.4 million euro, 27.9% higher than in 2013. The bonds of ABLV Bank JSC and those of Latvian government posted the largest turnover in the amount of 116.1 million euro and 26.4 million euro respectively.

The NASDAQ OMX Riga stock turnover stood at 17.3 million euro in 2014, down from 21.7 million euro in 2013. The highest turnover was recorded for the shares of the JSC *Olainfarm* (7.7 million euro), JSC *Grindeks* (4.8 million euro) and JSC *Valmieras stikla šķiedra* (1.4 million euro).

In 2014, NASDAQ OMX Riga index OMXR decreased by 11.3% and the Baltic gross index OMXBBGI fell by 7.7%. OMXR development was affected by the sanctions imposed by Russia: due to these sanctions, many joint stock companies included in the index could no longer export their goods to Russia.

OPERATIONS AND ACTIVITIES OF LATVIJAS BANKA

LEGAL FRAMEWORK AND FUNCTIONS. LATVIJAS BANKA IN THE EUROSYSTEM AND INSTITUTIONS OF THE EUROPEAN UNION

Latvijas Banka is the central bank of the Republic of Latvia. Like the national central banks of other EU countries, Latvijas Banka is participating in the ESCB. As of 1 January 2014, Latvijas Banka is a participant in the Eurosystem. In its activities, Latvijas Banka complies with the Republic of Latvia and EU legislation, as well as ECB legal acts in compliance with the Treaty on the Functioning of the European Union and the Statute of the European System of Central Banks and the European Central Bank (hereinafter, the Statute of the ESCB and ECB).

The objective and tasks of Latvijas Banka are set forth by the Law on Latvijas Banka. The primary goal of Latvijas Banka is to maintain price stability. Latvijas Banka has the following primary tasks:
– participate in the formulation and implementation of the Eurosystem's monetary policy;
– manage foreign reserves and other financial investments;
– ensure cash circulation in Latvia and participate in ensuring the cash circulation process in the euro area;
– participate in promoting smooth operation of the payment systems;
– compile and publish statistical information in order to ensure the fulfilment of the tasks of Latvijas Banka;
– cooperate with the ECB, the central banks of other EU Member States and other countries, as well as other financial institutions;
– act as the financial agent of Latvia's government and provide financial services to other market participants;
– act as an advisor to the Saeima (Parliament) and Cabinet of Ministers of the Republic of Latvia on monetary policy issues and other issues related to the fulfilment of the tasks of Latvijas Banka;
– maintain the Credit Register;
– issue licences to legal persons listed in the Register of Enterprises of the Republic of Latvia, except credit institutions, for the purchase and sale of foreign currency as a commercial activity.

Latvijas Banka is not subject to decisions and instructions by the government or other institutions. Latvijas Banka is independent in making and implementing decisions. Latvijas Banka is supervised by the Saeima of the Republic of Latvia.

In 2014, the Governor of Latvijas Banka participated in the work of the Governing Council and the General Council of the ECB, namely, in the formulation of the euro area's monetary policy and decision-making related to other tasks of the Eurosystem and the ESCB. The representatives of Latvijas Banka actively participated in ESCB committees (see Appendix 4) and working groups, dealing with issues related to monetary policy, market operations, financial stability, payment systems, euro banknotes, statistics, international relations, communication, accounting etc.

Experts of Latvijas Banka also participated in committees and working groups of the Council of the EU and the EC.

Sitting on the EFC and its subcommittees, the representatives of Latvijas Banka regularly participated in the decision-making concerning the economic development and financial stability of the EU as well as the development of the EU economic policy strategy, inter alia, concerning the instruments for ensuring sustainable growth and investment in the EU economy, and discussed policies of international financial institutions. The representatives of Latvijas Banka participated in the EC and Eurostat working groups addressing issues related to euro coins, payment systems, economic forecasting and statistics.

In 2014, the Governor of Latvijas Banka participated in the work of the ESRB, making decisions on recommendations towards preventing the systemic risks of the EU financial system as well as other issues related to the macro-prudential policy. The representatives of Latvijas Banka engaged actively in the work of the Advisory Technical Committee of the ESRB and its working groups.

With the FCMC's consent, a representative from Latvijas Banka also participated in the work of the Board of Supervisors of the EBA whose objective is to safeguard public values, supporting the short-term, medium-term and long-term financial stability and the efficiency of the financial system.

In compliance with the requirements of the Statute of the ESCB and ECB, Latvijas Banka ensured translation of the ECB Annual Report 2013, the summary of the ECB Convergence Report of June 2014, and the quarterly version of the ECB's Monthly Bulletin (published on the Internet).

DEVELOPMENT, ADOPTION AND IMPLEMENTATION OF THE EUROSYSTEM'S MONETARY POLICY

ECONOMIC RESEARCH, ANALYSIS AND FORECASTING

Economic research and analysis are an important function of a national central bank for the purpose of acquiring quantitative and scientifically sound accounts of economic processes, thus enhancing the adoption of quality economic policy decisions. Research is also necessary to develop econometric models for forecasting macroeconomic indicators and considering alternative scenarios. With Latvia having joined the euro area, the role of quantitative research has further increased, since an in-depth economic analysis both of Latvia and the entire euro area and its individual countries is necessary for the adoption of monetary policy decisions.

Upon a full-fledged membership of Latvijas Banka in the EMU, it participates in all forecasting procedures of the Eurosystem both by developing macroeconomic forecasts for the Latvian economy and by taking part in the discussions of the forecasts of other euro area countries organised in the framework of the ESCB Working Group on Forecasting and the Monetary Policy Committee. The Eurosystem staff macroeconomic projections are published twice a year (in June and December), and they summarise macroeconomic projections by experts of all euro area countries. The forecasting models and infrastructure of Latvijas Banka are adapted for successful participation in forecasting procedures of the Eurosystem and provision of forecasts for the Latvian economy in a timely manner. These forecasts arise from assumptions developed by ECB experts in relation to global economic growth, oil prices and other external factors. Experts of Latvijas Banka also participate in the regular forecasting meetings of the EC and OECD working groups on forecasting.

Upon Latvia's integration into the family of the euro area countries, Latvijas Banka extended international cooperation through active participation in the three ESCB research networks, i.e. the Competitiveness Research Network (CompNet), Wage Dynamic Network and Household Finance and Consumption Network.

In 2014, Latvijas Banka published six working papers and three discussion papers on its website. In addition, three working papers developed in cooperation with ESCB staff were published in the Working Paper Series of the ECB and *Oesterreichische Nationalbank*. From 2014, external reviewers were attracted for assessment of Latvijas Banka's working papers to further improve their quality. Two expert discussions on lending in Latvia and development of productivity in Latvia were underpinned by the published working papers of Latvijas Banka. The conclusions of Latvijas Banka's working papers were disseminated to the general public also through articles and blogs, including www.makroekonomika.lv, www.delfi.lv and www.voxeu.org.

Working paper No. 1/2014 of Latvijas Banka presents an approach based on a perturbation technique to construct global solutions to dynamic stochastic general equilibrium (DSGE) models. The results of this theoretical paper provide an effective way of solving complex non-linear models to prepare conclusions on economic issues more precisely.

In response to the structural changes in the economy and participation in the ESCB forecasting process, working paper No. 2/2014 describes Latvia's DSGE model Latvijas Banka can use for the purposes of monetary policy analysis and in the forecasting process. The DSGE model includes financial frictions, and it is adapted for the needs of Latvian data. The model developed within the working paper was examined during Latvijas Banka's expert discussions.

Working paper No. 3/2014 was prepared in cooperation with experts of *Oesterreichische Nationalbank* within the ESCB Competitiveness Research Network. The paper proposes a theoretical framework for explaining gains and losses in export market shares by considering both price and non-price determinants. The empirical analysis of the major world exporters carried out by the authors of the working paper reveals the dominant role of non-price factors in explaining the competitive gains of BRIC countries and concurrent decline in the G7 market share of world exports. It is possible to prove the positive and dominant role of non-price factors in Latvia's exports by using the above analysis. The paper is also published in the ECB Working Paper Series (No. 1640).

As a follow-up to the above project concerning the explanation of export market shares, working paper No. 4/2014 offers a comprehensive analysis of price and non-price competitiveness, taking account of changes in the value added content of trade. The paper was developed in cooperation with experts of *Oesterreichische Nationalbank* in the framework of the ESCB Competitiveness Research Network. With respect to the impact of the fragmentation of the production process, it has been concluded that the relative quality of production from the US, Canada, Germany and the UK, when tracing value added in exports, remained unchanged or even increased. Meanwhile, the improving relative quality of BRIC countries' (except China) export goods largely arose from outsourcing rather than from improvements in the quality of domestic production. The paper is also published in the Working Paper Series of *Oesterreichische Nationalbank* (No. 193).

Another working paper produced in cooperation with experts of *Oesterreichische Nationalbank* examines international transmission of the negative credit supply shock, which originated in the euro area and the US (working paper No. 5/2014 of Latvijas Banka). Using the global vector autoregression (GVAR) approach, it was proved that the credit supply shocks of the US and euro area played a significant role in lending both in the euro area and Latvia. The results of the working paper were examined during Latvijas Banka's expert discussions.

Working paper No. 6/2014 of Latvijas Banka addresses the effect of traditional determinants of exports and imports with a focus on the role of price competitiveness in restoring external balances. The paper was developed in cooperation with ECB experts in the framework of the ESCB Competitiveness Research Network. The authors found evidence that the harmonised competitiveness indicators based on broader cost and price measures have a larger effect on exports of goods. Meanwhile, imports of goods and services are quite insensitive to the changes in relative prices. The paper is also published in the ECB Working Paper Series (No. 1736).

Discussion paper No. 1/2014 of Latvijas Banka was produced to provide insight into the debt servicing capacity of Latvian households and its sustainability under the impact of different macroeconomic shocks. The results obtained lead to a conclusion that following the financial crisis household solvency is still fragile and possible negative shocks might contribute to higher potential losses of credit institutions. At the same time, it can be considered that possible losses to lenders arising from such adverse shocks might be lower than two years ago, since the value of collateral has increased with real estate prices moving up, while outstanding loans granted for house purchase have declined.

Discussion paper No. 2/2014 of Latvijas Banka analyses trade links between the EU Member States and Russia, taking into account the indirect trade links through global value chains. The project was carried out in cooperation with experts of *Oesterreichische Nationalbank*. In terms of direct export shares, Russia represents the EU's fourth largest trade partner, while the EU is Russia's largest trade partner. Economic dependence of Russia on EU value added in terms of both final use and producing output is considerably higher than vice versa. However, the degree of integration varies greatly across the EU Member States. For example, the Baltic States are notably more dependent on Russia's value added than vice versa. Moreover, certain EU economic sectors, such as energy, utilities and air transport, are strongly dependent on inputs of Russian resources.

Discussion paper No. 3/2014 of Latvijas Banka is devoted to the natural population change forecast for the time horizon until 2030. Although the applied approach is a technical one, it is useful for understanding what complex tasks policy makers will have to deal with in 15–20 years from now in the case of a no-population-habits-change scenario. It is estimated that the natural population decrease in 19 years will reach 200 000, including the decrease of about 190 000 in population aged 20–64, while the old-age dependency ratio will increase to 36.5%. This will have a significant impact both on labour market developments and sustainability of the state pension system.

Four working papers of Latvijas Banka were published in international peer-reviewed journals. Working paper No. 1/2013 of Latvijas Banka on the effect of VAT rate changes on inflation in Latvia was published in the journal *Applied Economics*, Volume 46. Discussion paper No. 2/2014 of Latvijas Banka on trade links between the EU Member States and Russia was published in the journal *Focus on European Economic Integration* (Q3/14) issued by *Oesterreichische Nationalbank*. Working paper No. 4/2012 of Latvijas Banka on the assessment of equilibrium of the lats real exchange rate was published in the *Baltic Journal of Economics*, Volume 14. Meanwhile, a joint project of Latvijas Banka and *Oesterreichische Nationalbank* on the assessment of import prices, taking into consideration quality and taste factors, was published in the journal *Review of World Economics*, Volume 150.

DECISIONS AND INSTRUMENTS OF THE EUROSYSTEM'S MONETARY POLICY

In 2014, the Eurosystem continued to pursue an accommodative monetary policy, since the average inflation of the euro area remained low and continued to decline. Moreover, inflation and economic growth forecasts were revised downwards several times, confirming that the period of low inflation could last longer than initially planned. In such circumstances, when interest rates were already close to zero and possibilities of the traditional monetary policy instruments became increasingly limited, new monetary policy instruments, including new securities purchase programmes, were necessary. The meetings of the Governing Council of the ECB of 5 June and 4 September played the most important role in relation to monetary policy decisions.

As of 5 June, the Governing Council of the ECB decided to reduce the key interest rates. The rate on deposit facility in euro turned negative (–0.10%) for the first time, and this negative rate also referred to credit institutions' excess financial resources kept at the central bank and exceeding the minimum reserve requirements (see Table 1). This decision of the Governing Council of the ECB was aimed at supporting lending and accelerating the pace of economic growth. At the same time, it was announced at the meeting that the Eurosystem would launch TLTROs in September, allowing the central banks of the Eurosystem to grant funds to credit institutions with a maturity of up to four years, depending on their lending activities. In addition to these efforts, the Eurosystem discontinued the organisation of fixed-term deposit tenders, thus increasing excess liquidity of credit institutions.

Table 1

KEY INTEREST RATES SET BY THE GOVERNING COUNCIL OF THE ECB
(%)

Key interest rates	Until 10 June 2014	11.06.2014–09.09.2014	From 10 September 2014
Deposit facility	0.00	–0.10	–0.20
Main refinancing operations	0.25	0.15	0.05
Marginal lending facility	0.75	0.40	0.30

At its meeting of 4 September, the Governing Council of the ECB decided to further reduce the key interest rates and cut the main refinancing operation rate to 0.05%, but the deposit facility rate – to –0.20%. Since the potential of the traditional liquidity providing monetary policy instruments to facilitate lending development with interest rates as low as the above was exhausted, the Governing Council of the ECB at its meeting of 4 September decided to supplement TLTROs with two new programmes ABSPP and CBPP3.

Every week the Eurosystem carried out the main refinancing operations as fixed-rate tenders with full allotment and a maturity of one week. The amount allotted at tenders fluctuated within the range of 83 billion euro to 174 billion euro, averaging 111 billion euro per tender. The Eurosystem also announced that the main refinancing operations with full allotment would continue as long as necessary, at least until the end of the Eurosystem's reserve maintenance period ending in December 2016.

LTROs with a maturity of one maintenance period were executed by the Eurosystem every month up until the middle of the year, when their use was ceased. The amount allotted at these tenders fluctuated from 6 billion euro to 32 billion euro. In 2014, 12 tenders of LTROs with a maturity of three months were held. The amount allotted was within the range of 5 billion euro to 22 billion euro. It augmented in the last two months of the year, since LTRO with a maturity of three years repayment was approaching.

The first two TLTROs took place in September and December when 83 billion euro and 130 billion euro were allotted respectively, with the number of participants reaching 255 credit institutions and 306 credit institutions respectively. The first two tenders provided an opportunity for credit institutions to borrow up to 7% of their loans to the euro area non-financial sector, except loans to households for house purchase. In turn, during the next tenders organised until June 2016, credit institutions will be able to borrow funds up to three times exceeding the net increase in their new loans (new loans minus repaid loans) to the euro area non-financial sector, except loans to households for house purchase. The interest rate at the first two TLTROs was composed of the interest rate on the main refinancing operations plus 10 basis points. TLTRO maturity of all tenders is September 2018. After a two-year-period, credit institutions will have an opportunity to make early repayments of their funds raised from TLTRO tenders; however, they will have to repay the resources not used for the intended purpose before their maturity.

Tenders of fixed-term deposits in euro were organised until mid-June, and since these were not fixed-rate tenders, their interest rate was usually a couple of basis points lower than that on the main refinancing operations. The amount of deposits received fluctuated from 103 billion euro to 179 billion euro. Owing to decreased excess liquidity, credit institutions' interest in these deposits declined at the last tenders.

The Eurosystem also continued to offer liquidity in US dollars with maturity of 7 days to credit institutions every week and organised US dollar liquidity operations with maturity of 84 days until April; however, credit institutions' demand for these resources was low.

CBPP3 was launched in the second half of October, but ABSPP was started at the end of November. Duration of the two programmes will continue at least two years, and the Eurosystem will purchase securities both in the primary and secondary markets. The minimum credit rating (BBB–/Baa3/BBBL) thresholds set in compliance with the collateral requirements of the Eurosystem monetary policy operations are applied to the securities to be purchased. At the end of 2014, CBPP3 constituted 29.6 billion euro, but ABSPP – 1.7 billion euro.

The minimum reserve ratio of the Eurosystem was not changed in 2014. It was 1% on deposits with a maturity of up to two years, deposits with the period of notice of up to two years and debt securities issued with a maturity of up to two years. Meanwhile, if the maturity of deposits and issued securities exceeds two years, the minimum reserve ratio is 0%.

USE OF MONETARY POLICY INSTRUMENTS IN LATVIA

Since Latvia became a member of the euro area in 2014, the substantial lats liquidity surplus of credit institutions recorded in late 2013 was converted from lats to euro at Latvijas Banka. The reduction of the minimum reserve ratio from 2014, applying the minimum reserve ratio set by the Eurosystem, also had a positive impact on excess liquidity. Thus, decline in excess liquidity was observed in Latvia's credit institutions early in the year. They had an opportunity to place their excess euro funds outside Latvia (mainly credit institutions having affiliated and associated credit institutions in Europe). Meanwhile, other credit institutions continued to keep significant excess reserves at Latvijas Banka. In 2014, the average reserve requirements applied to Latvia's credit institutions was 195.6 million euro (841.0 million euro in 2013), while the excess of the average daily balance of credit institutions' demand deposits over the minimum reserves was 778.1 million euro.

Since credit institutions had excess liquidity, they kept their participation in the main refinancing operations and LTROs with a maturity of three months to a minimum. Credit institutions were interested in the ECB's new instrument, TLTROs, which provided an opportunity to borrow long-term funding with a maturity of up to four years with a very low interest rate (0.15% in 2014). In general, two TLTRO tenders were held. Latvian credit institutions requested and received funds totalling 25.0 million euro at the September tender and 60.5 million euro – at the December tender. A total of five credit institutions participated in both tenders.

Latvian credit institutions took part in fixed-term deposit tenders organised by the Eurosystem until the middle of 2014. Between 1 January and 17 June 2014, the daily balance of credit institutions' time deposits averaged 938.7 million euro. Meanwhile, deposit facility was used very rarely by Latvian credit institutions in 2014 as its interest rate was 0% until 10 June, turning negative at a later stage. This situation did not contribute to keeping excess funds in deposit facility.

In 2014, Latvijas Banka did not participate in ABSPP and CBPP3, since the market for such securities is not developed in Latvia.

INVESTMENT MANAGEMENT

Foreign reserves comprising gold and foreign currencies, and other financial investments of Latvijas Banka amounted to 4 439.4 million lats at the end of 2014 (4 429.5 million lats at the end of 2013).

Latvijas Banka manages its investments in compliance with the guidelines adopted by the Council of Latvijas Banka. The benchmark portfolio currency is the euro and the benchmark assets consist of 41.73% of US dollar-denominated assets, 26.98% of euro-denominated assets, 10.43% of Japanese yen-denominated assets, 8.35% of Canadian dollar-denominated assets, 7.30% of British pound sterling-denominated assets, 3.13% of Danish krone-denominated assets and 2.08% of Singapore dollar-denominated assets. At the beginning of 2014, a long-term securities portfolio was established by investing part of the financial assets in euro area 10-year government bonds. Latvijas Banka invests the financial assets in safe and liquid financial instruments, primarily in debt securities issued by governments of EU countries and the US, their agencies, and international organisations, as well as in highly rated bank and corporate debt securities, asset-backed debt securities and callable bonds. Interest rate futures are used to regulate the duration of reserves. For the purpose of implementing yield curve strategies on the interest rate market, interest rate swaps are used, whereas currency futures and forward exchange rate contracts are applied to ensure the optimal currency composition of financial assets.

Investments are managed relative to the benchmark comprised of 1–3 year government bond weighted indices of the US, euro area countries, Japan, Canada, the UK, Denmark and Singapore; therefore, investments are primarily made in securities with maturity of 1–3 years. Particular attention is paid to the interest rates of 2-year bonds. Over 2014, the weighted average yield of 2-year Treasury bonds declined from 0.21% to –0.1% in Germany, from 0.56% to 0.45% in the UK, from 0.26% to –0.03% in Denmark, from 0.09% to –0.03% in Japan and from 1.14% to1.01% in Canada, while increasing from 0.38% to 0.67% in the US and from 0.35% to 0.61% in Singapore. With interest rates remaining historically very low, it is complicated for the national central bank as a conservative investor with a low risk tolerance level to generate high returns. An interest rate decline in most financial asset investment markets and investment in securities outside the benchmark had a positive effect on Latvijas Banka's income from financial asset management in 2014.

Latvijas Banka stored its gold reserves with the Bank of England. Latvijas Banka hedged the risk related to fluctuations in the gold reserves market value by entering into currency futures and foreign exchange forward contracts and foreign exchange swaps.

Latvijas Banka used the services provided by four external investment managers. They manage a small portion of Latvijas Banka's financial assets pursuant to the guidelines adopted by the Council of Latvijas Banka.

In investment management, much attention is paid to risk management and control. The compliance of financial asset and gold portfolios with the guidelines is checked on a regular basis, and risk allocation is managed in line with various investment decisions.

Latvijas Banka, together with *Oesterreichische Nationalbank*, managed its share of the foreign reserve assets in Japanese yen, transferred to the ECB.

CURRENCY IN CIRCULATION

At the end of 2014, the amount of euro banknotes and coins in circulation issued by Latvijas Banka reached 735.7 million euro; euro banknotes represented 692.0 million euro or 94.1% of this amount, while coins accounted for 43.7 million euro or 5.9%.

At the end of 2014, 20 euro and 50 euro banknotes (13.6 million and 9.6 million respectively; see Chart 19) accounted for the majority of banknotes in circulation issued by Latvijas Banka in terms of number, while 1 cent and 2 cent coins (42.4 million and 36.8 million respectively; see Chart 20) made up the majority of coins issued by Latvijas Banka.

The cash received from credit institutions were checked for wear and tear and authenticity by automated cash processing systems which processed 133.4 million banknotes in 2014. 15.2% (20.3 million) of the processed banknotes were identified as unfit for circulation and destroyed.

Chart 19

AMOUNT OF EURO BANKNOTES ISSUED IN NET TERMS BY LATVIJAS BANKA
(face value; number in millions)

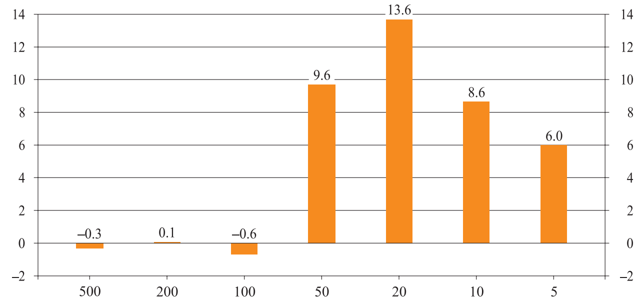
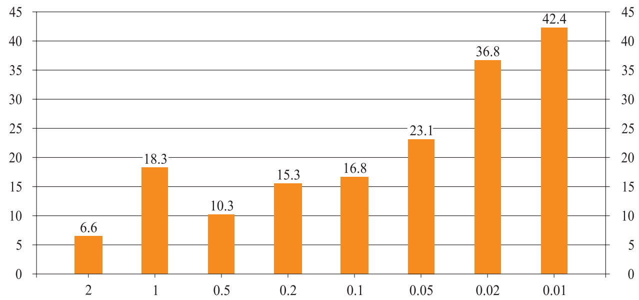


Chart 20

EURO COINS ISSUED BY LATVIJAS BANKA
(face value; number in millions)



In 2014, Latvijas Banka started to register merchants engaged in processing and recirculating euro banknotes and coins and to monitor their operation. A merchant is entitled to carry out the processing and recirculating of euro banknotes and coins in the Republic of Latvia by registering as a cash processing institution with Latvijas Banka. At the end of 2014, 85 cash processing institutions were registered in Latvia. Latvijas Banka conducted the inspections of the cash processing institutions by assessing their compliance with the requirements of the legislative acts regulating the cash processing.

The total nominal value of counterfeits detected in 2014 (51.6 thousand euro) accounted for only 0.007% of the amount of cash in circulation issued by Latvijas Banka. 968 counterfeit banknotes and 351 counterfeit coins were detected in 2014.

In 2014, withdrawal of lats banknotes and coins from circulation continued. At the end of the year, the value of lats banknotes in circulation was only 54.7 million lats and that of lats coins – 45.5 million lats. At the end of December 2014, 5 lats and 20 lats banknotes accounted for the majority of banknotes in circulation in terms of number (1.8 million and 1.1 million respectively; see Table 2), while 1 santims and 2 santims coins (151.8 million and 91.4 million respectively; see Table 3) made up the majority of coins.

Table 2

LATS BANKNOTES IN CIRCULATION AT THE END OF THE YEAR

Nominal	Amount (in millions of lats)		Number (in millions of units)	
	2014	2013	**2014**	2013
LVL 500	**5.9**	36.8	**0**	0.1
LVL 100	**7.0**	76.9	**0.1**	0.8
LVL 50	**4.0**	41.9	**0.1**	0.8
LVL 20	**21.6**	312.5	**1.1**	15.6
LVL 10	**7.0**	42.2	**0.7**	4.2
LVL 5	**9.2**	53.3	**1.8**	10.7
Total	**54.7**	563.6	**x**	x

In 2014, to mark anniversaries significant to Latvian history and culture, Latvijas Banka issued collector coins "Ainaži Nautical School" (in circulation as of 5 March 2014), "The White Book" (in circulation as of 17 June 2014), "Baltic Way" (in circulation as of 19 August 2014) and "Old Stenders" (in circulation as of 4 September 2014). The "Coin of the Seasons" is dedicated to Latvian traditions (in circulation as of 12 November

Table 3

LATS COINS IN CIRCULATION AT THE END OF THE YEAR

Nominal	Amount (in millions of lats)		Number (in millions of units)	
	2014	2013	**2014**	2013
LVL 2	**5.2**	7.5	**2.6**	3.8
LVL 1	**24.7**	37.3	**24.7**	37.3
50 s	**5.2**	7.9	**10.3**	15.9
20 s	**3.0**	4.6	**15.1**	23.1
10 s	**1.9**	2.8	**19.3**	28.4
5 s	**1.6**	2.2	**31.3**	43.5
2 s	**1.9**	2.4	**91.4**	121.0
1 s	**1.5**	1.9	**151.8**	185.6
LVL 100 and LVL 10 collector coins	**0.5**	0.5	**0**	0
Total	**45.5**	67.2	**x**	x

2014). To further support the restoration project of the Lestene Church, a collector coin "Baroque of Courland" featuring the elements of wood carvings of the Lestene Church was issued (in circulation as of 9 December 2014).

LATVIAN EURO CIRCULATION COINS

2 EURO

Weight: 8.50 g; diameter: 25.75 mm; thickness: 2.20 mm
Shape: round; colour: outer part – silver, inner part – gold
Composition: outer part – copper-nickel (Cu, Ni);
inner part – three layers: nickel brass, nickel, nickel brass (Ni, Cu, Zn; Ni; Ni, Cu, Zn)

1 EURO

Weight: 7.50 g; diameter: 23.25 mm; thickness: 2.33 mm
Shape: round; colour: outer part – gold, inner part – silver
Composition: outer part – nickel brass (Ni, Cu, Zn);
inner part – three layers: copper-nickel, nickel, copper-nickel (Cu, Ni; Ni; Cu, Ni)

The national side of the coin features the portrait of a Latvian maiden in profile, originally depicted on the reverse of the 5 lats silver coin in 1929. It is semi-encircled by the inscriptions LATVIJAS on the left and REPUBLIKA on the right. The coin's outer ring bears 12 stars. The edge of the 2 euro coin bears the inscription * DIEVS * SVĒTĪ * LATVIJU (God, Bless Latvia).
Artists: common side: Luc Luycx; national side: Guntars Sietiņš and Ligita Franckeviča

50 CENT

Weight: 7.80 g; diameter: 24.25 mm; thickness: 2.38 mm
Shape: round; colour: gold
Composition: Nordic gold (Cu, Al, Zn, Sn)

20 CENT

Weight: 5.74 g; diameter: 22.25 mm; thickness: 2.14 mm
Shape: Spanish flower shape; colour: gold
Composition: Nordic gold (Cu, Al, Zn, Sn)

10 CENT

Weight: 4.10 g; diameter: 19.75 mm; thickness: 1.93 mm
Shape: round; colour: gold
Composition: Nordic gold (Cu, Al, Zn, Sn)

5 CENT

Weight: 3.92 g; diameter: 21.25 mm; thickness: 1.67 mm
Shape: round; colour: copper
Composition: copper-covered steel

2 CENT

Weight: 3.06 g; diameter: 18.75 mm; thickness: 1.67 mm
Shape: round; colour: copper
Composition: copper-covered steel

1 CENT

Weight: 2.30 g; diameter: 16.25 mm; thickness: 1.67 mm
Shape: round; colour: copper
Composition: copper-covered steel

The national side features the large coat of arms of the Republic of Latvia (50, 20 and 10 cent coins) or the small coat of arms of the Republic of Latvia (5, 2 and 1 cent coins), with the year 2014 on the left and the inscription LATVIJA beneath it, surrounded by 12 stars.
Artists: common side: Luc Luycx; national side: Laimonis Šēnbergs and Jānis Strupulis

2 EURO COMMEMORATIVE COIN

RIGA – EUROPEAN CAPITAL OF CULTURE 2014

Weight: 8.50 g; diameter: 25.75 mm; thickness: 2.20 mm
Shape: round; colour: outer part – silver, inner part – gold
Composition: outer part – copper-nickel (Cu, Ni), inner part – three layers: nickel brass, nickel, nickel brass (Ni, Cu, Zn; Ni; Ni, Cu, Zn)
Struck in 2014 by *Staatliche Münzen Baden-Württemberg* (Germany)
The national side of the coin shows the skyline of Riga, with inscriptions "RĪGA – 2014" and "LV" underneath. At the top of the image there is a semi-circled inscription "EIROPAS KULTŪRAS GALVASPILSĒTA" (European Capital of Culture). The coin's outer ring depicts 12 stars. The edge of the coin bears the inscription * DIEVS * SVĒTĪ * LATVIJU (God, Bless Latvia).
Artists: common side: Luc Luycx; national side: Henrihs Vorkals and Jānis Strupulis

5 EURO COLLECTOR COINS

AINAŽI NAUTICAL SCHOOL

Weight: 22.00 g; diameter: 35.00 mm
Metal: silver of .925 fineness; quality: proof
Struck in 2014 by *Koninklijke Nederlandse Munt* (the Netherlands)
Artist: Ivars Drulle

THE WHITE BOOK

Weight: 25.80 g; poligonal form
Metal: silver of .925 fineness; quality: proof
Struck in 2014 by *Koninklijke Nederlandse Munt* (the Netherlands)
Artist: Sandra Krastiņa

BALTIC WAY

Weight: 22.00 g; diameter: 35.00 mm
Metal: silver of .925 fineness; quality: proof with colour print (7 colours) on the obverse
Struck in 2014 by *Koninklijke Nederlandse Munt* (the Netherlands)
Artists: Visvaldis Asaris (graphic design), Ligita Franckeviča (plaster model)

OLD STENDERS

Weight: 22.00 g; diameter: 35.00 mm
Metal: silver of .925 fineness; quality: proof
Struck in 2014 by *Koninklijke Nederlandse Munt* (the Netherlands)
Artists: Aigars Ozoliņš (graphic design), Jānis Strupulis (plaster model)

COIN OF THE SEASONS

Weight: 22.00 g; diameter: 35.00 mm
Metal: silver of .925 fineness; quality: proof
Struck in 2014 by *Koninklijke Nederlandse Munt* (the Netherlands)
Artists: Arvīds Priedīte (graphic design), Ligita Franckeviča (plaster model)

BAROQUE OF COURLAND

Weight: 22.00 g; diameter: 35.00 mm
Metal: silver of .925 fineness; quality: proof with gilded elements
Struck in 2014 by *Mennica Polska S.A.* (Poland)
Artists: Laimonis Šēnbergs (graphic design), Ligita Franckeviča (plaster model)

The first Latvian 2 euro commemorative coin "Riga – European Capital of Culture 2014" was put into circulation (in circulation as of 11 August 2014).

The design of Latvian coins has received high international recognition. In 2014, the coin dedicated to the 200th anniversary of the birth of composer Richard Wagner issued by Latvijas Banka in 2013 was announced the winner in the category "Best Silver Coin" at the international contest "The Coin of the Year".

In March 2014, Latvijas Banka held the traditional public survey "Latvia's Coin of the Year 2013" which is the most significant annual event dedicated to the coin art of Latvia, enabling Latvijas Banka to elicit public opinion on the work done in the field of collector coins and the attractiveness of coin themes and artistic presentations. The public survey named the "Baby Coin" as the winner of "Latvia's Coin of the Year 2013" award.

PAYMENT AND SETTLEMENT SYSTEMS

TARGET2-LATVIJA OPERATION

Latvijas Banka, together with other participants of the ESCB, ensured the operation of TARGET2, the Trans-European Automated Real-time Gross settlement Express Transfer system. Latvijas Banka operated the component system TARGET2-Latvija, providing settlement of the Eurosystem's monetary policy operations, interbank settlement of large-value payments and that of urgent customer payments in euro.

Latvijas Banka terminated the operation of the SAMS for the lats settlement as of the introduction of the euro, converted the settlement account balances of financial institutions, including Latvia's credit institutions, the Treasury and Latvijas Banka, into the euro and transferred the above funds to TARGET2-Latvija which had been adjusted for operation within the Eurosystem. Latvijas Banka also ensured a changeover to the settlement in euro for DENOS, the securities settlement system of the LCD, and the card payment system of First Data Latvia Ltd. In 2014, one credit institution joined TARGET2-Latvija, hence 22 credit institutions, the Treasury and Latvijas Banka were the participants in TARGET2-Latvija at the end of the year. TARGET2-Latvija also provided for the final settlement in euro for the EKS, DENOS, the securities settlement system of the LCD, and the card payment system of First Data Latvia Ltd. In 2014, 356.3 thousand payments in the amount of 343.0 billion euro were processed in TARGET2-Latvija (see Table 4; for the monthly data on payments processed in TARGET2-Latvija see Chart 21). The total value of payments executed in TARGET2-Latvija increased 2.6 times year-on-year. This development is associated with the settlement of monetary policy transactions, transactions of market operations and settlement of other types of transactions executed in the SAMS prior to the introduction of the euro. At the same time, the total volume of payments processed in TARGET2-Latvija recorded a moderate rise of 1.8% since the volume of customer payments declined along with the changeover to the euro as the system's participants transferred part of their payments to the SEPA compliant payment systems.

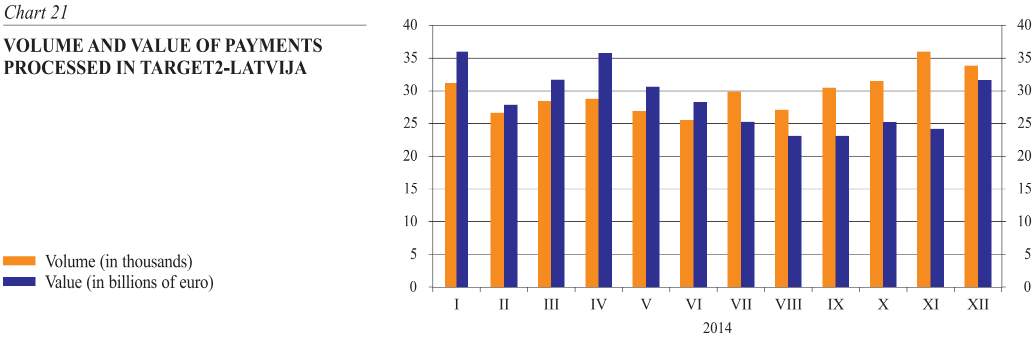
Table 4

PAYMENTS PROCESSED IN TARGET2-LATVIJA

	Volume (in thousands)			Value (in billions of euro)		
	Interbank payments	Customer payments		Interbank payments	Customer payments	
2014	**75.1**	**281.2**	**356.3**	**326.9**	**16.1**	**343.0**
2013	38.3	311.5	349.8	116.4	15.6	132.0
2012	35.7	292.4	328.1	173.1	12.9	186.0
2011	35.2	272.2	307.4	215.2	12.6	227.8
2010	39.5	247.6	287.1	190.7	9.3	200.0

Chart 21

VOLUME AND VALUE OF PAYMENTS PROCESSED IN TARGET2-LATVIJA



OPERATION OF THE EKS, A SYSTEM MAINTAINED BY LATVIJAS BANKA, AND PAYMENT SERVICES

Latvijas Banka terminated the payment settlement in lats in the EKS along with the changeover to the euro in 2014. The EKS continued to ensure convenient, rapid and cheap interbank customer payments in euro, enabling a fully automated processing of electronic payment documents with the final settlement executed via TARGET2-Latvija on the participants' settlement accounts opened with Latvijas Banka. The EKS, as a SEPA-compliant system, enabled its participants to make and receive SEPA credit transfers in euro throughout SEPA.

As of November 2014 upon enhancing the EKS, Latvijas Banka also ensured the EKS operation on the business days, transferred by the Cabinet of Ministers Decree, that were TARGET2 holidays. Credit institutions participating in the EKS could accelerate the execution of the customer payments and support the activities of businesses on the transferred business days. On 9 December 2014, Latvijas Banka started to provide a direct link of the EKS with the interbank payment system STEP2 operated by EBA Clearing, whereby Latvijas Banka became a direct participant in STEP2. Direct link with STEP2 has accelerated the payment execution with credit institutions, including Latvia's credit institutions other than the participants in the EKS, and has enabled the EKS participants to extend the time period for payment receipt and improve the customer service.

Six credit institutions terminated their participation in the EKS as of the introduction of the euro in Latvia, and took a decision to participate in other SEPA-compliant payment systems. At the end of 2014, the EKS comprised the following direct participants: 16 credit institutions, the Treasury and Latvijas Banka as well as two indirect participants. The EKS processed 35.7 million payments in the amount of 48.2 billion euro (see Table 5; for the monthly data on payments processed in the EKS see Charts 22 and 23). The declining number of participants notwithstanding, the volume and value of payments processed in the EKS recorded a growth of 3.2% and 85.9% respectively in comparison with 2013 (payments in lats and euro taken into account). This can be attributed to the introduction of SEPA credit transfers in Latvia and the fact that all EKS participants commenced sending and receiving of payments via the EKS. The increase in the total value of payments processed in the EKS was primarily on account of lifting the restrictions imposed on the amount of payments processed in the EKS, resulting in the transition of customer payments from TARGET2-Latvia. The EKS ensured 99.77% availability to its participants (99.83% in 2013; the EKS final settlement was delayed on four occasions over the year).

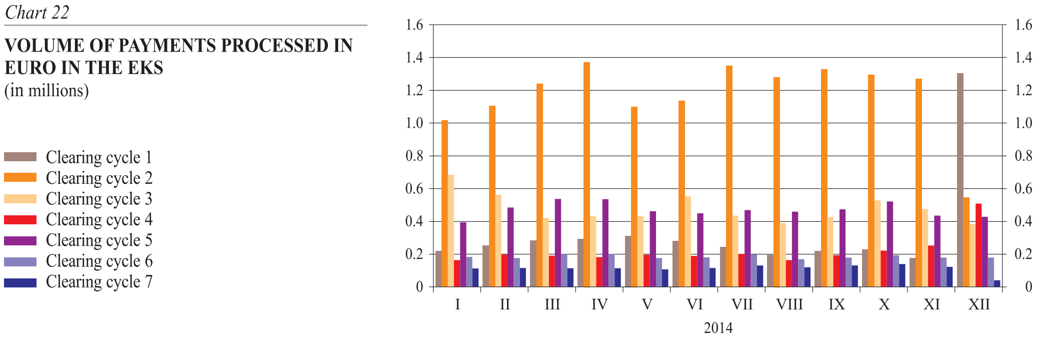
Table 5

PAYMENTS PROCESSED IN THE EKS

	Volume (in thousands)			Value (in billions of euro)		
	Payments in lats	Payments in euro		Payments in lats	Payments in euro	
2014	**–**	**35 658.3**	**35 658.3**	**–**	**48.2**	**48.2**
2013	33 664.1	900.3	34 564.4	17.6	8.4	26.0
2012	33 544.8	703.8	34 248.6	17.3	6.2	23.5
2011	34 597.9	464.0	35 061.9	17.1	2.8	19.9
2010	32 796.8	310.1	33 107.0	15.0	1.5	16.5

Chart 22

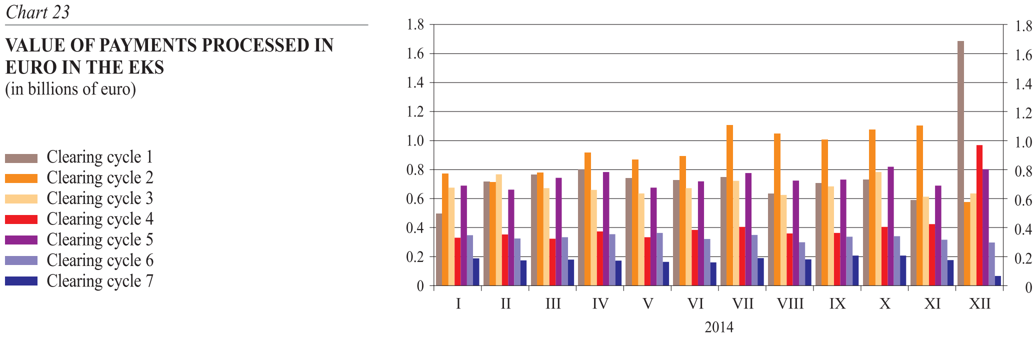
VOLUME OF PAYMENTS PROCESSED IN EURO IN THE EKS
(in millions)



In 2014, Latvijas Banka rendered payment services to domestic, foreign and international financial institutions in euro, with the value of processed payments totalling 1.2 billion euro. Latvijas Banka started to offer SEPA credit transfer orders to its customers and

Chart 23

VALUE OF PAYMENTS PROCESSED IN EURO IN THE EKS
(in billions of euro)



executed SEPA credit transfers on its own behalf for those customers who had not migrated to SEPA Credit Transfer Scheme. As of April 2014, Latvijas Banka ensured its participants an indirect participation in the EKS by processing files of those SEPA credit transfer orders and SEPA payment return orders which an indirect participant had submitted on its own or its customer's behalf.

OVERSIGHT OF PAYMENT AND SECURITIES SETTLEMENT SYSTEMS

The oversight policy of the ECB became binding on Latvijas Banka upon joining the Eurosystem. As of 1 January 2014, Latvijas Banka, in the capacity of one of the participants in the Eurosystem, performed the oversight of payment and securities settlement systems in line with the Eurosystem oversight policy.

Latvijas Banka was actively involved in the oversight of TARGET2, participating in the assessment of changes effected in the system and analysing its operation on a regular basis. Latvijas Banka performed a day-to-day oversight of the EKS operated by it and the securities settlement system DENOS operated by the LCD, analysing the technical and operational functions of the systems and compiling statistical data on these systems. Within the framework of the payment system oversight, Latvijas Banka cooperated with the institutions ensuring the operation of clearing and payment systems (First Data Latvia Ltd. and credit institutions), providing consultations and expressing opinion on the payment system issues.

Latvijas Banka compiled data on the payment instruments used in Latvia (see Table 6). Payments by payment cards comprised 191.0 million payments or 57.1% of all payment instruments used and customer credit transfers stood at 138.3 million payments or 41.4% in 2014. The value of such payments amounted to 3.8 billion euro and 437.9 billion euro respectively. Other payment instruments (direct debit, cheques, e-money) were relatively seldom used.

Table 6

PAYMENT INSTRUMENTS USED IN LATVIA

	Volume (in millions)				Value (in billions of euro)			
	Customer credit transfers	Card payments	Direct debits, cheques and e-money payments		Customer credit transfers	Card payments	Direct debits, cheques and e-money payments	
2014	**138.3**	**191.0**	**5.0**	**334.3**	**437.9**	**3.8**	**0.3**	**442.0**
2013	139.7	151.6	6.4	297.7	575.7	3.2	0.3	579.2
2012	130.3	128.0	5.7	264.0	488.9	2.7	0.3	491.9
2011	119.3	114.0	5.3	238.6	422.7	2.4	0.1	425.3
2010	115.7	101.9	5.3	222.9	370.9	2.0	0.3	373.2

In 2014, Latvijas Banka finalised successfully the integration of Latvia's payment system into SEPA in cooperation with other participants in the SEPA Project in Latvia and completed the SEPA Project implementation in Latvia in July. Latvijas Banka engaged in the SEPA Project by steering the National SEPA Working Group (NSWG) which ceased its activity in 2014. The implementation of SEPA credit transfers in Latvia, a notable phase of SEPA, was completed on 1 January 2014 along with the introduction of the euro in Latvia. In July 2014, market stakeholders agreed that the national direct debit payments would not be converted into SEPA direct debit payments, albeit would be replaced by e-invoicing and SEPA credit transfers up to 1 January 2015.

In 2014, Latvijas Banka participated, in cooperation with the FCMC, in the European Forum on the Security of Retail Payments (SecuRe Pay) established by the ECB, and was involved in drafting the "Recommendations for Payment Account Access Services" and "Recommendations for the Security of Mobile Payments".

FINANCIAL STABILITY

In 2014, Latvijas Banka continued to engage in the activities performed by the ECB in preparation for the establishment of SSM. Along with launching the SSM on 4 November 2014 and conferring the function of prudential supervision to the ECB, Latvijas Banka, in close cooperation with the FCMC and within the scope of its competence, contributed to the assessment of financial stability in Latvia and in the euro area overall. Latvijas Banka was involved in the assessment of systemic risk to financial stability in the euro area, the development of instruments for the analysis of financial stability and evaluation of macro-prudential policy instruments. Towards the end of 2014, a meeting of the experts of Latvijas Banka and the ECB was convened for the purpose of exchanging views with the ECB experts on the assessment of financial stability risk, conducted by Latvijas Banka, and the relevant analytical framework.

The development of other elements of the banking union was further pursued in 2014 as well. Latvijas Banka provided opinion, within the scope of its competence, both on the Bank Recovery and Resolution Directive of the European Parliament and the Council establishing a framework for the recovery and resolution of credit institutions and investment firms and draft legal framework for the Single Resolution Mechanism.

Latvijas Banka continued to participate actively in drafting the ESRB policy and analysis documents and defining opinion. The representative of Latvijas Banka was involved in the analytical project of the ESRB upon designing the stress scenarios for a comprehensive stress testing of the EU banks.

In 2014, close cooperation among the Nordic and Baltic countries continued in the field of financial stability, providing for the discussion of common and specific risks in the region, risk mitigation measures, application of the financial sector's regulatory framework, as well as other topical financial stability issues. Latvijas Banka and the FCMC were engaged in the Nordic-Baltic Macro-prudential Forum and the relevant working groups, and together with the FCMC and the Ministry of Finance – in the Nordic-Baltic Cross-Border Stability Group.

Latvijas Banka continued to develop and enhance tools for the assessment of risks to the financial system in 2014. The enhancement of risk panel was commenced by complementing it with new financial soundness indicators and developing criteria for assessing the risk level of the indicators and risk categories (determining the level of risk significance by applying the so-called threshold method).

Latvijas Banka conducted the economic analysis fostering the decision on the countercyclical capital buffers for credit institutions, based on Latvijas Banka's expertise in the assessment of the economic development cycles, the ESRB recommendations and the best international practice. Latvijas Banka submitted the results of the above analysis to the FCMC (the authority responsible for applying the countercyclical capital buffer in Latvia).

In 2014, Latvijas Banka organised two experts' roundtables devoted to the financial stability. Latvijas Banka's discussion paper on survey-based assessment of household borrowers' financial vulnerability was presented to the participants of the roundtable discussion "The Analysis of Household Borrowers: a Survey and Financial Vulnerability Assessment" organised by Latvijas Banka. The factors contributing to a continuously negative lending dynamics that dampened the outlook for the economic development over a longer horizon were comprehensively analysed by the participants of the roundtable discussion "Lending in Latvia – the Theory versus Reality".

Financial Stability Department was established in 2014, taking into account the need to separate the functions of the monetary policy and financial stability.

OPERATION OF THE CREDIT REGISTER

In 2014, Latvijas Banka continued to collect, accumulate and store in the Credit Register the data of the Credit Register participants (such as credit institutions, companies having close links with credit institutions, credit unions and insurers; hereinafter, the participants) on the obligations of the customers and customer guarantors and the performance thereof and default.

The objectives of the Credit Register are to enable the participants to assess the credit worthiness of the customers and customer guarantors more accurately, manage credit risks more efficiently, provide the FCMC with additional opportunities of receiving the data necessary for performing the supervision of financial market participants, enable the consumer creditors of the EU Member States and the EEA countries to assess the consumers' creditworthiness, furnish data to Latvijas Banka and the FCMC required for macroeconomic analysis, ensure that Latvijas Banka is also granted an additional opportunity to receive data needed for financial statistics, contribute to the promotion of fulfilling the tasks of public administration, providing the public institutions with additional opportunities of receiving the data necessary for performing the analysis required by the tasks stipulated by laws and regulations, and ensure also an additional opportunity to enhance the performance of the obligations of a financially troubled customer and customer's guarantor.

The operation of the Credit Register was successfully adjusted along with the introduction of the euro in 2014. Amendments to the Law on Credit Register have become effective, providing for more comprehensive goals of the Credit Register which stipulate that Latvijas Banka is also entitled to furnish the Credit Register data to the EU institutions and complement the rights of the participants to submit the requests for the Credit Register data also pertaining to the potential recipients of the letter of credit service and warranty (a guarantee) service, as well as include in the list of the Credit Register participants the state capital companies which fulfil a special task (implement the state development and aid programmes).

In 2014, Latvijas Banka provided the Credit Register data to the ECB in accordance with the ECB Decision of 24 February 2014 on the organisation of preparatory measures for the collection of granular credit data by European System of Central Banks (ECB/2014/16). Pursuant to the above Decision, the ECB lays down the preparatory measures necessary for establishing a long-term framework for the collection of granular credit data gradually, based on the ECB's statistical reporting requirements. The Decision is binding on all national central banks of the euro area.

At the end of 2014, the Credit Register comprised 101 participants who authorised 743 users to work with the Credit Register (in 2013 – 102 participants and 718 users respectively). The Credit Register contained data on 3.6 million obligations (of which 1.1 million were outstanding obligations) pertaining to 1.1 million persons (at the end of 2013, on 3.3 million obligations pertaining to 1.0 million persons). The total outstanding obligations of the participants amounted to 19.67 billion euro, including outstanding obligations recognised in the balance sheet – 17.3 billion euro (at the end of 2013, the total outstanding obligations were 14.5 billion lats or 20.4 billion euro, of which outstanding obligations recognised in the balance sheet stood at 12.9 billion lats or 18.4 billion euro). In 2014, the Credit Register participants submitted 13.4 million requests, representing a 4.3% year-on-year decrease. Latvijas Banka provided the Credit Register data to 4.7 thousand natural and legal persons in 2014 (to 4.6 thousand persons in 2013), while natural persons submitted 638 requests to the Credit Register website for servicing natural persons electronically for the purpose of receiving data pertaining to themselves.

STATISTICS

Latvijas Banka collects and compiles financial and monetary statistics and balance of payments statistics as well as prepares quarterly financial account statistics and government finance statistics. Following the ECB's request, Latvijas Banka has also been involved in addressing the methodology related issues of some fields of economic statistics and compiling specific aggregates. Latvijas Banka uses statistical data to perform analysis of finance and macroeconomics as well as raise public awareness of the developments in the financial sector and the economy. The ECB uses statistical data produced by Latvijas Banka to compile data on the Eurosystem's monetary statistics and the relevant statistics of the euro area as well as to fulfil its other tasks.

As regards the Republic of Latvia accession negotiations with the OECD, Latvijas Banka provided the OECD with data on the financial statistics, direct investment, balance of payments, imports and exports of services and quarterly financial accounts as well as gave an explanation of the methodology of the above data compilation.

Latvijas Banka continued the regular transmission of statistical data to the ECB, BIS and IMF and transmitted statistical information to other domestic and foreign data users. To furnish a wide range of data users with timely information, Latvijas Banka disseminated financial and monetary statistics, balance of payments statistics and quarterly financial account statistics of Latvia via its regular publications and website of Latvijas Banka and compiled data for publishing in the ECB publications and the ECB Statistical Data Warehouse as well as the IMF publications and within the framework of the IMF Special Data Dissemination Standard. Latvijas Banka expanded the range of data transmitted to the BIS as well as continued to compile and transmit financial soundness indicators to the IMF. Latvijas Banka participated in the IMF's Financial Access Survey also in 2014, reporting data on the access to and scope of the services provided to households by Latvia's financial institutions.

FINANCIAL AND MONETARY STATISTICS

The year 2014 was significant for the field of financial and monetary statistics since the transition to the data collection, processing, compilation and release in euro was successfully implemented, an in-depth methodological work was performed in order to draft and introduce new regulations of Latvijas Banka in the field of statistics pursuant to the requirements of the ECB Regulations, as well as the "Statistical Reporting Guidelines for MFIs" published on the website of Latvijas Banka were updated, and MFI statistics, released in the internet statistical database INTS was expanded to include the date of deposits received by MFIs in breakdown by sector, currency and maturity. Taking into consideration the changes in the methodology for compiling statistical data, Latvijas Banka modified substantially the software used for the compilation and publishing of financial and monetary statistics. At the same time, the compilation of statistical data in accordance with the requirements of the ECB and other data users was successfully ensured on a regular basis and transmission of additional data necessary for fulfilling the tasks of SSM commenced.

The revised Latvijas Banka's "Regulation for Compiling the 'Monthly Financial Position Report' of Monetary Financial Institutions" and "Regulation for Compiling the 'Report on Adjustments in Respect of Write-Offs/ Write-Downs of Loans and Price Revaluations of Securities' " were approved. The above Regulations have been adopted subject to the requirements of Regulation (EU) No. 1071/2013 of the European Central Bank of 24 September 2013 concerning the balance sheet of the monetary financial institution sector (ECB 2013/33). This ensured the introduction of a breakdown by sector consistent with the requirements laid out in Regulation (EU) No. 549/2013 of the European Parliament and of the Council of 21 May 2013 on the European system of national and regional accounts in the European Union.

Latvijas Banka's "Regulation for Compiling Interest Rate Reports of Monetary Financial Institutions" was also approved, thus implementing the requirements of Regulation (EU) No. 1072/2013 of the European Central Bank of 24 September 2013 concerning statistics on interest rates applied by monetary financial institutions (ECB/2013/34).

Latvijas Banka's "Regulation for Compiling 'Credit Institution and Electronic Money Institution Payment Statistics Report' " was approved in order to transpose Regulation (EU) No. 1409/2013 of the European Central Bank of 28 November 2013 on payments statistics (ECB/2013/43). In 2014, Latvijas Banka also ensured the implementation of the requirements of Regulation (EU) No. 1073/2013 of the European Central Bank of 18 October 2013 concerning statistics on the assets and liabilities of investment funds (ECB/2013/38) and the Guideline of the European Central Bank of 4 April 2014 on monetary and financial statistics (ECB/2014/15) (EU 2014/810).

Following the ECB's request, issues pertaining to the method of cash management employed by credit institutions upon cash pooling were dealt with, as well as comments and proposals were provided in respect of drafting the ECB regulation on money market statistics. Latvijas Banka participated in the ECB cost exercise evaluating set-up and regular costs which would be incurred upon reporting the credit institution lending data required for the Analytical Credit Dataset (AnaCredit), the ECB project aimed at establishing a central credit register.

BALANCE OF PAYMENTS STATISTICS

In 2014, the compilation and publishing of balance of payments statistics in compliance with the new requirements of the ECB, Eurostat and IMF was commenced, thus providing for the compilation of balance of payments statistics consistently with the requirements of the Sixth Edition of the IMF's Balance of Payments and International Investment Position Manual (BPM6). A number of significant reclassifications were made to the current account of balance of payments, financial account and international investment position. Along with the introduction of the new methodology for compiling balance of payments statistics, statistical data are reported to international organisations in accordance with SDMX/ML 2.0 format, applying a uniform approach to the data coding.

To ease the reporting burden of respondents, Latvijas Banka's "Regulation for Compiling Reports on Securities" was amended, stipulating a smaller amount of data to be reported on securities issue and providing better opportunities for the use of the ECB's Centralised Securities Database information. The ECB information requirements have been implemented in the securities holders' statistics, and data reporting to the ECB has commenced.

GENERAL ECONOMIC AND GOVERNMENT FINANCE STATISTICS

The primary tasks in the area of general economic and government finance statistics were as follows: the reporting of quarterly financial account statistics in accordance with the ECB requirements set for the euro area countries, implementing the requirements for the compilation of quarterly financial accounts and government finance statistics stipulated by two ECB Guidelines which took effect on 1 September 2014, and transition to the new data reporting format SDMX/ML 2.0.

Comprehensive data revisions were carried out in the field of quarterly financial account statistics in order to comply with the reporting requirement set by the ECB for the euro area countries – to report the data starting from the year the relevant country had joined the EU. The revised data for the time period from the first quarter of 2004 to the first quarter of 2014 were transmitted to the ECB in July 2014 and published on the website of Latvijas Banka.

A step by step introduction of the Guideline of the European Central Bank of 25 July 2013 on the statistical reporting requirements of the ECB in the field of quarterly financial accounts (recast) (ECB/2013/24) continued in 2014. The Guideline stipulates a new breakdown by sector and instrument in line with the requirements of ESA 2010 and shortening of the reporting period to the 85th calendar day following the end of the reference quarter. In September 2014, the data for the time period from the fourth quarter of 2012 to the second quarter of 2014 were released and information on the website of Latvijas Banka amended respectively. In addition, data on deposits, securities and loans by counterparty sectors and data on other changes have been published. The revision of data on quarterly financial account statistics continued until December 2014 when the revised data on quarterly financial accounts for the time period from the first quarter of 2004 to the third quarter of 2012 and the data for the third quarter of 2014 were transmitted to the ECB and published on the website of Latvijas Banka. Hence the introduction of the above Guideline was successfully completed in Latvia and all data on quarterly financial accounts are available to the users in accordance with the new requirements for the compilation of quarterly financial accounts.

Pursuant to the requirements of the Guideline of the European Central Bank of 3 June 2014 amending Guideline ECB/2013/23 on government finance statistics (ECB/2014/21), stipulating primarily the changes in the framework of the general government sector and accounting of the accruals in the second tier pension fund and results of derivative financial instruments in line with ESA 2010, Latvijas Banka revised the historical time series of the general government finance statistics and transmitted the data consistent with the new requirements to the ECB in October 2014.

PROVIDING FINANCIAL SERVICES TO THE GOVERNMENT

Latvijas Banka ensured the management of the Treasury's current accounts opened with Latvijas Banka subject to the requirements of the Law on Latvijas Banka. The Treasury also participated in the payment systems of Latvijas Banka in the capacity of a direct participant.

In 2014, the Treasury had settlement accounts in euro and seven foreign currencies with Latvijas Banka. Over the year, Latvijas Banka settled 1.3 thousand payments of the Treasury in euro and foreign currencies totalling 28.0 billion euro.

ADVISORY ACTIVITIES AND INFORMATION TO THE PUBLIC

ADVISORY SERVICES TO THE GOVERNMENT AND OTHER INSTITUTIONS

One of the tasks of Latvijas Banka is to advise the Saeima and the Cabinet of Ministers of the Republic of Latvia on monetary policy and other issues related to the performance of tasks of Latvijas Banka.

The Governor of Latvijas Banka, other officials of Latvijas Banka and its employees held regular meetings with representatives of the Republic of Latvia government, including participation in meetings of the Cabinet of Ministers and in the work of different committees established both by the Republic of Latvia ministries and pursuant to the Prime Minister's Order.

Employees of Latvijas Banka contributed to promotion of Latvia's economic development by participating in different working groups and professional organisations, sharing experience and providing advice to them.

Employees of Latvijas Banka in their capacity as experts participated in the work of the EU funds Monitoring Committee and Temporary Monitoring Committee; they provided advice on the EU programming periods 2007–2013 and 2014–2020 during committee meetings and working group meetings of subcommittees.

Until the complete closure of the euro changeover project on 30 June 2014, representatives of Latvijas Banka took part in regular monitoring of activities implemented by working groups of the Steering Committee, including regular reporting to the Euro Changeover Coordination Council and the Cabinet of Ministers on the work accomplished in relation to all euro changeover processes in the country. A document "Benefit Management in the Follow-up Stage of the National Euro Changeover Project" was also developed.

Employees of Latvijas Banka were engaged in the work of the Public Awareness and Communication Working Group established within the Euro Changeover Project and active until 30 June 2014. In January–March the population was actively informed on the process of the euro changeover via the media and other channels, followed by aggregation of results and their dissemination to stakeholders in the second quarter. Representatives of Latvijas Banka prepared materials for the media and participated in press conferences on the euro changeover (the introduction of cash, analysis of price changes). Within the scope of their competence, they took part in the development of material on the benefits to the economy and population provided by the introduction of the euro. Latvijas Banka, by means of its website, social networks, etc., continues to inform the public that the period for exchanging the lats cash to the euro is unlimited.

Representatives of Latvijas Banka provided advice on fiscal discipline issues, the assessment of fiscal risks and the potential GDP estimation necessary for the purpose of drawing up the Fiscal Discipline Compliance Report on the draft state budget for 2015 and draft budget frameworks for 2016 and 2017. It was done through the participation in the Ministry of Finance working group on the development of the draft Fiscal Discipline Law.

In July 2014, Latvijas Banka in cooperation with other participants of the SEPA project closed the SEPA implementation project in Latvia. Latvijas Banka engaged in the SEPA Project by chairing the National SEPA Working Group (NSWG), which finalised it work in 2014. The NSWG ensured the introduction of SEPA credit transfers in Latvia as of 1 January 2014, as well as assigned and maintained the SEPA creditor identifiers in the Register of Enterprises of the Republic of Latvia. The NSWG coordinated discussions of market operators on the most effective solution for the replacement of the national direct debit payments. In July 2014, market operators agreed that the national direct debit payments would not be transformed into SEPA direct debit payments, but instead they would be replaced by e-invoicing and SEPA credit transfers by 1 January 2015.

A representative of Latvijas Banka took part in consultations of European institutions on SEPA issues and in drawing up recommendations of the European Forum on the Security of Payments. Experts of Latvijas Banka engaged in discussions of market operators and in drafting Latvia's positions on recommendations in relation to the revised Directive on payment services and the Regulation on interbank fees.

Representatives of Latvijas Banka participated in the work of the committee established by the Investment and Development Agency of Latvia for assessing high value-added investment project applications and in the assessment of the enterprises that had applied for winning the Export and Innovation Award.

Employees of Latvijas Banka in their capacity as experts continued to participate in the work of the Working Group for the Preparation of the Notification of General Government Deficit and Debt chaired by the CSB. The working group compiled data with regard to the notification of general government deficit and debt for 2013 and addressed the related methodological issues. In line with the ESA 2010 requirements stipulating changes in the government sector framework, in making contributions to the 2nd tier of the pension scheme and in accounting of gains/losses from derivative financial instruments, historical time series of the government finance statistics were revised and made public in autumn 2014.

Experts of Latvijas Banka took an active part in the process of accession of the Republic of Latvia to the OECD. They provided support to the government by engaging in the Working Group for Negotiations on the Accession of the Republic of Latvia to the OECD and by explaining Latvia's standpoint in negotiations with several OECD committees throughout their report drafting process. With the assistance of Latvijas Banka's experts, data obtained from the Survey of Implementation of Methodological Standards for Direct Investment (SIMSDI) on the methodology used to compile data on foreign direct investment and data on foreign direct investment were submitted to the OECD. Latvia was represented at the examination of the methodology for the compilation of data on foreign direct investment. Information on Latvia's macroeconomic and financial market development, on the methodology used to compile data on the quarterly financial account, interest rates, balance of payments and imports and exports of services, as well as the respective data were provided to OECD committees. The subsequent procedure for transmission of regular data was also coordinated.

Experts of Latvijas Banka were actively engaged in the work of the Working Group for Improving Cooperation with International Rating Agencies, in drafting a report on Latvia's credit rating and the factors impacting it. They provided proposals for the enhancement of cooperation with international rating agencies and ensured information exchange for the purpose of hosting regular visits of agency representatives.

OPERATION OF THE VISITORS CENTRE

The Visitors Centre of Latvijas Banka "Money World" offering a modern exposition for obtaining financial education and information had 6 400 visitors in 2014.

Secondary school seniors and university students majoring in social sciences are the primary target audience of the Visitors Centre: this group, as previously, accounted for approximately 80% of total attendance. The overwhelming presence of youth among the visitors is of importance also because the information communicated by the Visitors Centre helps them master educational programmes; likewise, dialogue arouses interest in macroeconomic and financial topics also stirring up discussions by public at large.

Topics about the euro changeover in Latvia, financial stability in the euro area and its maintenance, changes in the role and functions of Latvijas Banka, the general government debt and financial discipline as well as recovery of the economic competitiveness were among the most discussed in 2014. The exposition was rearranged so that stands, films, multi-media programmes and other visual aids would basically tell the story of the EMU, the tasks and activities of the Eurosystem and the euro circulation. In addition to information communicated to other target audiences by other means, Latvijas Banka presented the design and security features of euro banknotes and coins to groups of visitors, using a wide range of visual aids and stressing the need to know their money to prevent dissemination of counterfeits.

INFORMATION AND EDUCATIONAL FACILITIES PROVIDED TO THE PUBLIC

The euro changeover which had a significant impact on Latvia's economy and population made the year 2014 special in terms of Latvijas Banka's communication with the general public.

At the beginning of the year, practical euro changeover issues – exchange of the lats to the euro, alignment of the payment system, design and security features of euro banknotes and coins promoted the strongest public interest and Latvijas Banka's communication, while Latvia's participation in the formulation of the Eurosystem's monetary policy and Latvijas Banka's expert role in analysis of the euro area economic developments gradually became increasingly topical. Latvia's economic development was influenced by the ECB Governing Council's decision on cutting the key interest rates to historic lows, resolutions on the use of new monetary policy instruments and discussion about further activities to ensure price stability by keeping annual inflation rates close to 2% over the medium term. Latvijas Banka also continued active communication with the general public about other issues important for the economic development and the progress on fulfilling the tasks of Latvijas Banka.

Taking into account the diverse and extensive use of communication channels, a significant part of the general public (81%; TNS Latvia Ltd. data) felt well informed about the appearance of euro banknotes and coins just before the euro changeover, while the largest part of the general public (68%) felt informed about the security features of euro banknotes and coins in January 2014.

Public perception and sentiment are important factors for achieving future economic growth, and they are largely dependent on the understanding of macroeconomic processes and decisions. This is why communicating the macroeconomic and financial developments to the general public and to specific target groups is one of the key communication areas for Latvijas Banka.

Latvijas Banka continued to prepare a wide range of regular publications. Incorporating the data provided by Latvijas Banka, CSB, Ministry of Finance, FCMC and other institutions, the Macroeconomic Developments Report discussed the developments of external sector, financial market, domestic demand and supply, costs and prices, and balance of payments, and presented economic growth and inflation forecasts. The publication Financial Stability Report assessed major financial stability risks.

Six working papers by the experts of Latvijas Banka (incl. in cooperation with the experts of the ESCB) were published on the websites of Latvijas Banka in 2014. Economists of Latvijas Banka also published three working papers in international peer-reviewed journals in economics. 34 analytical articles on different economic topics and regular monthly or quarterly commentaries on Latvia's key macroeconomic indicators were published on Latvijas Banka's website dedicated to the economic analysis (www.makroekonomika.lv). The economists of Latvijas Banka presented their views about economic developments in 33 blog entries published on the website.

In the survey of economic experts conducted in early summer of 2014, 68% of the respondents assessed Latvijas Banka's communication on economic topics as sufficient.

In 2014, a competition for students' research papers was organised already for the 12th time with a view to promoting interest about researching topical macroeconomical subjects. Overall, 24 papers were submitted, and the authors of them were 31 students from eight Latvia's higher educational establishments. Prizes were awarded to five papers submitted by students from different Latvia's higher educational establishments.

In 2014, a practice of organising press conferences of the Governor of Latvijas Banka on a quarterly basis was launched with the aim to inform the public about the economic development of the euro area and Latvia, fiscal discipline and lending developments as well as the decisions made by the Council of Latvijas Banka and the Governing Council of the ECB.

Economists of Latvijas Banka published their commentaries on the decisions taken at the meetings of the Governing Council of the ECB and the development of the euro area economy and financial markets on a regular basis on the website at www.bank.lv to familiarise the general public with the operation of the Eurosystem and the monetary policy purposes and instruments.

Latvijas Banka continued active communication, publishing more than 50 press releases and answering more than 400 journalists' questions in 2014. Overall, throughout the year more than 10 000 publications on issues concerning the activities of Latvijas Banka and the macroeconomic and financial analysis appeared in different mass media. To communicate with the general public via social media channels, Latvijas Banka used social networks (Twitter, YouTube, Slideshare and Flickr).

As the euro area addressed important complex tasks and the role of the fiscal policy and structural reforms strengthened, Latvijas Banka held its annual conference "Have we learnt anything from the crisis?" on 17 October. The conference brought together very prominent officials and scientists. Jens Weidmann, Member of the Governing Council of the ECB, President of Deutsche Bundesbank, Benoît Cœuré, Member of the Executive Board of the ECB, the officials of international and national economic policy institutions (IMF, EC and the German government) and high-level academicians also participated in it. In the conference speeches and panel discussions answers were sought to the questions as to what lessons have been learnt from the economic crisis of 2008 in some distressed countries and the euro area on the whole and what measures are to be taken to ensure sustainable economic growth. The conference brought together European and national policy makers, economists, opinion leaders, businesses, representatives of academia and Latvian and global mass media.

The tradition of organising experts' roundtable discussions was restarted in 2014. Experts of Latvijas Banka, businesses and representatives of academia and the financial sector debated about several issues relevant for the Latvian economy. Both the conference and experts' roundtable discussions were webcast and subsequently posted on the website www.makroekonomika.lv.

With Latvia joining the euro area and people starting to use the euro in their daily settlements, Latvijas Banka actively informed the general public about the design and security features of euro banknotes and coins as well as the introduction of the second series – Europa series – 10 euro banknote in 2014. To provide more comprehensive information about the new banknote to the general public and professional cash handlers, printed information leaflets on the design and security features of the new banknote, in cooperation with the ECB, were sent to different population and business groups in summer and autumn. As previously, special materials and a training programme were prepared and, in cooperation with the Latvian Society of the Blind, delivered to the visually impaired. Latvijas Banka presented the security features of the new 10 euro banknote to the population, demonstrating informative video material on the national TV channels, thus addressing a vast audience (the level of awareness on the design and security features of the new banknote in Latvia – 91%).

In spring of 2013, the interactive exhibition dedicated to money design and held in Riga offered an insight into the work done in the field of Latvia's coin design to the public in Latvia. The exhibition was supplemented and updated with euro collector coins and, renewed and renamed "Money Design. PIN Code", travelled to Ventspils Museum in summer of 2014 so that a wider range of Latvian people could familiarise themselves with the money design. The exhibition was seen by more than 19 000 visitors there, and it was displayed also at the Embassy of Latgale GORS in Rēzekne from 18 November 2014 to 15 February 2015 (26 400 visitors).

To familiarise the general public with the operation of the interbank payment system, Latvijas Banka held a press conference on the development trends of non-cash settlements, payment instruments and interbank payment systems in April 2014.

To improve the financial and economic literacy of different population groups, Latvijas Banka in a partnership engaged in the development of the "Strategy for Financial Literacy of Latvian Population 2014–2020" and maintained the financial and economic literacy website "Money School". In March, Latvijas Banka together with other participants involved in the implementation of the above strategy organised the second Financial Literacy Week in Latvia and educational seminars for different subject teachers from schools in regions of Riga, Tukums and Cēsis. In autumn 2014, teachers from regions of Latvia were informed through seminars about changes in the functions and monetary policy of Latvijas Banka after the introduction of the euro in Latvia. Latvijas Banka continued its cooperation with Junior Achievement – Young Enterprise Latvija for the second year, organising the final of the competition for primary school students "My Dictionary" and thus facilitating their ability to discuss economic issues with the representatives of different generations. Within the framework of the Museum Night, Latvijas Banka participated in the event "My Way. Latvia" to tell about the way of safe and quality cash from production to consumers.

In the autumn semester of the academic year 2014/2015, experts of Latvijas Banka visited Latvia's higher educational establishments in Riga and regions and delivered 28 lectures on the challenges for the global economy and the global economic prospects, purposes of the euro area monetary policy, economic governance, fiscal discipline and crisis management instruments of the EU and the euro area countries, concept of competitiveness in modern economic theories, payment instruments and systems across the globe and in Latvia. 89% of more than 700 participants in the lecture cycle generally estimated them as good and very useful. At the same time, 90% of the lecture participants stated that they would like to attend the educational guest lectures on economic and financial topics delivered by the experts of Latvijas Banka also in the future.

COOPERATION WITH INTERNATIONAL ORGANISATIONS AND FOREIGN CENTRAL BANKS

Latvijas Banka is the representative of the Republic of Latvia in foreign central banks and international financial institutions. Latvijas Banka may participate in operations of other international financial and credit organisations consistent with its objectives and tasks.

In 2014, Latvijas Banka continued to represent Latvia's interests at meetings of the IMF Board of Governors and in the coordination of operational issues. Priorities of the IMF policy were mainly related to strengthening the global economic and financial system, with a particular emphasis placed on the need for the structural reforms. It was decided that the oversight carried out by the IMF would focus more on analysing risks and risk dissemination channels, while the assessment of the financial sector stability – on the systemic risk analysis. The IMF assessed its precautionary financial instruments, the framework for sovereign debt restructuring and collective action clauses included in sovereign bonds. The implementation of the 2010 IMF quota and governance reform and the next general review of quotas still remained topical issues.

Latvia's interests in the IMF were represented in the Nordic-Baltic Constituency that includes Denmark, Estonia, Finland, Iceland, Latvia, Lithuania, Norway and Sweden. One Executive Director represented this constituency on the IMF Executive Board, with a total of 3.41% votes.

Representatives of Latvijas Banka continued to participate in the work of the Nordic-Baltic Monetary and Financial Committee established for setting strategic directions and laying down guidelines and developing a joint opinion on operational issues of the IMF.

In 2014, cooperation with the IMF, based on consultations under Article IV of the IMF Articles of Agreement, continued. In May, the IMF Executive Board reviewed the IMF Staff Report on Latvia's macroeconomic situation and financial sector development, and the implemented economic policy, as well as the regional report on the economic development of the Baltic States.

In 2014, Latvijas Banka continued its membership in the BIS.

Latvijas Banka pursued its cooperation with the central banks of other countries, sharing expertise and information. Latvijas Banka organised several international meetings and seminars.

ESCB training workshops to improve skills to chair meetings and managers' skills took place in May and October, while an ESCB and SSM training workshop to improve presentation and effective communication skills was held in November. In June, Latvijas Banka organised an external meeting of the ESCB's Accounting and Monetary Income Committee and in cooperation with the US National Bureau of Economic Research – a seminar on the latest macroeconomic developments. In July, an external meeting of the Payment and Settlement Systems Committee of the ESCB took place in Riga. In October, Latvijas Banka organised the international economic conference during which Latvian and EU economic policy-makers and economists discussed the lessons gained from the economic crisis in some EU countries and the euro area and the measures to be taken to ensure sustainable economic growth. In November, the meeting of the ESCB informal group of network of museums took place in Riga, while the meeting of experts of the national central banks on the financial and monetary statistics issues was organised in December.

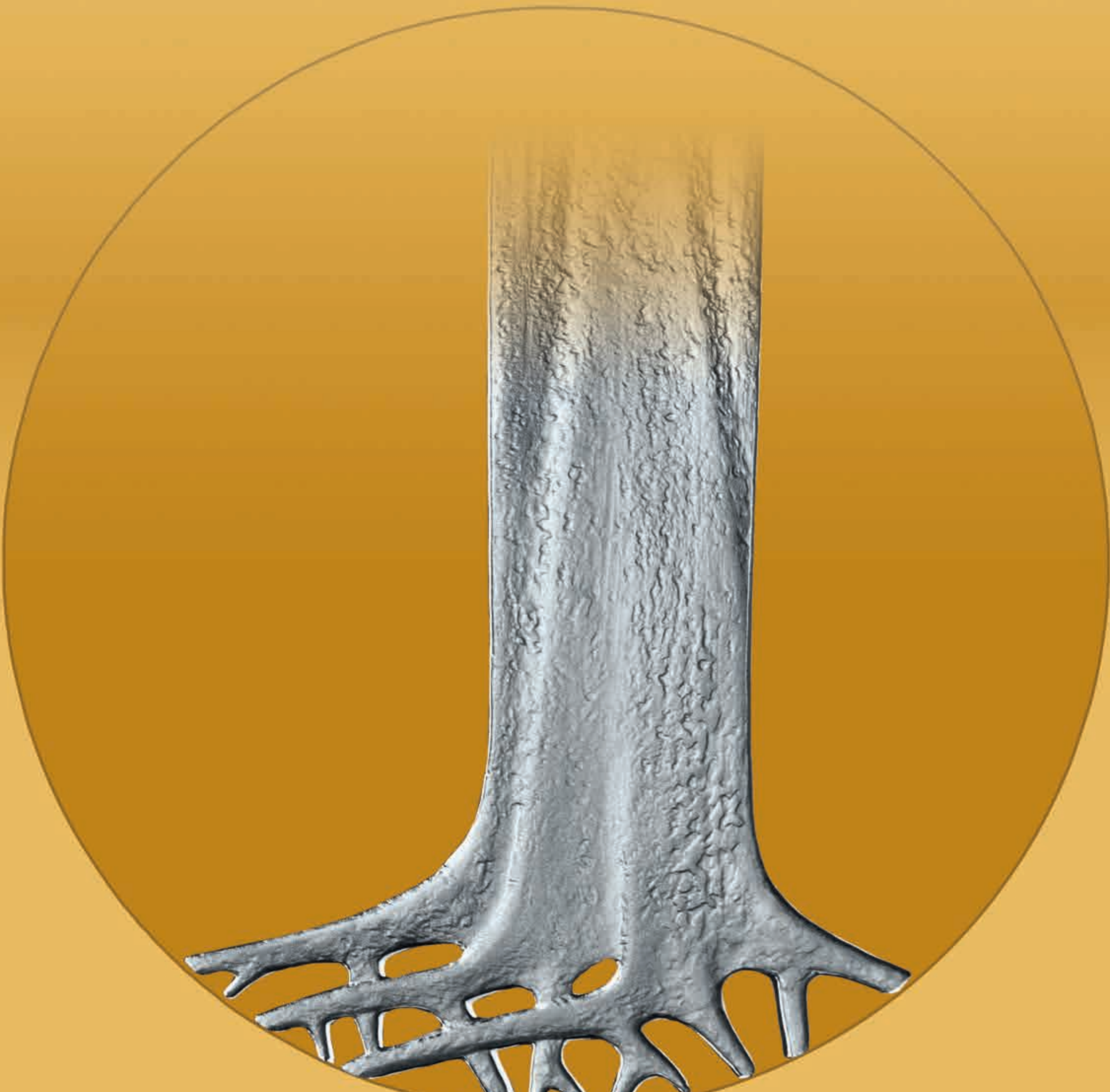
In 2014, experts of Latvijas Banka shared their expertise regarding the introduction of the euro with specialists of the Lithuanian institutions.

In 2014, international financial organisations and foreign central banks extended support to Latvijas Banka, providing opportunities to participate in the workshops and courses hosted by these institutions, as well as to receive consultations on issues related to the central bank operations. Employees of Latvijas Banka participated in courses, seminars and professional experience exchange programmes organised by the ECB, IMF, Joint Vienna Institute, Study Center Gerzensee, Federal Reserve Bank of New York, as well as by the central banks of Austria, Belgium, Canada, Finland, France, Germany, Hungary, Italy, Lithuania, the Netherlands, Norway, Slovenia and the UK.

Latvijas Banka participated in the process of negotiations over the accession of the Republic of Latvia to the OECD, representing Latvia's interests in the OECD committees, and provided the necessary statistical data.

Representatives of Latvijas Banka took part in the Nordstat meeting held by the central banks and central statistical authorities of the Nordic countries and the Baltic States in Lithuania during which they acquainted representatives of other countries with practice of Latvijas Banka with regard to the use of the data of insurance corporations in different statistical areas and exchanged information on the progress in introducing Regulation (EU) No 1374/2014 of the European Central Bank of 28 November 2014 on statistical reporting requirements for insurance corporations (ECB/2014/50). Latvijas Banka also organised the meeting for the permanent expert group on financial and monetary statistics of the central banks of Austria, Finland, Slovakia and Latvia.

MANAGEMENT AND ORGANISATION OF LATVIJAS BANKA



ORGANISATIONAL STRUCTURE OF LATVIJAS BANKA

THE COUNCIL OF LATVIJAS BANKA

The Council of Latvijas Banka takes decisions on behalf of Latvijas Banka. The Council of Latvijas Banka comprises: the Governor, Deputy Governor and six members (one position of the Member of the Council of Latvijas Banka has been vacant from 13 March 2014). Their term of office is six years. At the end of 2014, the composition of the Council of Latvijas Banka was as follows:

– Governor	**Ilmārs Rimšēvičs**;
– Deputy Governor	**Zoja Razmusa**;
– Members of the Council:	**Leonīds Gricenko**, **Edvards Kušners**, **Vita Pilsuma**, **Arvils Sautiņš**, **Aivars Skopiņš**.

On 13 February 2014, the term in office of Andris Ruselis, the Deputy Governor of Latvijas Banka, expired. On 13 March 2014, the Saeima of the Republic of Latvia appointed Zoja Razmusa, Member of the Council of Latvijas Banka, to the position of the Deputy Governor.

Meetings of the Council of Latvijas Banka are held as appropriate, but at least once a quarter. The Council of Latvijas Banka held twelve meetings in 2014. When performing the tasks stipulated in the Law on Latvijas Banka, the Council of Latvijas Banka adopted 121 legal acts overall in 2014 regarding the use of monetary policy instruments, investment management, provision of currency in circulation, the operation and oversight of the payment and securities settlement systems, operation of the Credit Register, provision of statistics, licensing and supervising the purchase and sales of cash foreign currency and other issues pertaining to the operation, management and organisation of Latvijas Banka.

THE BOARD OF LATVIJAS BANKA

To carry out and manage day-to-day activities of Latvijas Banka, the Council of Latvijas Banka has established the Board of Latvijas Banka that comprises six members and performs activities on a continuous basis. Changes in the composition of the Board of Latvijas Banka were effected, based on the Council of Latvijas Banka's Resolution No. 223/19 of 16 May 2014. On 1 June 2014, Reinis Jakovļevs, the Deputy Chairman of the Board of Latvijas Banka, and Andris Ņikitins, a Member of the Board of Latvijas Banka, discontinued their work in the Board. Ilze Posuma, a former Member of the Board of Latvijas Banka, Head of Legal Department, was appointed the Deputy Chairperson of the Board of Latvijas Banka, and Jānis Caune, Head of Accounting Department and Chief Accountant of Latvijas Banka, and Jānis Blūms, Head of Cash Department, were appointed Members of the Board of Latvijas Banka. The composition of the Board of Latvijas Banka, as at the end of 2014, was as follows:

– Chairman of the Board	**Māris Kālis**;
– Chairperson of the Board:	**Ilze Posuma**;
– Members of the Board:	**Jānis Blūms**, **Jānis Caune**, **Harijs Ozols**, **Raivo Vanags**.

The Board of Latvijas Banka conducted daily activities of Latvijas Banka in compliance with the requirements of the Law on Latvijas Banka and other legal acts, as well as by implementing decisions of the Council of Latvijas Banka.

EMPLOYEES OF LATVIJAS BANKA

At the end of 2014, the number of Latvijas Banka employees was 540, of which 16 had fixed-term employment contracts (573 and 25 employees at the end of 2013, respectively). At the end of 2014, the staff of Latvijas Banka was 56% male and 44% female.

To ensure exchange of information between Latvijas Banka and EU institutions, the Counsellor of Latvijas Banka at the Permanent Representation of Latvia to the EU continued her work in 2014.

Structural improvements continued at Latvijas Banka in 2014. To provide for effective execution of payments and settlements and improve Latvijas Banka's customer service, the Payment and Settlement Division was established in the Payment Systems Department at the end of 2014 by merging those divisions of the Market Operations Department and the Payment Systems Department which ensured discharge of the related functions.

To implement the functions of monetary policy and financial stability safeguarding successfully and prevent the potential conflict of interest that might arise in pursuit of different objectives (price stability and financial system's stability) of the functions, the function of financial stability has been separated from the functions of the Monetary Policy Department since 1 June, and the Financial Stability Department has been established.

The Daugavpils Branch was closed in 2014 due to changes introduced in the operational organisation of credit institutions operating in Latvia.

COMMISSIONS, COMMITTEES AND WORKING GROUPS OF LATVIJAS BANKA

In order to ensure successful and secure performance of tasks of Latvijas Banka, several committees, commissions and working groups approved by the Council of Latvijas Banka, the Governor of Latvijas Banka or the Board of Latvijas Banka carried on their work in 2014.

The Audit Committee of Latvijas Banka, authorised by the Council of Latvijas Banka, was responsible for oversight of the internal auditing function, activities of external auditors of Latvijas Banka and preparation of financial statements, as well as for facilitating the functioning of the internal control system of Latvijas Banka. A wide range of issues related to security were addressed by the Security Oversight Commission of Latvijas Banka. The Information Systems Management Committee of Latvijas Banka monitored and coordinated the issues related to operation, security and development of Latvijas Banka information systems, as well as personal data processing. The Operational Risk Management Committee of Latvijas Banka monitored the operational risk management at Latvijas Banka.

COMMITTEES AND COMMISSIONS OF LATVIJAS BANKA AT THE END OF 2014

The Audit Committee of Latvijas Banka	The Information Systems Management Committee of Latvijas Banka
The Budget Commission of Latvijas Banka	The Investment Committee of Latvijas Banka
The Coin Design Commission of Latvijas Banka	The Licensing Committee of Latvijas Banka
The Commission for Examination of Banknotes and Coins and for Controlling Cash Processing of Latvijas Banka	The Operational Risk Management Committee of Latvijas Banka
The Document and Archives Management Expert Commission of Latvijas Banka	The Security Oversight Commission of Latvijas Banka
The Ethics Committee of Latvijas Banka	The Standing Commission for Procurement of Latvijas Banka

The Commission for Examination of Banknotes and Coins and for Controlling Cash Processing of Latvijas Banka examined banknotes and coins of both lats and euro, identifying the counterfeits of banknotes as well as establishing the procedure for identifying the damaged banknotes as legal tender and replacing the damaged banknotes with valid ones, and provided for testing cash processing equipment of merchants releasing the euro in secondary circulation, ensuring inspection of cash processing equipment to decrease the potential risk of euro counterfeits in cash circulation. The Coin Destruction Commission of Latvijas Banka providing for decoining of the lats coins unnecessary for circulation and organising transportation of the demonetised coins for remelting terminated its activity due to the fulfilment of the assigned task on 18 December 2014. To ensure fulfilment of the requirements specified for purchasing and selling cash foreign currency as a financial service, the Licensing Committee of Latvijas Banka issued licences for purchasing and selling cash foreign currency to capital companies as a commercial activity and controlled operation of the licensed capital companies.

The Budget Commission of Latvijas Banka, whose aim is to facilitate proper utilisation of financial resources of Latvijas Banka, contributed to the operational management of Latvijas Banka. The Standing Commission for Procurement of Latvijas Banka achieved this objective in the area of procurements organised by Latvijas Banka.

The Investment Committee of Latvijas Banka developed and defined a strategy for and an approach to financial assets and gold in accordance with the Regulation for the Investment Committee of Latvijas Banka. The Document and Archives Management Expert Commission of Latvijas Banka, whose objective is to examine the value of documents, prepare the document nomenclature, establish time limits for document storage and address other issues related to the document management, ensured fulfilment of the requirements of "The Procedure for the Document Management at Latvijas Banka" and the Law on Archives within the context of archive activities of Latvijas Banka. The

Ethics Committee of Latvijas Banka monitored the implementation of the "Code of Conduct of Latvijas Banka".

MANAGEMENT PRINCIPLES AND DEVELOPMENT

Excellent implementation of the tasks stipulated in the Law on Latvijas Banka has to be ensured for the management of Latvijas Banka on a sustainable basis. The "Plan-Do-Check-Act" cycle, which also serves as the basis for the Common Assessment Framework used by Latvijas Banka for streamlining its managerial processes, has been used for the management of Latvijas Banka. It enables detection of gaps in the areas of strategies, resources, staff and processes management and leadership, as well as provides an opportunity to measure the results achieved vis-à-vis customers, employees and the general public.

"The Vision, Mission and Values Statement of Latvijas Banka" forms the basis for the operation and development planning. The strategic goals revised in 2013 were taken into account during its operation in 2014. Three areas Latvijas Banka attaches high importance to were identified, i.e. ensuring quality implementation of the core tasks to facilitate the achievement of the Eurosystem objectives, strengthening links with the general public, developing professional competence and improving performance.

Every year, the progress towards achieving the set objectives is measured. The execution of functions and processes is monitored daily, implementation of work plans is reviewed biannually and customer satisfaction surveys are conducted biennially asking customers to assess the quality of Latvijas Banka's services, the level of their accessibility and convenience, competence and responsiveness of the staff.

The customer satisfaction survey of 2014 shows that the rating of the performance of the core functions is high (4.57 points out of 5), and the employee survey of 2014 demonstrates that the rating of the quality of the implementation of support functions is also high (4.58 points out of 5).

RESOURCE MANAGEMENT

HUMAN RESOURCES

In 2014, Latvijas Banka continued to pursue its key principles of human resources policy by hiring well-qualified and professional employees as a result of an effective staff recruitment process and established long-term employment relationships, creating a motivating working environment and enhancing professional development opportunities.

Similarly to the practice of the previous years, Latvijas Banka used internal and external staff rotation to promote personnel development and career. Within the framework of the internal rotation programme, six employees were promoted to another structural unit of Latvijas Banka, and 19 employees were promoted within the same structural unit in 2014. Within a short-term ECB secondment programme one staff member went to the ECB to complement his work experience in the Directorate General Economics of the ECB, but one employee continued his work in the IMF.

Staff of Latvijas Banka continued to broaden their expertise in the fields of monetary policy, financial stability, macroeconomics, econometrics, financial markets, statistics, financial accounting, internal audit, human resources management, translation, law, risk management and information technologies. Several employees of Latvijas Banka further develop their professional knowledge by participating in international professional certification programmes.

Latvijas Banka's staff training costs amounted to 1.4% of the total expenses on remuneration (1.7% in 2013).

FINANCIAL RESOURCES

The financial management system of Latvijas Banka has been developed in a way that it ensures support to decision making, financial risk management and efficient use of financial resources.

Latvijas Banka primarily finances its operation out of the income generated from investment management. Latvijas Banka does not receive financing from the state budget. Instead, it transfers 65% of the profit made during the reporting year to the state budget. In 2014, Latvijas Banka's profit earned was 36.8 million euro; of that, 23.9 million euro are to be transferred to the state budget. Latvijas Banka has contributed to the state budget a total of 190.2 million euro from its profit earned between 2009 and 2013.

Major financial transactions of Latvijas Banka are related to the management of financial assets and implementation of monetary policy. Financial assets are managed in compliance with the basic principles set out in the "Guidelines for Managing Financial Assets and Gold of Latvijas Banka" adopted by the Council of Latvijas Banka. They include preserving the value of investments, ensuring their liquidity and earning income within the framework of acceptable risk standards without contradicting the monetary policy implemented by the Eurosystem. Meanwhile, operations related to the implementation of monetary policy are performed by Latvijas Banka in line with the "Procedure for Participation in the Eurosystem Monetary Policy Operations Organised by Latvijas Banka" adopted by the Council of Latvijas Banka.

In order to ensure comprehensive and transparent information about financial transactions, financial risks and their management, as well as about performance results of Latvijas Banka, it prepares and publishes annual financial statements. They are drafted in accordance with the mandatory requirements of the ECB legal framework for accounting and financial reporting binding on the ESCB and in line with the "Financial Accounting Policy of Latvijas Banka", adopted by the Council of Latvijas Banka, by organising accounting in compliance with the "Financial Accounting Regulation of Latvijas Banka", adopted by the Board of Latvijas Banka, and other regulations of Latvijas Banka pursuant to the Law on Latvijas Banka and requirements of other laws and regulations of the Republic of Latvia binding on Latvijas Banka.

Latvijas Banka publishes a monthly closing balance sheet and Notes to it, as well as other financial information available also on the website of Latvijas Banka. Latvijas Banka's integrated information system ensures a standardised, automated, safe and efficient execution of financial transactions of Latvijas Banka, their uniform accounting and drawing up of financial statements. Within the framework of the internal financial control system, the management of Latvijas Banka regularly assesses changes in assets and liabilities, as well as in income and expenses of Latvijas Banka, paying particular attention both to the results of investment management and compliance of operating costs and long-term investments with the approved budget of Latvijas Banka. The Council of Latvijas Banka approves the annual budget of Latvijas Banka; the management of the budget is carried out according to the "Regulation for Managing the Budget of Latvijas Banka" adopted by the Council of Latvijas Banka and aimed at ensuring efficient use of Latvijas Banka's financial resources. The Regulation provides for the procedure of drafting, approving and monitoring the execution of Latvijas Banka's budget. Within the budget management framework, Latvijas Banka assesses the effectiveness, costs and human resources of each project on a continuous basis in order to ensure efficient use of funds. To assure the independence of internal audit, the Council of Latvijas Banka also approves an expenditure plan for the Internal Audit Department.

The Council of Latvijas Banka has set up a Budget Commission, which comprised five members of the Council of Latvijas Banka in 2014. The main tasks of the Budget

Commission of Latvijas Banka are evaluation of a draft budget prepared by the Board of Latvijas Banka and monitoring of budget execution. In turn, the key tasks of the Board of Latvijas Banka vis-à-vis the budgetary management are to draw up a draft budget together with the heads of the relevant structural units of Latvijas Banka and submit it to the Budget Commission and the Council of Latvijas Banka, as well as to report on budget execution on a regular basis.

INFRASTRUCTURE RESOURCES

Engineering and technical infrastructure resources

Latvijas Banka provides and maintains the infrastructure necessary for its operation in good condition. To ensure the compliance of the constructive solution, including thermal insulation, of the building's roof and roof floor covering with requirements of construction standards, as well as to improve the roof constructive protection from penetration of moisture into the building, a technical project for thermal insulation of the roof of Latvijas Banka's building at K. Valdemāra iela 2A, Riga, was developed in 2014. The implementation of this project will improve energy efficiency of the building.

To ensure renovation of the engineering communications located under the surface of the yard of Latvijas Banka's building at K. Valdemāra iela 2A, Riga, a technical project was developed in 2014. It comprises replacement of certain sections of the water supply and sewerage systems, laying down a new power cable intended for electricity supply of the ventilation system equipment and replacement of the surface of the yard following the renovation of the engineering communications.

Works necessary for maintenance of buildings were carried out in the buildings of Latvijas Banka's branches and in the building of the Training Centre.

Resources of information technologies

Within the framework of ESCB cooperation, the single telecommunications network was modernised by introducing CoreNet3, which is a significantly improved and high-speed solution from a technological point of view. At the same time, maintenance costs of this network were considerably reduced. A new teleconferencing system based on IP technologies was also introduced. It provides both a broader functionality and more efficient management.

For the purpose of the operation of the SSM, access of the FCMC to the ESCB information systems infrastructure and information systems was ensured through Latvijas Banka's connection and information systems infrastructure.

The centralised data storage system was modernised by introducing a most recent technology-based solution, which ensures a significantly higher level of continuity when using several data centres. The system includes data array virtualisation technologies that make it possible to combine both the new data arrays and the ones utilised until now in a single solution, thus ensuring efficient use of the previous investments in the long term. The new solution also provides a considerably higher performance and volume of data storage, as well as security and management.

The document management and electronic services infrastructure was modernised, thus ensuring more effective possibilities both for the development of new solutions and improvement of the existing ones, as well as more efficient centralised management of this infrastructure.

An enhanced security printout management system was introduced, thus reducing information risk in this area and at the same time also costs in relation to erroneous printouts.

Security solutions were improved to mitigate risks associated with the most topical technological threats.

More efficient use of environmental resources

Latvijas Banka is an environmentally friendly institution focusing on more efficient use of environmental resources.

Over time, several measures have been taken to reduce the usage of paper and, consequently, also production resources required for its production. The document circulation is fully provided in electronic format at Latvijas Banka, substantially reducing the need for document printing. Meanwhile, waste paper is recycled.

Raw material (toner, ink and paper) efficient printing mode of printers has been used, ensuring lower consumption of raw materials and paper (by applying duplexing). The staff are encouraged to choose a more efficient printing mode by assessing the necessity of printing (colour material printing in particular). It is impossible to print black and white material from a colour printer. E-mail messages sent by Latvijas Banka contain a request to assess the need for printing them out, encouraging recipients to reduce useless consumption of natural resources.

As regards the area of energy efficiency, Latvijas Banka also focuses on energy consumption of new equipment when implementing projects in relation to technical modernisation of equipment. Energy efficiency ratio is taken into account when upgrading hardware and other technical equipment.

Successful continuation of server virtualisation and consolidation of server resources has led to a further decrease in the amount of electricity consumed by servers and the heat generated by them. Consequently, fewer resources are needed for their cooling. Reduced electricity consumption has been achieved by ensuring that the computers not servicing information systems are turned off after office hours.

RISK MANAGEMENT

Latvijas Banka manages strategic, financial and operational risks. Risks at Latvijas Banka are managed pursuant to "The Risk Management Policy of Latvijas Banka", "The Business Continuity Management Policy of Latvijas Banka", "The Information and Information Systems Security Policy of Latvijas Banka", and "The Physical Security Policy of Latvijas Banka" adopted by the Council of Latvijas Banka. A comprehensive and uniform supervision of the implementation of these policies is carried out by the Security Oversight Commission of Latvijas Banka.

Market risk (price, interest rate and currency risks), credit and liquidity risks are the most significant financial risks Latvijas Banka is exposed to in its daily activities. Latvijas Banka manages financial risks related to its investments in accordance with "The Procedure for Managing Financial Assets and Gold of Latvijas Banka" adopted by the Council of Latvijas Banka. Investments are managed by classifying them into different investment portfolios. Parameters for a benchmark reflecting the acceptable level of financial risks and the return target are set out for each financial instrument portfolio, and the Risk Management Division of the Market Operations Department controls compliance with them. For the purpose of investment management, including management of the related financial risks, the Investment Committee of Latvijas Banka develops an investment management strategy, approves tactical decisions and sets detailed limits for financial risks, as well as oversees the operation of the external investment managers. The Investment Committee of Latvijas Banka reviews the investment strategy once a quarter, and receives and reviews, on a weekly basis, reports on and forecasts for developments in financial markets, prepared by financial investment portfolio managers, reports by financial risk managers, and approves the investment management tactical decisions for the forthcoming week. Once every two months the Market Operations Department informs the Council of Latvijas Banka about the results of investment management.

Latvijas Banka manages its operational risks related to processes and projects in compliance with "The Procedure for Managing Operational Risks of Latvijas Banka" adopted by the Board of Latvijas Banka. Risks are identified, analysed and assessed, opting for the most appropriate risk mitigation measures. The management of operational risks is conducted by the structural units of Latvijas Banka, project managers and other employees of Latvijas Banka responsible for the execution of Latvijas Banka's processes. Operational risk management is supervised by the Operational Risk Management Committee of Latvijas Banka, appointed by the Board of Latvijas Banka, which ensures coordination of the measures to be carried out under the operational risk management process and provides support to the Board of Latvijas Banka in the area of risk management. In 2014, the main focus was on the management of the risks related to the integration of Latvijas Banka into the Eurosystem.

The business continuity management of Latvijas Banka is aimed at ensuring continuity of the processes critical to the performance of the core functions of Latvijas Banka or to the achievement of its objectives or, in case a critical process is interrupted, its re-establishment at an appropriate level and in an acceptable timeframe, as well as an efficient incident and crisis management. In 2014, within the framework of the business continuity management process of Latvijas Banka, the main focus was on the introduction of the Register of Incidents and Other Events, as well as on ensuring the continuity of the measures related to the integration of Latvijas Banka into the Eurosystem.

Latvijas Banka continued risk analysis of the critical and important information systems based on the information system risk management methodology. Risk analysis is also performed as part of any information system development or upgrading project and an information system infrastructure modification project.

In the first half of 2014, continuous management of the risks related to Latvijas Banka joining the Eurosystem and the euro changeover in Latvia in the areas of cash transactions and cashless payments was maintained. Risk reports were reviewed at the meetings of the Euro Settlement Implementation Working Group of Latvijas Banka and the Council of Latvijas Banka on a regular basis. Moreover, in the critical period between 29 December 2013 and 2 January 2014 Latvijas Banka ensured continuous control of the implementation of the measures related to the euro changeover in Latvia in the areas of cash transactions and cashless payments.

As a result of the implementation of risk mitigation measures, none of the previously identified major risks related to Latvijas Banka joining the Eurosystem and the euro changeover in Latvia in the areas of cash transactions and cashless payments materialised, and the euro changeover process proceeded without incidents.

Staff members were trained in the areas of information and information system security, business continuity and operational risk management.

INTERNAL AND EXTERNAL AUDIT

By applying a systemic and planned approach, the internal audit provides the management of Latvijas Banka with an objective and independent evaluation of the effectiveness of Latvijas Banka's governance, risk management, internal control system and operational processes and advises on improvement in Latvijas Banka's operation. The internal audit at Latvijas Banka is conducted by the Internal Audit Department. The Audit Committee of Latvijas Banka oversees the internal audit and supports its development. The internal audit is organised and conducted in accordance with "The Internal Audit Policy of Latvijas Banka", adopted by the Council of Latvijas Banka, and the Regulation of Internal Audit Department. It is carried out in line with the "International Standards for the Professional Practice of Internal Auditing" and the "Code of Ethics" of the Institute of Internal Auditors.

The compliance of internal audit activities with the "International Standards for the Professional Practice of Internal Auditing" and the "Code of Ethics" of the Institute of Internal Auditors has been attested by the external assessment of the internal audit quality in 2010 and the periodic internal assessment of the internal audit quality in 2014.

The internal audit covers all business areas of Latvijas Banka. Internal audits are planned and conducted using a risk based approach. The outcome of each internal audit is reported to the Governor and the Audit Committee of Latvijas Banka by the Head of the Internal Audit Department. The Audit Committee of Latvijas Banka jointly with the Head of the Internal Audit Department reviews the internal audit findings, recommendations and their implementation on a quarterly basis. The results of internal audit activities are reported to the Council of Latvijas Banka on an annual basis.

The Internal Audit Department also carries out internal audits based on the audit plan approved by the ESCB Internal Auditors Committee. The internal audits of the ESCB are carried out in accordance with the Audit Charter for the Eurosystem/ESCB and the Single Supervisory Mechanism. In 2014, six such internal audits were performed. An experienced internal auditor of De Nederlandsche Bank supplemented the internal auditors' team of Latvijas Banka in one of them.

Pursuant to the Law on Latvijas Banka, Latvijas Banka's financial statements are audited by independent external auditors recommended by the Governing Council of the ECB and approved by the EU Council, i.e. SIA Ernst & Young Baltic, a company of certified auditors.

FINANCIAL STATEMENTS OF LATVIJAS BANKA
FOR THE YEAR ENDED 31 DECEMBER 2014

BALANCE SHEET

(at the end of the year; in thousands of euro)

	Note[1]	2014	2013[2]
ASSETS			
Gold and gold receivables	6	**210 774**	217 923
Claims on non-euro area residents denominated in foreign currency	7	**2 441 368**	2 370 157
Receivables from the International Monetary Fund		144 069	136 157
Balances with banks and security investments, external loans and other external assets		2 297 299	2 234 000
Claims on euro area residents denominated in foreign currency	8	**486 242**	472 800
Claims on non-euro area residents denominated in euro	9	**214 953**	441 866
Lending to euro area credit institutions related to monetary policy operations denominated in euro	10	**85 520**	14 229
Main refinancing operations		–	14 229
Longer-term refinancing operations		85 520	–
Other claims on euro area credit institutions denominated in euro	11	**4 475**	1 295
Securities of euro area residents denominated in euro	12	**1 095 446**	1 094 153
Intra-Eurosystem claims	13	**3 393 275**	1 167 262
Participating interest in the European Central Bank		115 082	1 038
Claims equivalent to the transfer of foreign reserves		163 480	–
Claims related to TARGET2 and correspondent accounts (net)		–	1 166 224
Other claims within the Eurosystem		3 114 713	–
Other assets	14	**92 455**	110 119
TOTAL ASSETS		**8 024 508**	5 889 804

[1] The accompanying Notes set out on pages 76 to 120 are an integral part of these financial statements.
[2] The comparison of the layout of the published balance sheet of Latvijas Banka for 2013 with the changed layout of the balance sheet for 2013 is provided in Note 47. Assets and liabilities denominated in lats as at 31 December 2013 are reported in euro.

(at the end of the year; in thousands of euro)

	Note	**2014**	2013
LIABILITIES			
Banknotes in circulation	15	**3 849 170**	801 869
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	16	**2 423 356**	4 127 804
Current accounts (covering the minimum reserve system)		2 073 356	4 013 974
Deposit facility		350 000	113 830
Other liabilities to euro area credit institutions denominated in euro	17	**540**	–
Liabilities to other euro area residents denominated in euro	18	**126 919**	226 372
General government		50 900	202 263
Other liabilities		76 019	24 109
Liabilities to non-euro area residents denominated in euro	19	**23 986**	12 685
Liabilities to euro area residents denominated in foreign currency	20	**144 579**	138 070
Liabilities to non-euro area residents denominated in foreign currency	21	**–**	983
Intra-Eurosystem liabilities	13	**796 980**	–
Liabilities related to TARGET2 and correspondent accounts (net)		796 980	–
Other liabilities	22	**180 089**	112 028
Capital and reserves	23	**478 889**	469 993
TOTAL LIABILITIES		**8 024 508**	5 889 804

PROFIT AND LOSS STATEMENT

(in thousands of euro)

	Note	**2014**	2013
Net interest income	33	**38 799**	41 853
Interest income		**49 574**	55 989
Interest expense		**–10 775**	–14 136
Net result of financial operations, write-downs and risk provisions		**–5 310**	56 418
Realised gains arising from financial operations	34	**11 135**	63 360
Write-downs of revaluation result on financial assets and positions	23, 35	**–1 645**	–6 942
Provisions for market risk and credit risk	36	**–14 800**	–
Net expense from fees and commissions		**–1 213**	–931
Fees and commissions income		**302**	512
Fees and commissions expense		**–1 515**	–1 443
Income from participating interest	37	**3 650**	388
Net result of pooling of monetary income	38	**31 953**	–
Other operating income	39	**3 666**	3 499
NET INCOME		**71 545**	101 227
Remuneration	40	**–16 839**	–15 563
Social security costs	40	**–3 382**	–3 669
Depreciation of fixed assets and amortisation of intangible assets	14	**–3 685**	–3 776
Banknote and coin acquisition costs	41	**–2 633**	–10 781
Other operating expenses	42	**–8 246**	–8 440
PROFIT OF THE REPORTING YEAR		**36 760**	58 998

STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

(in thousands of euro)

	Note	**2014**	2013
Profit of the reporting year		**36 760**	58 998
Revaluation	23	**36 006**	–43 453
Realisation of the accumulated revaluation result	23	**–27 166**	–36 169
Write-downs of revaluation result on financial assets and positions	23, 35	**1 645**	6 942
Total changes in the valuation account	23	**10 485**	–72 680
TOTAL		**47 245**	–13 682

The financial statements, which are set out on pages 72 to 120, were authorised by the Board of Latvijas Banka on 10 March 2015.

BOARD OF LATVIJAS BANKA

M. Kālis

I. Posuma

J. Blūms

J. Caune

H. Ozols

R. Vanags

NOTES TO THE FINANCIAL STATEMENTS

1. PRINCIPAL ACTIVITIES

Latvijas Banka is the central bank of the Republic of Latvia and a member of the ESCB and the Eurosystem. It was established on 19 September 1922 (re-established in 1990). In its activities, Latvijas Banka complies with the Republic of Latvia and EU legislation as well as ECB legal acts in compliance with the Treaty on the Functioning of the European Union and the Statute of the ESCB and ECB.

The objectives and tasks of Latvijas Banka are set forth by the Law on Latvijas Banka. The primary goal of Latvijas Banka is to maintain price stability. As of 1 January 2014, the euro changeover day in Latvia, Latvijas Banka has the following primary tasks:
– participate in the formulation and implementation of the Eurosystem's monetary policy;
– manage the foreign reserves and other financial investments;
– ensure cash currency circulation in Latvia and participate in shaping the cash currency circulation in the euro area;
– participate in promoting smooth functioning of payment systems;
– compile and publish statistical information in order to ensure the performance of the tasks of Latvijas Banka;
– cooperate with the ECB, the central banks of other EU Member States and other countries, as well as other financial institutions;
– operate as the financial agent of Latvia's government and provide financial services to other market participants;
– act as an advisor to the Saeima (Parliament) and Cabinet of Ministers of the Republic of Latvia on monetary policy issues and other issues related to the implementation of the tasks of Latvijas Banka;
– maintain the Credit Register;
– issue licences to legal persons listed in the Register of Enterprises of the Republic of Latvia, except credit institutions, for the purchase and sale of foreign currency as a commercial activity.

Latvijas Banka neither seeks nor takes instructions from the government of Latvia and other EU Member States, EU institutions and other national, foreign or international institutions and their entities. Latvijas Banka is independent in setting and implementing policy under its legal mandate. Latvijas Banka is supervised by the Saeima of the Republic of Latvia.

Latvijas Banka does not engage in any commercial activity, and its operation related to the execution of its tasks is mainly financed from income received from its investment management.

The Head Office of Latvijas Banka is situated at K. Valdemāra iela 2A, Riga. Latvijas Banka manages the storage, processing and circulation of cash through its Riga Branch and the regional branch in Liepāja. In 2014 Latvijas Banka closed down its branch in Daugavpils.

2. PRINCIPAL ACCOUNTING POLICIES

A summary of the principal accounting policies adopted by Latvijas Banka in the preparation of these financial statements is set out below.

2.1 CHANGE IN ACCOUNTING POLICIES

Upon joining the Eurosystem, the structure of Latvijas Banka's balance sheet has been changed in line with the breakdown used by other central banks of the euro area and in drafting the consolidated financial statements of the Eurosystem. Apart from the breakdown by residence (euro area residents and non-euro area residents), the new structure of Latvijas Banka's balance sheet also provides breakdown by currency and reporting of transactions related to monetary policy operations (see also Note 47).

In accordance with the ECB's legal framework for accounting and financial reporting, on 1 January 2014 Latvijas Banka reclassified the accumulated revaluation result of foreign currency in the amount of 23 055 thousand euro to the initial valuation account. The balance on the initial valuation account is recognised in the profit and loss statement to compensate lower income on claims for the allocation of banknotes within the Eurosystem (see also Notes 23 and 33).

In 2014 the Council of Latvijas Banka decided to make provisions in the amount of 14 800 thousand euro for market risk and credit risk associated with transactions related to financial investment management of Latvijas Banka (see Notes 2.23 and 36).

2.2 BASIS OF PRESENTATION

These financial statements have been prepared in accordance with the Guideline of the ECB of 11 November 2010 on the legal framework for accounting and financial reporting in the European System of Central Banks (recast) (ECB/2010/20), Financial Accounting Policy of Latvijas Banka approved by Latvijas Banka's Council, and the requirements of the Law on Latvijas Banka governing financial reporting.

2.3 BASIS OF MEASUREMENT

These financial statements have been prepared in accordance with the historical cost basis of accounting. Gold, debt securities other than those held to maturity, participating interest (except the participating interest in the ECB), currency future contracts and interest rate derivatives are accounted for at fair value. Forward exchange rate contracts and currency swap arrangements are valued according to the principles described in Note 2.16. The comparison of the book value and fair value of these instruments is provided in Note 24.

2.4 FAIR VALUE OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

Fair value is the price at which a financial asset could be sold or financial liability could be transferred in an orderly transaction between market participants at the measurement date.

Fair value of financial instruments is determined by Latvijas Banka using quoted prices in active markets, other financial market information sources or discounted cash flows. The discounted cash flows are modelled using quoted market prices of financial instruments and money market interest rates. The breakdown of assets measured at fair value, taking into account the hierarchy of fair value determination, is provided in Note 5.

Fair value of the financial assets and financial liabilities of Latvijas Banka (except debt securities held to maturity; see Note 12) does not differ materially from the reported book value of the respective assets and liabilities.

2.5 FOREIGN CURRENCY AND GOLD TRANSLATION

For foreign currency translation Latvijas Banka applies foreign exchange rates published by the ECB. The price of gold is set on the basis of the gold market price quoted on the London Stock Exchange in US dollars and the exchange rate of the US dollar against the euro published by the ECB. The exchange rate of SDR is set on the basis of the weights of the SDR basket of currencies published by the IMF and the exchange rates of the respective currencies published by the ECB.

Transactions denominated in foreign currencies are recorded in euro at the respective exchange rates on the day of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into euro at the exchange rates at the end of the reporting period. Non-monetary assets and liabilities, measured at cost or amortised cost, are translated into euro at the exchange rate for the respective foreign currency on the day of the transaction.

The exchange rates set by Latvijas Banka on the basis of the exchange rate of the euro against the US dollar and the US dollar against other foreign currencies, as quoted in the electronic information system Reuters, as well as the lats peg to the euro have been used in the preparation of the financial statements for the year 2013.

Transactions in foreign currencies are included in the calculation of net foreign currency position of the respective currency. The transactions in foreign currencies reducing the respective currency position result in realised gains or losses. Any gain or loss arising from revaluation of transactions in foreign currencies and foreign currency positions are credited or charged to the profit and loss statement or the balance sheet caption "Capital and reserves" as the foreign currency revaluation reserve ("Valuation account") in accordance with the principles referred to in Note 2.24. The principles referred to herein and in Note 2.24 for valuation and recording of transactions denominated in foreign currencies are also applied to gold.

The exchange rates of major foreign currencies (currency units per euro) and gold price (euro per troy ounce) in euro used in the preparation of the balance sheet for the year ended 31 December 2014 and the year ended 31 December 2013 are as follows:

(at the end of the year)

	2014	2013	Changes (%)
US dollar (USD)	**1.2141**	1.3647	–11.0
Japanese yen (JPY)	**145.23**	142.56	1.9
Canadian dollar (CAD)	**1.4063**	1.4671	–4.1
British pound sterling (GBP)	**0.7789**	0.8337	–6.6
Gold (XAU)	**987.769**	876.229	12.7

2.6 RECOGNITION AND DERECOGNITION OF FINANCIAL ASSETS AND LIABILITIES

Financial assets and financial liabilities are recognised in the balance sheet when Latvijas Banka becomes a contractual party in the respective financial transaction.

A financial asset is derecognised when the contractual rights to cash flows arising from the respective financial asset expire or are transferred, thereby risks and rewards related to the particular asset are transferred, and Latvijas Banka does not retain control over the asset. Financial liabilities are derecognised when the respective obligations are settled.

A regular way purchase or sale of financial assets is recognised and derecognised on the settlement day.

2.7 OFFSETTING FINANCIAL ASSETS AND FINANCIAL LIABILITIES

Financial assets and financial liabilities are offset and the net amount in the financial statements is reported only in cases when there is a legally enforceable right to set off the recognised amounts, and there is an intention to dispose of the respective assets and settle the liability simultaneously.

2.8 USE OF ESTIMATES AND ASSUMPTIONS

Estimates and assumptions have been made in the preparation of the financial statements that affect the amounts of certain assets, liabilities and contingent liabilities reported in the financial statements. Future events may affect the above mentioned estimates and assumptions. The effect of a change in such estimates and assumptions is reported in the financial statements for the reporting year and each year in the future to which it refers.

The major estimates and assumptions in the preparation of the financial statements have been made with respect to the following: impairment of assets (see Note 2.20), the method for establishing the fair value of the BIS shares (see Note 14.2), the useful life of fixed assets and intangible assets (see Notes 2.18 and 2.19), the repurchasing probability of collector coins (see Note 2.22), provisions for market risk and credit risk (see Notes 2.23 and 36), and the method for the initial valuation account write-downs (see Note 23).

2.9 GOLD AND GOLD RECEIVABLES

Gold is stated at market value in the balance sheet in accordance with the principles described in Note 2.5.

Any gain or loss arising from transactions in gold and revaluation of gold reserves is credited or charged to the profit and loss statement or the balance sheet caption "Capital and reserves" as the foreign currency revaluation reserve in accordance with the principles described in Note 2.24.

2.10 DEBT SECURITIES

Debt securities are stated at fair value in the balance sheet, except those held to maturity measured at amortised cost.

Interest on securities, including premium and discount, is recognised in the profit and loss statement as interest income.

Gain or loss arising from transactions in debt securities and revaluation of the debt securities stated at fair value are credited or charged to the profit and loss statement or the balance sheet caption "Capital and reserves" as the securities revaluation reserve in accordance with the principles referred to in Note 2.24.

2.11 REVERSE REPURCHASE AGREEMENTS

Reverse repurchase agreements are accounted for as financing transactions. Securities purchased under reverse repurchase agreements are not reported on Latvijas Banka's balance sheet. The related funding provided to the counterparty is reported on Latvijas Banka's balance sheet at nominal value as claims on the seller of the securities.

The difference between the purchase and resale price of securities is gradually recognised as interest income in the profit and loss statement over the term of the agreement.

2.12 REPURCHASE AGREEMENTS

Repurchase agreements are accounted for as financing transactions. Securities sold under repurchase agreements are reported on Latvijas Banka's balance sheet along with other securities that are not involved in these transactions. Funding received from such sales is reported on the balance sheet at nominal value as a liability to the purchaser of the securities.

The difference between the sale and repurchase price of securities is recognised as interest expense in the profit and loss statement over the term of the agreement.

2.13 SECURITIES LENDING

Securities lent under automatic securities lending programme agreements are reported on Latvijas Banka's balance sheet along with other securities that are not involved in these transactions. Only cash collateral placed on the account of Latvijas Banka is recognised in the balance sheet.

Income from securities lending transactions is recognised as interest income in the profit and loss statement.

2.14 LOANS TO CREDIT INSTITUTIONS, DEPOSITS AND SIMILAR FINANCIAL CLAIMS AND FINANCIAL LIABILITIES

Loans to credit institutions, deposits and similar financial claims and liabilities are recorded at nominal value in the balance sheet.

2.15 PARTICIPATING INTEREST

Participating interest includes long-term investments of Latvijas Banka in equity instruments. Latvijas Banka has no control or significant influence in any institution, therefore participating interest is not accounted for as an investment in a subsidiary or an associate. Equity instruments are reported at fair value in the balance sheet, except participating interest in the ECB, which is reported at cost in the balance sheet in accordance with the ECB's legal framework for accounting and financial reporting.

The change in fair value of participating interest is reported under the balance sheet caption "Capital and reserves" as the revaluation reserve for equity instruments.

2.16 DERIVATIVE FINANCIAL INSTRUMENTS

Latvijas Banka enters into commitments involving forward exchange rate contracts, currency and interest rate swap arrangements, and interest rate and currency future contracts, which are reported in off-balance sheet accounts at their contract or notional amount. Forward exchange rate contracts and currency swap arrangements are included in the net position of the respective currency on the transaction day at the spot rate of the transaction and are recorded in the balance sheet in euro at the exchange rate of the respective currency at the end of the reporting period. Other derivative financial instruments are reported in the balance sheet at fair value.

Interest on derivative financial instruments, including the spot and forward interest rate spread of forward exchange rate contracts and currency swap arrangements, is recognised in the profit and loss statement as interest income or interest expense over the term of the agreement. Any gain or loss arising from a change in fair value of interest rate and currency future contracts is included in the profit and loss statement taking into account settlement. Any gain or loss arising from a change in fair value of other derivative financial instruments is credited or charged to the profit and loss statement or the balance sheet caption "Capital and reserves" as the revaluation reserve in accordance with the principles referred to in Note 2.24.

2.17 ACCRUED INTEREST INCOME AND EXPENSE

Accrued interest income and expense are reported under balance sheet captions of other assets or other liabilities.

2.18 FIXED ASSETS

Fixed assets are tangible long-term investments with the useful life of over one year. Capitalisation limit of fixed assets is 150 euro, except the costs related to real estate improvements and replacement of fixed asset parts for which the Board of Latvijas Banka has set a higher capitalisation limit depending on their significance. These assets are used in the provision of services as well as in the maintenance of other fixed assets and to ensure operation of Latvijas Banka.

Fixed assets are recorded at cost less accumulated depreciation and impairment, if any.

Depreciation is recognised using the straight-line method over the estimated useful life of the asset. Assets under construction or development, land and works of art are not depreciated. Buildings and structures are accounted by separate components, with individual useful life set for each such component.

In 2014 and 2013, the useful lives set for fixed assets were as follows:

(years)

	2014	2013
Buildings and their components, improvements to the territory, incl.	**5–100**	5–100
structures	**100**	100
finishing, equipment and engineering communications	**5–20**	5–20
Transport vehicles	**10–15**	10–15
Office equipment and tools	**5–25**	5–25
Cash processing, verifying and storage equipment	**5–15**	5–15
Computer and telecommunication equipment	**2–7**	2–7
Other fixed assets	**5–15**	5–15

In accordance with generally accepted principles for hedge accounting, the cost of individual fixed assets includes an effective result arising from financial instruments designated as hedges of exchange risk associated with development of the respective fixed assets.

2.19 INTANGIBLE ASSETS

Intangible assets are long-term investments without physical substance with a useful life of over one year. Capitalisation limit of intangible assets is 150 euro. Intangible assets include software application rights and other rights.

Intangible assets are reported in the balance sheet at cost less accumulated amortisation and impairment, if any.

Acquisition costs of intangible assets are amortised over the useful life of the respective assets using the straight-line method; however, this period may not exceed 10 years.

Costs related to software development by Latvijas Banka are recognised in the profit and loss statement when incurred.

2.20 IMPAIRMENT OF ASSETS

An asset is impaired when its carrying amount exceeds its recoverable amount. Upon detecting any indications of impairment of an asset, the recoverable amount of the respective asset is estimated. If the recoverable amount is less than the carrying amount of the respective asset, adequate allowances for the respective asset are made. Such allowances are recognised in the profit and loss statement with a respective reduction in the asset's carrying amount.

2.21 CURRENCY IN CIRCULATION

In view of the fact that euro cash is issued by all NCBs of the Eurosystem and the ECB, they report a certain share of the total amount of euro banknotes issued by the Eurosystem on their balance sheets. The share allocated to the ECB is 8% of the total amount of euro banknotes issued by the Eurosystem; the remaining 92% are allocated to the NCBs in proportion to their share in the ECB's capital and reported under the balance sheet item "Banknotes in circulation". Of the total amount of euro banknotes issued by the Eurosystem, the share allocated to Latvijas Banka is larger than the actual amount of euro banknotes it has issued (see Note 15); consequently, claims on the ECB for the allocation of banknotes are reported under the balance sheet item "Intra-Eurosystem claims". In accordance with the ECB's legal framework for accounting and financial reporting, the balance sheet caption "Banknotes in circulation" at the end of 2014 and 2013 also comprises the nominal value of the lats banknotes in circulation which had not been exchanged for euro yet.

Pursuant to the Law on the Procedure for Introducing the Euro, the period for exchanging the lats cash to the euro at Latvijas Banka is unlimited.

Euro and lats coins in circulation issued by Latvijas Banka, except collector coins, are reported under the balance sheet caption "Other liabilities" at nominal value.

2.22 COLLECTOR COINS

Collector coins sold are not included in the balance sheet liabilities, as the repurchasing probability of those coins is low or the value of precious metals of which the coins are made exceeds the nominal value. Proceeds from sales of collector coins are recognised in the profit and loss statement when incurred. The accounting principles established with respect to collector coins are applied to the lats gold circulation coins and collector coins.

2.23 PROVISIONS

Provisions are recognised in the financial statements when Latvijas Banka has incurred a present legal or constructive obligation arising from a past event or transaction and a reliable estimate can be made of the obligation and it can be expected to result in a cash outflow from Latvijas Banka.

On the basis of reasonable risk estimates, Latvijas Banka's Council may decide on making provisions for market risk (price, interest rate and foreign exchange risks) and credit risk associated with Latvijas Banka's investment management and other financial transactions (see also Note 36).

2.24 RECOGNITION OF GAINS OR LOSSES ON FINANCIAL INSTRUMENTS, FOREIGN CURRENCY AND GOLD

Gains or losses on financial instruments, foreign currency or gold position are recognised in accordance with the following principles provided by the ECB's legal framework for accounting and financial reporting:
(a) realised gains and losses shall be recognised in the profit and loss statement;
(b) unrealised gains shall be recognised in the balance sheet caption "Capital and reserves" as the revaluation reserve;
(c) unrealised losses recognised in the balance sheet caption "Capital and reserves" as the revaluation reserve at the end of the reporting year shall be transferred to the profit and loss statement if they exceed the previous revaluation gain on the respective financial instrument, foreign currency or gold position;
(d) unrealised losses recognised in the profit and loss statement at the end of the reporting year shall not be reversed and offset by unrealised gains of the respective financial instrument, foreign currency or gold position in the subsequent years;
(e) there shall be no netting of unrealised losses in a financial instrument, foreign currency or gold position against unrealised gains in other financial instrument, foreign currency or gold position.

The average cost method shall be used to calculate realised and unrealised gains and losses of financial instrument, foreign currency or gold position. The average cost of financial instrument, foreign currency or gold position shall be increased or reduced by unrealised losses that are recognised in the profit and loss statement at year-end.

2.25 INTEREST INCOME AND EXPENSE

Interest income and expense are recognised in the profit and loss statement on an accrual basis.

Interest income includes interest on securities, securities lending, deposits, loans granted, forward exchange rate contracts, currency and interest rate swap arrangements, as well as intra-Eurosystem claims. Interest on securities also includes premium and discount, which is amortised over the remaining life of the respective securities using the straight-line method.

Interest expense includes interest on deposits received from the Latvian government, credit institutions and other financial institutions, as well as interest on forward exchange rate contracts and currency and interest rate swap arrangements, as well as intra-Eurosystem liabilities.

2.26 REALISED GAINS OR LOSSES FROM FINANCIAL OPERATIONS

Realised gains or losses from financial operations are recognised in the profit and loss statement at the time of disposal of financial instrument or at the time of settlement.

Realised gains or losses from financial operations include realised gains or losses of derivative financial instruments, disposal of debt securities, and foreign exchange transactions.

2.27 INCOME FROM PARTICIPATING INTEREST

The change in fair value of participating interest is reported under the balance sheet caption "Capital and reserves" as the revaluation reserve for equity instruments.

Dividends on participating interest are recognised in the profit and loss statement when the right to receive payment is established.

Pursuant to the decision of the Governing Council of the ECB, the income of the ECB gained on the claims for the allocation of banknotes within the Eurosystem and arising from the Securities Markets Programme, outright monetary transactions, the asset-backed securities purchase programme and the third covered bond purchase programme shall be distributed as interim profit for the reporting year in which it accrues. The Governing Council of the ECB distributes interim profit in January of the following year; however, it may resolve not to do so in cases when the ECB's net profit for the reporting year is less than its income included in the interim profit distribution, as well as in the event the Governing Council decides to establish provisions for foreign exchange rate, interest rate, credit and gold price risks. In addition, the Governing Council of the ECB may resolve to make deductions from the interim profit distribution result in respect of expenses incurred by the ECB in connection with the issue and handling of euro banknotes.

Moreover, after the approval of the ECB's annual accounts, the Governing Council distributes the remainder of the ECB's annual profit of the reporting year to euro area NCBs in proportion to their shares in the ECB's capital (see Note 13.1).

Income from participating interest in the ECB is reported under the profit and loss statement caption "Income from participating interest".

2.28 NET RESULT OF POOLING OF MONETARY INCOME

Pursuant to the Statute of the ESCB and the ECB, NCBs of the Eurosystem gain income from the implementation of the single monetary policy of the Eurosystem. Total monetary income of the Eurosystem equals the income on assets arising from the issue of euro banknotes and receiving deposits from credit institutions. The income is allocated to euro area NCBs in proportion to their shares in the capital of the ECB. For the first six years following the joining of the Eurosystem an NCB's monetary income is adjusted in compliance with a definite coefficient to avoid significant NCB income fluctuations (see also Note 33).

The net monetary income pooled by Latvijas Banka includes the income derived from earmarkable assets of Latvijas Banka, reduced by expenses for the monetary liabilities of Latvijas Banka. The earmarkable assets of Latvijas Banka for the allocation of monetary income include gold, assets acquired as a result of monetary policy operations, intra-Eurosystem claims as well as other assets in the amount necessary to fully cover the monetary liabilities. Monetary liabilities of Latvijas Banka include banknotes in circulation, deposits of credit institutions resulting from monetary policy operations and intra-Eurosystem liabilities.

Latvijas Banka's monetary income received comprises Latvijas Banka's share in the Eurosystem's total monetary income set on the basis of Latvijas Banka's share in the ECB's capital.

2.29 BANKNOTE AND COIN ACQUISITION COSTS
Banknote and coin acquisition costs are charged to the profit and loss statement at the time of banknote and coin acquisition.

2.30 OTHER EXPENSE AND INCOME
Bank's other operating expense and income are recognised in the profit and loss statement on an accrual basis. The amount of accrued expense and income for the reporting period is calculated in accordance with the volume of services received or rendered in the reporting period. Lease payments are recognised in the profit and loss statement proportionally over the term of the respective agreement.

3. SUMMARY OF THE FINANCIAL POSITION AND FINANCIAL PERFORMANCE OF LATVIJAS BANKA

3.1 FINANCIAL POSITION
In 2014, Latvijas Banka's assets grew by 2 134.7 million euro, mainly on account of changes in intra-Eurosystem claims and liabilities related to Latvijas Banka's joining the Eurosystem.

Pursuant to the Statute of the ESCB and the ECB, euro area NCBs shall transfer a certain amount of their foreign reserves to the ECB. The amount of foreign reserves to be transferred is set in proportion to each euro area NCB's share in the ECB's subscribed capital. Upon joining the Eurosystem, Latvijas Banka transferred 205.3 million euro of its foreign reserves to the ECB which is Latvijas Banka's proportionate share of the market value of the foreign reserves already transferred by other euro area NCBs before. Gold accounted for 15% or 30.8 million euro of the transferred foreign reserves, and Japanese yen for 85% or 174.5 million euro. For the foreign reserves transferred to the ECB Latvijas Banka received a euro-denominated claim on the ECB in the amount of 163.5 million euro, in proportion to the value of the respective claims of other euro area NCBs. The difference between the market value of the transferred foreign reserves and the value of the euro-denominated claim in the amount of 41.8 million euro is reported as participating interest in the ECB. The above transactions had a decreasing effect on Latvijas Banka's balance sheet items "Gold and gold receivables" and "Claims on non-euro area residents denominated in euro", with a corresponding increase in the item "Intra-Eurosystem claims".

In 2014, the amount of loans granted to credit institutions by Latvijas Banka as a result of monetary policy operations grew by 71.3 million euro via conducting targeted longer-term refinancing operations. The main refinancing operations reported at the end of 2013 were conducted in line with the regulation for the use of monetary policy instruments of Latvijas Banka, in force by the time Latvijas Banka joined the Eurosystem.

The Statute of the ESCB and the ECB stipulates that a euro area NCB shall pay up its share in the ECB's capital in full, as well as in the ECB's reserve capital, provisions equivalent to reserves and the financial instrument revaluation account, in proportion to its share in the ECB's capital. At the beginning of 2014, the subscribed share of Latvijas Banka in the ECB's capital was 30.5 million euro (the percentage share was 0.2821%); pursuant to the transitional provisions of the Statute of the ESCB and the ECB and the decision of the ECB's General Council, it was paid up in the amount of 1.1 million euro or 3.75% up to 1 January 2014. At the beginning of 2014 Latvijas Banka paid up its remaining share in the ECB's capital in the amount of 29.4 million euro, as well as transferred 54.1 million euro to the ECB's provisions equivalent to reserves and the financial instrument revaluation account. The above contributions are reported as a contribution to the ECB's capital under the balance sheet item "Intra-Eurosystem claims".

In view of the fact that euro banknotes are issued by all NCBs of the Eurosystem and the ECB, they report a certain share of the total amount of euro banknotes issued by the Eurosystem on their balance sheets in proportion to their share in the ECB's capital. Of the total amount of euro banknotes issued, the share allocated to Latvijas Banka is larger than the amount of euro banknotes it has actually issued, therefore Latvijas Banka's balance sheet item "Banknotes in circulation" grew by 3 079.3 million euro in 2014, resulting in a corresponding increase in the claims on the ECB for the allocation of banknotes, reported under the balance sheet item "Intra-Eurosystem claims".

Upon joining the Eurosystem, the minimum reserve requirements for credit institutions in the Eurosystem took effect and the liquidity management policy of some credit institutions changed. At the beginning of June 2014, the ECB reduced its interest rates, setting a negative interest rate on credit institution deposits exceeding the minimum reserve requirements, as well as on the government sector deposits exceeding the limit established by the ECB Governing Council. In addition to the above, the ECB discontinued its tenders of fixed-term deposits. Consequently, deposits of credit institutions and the Latvian government with Latvijas Banka contracted. The balance sheet items "Liabilities to euro area credit institutions related to monetary policy operations denominated in euro" and "Liabilities to other euro area residents denominated in euro" decreased by 1 704.4 million euro and 99.5 million euro respectively.

As a result of cross-border payments made by credit institutions and the Latvian government, liabilities to the ECB for the settlement result in TARGET2, reported under the balance sheet item "Intra-Eurosystem liabilities", increased to 797.0 million euro (claims amounted to 1 166.2 million euro at the end of 2013).

Capital and reserves of Latvijas Banka grew by 8.9 million euro on account of net changes in valuation of financial instruments (10.5 million euro) and profits earned in 2014 (36.8 million euro), while the share of profits earned in 2013 and remitted to the state budget revenue in the amount of 38.3 million euro had a decreasing effect.

3.2 FINANCIAL PERFORMANCE

In 2014, Latvijas Banka's profit amounted to 36.8 million euro (59.0 million euro in 2013). Net interest income in 2014 decreased by 3.1 million euro as compared to 2013.

Further shrinking of actual securities yields in a low interest rate environment prevailing in the global financial markets notably contributed to a fall of 6.4 million euro in interest income. Interest income of Latvijas Banka was basically derived from debt securities totalling 45.3 million euro (51.9 million euro in 2013).

A 3.4 million euro drop in interest expense was a result of several factors: a lower minimum reserve ratio for credit institutions, a decrease in credit institution deposits and a reduction in the key ECB interest rates. At the beginning of June 2014, the Governing Council of the ECB adopted a decision to implement a series of measures aimed at ensuring price stability in the medium term. These measures included a reduction in all key ECB interest rates, including the rate on main refinancing operations, which decreased from 0.25% to 0.05%, and the deposit facility rate, which declined from 0% to –0.2%.

In 2014, realised gains from financial operations decreased by 52.2 million euro in comparison with 2013. The realised gains from financial operations fell on account of currency future contracts concluded for the purpose of hedging the currency risk and the result of interest rate future contracts. In view of Latvijas Banka hedging the risks related to gold price and foreign exchange fluctuations, the positive revaluation result of the respective hedged balance sheet items is reported under the balance sheet caption

"Capital and reserves". The realised gains from financial operations were positively affected by the result of the initial valuation account write-downs.

The write-downs of the revaluation result on financial assets and positions decreased by 5.3 million euro as compared to 2013.

In 2014, the Council of Latvijas Banka decided to establish provisions amounting to 14.8 million euro for market risk and credit risk with regard to transactions related to investment management of Latvijas Banka.

Pursuant to the Statute of the ESCB and ECB, the income generated by euro area NCBs through the implementation of the single monetary policy of the Eurosystem is allocated to euro area NCBs in proportion to their shares in the ECB's capital. In 2014, Latvijas Banka's net result of pooling of monetary income was 32.0 million euro.

After becoming a member of the Eurosystem, Latvijas Banka receives income from the participating interest in the ECB. For 2014, Latvijas Banka was allocated its share of interim profit totalling 3.4 million euro in proportion to Latvijas Banka's share in the ECB's capital key.

Latvijas Banka's future financial performance will be mostly affected by the monetary policy pursued by the Eurosystem, as well as by interest rate developments in the financial markets of the euro area and US since Latvijas Banka is exposed to interest rate risk.

4. FINANCIAL INVESTMENT POLICY

Investments are managed in compliance with the basic principles set out in the Procedure adopted by the Council of Latvijas Banka, inter alia preserving the value of investments, ensuring their liquidity and earning income within the framework of acceptable risk without contradicting the monetary policy implemented by the Eurosystem.

Investments include assets reported under the balance sheet captions "Gold and gold receivables", "Claims on non-euro area residents denominated in foreign currency", "Claims on euro area residents denominated in foreign currency", "Claims on non-euro area residents denominated in euro", "Other claims on euro area credit institutions denominated in euro" and "Securities of euro area residents denominated in euro", as well as derivative financial instruments and spot exchange rate contracts whose book value is reported under relevant balance sheet captions of other assets or other liabilities.

Investments are managed by classifying them into different investment portfolios by investment strategy and source of funding. Portfolios of borrowed funds include investments which correspond to Latvijas Banka's liabilities in foreign currencies to government or government deposits. Investments that are not included in the portfolios of borrowed funds (net investments) are included in the portfolios managed against multi-currency fixed income securities benchmark and asset-backed securities benchmark, as well as other portfolios. A part of investments included in the portfolios managed against multi-currency fixed income securities benchmark and asset-backed securities benchmark are managed by external investment managers.

The parameters for a benchmark reflecting the acceptable level of financial risks and return target are set out for the portfolios managed against multi-currency fixed income securities benchmark and asset-backed securities benchmark and portfolios of borrowed funds.

The breakdown of investments by type of investment portfolio at the end of 2014 and 2013 was as follows:

	Portfolio value (in thousands of euro)		Percentage (%)	
	2014	2013	**2014**	2013
Portfolios managed against multi-currency fixed income securities benchmark	**3 665 508**	3 792 126	**82.5**	85.6
Portfolios managed against asset-backed securities benchmark	**267 672**	255 363	**6.0**	5.8
Gold portfolio	**211 846**	223 224	**4.8**	5.0
Portfolio of long-term fixed income securities	**149 843**	–	**3.4**	–
Portfolios of borrowed funds	**144 579**	158 760	**3.3**	3.6
Total	**4 439 448**	4 429 473	**100.0**	100.0

At the beginning of 2014 Latvijas Banka established a long-term fixed income securities portfolio comprising euro denominated government bonds included in the Citigroup EMU Government Bond Index with the long term credit rating from AA–/AA–/Aa3 to AAA/AAA/Aaa.

Latvijas Banka's multi-currency fixed income securities benchmark is tied to the weighted 1–3 year government securities index of the UK, the US, Denmark, euro area countries, Japan, Canada, and Singapore.

The benchmark of portfolios managed against asset-backed securities benchmark is tied to the US mortgage-backed securities index.

The benchmark for borrowed fund portfolios is formed in compliance with the parameters of respective liabilities.

Latvijas Banka's investment benchmark currency is the euro, except for portfolios of borrowed funds, thus limiting the currency risk. For portfolios of borrowed funds, the benchmark currency structure is formed in compliance with the currency of respective liabilities.

The description of the main methods used in financial risk management is provided in Note 25.1.

BALANCE SHEET NOTES

5. ASSETS AT FAIR VALUE

Fair value of Latvijas Banka's assets is determined using the following hierarchy (see also Note 2.4):
– quoted market price. Fair value is determined using quoted prices for identical financial instruments in active markets;
– observable data. Fair value is determined using quoted prices for similar financial instruments in active markets, quoted prices for similar or identical financial instruments in inactive markets or using models where all significant inputs are observable;
– non-observable data. Fair value is determined using a model where significant inputs are non-observable.

At the end of 2014 and 2013, Latvijas Banka's assets carried at fair value were generally valued on the basis of a quoted market price.

At the end of 2014 and 2013, participating interest in the BIS was assessed using non-observable data. The assessment was conducted using the 70% net asset value model (see also Note 14.2).

At the end of 2014 and 2013, the breakdown of assets carried at fair value according to the fair value hierarchy was as follows:

(in thousands of euro)

	Quoted market price	Observable data	Non-observable data	Total
As at 31 December 2014				
Gold	210 774	–	–	210 774
Debt securities	3 231 897	527 134	–	3 759 031
Participating interest in the Bank for International Settlements	–	–	28 176	28 176
Total	**3 442 671**	**527 134**	**28 176**	**3 997 981**
As at 31 December 2013				
Gold	217 923	–	–	217 923
Debt securities	3 417 947	400 442	–	3 818 389
Participating interest in the Bank for International Settlements	–	–	28 446	28 446
Total	3 635 870	400 442	28 446	4 064 758

The debt securities, incl. accrued interest income on the above securities are reported under the balance sheet captions "Claims on non-euro area residents denominated in foreign currency", "Claims on euro area residents denominated in foreign currency", "Claims on non-euro area residents denominated in euro", "Securities of euro area residents denominated in euro" and "Other assets".

The average market prices on the last trading day of the reporting year are obtained from the electronic information systems Bloomberg and Interactive Data. Where the above price for a financial instrument is absent in the electronic information systems, the price provided by a market participant (broker) or the price determined by applying the discounted cash flow approach is used for evaluating the financial instrument.

6. GOLD AND GOLD RECEIVABLES

	Troy ounces	In thousands of euro
As at 31 December 2012	248 706	311 253
During 2013		
Decrease in gold market value	x	–93 330
As at 31 December 2013	248 706	217 923
During 2014		
Transfer of gold reserves to the ECB	–35 322	–30 774
Increase in gold market value	x	23 625
As at 31 December 2014	**213 384**	**210 774**

Pursuant to the Statute of the ESCB and the ECB, euro area NCBs shall transfer a definite amount of foreign reserves to the ECB. The amount of the foreign reserves to be transferred shall be defined according to the percentage share of each NCB in the ECB's capital. Upon joining the Eurosystem, Latvijas Banka transferred 205 273 thousand euro to the ECB which equals Latvijas Banka's proportionate share of the market value of the foreign reserves transferred by other euro area NCBs. Gold accounted for 15% or

30 774 thousand euro, and Japanese yen accounted for 85% or 174 499 thousand euro. The above share transferred in gold constituted a decrease in the balance sheet caption "Gold and gold receivables". For the foreign reserves transferred to the ECB Latvijas Banka received a euro-denominated claim on the ECB reported under the balance sheet item "Intra-Eurosystem claims".

Latvijas Banka hedges the risk related to gold price fluctuations by entering into forward exchange rate contracts, currency swap arrangements, and currency future contracts (see Notes 3.2 and 26). Revaluation of gold and gold receivables, forward exchange rate contracts, and currency swap arrangements is recognised under the balance sheet caption "Capital and reserves" as the revaluation reserve, whereas revaluation of currency future contracts, taking into account that they are settled, is recognised under the profit and loss statement caption "Realised gains/losses from financial operations".

At the end of 2014 and 2013, Latvijas Banka had no gold receivables.

7. CLAIMS ON NON-EURO AREA RESIDENTS DENOMINATED IN FOREIGN CURRENCY

7.1 RECEIVABLES FROM THE INTERNATIONAL MONETARY FUND

Pursuant to the Law On the Republic of Latvia Joining the International Monetary Fund, Latvijas Banka serves as a depository for the IMF and services the IMF accounts in the member state currency without compensation. The IMF holdings in euro comprise promissory notes issued by the Latvian government, Account No. 1 used for financial transactions with the IMF, and Account No. 2 used for the IMF administrative expenditure and receipts.

Latvia's claims on the IMF include SDR and Latvia's quota in the IMF. SDR is an international reserve asset created by the IMF and used in transactions between the IMF and its members. The quota in the IMF reflects the subscription in the IMF of respective members. Latvia's quota in the IMF is secured by the Latvian government promissory note issued to the IMF and is recorded as an asset denominated in SDR.

Latvia's liabilities to the IMF are made up of the IMF holdings in euro and IMF allocations. At the end of 2014, the receivables from the IMF in SDR as recorded on Latvijas Banka's balance sheet were equivalent to 144 069 thousand euro (136 157 thousand euro at the end of 2013), whereas the liabilities to the IMF are made up of funds at the disposal of the IMF in the amount of 445 thousand euro (420 thousand euro at the end of 2013) held on its Accounts No. 1 and No. 2.

At the end of 2014 and 2013, Latvia's net receivables from the IMF were as follows:

	(in thousands of euro)		(in thousands of SDR)	
	2014	2013	**2014**	2013
Latvia's quota in the IMF	**169 440**	160 134	**142 100**	142 100
IMF holdings in euro	**–169 395**	–160 092	**–142 062**	–142 062
Promissory notes of the Latvian government	–168 950	–159 672	–141 690	–141 690
Account No. 1	–424	–400	–355	–355
Account No. 2	–21	–20	–17	–17
Reserve position in IMF	**66**	62	**55**	55
SDR	**144 069**	136 157	**120 823**	120 824
General allocation	**–112 083**	–105 927	**–93 998**	–93 998
Special allocation	**–31 985**	–30 228	**–26 824**	–26 824
Latvia's net receivables from the IMF	**67**	64	**56**	57

The reserve position in the IMF is the difference between Latvia's quota in the IMF and the IMF holdings in euro, excluding the balance on Account No. 2.

7.2 BALANCES WITH CREDIT INSTITUTIONS AND SECURITY INVESTMENTS, EXTERNAL LOANS AND OTHER EXTERNAL ASSETS

(in thousands of euro)

	2014	2013
Debt securities	**2 108 735**	2 065 191
Demand deposits	**132 373**	133 698
Time deposits	**56 173**	17 147
Foreign currency in cash	**18**	17 964
Total	**2 297 299**	2 234 000

8. CLAIMS ON EURO AREA RESIDENTS DENOMINATED IN FOREIGN CURRENCY

(in thousands of euro)

	2014	2013
Debt securities	**482 752**	454 581
Demand deposits	**3 490**	18 219
Total	**486 242**	472 800

9. CLAIMS ON NON-EURO AREA RESIDENTS DENOMINATED IN EURO

(in thousands of euro)

	2014	2013
Debt securities	**203 266**	185 992
Demand deposits	**11 687**	255 874
Total	**214 953**	441 866

10. LENDING TO EURO AREA CREDIT INSTITUTIONS RELATED TO MONETARY POLICY OPERATIONS DENOMINATED IN EURO

At the end of 2014, the total amount of Eurosystem loans in monetary policy operations reached 630 341 million euro (752 288 million euro at the end of 2013), including 85.5 million euro of loans granted by Latvijas Banka. Pursuant to the Statute of the ESCB and the ECB, risks associated with the implementation of monetary policy (if any materialise) are allocated among euro area NCBs in proportion to their share in the ECB's capital.

10.1 MAIN REFINANCING OPERATIONS

Main refinancing operations are open market operations executed through liquidity providing reverse transactions, conducted through weekly standard tenders with a maturity of one week. These operations play a key role in steering interest rates, managing market liquidity and signalling the monetary policy stance. At the end of 2014, Latvijas Banka had granted no loans in main refinancing operations. In 2013, the main refinancing operations were conducted in line with the Regulation for the Use of Monetary Policy Instruments of Latvijas Banka, in force by the time Latvijas Banka joined the Eurosystem (balance of 14 229 thousand euro at the end of 2013).

10.2 LONGER-TERM REFINANCING OPERATIONS

Longer-term refinancing operations are open market operations with a maturity of over 1 week, executed through reverse transactions with the aim to provide credit institutions with additional longer-term refinancing. Following the decision of the Governing Council of the ECB, targeted longer-term refinancing operations were launched in September 2014. These liquidity providing reverse operations are planned to be conducted through standard tenders until 2016 by way of a fixed-rate tender procedure, aiming to promote lending to households and non-financial corporations by credit institutions in euro area countries. At the end of 2014, the balance of the targeted longer-term refinancing operations conducted by Latvijas Banka stood at 85 520 thousand euro. These operations mature on 26 September 2018.

11. OTHER CLAIMS ON EURO AREA CREDIT INSTITUTIONS DENOMINATED IN EURO

Other claims on euro area credit institutions denominated in euro mainly comprise the pledged assets of Latvijas Banka to provide collateral for transactions in financial derivatives. At the end of 2014, the market value of the pledged assets amounted to 3 590 thousand euro (430 thousand euro at the end of 2013; see also Note 44).

Other claims also include demand deposits in euro with euro area credit institutions amounting to 885 thousand euro at the end of 2014 (865 thousand euro at the end of 2013).

12. SECURITIES OF EURO AREA RESIDENTS DENOMINATED IN EURO

(in thousands of euro)

	2014	2013
Securities not held to maturity	**947 138**	1 094 153
Securities held to maturity	**148 308**	–
Total	**1 095 446**	1 094 153

At the end of 2014 the fair value of debt securities held to maturity by Latvijas Banka was 168 344 thousand euro.

13. INTRA-EUROSYSTEM CLAIMS/LIABILITIES(–)

(in thousands of euro)

	Note	**2014**	2013
Participating interest in the European Central Bank	13.1	**115 082**	1 038
Claims in respect of foreign reserves transferred to the European Central Bank	13.2	**163 480**	–
Claims related to TARGET2 and national central bank correspondent accounts (net)	13.3	**–**	1 166 224
Claims for the allocation of banknotes in the Eurosystem	13.4	**3 079 370**	–
Claims related to other operational requirements within the Eurosystem	13.5	**35 343**	–
Total intra-Eurosystem claims		**3 393 275**	1 167 262
Liabilities related to TARGET2 and national central bank correspondent acounts (net)	13.3	**–796 980**	–
Total intra-Eurosystem liabilities		**–796 980**	–
Total intra-Eurosystem claims (net)		**2 596 295**	1 167 262

13.1 PARTICIPATING INTEREST IN THE EUROPEAN CENTRAL BANK

With Latvia's accession to the EU, Latvijas Banka became a subscriber of the capital of the ECB. In accordance with the Statute of the ESCB and of the ECB, Latvijas Banka's ECB capital key is calculated on the basis of Latvia's population and gross domestic product data.The NCB capital keys are adjusted every five years or at shorter intervals depending on changes in the number of the EU Member States. Until 1 January 2014, Latvijas Banka's ECB capital key was 0.2742%, equivalent to 29 682 thousand euro. On 1 January 2014, the NCB capital keys were adjusted in compliance with the Statute of the ESCB and the ECB; as a result, as of 1 January 2014 Latvijas Banka's ECB capital key is 0.2821%, equivalent to 30 537 thousand euro.

The Statute of the ESCB and the ECB stipulates that a euro area NCB shall pay up its subscribed share in the ECB's capital in full, as well as in the ECB's reserve capital, provisions equivalent to reserves and the valuation account for financial instruments, in proportion to its share in the ECB's capital. At the beginning of 2014, Latvijas Banka paid up the unpaid subscribed share in the ECB's capital in the amount of 29 424 thousand euro (pursuant to the transitional provisions of the Statute of the ESCB and the ECB and the decision of the ECB's General Council, until 31 December 2013 it was paid up in the amount of 1 113 thousand euro or 3.75% of the subscribed share of Latvijas Banka in the ECB's capital). It also transferred 42 752 thousand euro to the ECB's provisions equivalent to reserves and in the valuation account for financial instruments. In addition, the difference between the market value of the transferred foreign reserves and the value of the corresponding euro-denominated claim on the ECB in the amount of 41 793 thousand euro is reported as participating interest in the ECB (see also Note 13.2).

ECB's capital shares are not traded in the public securities market, and Latvijas Banka's participating interest in the ECB can be increased or decreased only in the cases referred to in this Note.

	2014	2013
Total amount of the ECB's subscribed capital (in thousands of euro)	**10 825 007**	10 825 007
The subscribed share of Latvijas Banka in the ECB's capital (%)	**0.2821**	0.2742
The subscribed share of Latvijas Banka in the ECB's capital (in thousands of euro)	**30 537**	29 682
The paid-up share of Latvijas Banka in the ECB's capital (%)	**100.00**	3.75
The paid-up share of Latvijas Banka in the ECB's capital (in thousands of euro)	**30 537**	1 113

At the end of 2014 and 2013, the percentage shares of NCBs in the ECB's capital (capital key) were as follows:

(%)

	2014	2013
Nationale Bank van België/Banque Nationale de Belgique	**2.4778**	2.4176
Deutsche Bundesbank	**17.9973**	18.7603
Eesti Pank	**0.1928**	0.178
Banc Ceannais na hÉireann/Central Bank of Ireland	**1.1607**	1.1111
Bank of Greece	**2.0332**	1.9483
Banco de España	**8.8409**	8.2533
Banque de France	**14.1792**	14.1342
Banca d'Italia	**12.3108**	12.457
Central Bank of Cyprus	**0.1513**	0.1333
Latvijas Banka	**0.2821**	–
Banque centrale du Luxembourg	**0.203**	0.1739
Bank Ċentrali ta' Malta/Central Bank of Malta	**0.0648**	0.0635
De Nederlandsche Bank	**4.0035**	3.9663
Oesterreichische Nationalbank	**1.9631**	1.937
Banco de Portugal	**1.7434**	1.7636
Banka Slovenije	**0.3455**	0.327
Národná banka Slovenska	**0.7725**	0.6881
Suomen Pankki – Finlands Bank	**1.2564**	1.2456
Subtotal for euro area NCBs	**69.9783**	69.5581

(cont.) (%)

	2014	2013
Българска народна банка (Bulgarian National Bank)	**0.859**	0.8644
Česká národní banka	**1.6075**	1.4539
Danmarks Nationalbank	**1.4873**	1.4754
Hrvatska narodna banka	**0.6023**	0.5945
Latvijas Banka	–	0.2742
Lietuvos bankas	**0.4132**	0.4093
Magyar Nemzeti Bank	**1.3798**	1.374
Narodowy Bank Polski	**5.123**	4.8581
Banca Naţională a României	**2.6024**	2.4449
Sveriges Riksbank	**2.2729**	2.2612
Bank of England	**13.6743**	14.432
Subtotal for non-euro area NCBs	**30.0217**	30.4419
Total	**100.0**	100.0

In 2014, the subscribed capital of the ECB remained unchanged, while the adjustment of NCB percentage shares in the ECB's capital and Latvijas Banka's joining the Eurosystem resulted in an increase of 43 781 thousand euro in the ECB's total paid-up capital.

The subscribed and paid-up NCB shares in the ECB's capital at the end of 2014 and 2013 were as follows:

(in thousands of euro)

	Subscribed capital		Paid-up capital	
	2014	2013	**2014**	2013
Nationale Bank van België/ Banque Nationale de Belgique	**268 222**	261 705	**268 222**	261 705
Deutsche Bundesbank	**1 948 209**	2 030 804	**1 948 209**	2 030 804
Eesti Pank	**20 871**	19 269	**20 871**	19 269
Banc Ceannais na hÉireann/Central Bank of Ireland	**125 646**	120 277	**125 646**	120 277
Bank of Greece	**220 094**	210 904	**220 094**	210 904
Banco de España	**957 028**	893 420	**957 028**	893 420
Banque de France	**1 534 899**	1 530 028	**1 534 899**	1 530 028
Banca d'Italia	**1 332 645**	1 348 471	**1 332 645**	1 348 471
Central Bank of Cyprus	**16 378**	14 430	**16 378**	14 430
Latvijas Banka	**30 537**	–	**30 537**	–
Banque centrale du Luxembourg	**21 975**	18 825	**21 975**	18 825
Bank Ċentrali ta' Malta/Central Bank of Malta	**7 015**	6 874	**7 015**	6 874
De Nederlandsche Bank	**433 379**	429 352	**433 379**	429 352
Oesterreichische Nationalbank	**212 506**	209 680	**212 506**	209 680
Banco de Portugal	**188 723**	190 910	**188 723**	190 910
Banka Slovenije	**37 400**	35 398	**37 400**	35 398
Národná banka Slovenska	**83 623**	74 487	**83 623**	74 487
Suomen Pankki – Finlands Bank	**136 005**	134 836	**136 005**	134 836
Subtotal for euro area NCBs	**7 575 156**	7 529 669	**7 575 156**	7 529 669

(cont.) (in thousands of euro)

	Subscribed capital		Paid-up capital	
	2014	2013	**2014**	2013
Българска народна банка (Bulgarian National Bank)	**92 987**	93 571	**3 487**	3 509
Česká národní banka	**174 012**	157 385	**6 525**	5 902
Danmarks Nationalbank	**161 000**	159 712	**6 038**	5 989
Hrvatska narodna banka	**65 199**	64 355	**2 445**	2 413
Latvijas Banka	**–**	29 682	**–**	1 113
Lietuvos bankas	**44 729**	44 307	**1 677**	1 662
Magyar Nemzeti Bank	**149 363**	148 736	**5 601**	5 578
Narodowy Bank Polski	**554 565**	525 890	**20 796**	19 721
Banca Naţională a României	**281 710**	264 661	**10 564**	9 925
Sveriges Riksbank	**246 042**	244 775	**9 227**	9 179
Bank of England	**1 480 244**	1 562 265	**55 509**	58 585
Subtotal for non-euro area NCBs	**3 249 851**	3 295 338	**121 869**	123 575
Total	**10 825 007**	10 825 007	**7 697 025**	7 653 244

13.2 CLAIMS EQUIVALENT TO THE TRANSFER OF FOREIGN RESERVES TO THE EUROPEAN CENTRAL BANK

Pursuant to the Statute of the ESCB and the ECB, euro area NCBs shall transfer a definite amount of their foreign reserves to the ECB. The amount of foreign reserves to be transferred shall be fixed in proportion to the each euro area NCB's ECB capital key. Upon joining the Eurosystem, Latvijas Banka transferred its foreign reserves to the ECB in the amount of 205 273 thousand euro, which is equal to Latvijas Banka's proportionate share in the market value of the foreign reserves already transferred by other euro area NCBs before. Gold accounted for 15% or 30 774 thousand euro, and Japanese yen accounted for 85% or 174 499 thousand euro. For the foreign reserves transferred to the ECB Latvijas Banka received a euro-denominated claim on the ECB in the amount of 163 480 thousand euro, i.e. in proportion to the value of the respective claims of other euro area NCBs. The difference between the market value of the foreign reserves transferred to the ECB and the value of the corresponding euro-denominated claim in the amount of 41 793 thousand euro is reported as participating interest in the ECB (see also Note 13.1). For the foreign reserves transferred to the ECB Latvijas Banka receives interest income calculated at the rate on the main refinancing operations set by the ECB (see also Note 33).

13.3 CLAIMS/LIABILITIES(–) RELATED TO TARGET2 AND NATIONAL CENTRAL BANK CORRESPONDENT ACCOUNTS (NET)

TARGET2 system is a real-time gross settlement system for large value payments in euro. Claims and liabilities related to TARGET2 settlements originate as a result of cross-border payments settled in the EU central bank money. The above settlements result in bilateral claims and liabilities in the TARGET2 accounts held by NCBs of EU countries. The net positions for the bilateral balances are attributed to the ECB and calculated on a daily basis, leaving each NCB with a single net position vis-à-vis the ECB. This is reported on the NCB's balance sheet as net claims or liabilities related to TARGET2 settlements.

In 2014, liabilities related to TARGET2 and national central bank correspondent accounts (net) increased as a result of the cross-border payments effected by credit institutions and the government of Latvia.

Interest is paid on the above claims and liabilities as per the rate on the main refinancing operations set by the ECB.

13.4 CLAIMS FOR THE ALLOCATION OF BANKNOTES IN THE EUROSYSTEM

In view of the fact that euro banknotes are issued by all euro area NCBs and the ECB, they report a definite share of the total amount of euro banknotes issued by the Eurosystem on their balance sheets in proportion to their share in the ECB's capital. Of the total amount of euro banknotes issued, the share allocated to Latvijas Banka is larger than the amount of euro banknotes it has actually issued (see Note 15); in view of the above, the adjustment related to banknotes in circulation results in corresponding claims on the ECB for the allocation of banknotes, reported under the balance sheet item "Claims related to other operational requirements within the Eurosystem" (see Note 13).

13.5 CLAIMS RELATED TO OTHER OPERATIONAL REQUIREMENTS WITHIN THE EUROSYSTEM

Claims related to other operational requirements within the Eurosystem comprise claims on the ECB associated with the net result of pooling of monetary income and distribution of the interim profit of the ECB.

Monetary income received by Latvijas Banka in 2014 was higher than its monetary income pooled. It resulted in a claim on the ECB associated with the net result of pooling of monetary income, standing at 31 953 thousand euro at the end of 2014 (see also Notes 2.28 and 38).

Claims for the ECB's interim profit distribution in the amount of 3 390 thousand euro are set as per Latvijas Banka's ECB capital key (see also Notes 2.27 and 37).

14. OTHER ASSETS

(in thousands of euro)

	Note	**2014**	2013
Fixed assets	14.1	**40 256**	42 971
Participating interest in the Bank for International Settlement	14.2	**28 176**	28 447
Accrued income on debt securities		**17 871**	18 685
OTC financial derivative contracts and spot exchange rate contracts	24	**2 638**	18 255
Intangible assets	14.3	**1 815**	657
Prepaid expenses		**875**	820
Other accrued income		**391**	2
Other		**433**	282
Total		**92 455**	110 119

14.1 FIXED ASSETS AND LEASING

(in thousands of euro)

	Buildings, improvement of territory, and land	Furniture and office equipment	Computer and telecommunication equipment	Cash processing equipment	Transport vehicles	Other fixed assets	Total
As at 31 December 2012							
Cost	58 947	5 117	4 551	6 521	1 669	8 206	85 011
Accumulated depreciation	–20 559	–3 880	–3 368	–4 148	–1 175	–6 404	–39 534
Net book value	38 388	1 237	1 183	2 373	494	1 802	45 477
During 2013							
Additions	124	55	326	514	21	88	1 128
Change in classification	–	–	–	–	–30	–1	–31
Disposals and write-offs	–	–28	–138	–14	–	–238	–418
Net change in cost	124	27	188	500	–9	–151	679
Depreciation charge	–2 274	–138	–366	–341	–58	–425	–3 602
Change in classification	–	–	–	–	30	–30	–
Accumulated depreciation on disposals and write-offs	–	28	137	14	–	238	417
Net change in accumulated depreciation	–2 274	–110	–229	–327	–28	–217	–3 185
As at 31 December 2013							
Cost	59 071	5 144	4 739	7 021	1 660	8 055	85 690
Accumulated depreciation	–22 833	–3 990	–3 597	–4 475	–1 203	–6 621	–42 719
Net book value	36 238	1 154	1 142	2 546	457	1 434	42 971
During 2014							
Additions	212	82	832	356	65	86	1 633
Change in classification	–	–179	–	179	–	–	–
Disposals and write-offs	–2 026	–50	–548	–113	–84	–284	–3 105
Net change in cost	–1 814	–147	284	422	–19	–198	–1 472
Depreciation charge	–2 139	–144	–387	–430	–62	–307	–3 469
Change in classification	–	178	–	–178	–	–	–
Accumulated depreciation on disposals and write-offs	1 167	47	547	113	84	268	2 226
Net change in accumulated depreciation	–972	81	160	–495	22	–39	–1 243
As at 31 December 2014							
Cost	57 257	4 997	5 023	7 443	1 641	7 857	84 218
Accumulated depreciation	–23 805	–3 909	–3 437	–4 970	–1 181	–6 660	–43 962
Net book value	**33 452**	**1 088**	**1 586**	**2 473**	**460**	**1 197**	**40 256**

At the end of 2014, the total cadastral value of land under the ownership and possession of Latvijas Banka was 2 962 thousand euro (2 712 thousand euro at the end of 2013; the change is related to a revision in the cadastral value of land). Land is reported in the balance sheet of Latvijas Banka at cost (2 375 thousand euro at the end of 2014 and 2013).

At the end of 2014, Latvijas Banka's contractual commitments related to acquisition of fixed assets were 18 thousand euro (300 thousand euro at the end of 2013).

A small share of Latvijas Banka's fixed assets are given on lease. Latvijas Banka's assets subject to leases are premises and equipment. In the balance sheet they are reported as fixed assets. Asset lease agreements where Latvijas Banka acts as a lessor are operating leases. Lease payments, except those that are directly transferred to the state budget, are recognised in the profit and loss statement proportionally over the term of the respective agreement. The depreciation of the assets given on lease is calculated on the basis of the depreciation policy described in Note 2.18 and reported in the profit and loss statement as depreciation charges.

Carrying amount of assets given on lease at the end of 2014 and 2013 was as follows:

(in thousands of euro)

As at 31 December 2013	
Cost	1 660
Accumulated depreciation	–874
Net book value	786
As at 31 December 2014	
Cost	**997**
Accumulated depreciation	**–533**
Net book value	**464**

14.2 PARTICIPATING INTEREST IN THE BANK FOR INTERNATIONAL SETTLEMENTS

At the end of 2014 and 2013, Latvijas Banka owned 1 070 shares in the BIS, which corresponded to 0.19% of the total subscribed and paid-up BIS capital.

The total nominal value of Latvijas Banka's shareholding in the BIS is 5 350 thousand SDR (the nominal value per share is 5 thousand SDR), paid up in the amount of 1 338 thousand SDR or 25% (see also Note 46). At the end of 2014 and 2013, the BIS shareholding is reported in Latvijas Banka's balance sheet at fair value. The shares in the BIS are not traded in the public securities market. In the opinion of Latvijas Banka's management, the most appropriate method for establishing the fair value of the BIS shares is the use of 70% of the BIS net asset value based on the latest audited financial statements of the BIS. The BIS applied this valuation method for calculating the issue price of its shares; the International Court at the Hague has also recognised it as appropriate for the valuation of shares when repurchasing them from former private shareholders of the BIS. Pursuant to the Statutes of the BIS, only central banks can be shareholders in the BIS. At the end of 2014, the fair value of BIS shares was 28 176 thousand euro (28 447 thousand euro at the end of 2013).

14.3 INTANGIBLE ASSETS

(in thousands of euro)

As at 31 December 2012	
Cost	6 011
Accumulated amortisation	–5 434
Net book value	577
During 2013	
Additions	223
Change in classification	31
Derecognised intangible assets	–26
Net change in cost	228
Amortisation charge	–174
Accumulated amortisation on derecognised intangible assets	26
Net change in accumulated amortisation	–148

(cont.)	(in thousands of euro)
As at 31 December 2013	
Cost	6 239
Accumulated amortisation	–5 582
Net book value	657
During 2014	
Additions	1 374
Amortisation charge	–216
As at 31 December 2014	
Cost	7 613
Accumulated amortisation	–5 798
Net book value	**1 815**

15. BANKNOTES IN CIRCULATION

(in thousands of euro)

	2014	2013
Euro banknotes	**3 771 356**	–
Euro banknotes issued by Latvijas Banka	**691 986**	–
Adjustment for banknote allocation in the Eurosystem	**3 079 370**	–
Lats banknotes	**77 814**	801 869
Total	**3 849 170**	801 869

In 2014, an increase in banknotes in circulation relates to the reporting of the adjustment for banknote allocation in the Eurosystem on the balance sheet of Latvijas Banka following Latvijas Banka's joining the Eurosystem on 1 January 2014 (see also Note 2.21). The euro coins issued by Latvijas Banka and the non-exchanged lats coins are reported under the balance sheet caption "Other liabilities" (see also Note 22).

16. LIABILITIES TO EURO AREA CREDIT INSTITUTIONS RELATED TO MONETARY POLICY OPERATIONS DENOMINATED IN EURO

16.1 CURRENT ACCOUNTS (COVERING THE MINIMUM RESERVE SYSTEM)
Current accounts contain the credit balances on the transaction accounts of credit institutions that are required to hold minimum reserves. Minimum reserve balances have been remunerated at the latest available interest rate used by the Eurosystem in its tenders for main refinancing operations. Since June 2014 the reserves held in excess of the minimum requirements are remunerated at the lower rate of either zero per cent or the ECB's deposit facility rate. At the end of 2014 balance on the current accounts placed with Latvijas Banka was 2 073 356 thousand euro (4 013 974 thousand euro at the end of 2013).

16.2 DEPOSIT FACILITY
Deposit facility is a standing facility of the Eurosystem used by credit institutions to place their overnight deposits at a pre-specified rate. At the end of 2014 the balance on Latvijas Banka's balance sheet item "Deposit facility" was 350 000 thousand euro. In 2013, deposit facility was used in line with the Regulation for the Use of Monetary Policy Instruments of Latvijas Banka, in force by the time Latvijas Banka joined the Eurosystem (113 830 thousand euro at the end of 2013).

17. OTHER LIABILITIES TO EURO AREA CREDIT INSTITUTIONS DENOMINATED IN EURO

Other liabilities to euro area credit institutions denominated in euro resulted from funds received as collateral for forward exchange contracts accounting for 540 thousand euro at the end of 2014 (0 at the end of 2013).

18. LIABILITIES TO OTHER EURO AREA RESIDENTS DENOMINATED IN EURO

Liabilities to other euro area residents denominated in euro comprise demand deposits by the Latvian government and other financial institutions. Government deposits comprise the Treasury demand deposits received by Latvijas Banka acting as the financial agent of the Latvian government (see also Note 43).

Deposits of other financial institutions mostly include the funds of the FCMC and the Deposit Guarantee Fund and Fund for the Protection of the Insured, both managed by the FCMC, in the amount of 73 562 thousand euro (11 437 thousand euro at the end of 2013).

19. LIABILITIES TO NON-EURO AREA RESIDENTS DENOMINATED IN EURO

Liabilities to non-euro area residents denominated in euro mostly comprise funds on the EC account for settlement in euro. The EC account is used by the EC for the distribution of EU budgetary funds.

(in thousands of euro)

	2014	2013
European Commission	**23 052**	7 361
International Monetary Fund	**444**	420
Other financial instituions	**490**	4 904
Total	**23 986**	12 685

20. LIABILITIES TO EURO AREA RESIDENTS DENOMINATED IN FOREIGN CURRENCY

Liabilities to euro area residents denominated in foreign currency comprise demand deposits of the Latvian government in foreign currency standing at 144 579 thousand euro at the end of 2014 (138 070 thousand euro at the end of 2013; see also Note 43).

21. LIABILITIES TO NON-EURO AREA RESIDENTS DENOMINATED IN FOREIGN CURRENCY

At the end of 2013, liabilities to non-euro area residents denominated in foreign currency resulted from funds received as collateral for transactions in financial derivatives.

22. OTHER LIABILITIES

(in thousands of euro)

	Note	**2014**	2013
Lats coins in circulations	22.1	**64 741**	95 615
Euro coins in circulation	22.1	**43 742**	–
OTC financial derivative contracts and spot exchange rate contracts	24	**51 894**	9 674
Provisions for market risk and credit risk	36	**14 800**	–
Accrued expense and similar liabilities		**3 801**	3 619
Tax liabilities	22.2	**175**	211
Other		**936**	2 909
Total		**180 089**	112 028

22.1 COINS IN CIRCULATION

Apart from the lats and euro circulation coins issued by Latvijas Banka and reported on the liabilities side of the balance sheet, euro collector coins, lats collector coins and precious metal circulation coins were also in circulation with the total nominal value of 5 627 thousand euro at the end of 2014 (5 442 thousand euro at the end of 2013). The above coins in circulation have not been reported under the balance sheet caption "Other liabilities" (see also Note 2.22).

22.2 TAX LIABILITIES

At the end of 2014 and 2013, tax liabilities of Latvijas Banka were as follows:

(in thousands of euro)

	Personal income tax	Compulsory social security contributions (by employer)	Compulsory social security contributions (by employee)	Tax on real estate	Value added tax	Other taxes and duties	Total
Liabilities as at 31 December 2012	–	–	–	–	137	0	137
During 2013							
Calculated	2 940	3 668	1 618	142	747	6	9 121
Decrease in deferred liabilities	–	–125	–	–	–	–	–125
Paid	–2 940	–3 542	–1 618	–142	–585	–3	–8 830
Recalculation of liabilities	–	–	–	–	–92	–	–92
Liabilities as at 31 December 2013	–	1	–	–	207	3	211
During 2014							
Calculated	3 288	3 382	1 547	154	827	2	9 200
Increase in deferred liabilities	–	94	–	–	–	–	94
Paid	–3 288	–3 477	–1 547	–154	–859	–5	–9 330
Liabilities as at 31 December 2014	**–**	**–**	**–**	**–**	**175**	**0**	**175**

In addition to the tax payments indicated herein, Latvijas Banka transfers to the state budget 65% of the profit for the reporting year (38 349 thousand euro in 2014; 31 410 thousand euro in 2013; see also Notes 23 and 43). The transfer includes the payment for the usage of state capital. Latvijas Banka is not subject to corporate income tax.

23. CAPITAL AND RESERVES

(in thousands of euro)

	Nominal capital	Reserve capital	Valuation account	Profit of the reporting year	Capital and reserves
As at 31 December 2012	35 572	227 371	203 820	48 322	515 085
During 2013					
Revaluation, realisation, and write-downs	x	x	–72 680	x	–72 680
Profit appropriated to the state budget	x	x	x	–31 410	–31 410
Profit transferred to the reserve capital	x	16 912	x	–16 912	0
Profit of the reporting year	x	x	x	58 998	58 998
As at 31 December 2013	35 572	244 283	131 140	58 998	469 993
During 2014					
Revaluation, realisation, and write-downs	x	x	10 485	x	10 485
Profit appropriated to the state budget	x	x	x	–38 349	–38 349
Profit transferred to the reserve capital	x	20 649	x	–20 649	0
Increase in the nominal capital	64 428	–64 428	x	x	0
Profit of the reporting year	x	x	x	36 760	36 760
As at 31 December 2014	**100 000**	**200 504**	**141 625**	**36 760**	**478 889**

The capital of Latvijas Banka is comprised of the nominal capital, reserve capital and the valuation account, as well as the undistributed profit of the reporting year.

The legislation does not provide for any capital adequacy requirements for Latvijas Banka; nevertheless, the amount of its capital should be adequate to promote credibility of the monetary policy implemented by Latvijas Banka, and to ensure implementation of its operations and financial independence when performing the tasks set forth by the Statute of the ESCB and the ECB and the Law on Latvijas Banka. The implementation of the monetary policy as well as exposure to other financial and operational risks may adversely affect Latvijas Banka's income or result in losses to be covered from the capital and reserves of Latvijas Banka.

The nominal capital of Latvijas Banka is comprised of the state-allotted resources, transfers from the reserve capital and Latvijas Banka's profit allocations. Pursuant to Paragraph 2 of the transitional provisions of the Law on Latvijas Banka, on 3 January 2014 Latvijas Banka transferred part of its reserve capital into its nominal capital, raising it to 100 000 thousand euro.

The Law on Latvijas Banka establishes that a part of Latvijas Banka's profit of the reporting year, calculated by applying the same percentage as the tax rate set for resident corporate entities of Latvia by the Law on Corporate Income Tax, together with a payment in the amount of 50% of the profit of the reporting year for the usage of state capital shall be transferred to the state budget, as well as that the Council of Latvijas Banka, upon approving the annual report, may make a decision on reducing the percentage share of the payment for the usage of state capital where it is necessary for increasing the reserve capital of Latvijas Banka in relation to the financial risks Latvijas Banka is exposed to when executing its tasks. At the end of 2014 and 2013, the corporate income tax rate applicable to residents of Latvia was 15%. Therefore, unless the Council of Latvijas Banka decides otherwise, 65% of Latvijas Banka's profit of the reporting or 23 894 thousand euro year shall be transferred to the state budget within 15 days following the approval of the Annual Report of 2014 by the Council of Latvijas Banka.

Latvijas Banka's profit remaining after making the above deductions shall be transferred to the reserve capital as prescribed by the Law on Latvijas Banka. The reserve capital shall be formed to cover potential losses.

The valuation account comprises the positive result on revaluation of the financial instruments and gold. The accounting policy, harmonised with the principal accounting policies established by the ECB's legal framework for accounting and financial reporting and described in Note 2 stipulates that the realised gains are recognised in the profit and loss statement only after the disposal of a financial instrument or settlement while unrealised gains are recorded under the balance sheet caption "Capital and reserves" as the revaluation reserve, thus facilitating the preservation of the capital under the impact of financial instrument price, interest rate and exchange rate fluctuations.

In 2014 and 2013, changes in the valuation account were as follows:

(in thousands of euro)

	2014	Write-downs	Change in classification	Revaluation	Realisation	2013
Initial valuation account	**41 495**	x	23 055	x	–15 735	34 175
Revaluation reserve for equity instruments	**25 667**	–	–	–270	–	25 937
Result on revaluation of foreign currencies and gold	**28 509**	133	–23 055	8 350	–	43 081
Result on revaluation of securities	**45 954**	1 512	–	27 926	–11 431	27 947
Total	**141 625**	1 645	0	36 006	–27 166	131 140

(in thousands of euro)

	2013	Write-downs	Revaluation	Realisation	2012
Initial valuation account	34 175	x	x	–	34 175
Revaluation reserve for equity instruments	25 937	–	1	–	25 936
Result on revaluation of foreign currencies and gold	43 081	154	–34 024	–2 436	79 387
Result on revaluation of securities	27 947	6 788	–9 430	–33 733	64 322
Total	131 140	6 942	–43 453	–36 169	203 820

In accordance with the ECB's legal framework for accounting and financial reporting, on 1 January 2014 Latvijas Banka reclassified the accumulated result on revaluation of foreign currencies to the initial valuation account. The initial valuation account also comprises the accumulated result on revaluation of financial instruments and gold prior to the change in the accounting policy on 1 January 2007.

The balance on the initial valuation account is recognised in the profit and loss statement to compensate lower remuneration for claims related to the banknote allocation within the Eurosystem as per the coefficients applied in accordance with the decisions of the Governing Council of the ECB for the calculation of the remuneration adjustment for claims related to the banknote allocation within the Eurosystem in the first six years after an NCB joins the Eurosystem (see Note 33). The amount to be recognised in the profit and loss statement for the respective year is calculated by multiplying the balance on the initial valuation account as at 1 January 2014 with the share of the coefficient for calculating the compensation amount for the respective year in the total coefficients (indicated in Note 33) during the transition period when the adjustment amounts for the claims on banknote allocation in the Eurosystem are calculated.

The revaluation reserve for equity instruments has been established to account for the result on revaluation of the BIS shares.

24. DERIVATIVE FINANCIAL INSTRUMENTS AND SPOT EXCHANGE RATE CONTRACTS

Latvijas Banka enters into forward and spot exchange rate contracts, currency and interest rate swap arrangements and interest rate and currency future contracts in order to manage interest rate and currency risks associated with Latvijas Banka's investments.

(in thousands of euro)

	Contract or notional amount		Book value			
			Assets		Liabilities	
	2014	2013	**2014**	2013	**2014**	2013
OTC financial derivative and spot exchange rate contracts						
Forward exchange rate contracts and currency swap arrangements	**3 451 371**	3 543 833	**1 693**	14 312	**51 463**	9 167
Spot exchange rate contracts	**105 401**	266 706	**–**	3 650	**289**	–
Forward transactions in securities	**382 093**	244 674	**945**	293	**142**	507
Swap arrangements	**6 460**	–	**x**	–	**x**	–
Total	**x**	x	**2 638**	18 255	**51 894**	9 674
Traded financial derivative contracts						
Interest rate future contracts	**439 495**	991 430	**x**	x	**x**	x
Currency future contracts	**187 615**	183 855	**x**	x	**x**	x

The book value of the OTC financial derivative contracts and spot exchange rate contracts is reported under the balance sheet captions "Other assets" or "Other liabilities" (see also Notes 14 and 22). Since settlement has been made for the change in the fair value of future contracts, the change is reported as demand deposits under the respective balance sheet asset caption.

The reconciliation of the book value and net fair value of OTC contracts at the end of 2014 and 2013 was as follows:

(in thousands of euro)

	Net fair value		Net book value		Difference	
	2014	2013	**2014**	2013	**2014**	2013
OTC financial derivative and spot exchange rate contracts						
Forward exchange rate contracts and currency swap arrangements	**–50 576**	5 194	**–49 770**	5 145	**–806**	49
Spot exchange rate contracts	**–289**	3 651	**–289**	3 650	**–**	1
Total	**–50 865**	8 845	**–50 059**	8 795	**–806**	50

MAJOR RISKS AND PRINCIPLES FOR THEIR MANAGEMENT

25. RISK MANAGEMENT

Financial and operational risks are the main risks associated with the activities of Latvijas Banka. Management of Latvijas Banka's risks is organised and implemented according to the Risk Management Policy of Latvijas Banka approved by the Council of Latvijas Banka. Therefore, the Board of Latvijas Banka has established a risk management framework under the basic principles set forth by the Council of Latvijas Banka, which is improved in line with the developments in financial markets and operations of Latvijas Banka as well as changes in external environment. Management of Latvijas Banka's financial and operational risks is reviewed by the Internal Audit Department and is monitored by the Security Supervision Commission, Audit Committee, and Budget Commission of Latvijas Banka, each of which is comprised of Members of the Council of Latvijas Banka.

25.1 FINANCIAL RISKS

Market risk (price, interest rate and currency risks), credit and liquidity risks are the most significant financial risks Latvijas Banka is exposed to in its daily activities.

Latvijas Banka manages financial risks related to its investments in line with the Procedure adopted by the Council of Latvijas Banka; the basic principles of its investment policy are described in Note 4. Investments are managed by classifying them into different investment portfolios. Parameters for a benchmark reflecting the acceptable level of financial risks and return target are set out for each financial instrument portfolio. The Risk Management Division of the Market Operations Department monitors the investment compliance with the established requirements.

For the purpose of investment management, including management of the related financial risks, the Investment Committee of Latvijas Banka develops an investment management strategy, approves tactical decisions and sets detailed limits for financial risks, as well as oversees the operation of the external managers. The Investment Committee of Latvijas Banka reviews the investment strategy once a quarter, and on a weekly basis receives and reviews reports on and forecasts for developments in financial markets, prepared by financial investment portfolio managers, reports by financial risk managers, and approves the investment management tactical decisions for the forthcoming week. Once every two months the Market Operations Department informs the Council of Latvijas Banka about the results of investment management.

25.1.1 MARKET RISK
Market risk is exposure to losses due to adverse changes in financial markets (for example, movements in interest rates or exchange rates).

Latvijas Banka is exposed to interest rate risk primarily due to investing in foreign debt securities and interest rate derivatives that are subject to interest rate fluctuations and used within the course of investment management. Latvijas Banka manages interest rate risk by using a modified duration limit set individually for each investment portfolio.

Latvijas Banka's exposure to currency risk is determined by its investment structure, which cannot be formed in compliance with Latvijas Banka's liability parameters. Latvijas Banka manages currency risk by determining open currency position limits and using tracking error. Tracking error is calculated as the expected annualised standard deviation of the difference in return between the investment portfolio and the respective benchmark. The aggregate market and credit risk of portfolios managed against multi-currency fixed income securities benchmark and asset-backed securities benchmark (see Note 4) is managed by determining the tracking error limit. Tracking error in 2014 and 2013 is disclosed in Note 28.

For investment portfolios, except for portfolios of borrowed funds, the benchmark currency is the euro. For portfolios of borrowed funds, the benchmark currency structure is formed in compliance with the respective currency. Deviations from the benchmark currency structure give rise to the open currency position. In order to achieve the compliance of open foreign currency positions with the limits, Latvijas Banka hedges the currency risk by using forward exchange rate contracts, currency swap arrangements, and currency future contracts.

The Risk Management Division of the Market Operations Department monitors the compliance of the modified duration limits and open currency positions with the Procedure and the related resolutions passed by the Investment Committee of Latvijas Banka.

Latvijas Banka's exposure to market risk (as at the end of 2014 and 2013) is disclosed in Notes 26–28.

25.1.2 CREDIT RISK
Credit risk is exposure to losses resulting from counterparty default. Latvijas Banka's exposure to credit risk results mainly from investments in foreign financial instruments and short-term lending to domestic credit institutions.

Latvijas Banka manages exposure to credit risk related to investments made in foreign financial instruments by establishing limits on investments of different credit quality. Credit quality is evaluated on the basis of ratings assigned by the international credit rating agencies Fitch Ratings, Moody's Investors Service and Standard & Poor's. Latvijas Banka is allowed to invest in financial instruments of certain credit quality of the OECD countries. Limits are also set on the maximum investment in financial instruments of the same class and counterparty, as well as in financial instruments of one issuer. Forward transactions in mortgage-backed securities are partly secured with short-term financial instruments. To hedge the credit risk associated with OTC derivative counterparties, Latvijas Banka and the respective counterparties enter into Master Agreements of International Swaps and Derivatives Association, Inc. (ISDA Master Agreement) with Credit Support Annex, and the external reserves managers enter with their counterparties into Treasury Market Practices Group (TMPG) Master Securities Forward Transaction Agreements. In order to monitor Latvijas Banka's credit risk exposure associated with its investments, the Risk Management Division of the Market Operations Department monitors compliance with the Procedure, adopted by the Council of Latvijas Banka.

In 2014, loans granted to credit institutions in monetary policy operations were secured by securities collateral in compliance with the ECB requirements (in 2013 loans were secured by collateral of Latvian government securities and private sector debt securities in accordance with the requirements established by the Council of Latvijas Banka). The Market Operations Department reviews the compliance of credit ratings assigned to issuers of the securities provided as collateral with the requirements of the Council of Latvijas Banka and monitors the adequacy of collateral of the respective loans on a regular basis.

Latvijas Banka's exposure to market risk (as at the end of 2014 and 2013) is disclosed in Notes 30–32.

25.1.3 LIQUIDITY RISK

Liquidity risk is associated with a failure to dispose investment in a short time and at a competitive market price. Along with participation in the euro area, the need for liquidity as well as the risk associated with a failure to meet liabilities in a timely manner has moderated. Following its investment strategy, Latvijas Banka manages liquidity risk by investing in liquid debt securities issued by international institutions, foreign governments and the corporate sector, short-term deposits with foreign financial institutions and other financial instruments. The liquidity profile of Latvijas Banka's assets and liabilities as at the end of 2014 and 2013 is disclosed in Note 29.

Liquidity risk can be limited by investment diversification. Latvijas Banka manages liquidity risk also by setting limits on the maximum investment in financial instruments of the same class and in financial instruments of the same issuer.

25.2 OPERATIONAL RISKS

Operational risk is exposure to financial and other losses resulting from inadequate or failed internal processes, individual's actions, operation of information or technical systems, or from external events.

Latvijas Banka's operational risk management is implemented by the Board of Latvijas Banka according to the basic principles defined by the Council of Latvijas Banka. The Board of Latvijas Banka has established the Committee for Managing Latvijas Banka's Operational Risks to coordinate, on a day-to-day basis, the activities under the operational risk management process and to provide support to the Board of Latvijas Banka on operational risk management issues. The Committee is presided by a Member of the Board of Latvijas Banka and is composed of the Business Continuity Manager, Information Security Manager, Information Systems Security Manager, the Head of the Technical Support Department, and the Head of the Security Department.

The security management of the information and information systems of Latvijas Banka is organised and implemented in accordance with the Information and Information Systems Security Policy of Latvijas Banka approved by Latvijas Banka's Council. In order to ensure confidentiality, access to and integrity of information, information at Latvijas Banka is classified on the basis of its level of confidentiality and accessibility and is protected against its unauthorised processing, use or disclosure. The information systems of Latvijas Banka are classified into levels depending on their impact on the implementation of processes and the confidentiality, integrity and availability requirements regarding the processed information. The owners of Latvijas Banka's information systems in cooperation with the Information Systems Department have established rules for the usage and access rights of the information system, as well as ensure the implementation of risk analysis of the respective information system. The

Head of Information Systems Department ensures that the functionality and performance of Latvijas Banka's information system infrastructure complies with the requirements set for the information systems, as well as the infrastructure's safe and continuous operation. Latvijas Banka conducts, on a regular basis, analysis of information systems security risks and improves security measures and tools.

The management of Latvijas Banka's business continuity is organised and conducted in accordance with the Business Continuity Management Policy of Latvijas Banka, approved by the Council of Latvijas Banka, abiding by the internationally recognised standards and taking into account the ECB recommendations regarding business continuity management.

Latvijas Banka conducts, on a regular basis, educational sessions for employees on information and information systems security, operational risk management and management of business continuity.

The physical security of the officials and employees of Latvijas Banka and an environment protected against physical hazards is organised and ensured on the premises of Latvijas Banka and during transportation of cash and other valuables in accordance with the Physical Security Policy of Latvijas Banka , adopted by the Council of Latvijas Banka, and other legislative acts of Latvijas Banka regulating the physical security management procedure for Latvijas Banka. Fire training is organised for the staff of Latvijas Banka, and training for the employees of the Security Department to maintain and improve their qualification is organised on a regular basis.

In order to limit the implications of operational risks, Latvijas Banka is insured against a possible impact of certain types of operational risks.

In 2014 and 2013, operational risks were appropriately managed and did not substantially hamper Latvijas Banka's operation.

26. CURRENCY PROFILE

(in thousands of euro)

	EUR	USD	JPY	CAD	GBP	Gold	Other	Total
As at 31 December 2014								
Total assets	4 928 769	1 689 358	385 456	303 995	299 815	210 774	206 341	8 024 508
Total liabilities	7 929 904	66 766	10 148	186	17 402	–	102	8 024 508
Net position on balance sheet	–3 001 135	1 622 592	375 308	303 809	282 413	210 774	206 239	0
Net position on financial instruments' off-balance sheet accounts	2 950 588	–1 618 727	–373 470	–307 431	–278 226	–210 790	–211 200	–49 256
Net position on balance sheet and off-balance sheet accounts	**–50 547**	**3 865**	**1 838**	**–3 622**	**4 187**	**–16**	**–4 961**	**–49 256**
Profile of the net position on balance sheet and off-balance sheet accounts (%)	**–0.6**	**0**	**0**	**0**	**0.1**	**0**	**–0.1**	**–0.6**
Benchmark currency structure (%)	0	0	0	0	0	0	0	0
As at 31 December 2013[1]								
Total assets	2 870 598	1 643 635	377 710	302 646	280 976	217 923	196 316	5 889 804
Total liabilities	5 801 148	61 306	10 487	165	16 640	–	58	5 889 804
Net position on balance sheet	–2 930 550	1 582 329	367 223	302 481	264 336	217 923	196 258	0

[1] Assets and liabilities denominated in lats as at 31 December 2013 are reported in euro.

(cont.) (in thousands of euro)

	EUR	USD	JPY	CAD	GBP	Gold	Other	Total
Net position on financial instruments' off-balance sheet accounts	2 740 997	–1 568 987	–187 714	–300 862	–262 365	–217 919	–194 569	8 581
Net position on balance sheet and off-balance sheet accounts	–189 553	13 342	179 509	1 619	1 971	4	1 689	8 581
Profile of the net position on balance sheet and off-balance sheet accounts (%)	–3.2	0.2	3.0	0	0	0	0	0
Benchmark currency structure (%)	0	0	0	0	0	0	0	0

27. REPRICING MATURITY

The table below reflects Latvijas Banka's assets, liabilities and off-balance sheet accounts sensitive to a change in interest rates. Items reported in this table are stated at carrying amounts, except for interest rate and currency future contracts and forward transactions in securities that are stated at notional amounts and included in off-balance sheet accounts. A nearest contractual interest repricing or residual maturity date to 31 December of the reporting year is used for categorising items reported in this table.

(in thousands of euro)

	Up to 3 months	3–6 months	6–12 months	1–3 years	Over 3 years	Total
As at 31 December 2014						
Claims on non-euro area residents denominated in foreign currency	592 578	29 700	53 289	934 682	682 825	2 293 074
Claims on euro area residents denominated in foreign currency	36 037	–	–	209 065	238 082	483 184
Claims on non-euro area residents denominated in euro	39 830	25 470	–	110 965	33 165	209 430
Lending to euro area credit institutions related to monetary policy operations denominated in euro	–	–	–	–	85 520	85 520
Other claims on euro area credit institutions denominated in euro	4 458	–	–	–	–	4 458
Securities of euro area residents denominated in euro	405 212	37 388	–	332 484	320 362	1 095 446
Intra-Eurosystem claims	3 278 193	–	–	–	–	3 278 193
Other assets	1 329	985	69	8 697	5 956	17 036
Total interest-sensitive assets	**4 357 637**	**93 543**	**53 358**	**1 595 893**	**1 365 910**	**7 466 341**
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	2 423 356	–	–	–	–	2 423 356
Other liabilities to euro area credit institutions denominated in euro	540	–	–	–	–	540
Liabilities to other euro area residents denominated in euro	50 903	–	–	–	–	50 903
Liabilities to euro area residents denominated in foreign currency	23 502	–	–	–	–	23 502
Intra-Eurosystem liabilities	796 980	–	–	–	–	796 980
Total interest-sensitive liabilities	**3 295 281**	**–**	**–**	**–**	**–**	**3 295 281**
Net position on balance sheet	1 062 356	93 543	53 358	1 595 893	1 365 910	4 171 060
Assets on financial instruments' off-balance sheet accounts	4 004 686	–	–	280 929	283 887	4 569 502
Liabilities on financial instruments' off-balance sheet accounts	4 364 440	9 884	1 235	1 977	241 222	4 618 758
Net position on balance sheet and off-balance sheet accounts	**702 602**	**83 659**	**52 123**	**1 874 845**	**1 408 575**	**4 121 804**

(cont.) (in thousands of euro)

	Up to 3 months	3–6 months	6–12 months	1–3 years	Over 3 years	Total
As at 31 December 2013						
Total interest-sensitive assets	2 673 293	69 366	188 760	1 576 669	1 139 420	5 647 508
Total interest-sensitive liabilities	3 178 757	–	–	–	–	3 178 757
Net position on balance sheet	–505 464	69 366	188 760	1 576 669	1 139 420	2 468 751
Assets on financial instruments' off-balance sheet accounts	4 424 435	–	–	642 624	172 361	5 239 420
Liabilities on financial instruments' off-balance sheet accounts	4 809 718	–	–	69 614	351 506	5 230 838
Net position on balance sheet and off-balance sheet accounts	–890 748	69 366	188 760	2 149 679	960 275	2 477 332

28. TRACKING ERROR

The exposure to aggregate market risk and credit risk of investments, included in portfolios managed against multi-currency fixed income securities benchmark and asset-backed securities benchmark is characterised by the tracking error, which is measured as the expected annualised standard deviation of the difference in return between the investment portfolio and the respective benchmark (see also Note 25.1). At the end of 2014 and 2013, the actual (ex-post) tracking errors of the portfolios managed against multi-currency fixed income securities benchmark were 19 basis points and 23 basis points respectively, whereas the tracking errors of the portfolios managed against asset-backed securities benchmark were 66 basis points and 94 basis points respectively.

The expected (ex-ante) tracking error lay within the following basis point intervals during the year:

	Book value (at the end of the year; in thousands of euro)	Expected tracking error (number of business days)			
		10–39	40–69	70–99	100–110
During 2014					
Portfolios managed against multi-currency fixed income securities benchmark	3 665 508	249	–	–	–
Portfolios managed against asset-backed securities benchmark	267 672	–	41	208	–
During 2013					
Portfolios managed against multi-currency fixed income securities benchmark	3 792 126	158	92	–	–
Portfolios managed against asset-backed securities benchmark	255 363	–	145	93	12

29. LIQUIDITY PROFILE

In the liquidity profile, asset items are reported on the basis of Latvijas Banka's capability to convert them into cash. Liabilities items are reported by their expected settlement date.

(in thousands of euro)

	Up to 3 months	Over 3 months	No fixed maturity	**Total**
As at 31 December 2014				
Assets				
Gold and gold receivables	210 774	–	–	**210 774**
Claims on non-euro area residents denominated in foreign currency	2 441 368	–	–	**2 441 368**
Claims on euro area residents denominated in foreign currency	486 242	–	–	**486 242**
Claims on non-euro area residents denominated in euro	214 953	–	–	**214 953**
Lending to euro area credit institutions related to monetary policy operations denominated in euro	–	85 520	–	**85 520**
Other claims on euro area credit institutions denominated in euro	4 475	–	–	**4 475**
Securities of euro area residents denominated in euro	1 095 446	–	–	**1 095 446**
Intra-Eurosystem claims	35 343	–	3 357 932	**3 393 275**
Other assets	21 264	–	71 191	**92 455**
Total assets	4 509 865	85 520	3 429 123	**8 024 508**
Liabilities	–			
Banknotes in circulation	–	–	3 849 170	**3 849 170**
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	2 423 356	–	–	**2 423 356**
Other liabilities to euro area credit institutions denominated in euro	540	–	–	**540**
Liabilities to other euro area residents denominated in euro	126 919	–	–	**126 919**
Liabilities to non-euro area residents denominated in euro	23 986	–	–	**23 986**
Liabilities to euro area residents denominated in foreign currency	144 579	–	–	**144 579**
Intra-Eurosystem liabilities	796 980	–	–	**796 980**
Other liabilities	71 580	–	108 509	**180 089**
Total liabilities	3 587 940	–	3 957 679	**7 545 619**
Net position on balance sheet	921 925	85 520	–528 556	**x**

(in thousands of euro)

	Up to 3 months	No fixed maturity	Total
As at 31 December 2013			
Assets			
Gold and gold receivables	217 923	–	217 923
Claims on non-euro area residents denominated in foreign currency	2 370 157	–	2 370 157
Claims on euro area residents denominated in foreign currency	472 800	–	472 800
Claims on non-euro area residents denominated in euro	441 866	–	441 866
Lending to euro area credit institutions related to monetary policy operations denominated in euro	14 229	–	14 229
Other claims on euro area credit institutions denominated in euro	1 295	–	1 295
Securities of euro area residents denominated in euro	1 094 153	–	1 094 153
Intra-Eurosystem claims	1 166 224	1 038	1 167 262
Other assets	37 095	73 024	110 119
Total assets	5 815 742	74 062	5 889 804
Liabilities			
Banknotes in circulation	–	801 869	801 869
Liabilities to euro area credit institutions related to monetary policy			
operations denominated in euro	4 127 804	–	4 127 804
Liabilities to other euro area residents denominated in euro	226 372	–	226 372
Liabilities to non-euro area residents denominated in euro	12 685	–	12 685
Liabilities to euro area residents denominated in foreign currency	138 070	–	138 070
Liabilities to non-euro area residents denominated in foreign currency	983	–	983
Other liabilities	16 369	95 659	112 028
Total liabilities	4 522 283	897 528	5 419 811
Net position on balance sheet	1 293 459	–823 466	x

At the end of 2013, Latvijas Banka had no assets that could not be converted into cash within a period of three months and no liabilities with a maturity of over three months.

30. SECTORAL PROFILE OF ASSETS

	Amount (in thousands of euro)		Percentage (%)	
	2014	2013	**2014**	2013
European Central Bank	**3 393 621**	1 166 697	**42.3**	19.8
Foreign central governments and other governmental institutions	**1 728 885**	1 746 472	**21.5**	29.7
Other foreign financial institutions	**1 391 751**	1 340 280	**17.3**	22.8
Foreign central banks and credit institutions	**964 281**	1 150 741	**12.0**	19.5
International institutions	**326 059**	352 980	**4.1**	6.0
Domestic credit institutions	**85 520**	14 230	**1.1**	0.2
Foreign local governments	**76 882**	37 838	**1.0**	0.6
Non-financial corporations	**14 403**	17 459	**0.2**	0.3
Unclassified assets	**43 106**	63 107	**0.5**	1.1
Total	**8 024 508**	5 889 804	**100.0**	100.0

31. ASSETS BY THEIR LOCATION OR THE COUNTERPARTY'S DOMICILE

	Amount (in thousands of euro)		Percentage (%)	
	2014	2013	**2014**	2013
European Central Bank	**3 393 621**	1 166 697	**42.3**	19.8
Euro area countries	**1 681 741**	1 601 464	**21.0**	27.2
UK	**630 096**	657 745	**7.9**	11.2
US	**531 739**	534 724	**6.6**	9.1
Japan	**407 393**	397 410	**5.1**	6.7
Canada	**380 999**	388 370	**4.7**	6.6
Other European Union countries	**346 537**	317 804	**4.3**	5.4
Other countries and international institutions	**652 382**	825 590	**8.1**	14.0
Total	**8 024 508**	5 889 804	**100.0**	100.0

32. ASSETS BY CREDIT RATING ASSIGNED TO THE COUNTERPARTY

	Amount (in thousands of euro)		Percentage (%)	
	2014	2013	**2014**	2013
European Central Bank	**3 393 621**	1 166 697	**42.3**	19.9
AAA	**2 115 702**	2 611 961	**26.4**	44.3
AA	**1 845 629**	1 602 341	**23.0**	27.2
A	**521 962**	426 231	**6.5**	7.2
BBB	**17 843**	23 613	**0.2**	0.4
Different assets	**129 751**	58 961	**1.6**	1.0
Total	**8 024 508**	5 889 804	**100.0**	100.0

Based on Standard & Poor's credit ratings or other equivalent credit ratings assigned by other international credit rating agency to the counterparty, the above table show the breakdown of Latvijas Banka's assets as at the end of the reporting period. The rating "AAA" is the highest possible long-term creditworthiness rating, which indicates an extremely strong capacity of the counterparty to meet its financial commitments. The rating "AA" confirms the counterparty's very strong capacity and the rating "A" – the counterparty's strong capacity to meet its financial commitments in the long term. "BBB" is a medium grade considered to be the lowest level of investment-grade rating.

PROFIT AND LOSS NOTES

33. NET INTEREST INCOME

(in thousands of euro)

	2014	2013
Interest income	**49 574**	55 989
Interest on deposits	**47 802**	55 988
Interest on monetary policy operations	**19**	1
Interest on intra-Eurosystem claims	**1 753**	–
Interest expense	**–10 775**	–14 136
Interest on deposits	**–7 806**	–11 340
Interest on monetary policy operations	**–831**	–1 046
Interest on customer deposits	**–470**	–1 750
Interest on intra-Eurosystem liabilities	**–1 668**	–
Net interest income	**38 799**	41 853

Net interest income was mainly derived from debt securities. In 2014, net interest income decreased by 3 054 thousand euro in comparison with 2013, mostly on account of the shrinking actual securities yields in 2014 since yields remained at their lows.

Interest income from and interest expense on the intra-Eurosystem claims and liabilities are remunerated by applying the ECB rate on the main refinancing operations and include income from foreign reserves transferred to the ECB, claims on allocation of banknotes in the Eurosystem, as well as income from and expense on claims or liabilities related to TARGET2 settlements.

According to the ECB Governing Council's decision on the allocation of monetary income for first six years following the euro changeover the remunerable part of the claims on banknote allocation in the Eurosystem is reduced in compliance with a definite coefficient to avoid significant NCB income fluctuations. The adjustment of the reduction of the remunerable part of Latvijas Banka's claims on banknote allocation in the Eurosystem in the course of the following six years is as follows:

Reporting year	Coefficient (%)
2014	100.00000
2015	86.06735
2016	70.13472
2017	53.34835
2018	35.98237
2019	18.17225

Lower interest rates in 2014 (see Note 16) and smaller credit institution minimum reserve ratio had a positive impact on the interest expense on monetary policy operations. Interest expense on monetary policy operations also includes the received negative interest on credit institution deposits.

The contraction of interest expense on deposits in 2014 resulted from a change in Latvijas Banka's procedure for interest payment as a result of the application of the Guideline of the ECB of 20 February 2014 on domestic asset and liability management operations by the national central banks (ECB/2014/9) (2014/304/EU) and Guideline of the ECB of 5 June 2014 amending Guideline ECB/2014/9 on domestic asset and liability management operations by the national central banks (ECB/2014/22) (2014/339/EU) (see Note 43) as well as by the reduction of the key ECB interest rates. Interest expense on deposits also includes the received negative interest on deposits.

34. REALISED GAINS/LOSSES FROM FINANCIAL OPERATIONS

Realised gains or losses from financial operations comprise the gains and losses from the disposal of debt securities, as well as realised gains and losses on derivative financial instruments and foreign exchange transactions.

Gains from the disposal of debt securities increased by 2 038 thousand euro in comparison with 2013.

The realised gains and losses from financial operations were negatively affected by the result on derivative financial instruments posting a decrease of 66 173 thousand euro in comparison with 2013, mostly on account of the result of interest rate future contracts as well as the result of currency future contracts concluded for the purpose of hedging currency risks. In view of Latvijas Banka hedging the risks related to gold price and foreign exchange fluctuations, the negative result of the currency future contracts concluded for the purpose of hedging currency and gold price risk exposure is offset in equal value by the positive revaluation result of the hedged balance sheet items reported under the balance sheet caption "Capital and reserves" as the revaluation result of foreign currency and gold, and the realised gains on foreign exchange transactions recognised in the profit and loss statement.

The realised gains or losses from financial operations were positively affected by the write-downs on the initial valuation account (an increase of 15 735 thousand euro in comparison with 2013; see also Note 23).

35. WRITE-DOWNS OF REVALUATION RESULT ON FINANCIAL ASSETS AND POSITIONS

The revaluation result of several debt securities and foreign currency positions at the end of 2014 and 2013 was negative, and it has been recognised in the profit and loss statement while the positive result on the revaluation of debt securities and foreign currency positions has been reported under the balance sheet caption "Capital and reserves" as the revaluation result of securities and foreign currency (see also Note 23).

At the end of 2014, the negative result on revaluation of debt securities amounted to 1 512 thousand euro (6 788 thousand euro at the end of 2013). At the end of 2014, the negative result on revaluation of foreign currencies was 133 thousand euro (154 thousand euro at the end of 2013).

36. PROVISIONS FOR MARKET RISK AND CREDIT RISK

Financial risks of Latvijas Banka relate primarily to its investments in financial instruments, as well as the implementation of the single monetary policy and distribution of the related income and losses stemming from Latvijas Banka's participation in the Eurosystem. Latvijas Banka carries out assessment of its financial risks and financial buffers in compliance with the ECB's common methodology for Eurosystem financial risk assessment. According to the methodology for Eurosystem financial risk assessment, the Expected Shortfall (ES) measure with confidence level of 99% (ES99%) for a risk horizon of one year is used. ES99% describes the losses determined by the average value of 1% of the most unfavourable simulated profitability scenarios.

Based on the above risk estimates, in 2014 the Council of Latvijas Banka decided to establish provisions in the amount of 14 800 thousand euro for market risk and credit risk with regard to investment management transactions of Latvijas Banka. It has been planned to continue accumulating provisions for market risk and credit risk for a longer time period, reaching the targeted amount in five years. The above policy is based on the assessment of the overall level of financial risks, as well as the projected amount of income available for accumulating the provisions. Assessment of the necessary level of provisions takes place on a regular basis; the level of financial risks, the available financial reserves and long-term prospects of the financial market development are taken account of when setting it. Provisions for the market risk and credit risk are reduced when financial risks materialise provided they are not offset against the accumulated revaluation result and other income, as well as when financial risks moderate.

37. INCOME FROM PARTICIPATING INTEREST

Income from participating interest comprises dividends received from the participating interest in the BIS in the amount of 261 thousand euro (388 thousand euro in 2013; see also Note 14.2) and income from the ECB's interim profit distribution in the amount of 3 389 thousand euro (see also Note 2.27).

38. NET RESULT OF POOLING OF MONETARY INCOME

(in thousands of euro)

	2014	2013
Monetary income pooled	**–8 247**	–
Monetary income received	**40 200**	–
Net result of pooling of monetary income	**31 953**	–

39. OTHER OPERATING INCOME

(in thousands of euro)

	2014	2013
Income from disposal of demonetised lats coins	**1 583**	1 296
Income from sale of collector coins	**1 526**	1 655
Other	**557**	548
Total	**3 666**	3 499

40. REMUNERATION AND SOCIAL SECURITY COSTS

(in thousands of euro)

	2014	2013
Remuneration		
Remuneration of Members of the Council and the Board	**–1 557**	–1 259
Remuneration of other personnel	**–15 282**	–14 304
Total remuneration	**–16 839**	–15 563
Social security costs	**–3 382**	–3 669
Total remuneration and social security costs	**–20 221**	–19 232

Remuneration of those Members of the Board of Latvijas Banka who are also Heads of Departments of Latvijas Banka includes remuneration for performance of these duties.

The number of employees in 2014 and 2013 was as follows:

	2014	2013
Number of employees at the end of the year		
Members of the Council and the Board	**13**	14
Other personnel	**527**	559
Total at the end of the year	**540**	573
Average number of employees per period	**569**	567

41. BANKNOTE AND COIN ACQUISITION COSTS

(in thousands of euro)

	2014	2013
Acquisition of circulation coins	**–1 775**	–9 357
Acquisition of collector coins	**–858**	–1 047
Supply of banknotes	**–**	–377
Total	**–2 633**	–10 781

42. OTHER OPERATING EXPENSES

(in thousands of euro)

	2014	2013
Maintenance and operation of information systems	**–2 763**	–2 849
Municipal services	**–944**	–1 013
Disposal of material values	**–837**	–1
Maintenance of buildings, territory and equipment	**–626**	–882
Business travel	**–606**	–470
Information and public relations	**–538**	–911
Risk insurance	**–299**	–334
Telecommunications services and system maintenance	**–235**	–276
Personnel training	**–228**	–258
Acquisition of low value office supplies	**–178**	–232
Transport provision	**–162**	–179
Tax on real estate	**–152**	–139
Event services	**–130**	–525
Other	**–548**	–371
Total	**–8 246**	–8 440

An increase in the expenses of disposal of material values in 2014 is mostly related to the closing down of the Daugavpils Branch.

Other expenses also comprise the remuneration in the amount of 34 thousand euro paid to SIA Ernst & Young Baltic for the audit of 2014 financial statements of Latvijas Banka (34 thousand euro in 2013).

OTHER NOTES

43. TRANSACTIONS WITH THE LATVIAN GOVERNMENT

Latvijas Banka, whose capital is wholly owned by the Republic of Latvia, carries out transactions with the Treasury, acting as the financial agent of the Latvian government. Performing this function, Latvijas Banka services the Treasury's accounts in euro and foreign currencies. Latvijas Banka is independent in making its own decisions on entering into the above transactions. The Treasury demand deposits are recorded under the balance sheet captions "Liabilities to other euro area residents denominated in euro" and "Liabilities to euro area residents denominated in foreign currency".

The interest rates and foreign exchange rates used in the transactions with the Latvian government are market-based according to the ECB's decisions. No commission fees are applied to transactions with the Latvian government.

Pursuant to Guideline of the ECB of 20 February 2014 on domestic asset and liability management operations by the national central banks (ECB/2014/9) (2014/304/EU) and Guideline of the ECB of 5 June 2014 amending Guideline ECB/2014/9 on domestic asset and liability management operations by the national central banks (ECB/2014/22) (2014/339/EU), Latvijas Banka pays remuneration on the Treasury's deposits in euro in the amount of up to 200 million euro as per the euro overnight index average (EONIA) rate standing at 0.144% at the end of 2014. Latvijas Banka pays no remuneration to the Treasury on the total outstanding amount on its settlement accounts in euro and foreign currencies exceeding 200 million euro but applies the deposit facility rate set by the ECB which was –0.2% at the end of 2014.

At the end of 2014 and 2013, the breakdown of Latvijas Banka's liabilities to the Latvian government were as follows:

	Amount (in thousands of euro)	
	2014	2013
Liabilities		
Demand deposits in lats	–	177 867
Demand deposits in euro	**50 900**	24 396
Demand deposits in foreign currencies	**144 579**	138 070
Tax liabilities	**175**	211
Total net liabilities	**195 654**	340 544

In 2014 and 2013, the breakdown of Latvijas Banka's income and expense related to the Latvian government, as well as Latvijas Banka's profit of the previous reporting year appropriated to the state budget was as follows (see also Notes 22.2 and 23):

(in thousands of euro)

	2014	2013
Expense and Latvijas Banka's profit appropriated to the state budget		
Interest on government deposits	**504**	1 737
Taxes	**9 200**	9 121
Profit appropriated to the state budget	**38 349**	31 410
Total expense and Latvijas Banka's profit appropriated to the state budget	**48 053**	42 268

44. PLEDGED ASSETS

Securities and other financial instruments with the market value of 25 142 thousand euro, as at the end of 2014 (14 022 thousand euro at the end of 2013), have been pledged to provide collateral for forward exchange contracts and interest rate and currency future contracts.

45. SECURITIES LENDING

On behalf of Latvijas Banka its agents conclude securities lending transactions, as part of an automatic securities lending programme, where securities held by Latvijas Banka are lent against cash or other securities collateral. Securities lending transactions provide additional income without any material impact on investment liquidity as the securities lent are readily available to Latvijas Banka. The agent administers the securities lending programme and monitors the eligibility of the securities lending and related collateral.

At the end of 2014, the fair value of the securities lent was 305 181 thousand euro (185 864 thousand euro at the end of 2013).

At the end of 2014 and 2013, the fair value of collateral provided in securities lending transactions was as follows:

(in thousands of euro)

	2014	2013
Foreign currency cash	**284 876**	155 364
Debt securities of foreign governments, financial institutions and non-financial corporations	**26 196**	34 946
Total	**311 072**	190 310

Foreign currency cash or securities received in the agent account of Latvijas Banka's automatic securities lending programme as collateral for securities lending transactions is not recognised in Latvijas Banka's balance sheet (see also Note 2.13).

46. CONTINGENT LIABILITIES AND COMMITMENTS

The uncalled portion of the BIS shares held by Latvijas Banka is 75% of their nominal value. These shares are callable following a respective decision of the BIS Board. At the end of 2014 the uncalled portion of the BIS share holding was 4 013 thousand SDR (4 785 thousand euro; 4 013 thousand SDR (4 522 thousand euro) at the end of 2013; see also Note 14.2).

At the end of 2014, Latvijas Banka had issued euro collector coins, lats collector coins and precious metal circulation coins in the nominal value of 5 627 thousand euro (5 442 thousand euro at the end of 2013). These coins may be represented to Latvijas Banka at a nominal value. In the opinion of management of Latvijas Banka, the probability that Latvijas Banka will be required to repurchase these coins from their holders is considered low and no provisions have been made.

47. LAYOUT CHANGES OF FINANCIAL STATEMENTS

Beginning with 2014, Latvijas Banka changed the layout of its balance sheet in line with the one used by the central banks of the Eurosystem. This Note presents the comparison of the previous layout of the published balance sheet as at 31 December 2013 with the changed one, i.e. if the layout used by the central banks of the Eurosystem and applied in drafting the consolidated financial accounts of the Eurosystem had already been applied when drafting the financial statements for 2013.

(in thousands of euro)

	Foreign assets	Domestic assets	Foreign liabilities	Lats in circulation	Domestic liabilities	Capital and reserves	**Total**
Gold and gold receivables	217 923	–	–	–	–	–	**217 923**
Claims on non-euro area residents denominated in foreign currency	2 370 157	–	–	–	–	–	**2 370 157**
Claims on euro area residents denominated in foreign currency	472 800	–	–	–	–	–	**472 800**
Claims on non-euro area residents denominated in euro	441 866	–	–	–	–	–	**441 866**
Lending to euro area credit institutions related to monetary policy operations denominated in euro	–	14 229	–	–	–	–	**14 229**
Other claims on euro area credit institutions denominated in euro	1 295	–	–	–	–	–	**1 295**
Securities of euro area residents denominated in euro	1 094 153	–	–	–	–	–	**1 094 153**
Intra-Eurosystem claims	1 167 262	–	–	–	–	–	**1 167 262**
Other assets	66 103	44 016	–	–	–	–	**110 119**
Total assets	**5 831 559**	**58 245**	**–**	**–**	**–**	**–**	**5 889 804**
Banknotes in circulation	–	–	–	801 869	–	–	**801 869**
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	–	–	–	–	4 127 804	–	**4 127 804**
Liabilities to other euro area residents denominated in euro	–	–	9 900	–	216 472	–	**226 372**
Liabilities to non-euro area residents denominated in euro	–	–	12 685	–	–	–	**12 685**
Liabilities to euro area residents denominated in foreign currency	–	–	–	–	138 070	–	**138 070**
Liabilities to non-euro area residents denominated in foreign currency	–	–	983	–	–	–	**983**
Intra-Eurosystem liabilities	–	–	–	–	–	–	
Other liabilities	–	–	11 553	95 615	4 860	–	**112 028**
Capital and reserves	–	–	–	–	–	469 993	**469 993**
Total liabilities	**–**	**–**	**35 121**	**897 484**	**4 487 206**	**469 993**	**5 889 804**

47.1 COMPARISON OF THE LAYOUT OF FOREIGN ASSETS

(in thousands of euro)

	Gold	Special drawing rights	Convertible foreign currencies	Participating interest in the ECB	Participating interest in the BIS	Other foreign assets	**Foreign assets**
Gold and gold receivables	217 923	–	–	–	–	–	**217 923**
Claims on non-euro area residents denominated in foreign currency	–	136 157	2 234 000	–	–	–	**2 370 157**
Claims on euro area residents denominated in foreign currency	–	–	472 800	–	–	–	**472 800**
Claims on non-euro area residents denominated in euro	–	–	441 866	–	–	–	**441 866**
Other claims on euro area credit institutions denominated in euro	–	–	1 295	–	–	–	**1 295**
Securities of euro area residents denominated in euro	–	–	1 094 153	–	–	–	**1 094 153**
Intra-Eurosystem claims	–	–	1 166 224	1 038	–	–	**1 167 262**
Other assets	–	–	18 685	–	28 447	18 971	**66 103**
Total	**217 923**	**136 157**	**5 429 023**	**1 038**	**28 447**	**18 971**	**5 831 559**

47.2 COMPARISON OF THE LAYOUT OF DOMESTIC ASSETS

(in thousands of euro)

	Loans to credit institutions	Fixed assets	Other domestic assets	**Domestic assets**
Lending to euro area credit institutions related to monetary policy operations denominated in euro	14 229	–	–	**14 229**
Other assets	–	42 971	1 045	**44 016**
Total	**14 229**	**42 971**	**1 045**	**58 245**

47.3 COMPARISON OF THE LAYOUT OF FOREIGN LIABILITIES

(in thousands of euro)

	Convertible foreign currencies	International Monetary Fund	Other international institution deposits in lats	Foreign bank deposits in lats	Other foreign liabilities	**Foreign liabilities**
Liabilities to other euro area residents denominated in euro	4 131	–	–	5 769	–	**9 900**
Liabilities to non-euro area residents denominated in euro	7 601	420	4 664	–	–	**12 685**
Liabilities to non-euro area residents denominated in foreign currency	983	–	–	–	–	**983**
Other liabilities	–	–	–	–	11 553	**11 553**
Total	**12 715**	**420**	**4 664**	**5 769**	**11 553**	**35 121**

47.4 COMPARISON OF THE LAYOUT OF DOMESTIC LIABILITIES

(in thousands of euro)

	Credit institution deposits	Government deposits	Deposits of other financial institutions	Other domestic liabilities	**Domestic liabilities**
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	4 127 804	–	–	–	**4 127 804**
Liabilities to other euro area residents denominated in euro	–	202 263	14 209	–	**216 472**
Liabilities to euro area residents denominated in foreign currency	–	138 070	–	–	**138 070**
Other liabilities	–	–	–	4 860	**4 860**
Total	**4 127 804**	**340 333**	**14 209**	**4 860**	**4 487 206**

TO THE COUNCIL OF THE BANK OF LATVIA

We have audited the accompanying financial statements of the Bank of Latvia ("the Bank") set out on pages 72 to 120, which comprise the balance sheet as at 31 December 2014, and the related statements of profit and loss and total recognised gains and losses for the year then ended, and a summary of principal accounting policies and other explanatory notes.

Board's Responsibility for the Financial Statements
The Board of the Bank is responsible for the preparation and fair presentation of these financial statements in accordance with the Guideline of the European Central Bank of 11 November 2010 on the Legal Framework for Accounting and Financial reporting in the European System of Central Banks (recast) (ECB/2010/20), and "Financial Accounting Policy of the Bank of Latvia" approved by the Council of the Bank, and the requirements of the law "On the Bank of Latvia" governing financial reporting. The Board of the Bank is responsible for such internal control as the Board of the Bank determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility
Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the Board of the Bank, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Opinion
In our opinion, the financial statements of the Bank give a true and fair view of the financial position of the Bank as at 31 December 2014, and of its financial performance for the year then ended in accordance with the Guideline of the European Central Bank of 11 November 2010 on the Legal Framework for Accounting and Financial reporting in the European System of Central Banks (recast) (ECB/2010/20), and "Financial Accounting Policy of the Bank of Latvia" approved by the Council of the Bank, and the requirements of the law "On the Bank of Latvia" governing financial reporting.

Ernst and Young Baltic SIA
Licence No. 17

Diāna Krišjāne
Chairperson of the Board
Latvian Certified Auditor
Certificate No. 124

Riga, Latvia
10 March 2015

APPENDICES

Appendix 1

MONETARY INDICATORS IN 2014

(at the end of the period; in millions of euro)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	**XII**
LATVIJAS BANKA												
Latvia's contribution to the euro area monetary base	5 831.9	5 905.9	5 852.2	5 692.5	5 785.1	4 762.3	4 528.9	4 484.6	4 627.5	4 429.1	4 617.1	**6 381.1**
Currency in circulation	3 779.6	3 727.9	3 715.4	3 736.3	3 745.6	3 753.7	3 783.0	3 782.4	3 788.6	3 803.0	3 824.7	**3 957.7**
Current accounts (covering the minimum reserve system)	1 417.3	1 218.9	1 191.8	1 206.2	999.5	1 008.6	745.9	702.2	838.9	626.1	792.4	**2 073.4**
Deposit facility and other liabilities related to monetary policy operations	635.0	959.1	945.0	750.0	1 040.0	0	0	0	0	0	0	**350.0**
Foreign assets outside the euro area	2 768.3	2 734.1	2 752.2	2 729.0	2 813.4	2 796.3	2 815.4	2 830.6	2 837.6	2 798.4	2 764.3	**2 867.1**
Foreign liabilities outside the euro area	46.5	20.5	3.3	28.4	62.0	9.3	5.2	28.9	5.4	23.2	73.7	**24.0**
Credit	1 683.9	1 595.5	1 615.8	1 611.8	1 583.2	1 577.6	1 586.4	1 577.2	1 656.9	1 628.8	1 634.5	**1 670.7**
To MFIs in the euro area	522.8	434.8	451.6	487.8	493.3	483.5	497.2	496.2	564.9	560.7	557.5	**570.5**
To the general government sector in the euro area	298.6	298.7	283.1	273.1	273.6	272.7	272.7	274.1	273.5	281.2	281.1	**306.5**
To other euro area residents	862.5	862.0	881.1	850.9	816.3	821.4	816.5	806.9	818.5	786.9	795.8	**793.7**
MFI												
Overnight deposits (Latvia's contribution to M1 of the euro area)	7 579.0	7 464.0	7 505.6	7 447.5	7 396.3	7 487.6	7 595.5	7 807.7	7 784.8	7 840.9	7 975.9	**8 301.7**
Deposits with an agreed maturity of up to 2 years	1 871.5	1 827.4	1 880.2	1 822.1	1 807.0	1 748.5	1 687.0	1 624.7	1 647.2	1 578.7	1 593.7	**1 532.4**
Deposits redeemable at notice of up to 3 months	484.7	491.3	494.4	502.9	514.0	531.6	541.0	542.4	553.3	567.2	578.6	**687.9**
Latvia's contribution to M2 of the euro area	9 935.2	9 782.7	9 880.2	9 772.5	9 717.3	9 767.7	9 823.5	9 974.8	9 985.3	9 986.8	10 148.2	**10 522.0**
Money market fund shares and units	67.8	67.0	68.2	70.1	68.7	67.0	64.6	64.6	62.8	59.7	56.2	**40.6**
Debt securities with a maturity of up to 2 years	6.0	13.6	13.9	28.7	28.8	26.7	31.6	31.9	32.2	34.8	32.6	**36.8**
Latvia's contribution to M3 of the euro area	10 009.0	9 863.2	9 962.3	9 871.4	9 814.7	9 861.4	9 919.8	10 071.4	10 080.3	10 081.3	10 236.9	**10 599.4**
Net foreign assets outside the euro area	–661.8	–900.2	–842.3	–1 130.1	–736.5	–110.5	41.7	129.3	169.5	30.1	68.1	**–1 705.7**
Credit to euro area financial institutions, non-financial corporations and households	14 466.6	14 390.7	14 305.3	14 257.8	14 112.3	14 083.0	14 142.2	14 165.2	14 132.4	14 114.9	14 128.5	**14 048.6**
Loans to resident financial institutions, non-financial corporations and households	13 152.1	13 096.1	13 028.7	13 019.6	12 983.8	12 926.1	12 901.5	12 928.1	12 942.0	12 879.1	12 860.5	**12 570.1**
Deposits by resident financial institutions, non-financial corporations and households	8 936.7	8 953.9	8 917.0	8 837.0	8 821.1	8 883.2	8 918.1	8 997.2	8 959.0	8 988.8	9 113.4	**9 476.7**
INTEREST RATES												
Rate on the main refinancing operations (at end of period; %)	0.25	0.25	0.25	0.25	0.25	0.15	0.15	0.15	0.05	0.05	0.05	**0.05**
Weighted average interest rates on transactions in euro (%)												
Interbank loans	0.09	0.08	0.08	0.10	0.13	0.08	0.03	0.01	0	0	0	**0**
Loans to non-financial corporations and households with a floating interest rate and an initial rate fixation of up to 1 year (new business)	3.6	4.1	3.7	4.4	3.0	3.2	3.9	3.5	4.4	4.0	3.3	**3.7**
Time deposits by non-financial corporations and households (new business)	0.3	0.2	0.2	0.3	0.3	0.1	0.1	0.1	0.1	0.2	0.1	**0.2**

Appendix 2

MONTH-END BALANCE SHEETS OF LATVIJAS BANKA FOR 2014

(at the end of the month; in thousands of euro)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	**XII**
ASSETS	7 701 444	7 610 698	8 629 114	7 592 859	7 662 568	7 649 086	7 733 149	7 748 225	7 857 588	7 832 872	7 824 098	**8 024 508**
Gold and gold receivables	196 791	205 111	200 260	199 055	196 651	205 135	206 542	208 036	205 193	199 898	202 478	**210 774**
Claims on non-euro area residents denominated in foreign currency	2 375 971	2 337 647	2 355 461	2 319 486	2 401 408	2 375 044	2 396 706	2 408 091	2 416 391	2 390 941	2 355 710	**2 441 368**
Receivables from the IMF	137 026	135 467	135 407	135 274	136 771	136 783	138 245	139 103	142 317	142 305	141 749	**144 069**
Balances with banks and security investments, external loans and other external assets	2 238 945	2 202 180	2 220 054	2 184 212	2 264 637	2 238 261	2 258 461	2 268 988	2 274 074	2 248 636	2 213 961	**2 297 299**
Claims on euro area residents denominated in foreign currency	465 236	467 046	478 240	504 473	483 059	470 470	469 773	471 948	514 971	500 846	508 685	**486 242**
Claims on non-euro area residents denominated in euro	195 526	191 316	196 491	210 434	215 304	216 125	212 187	214 448	216 046	207 569	206 102	**214 953**
Lending to euro area credit institutions related to monetary policy operations denominated in euro	1 000	5 000	4 000	4 000	–	–	6 000	6 000	31 020	25 020	25 020	**85 520**
Main refinancing operations	1 000	1 000	–	–	–	–	–	–	–	–	–	**–**
Longer-term refinancing operations	–	4 000	4 000	4 000	–	–	6 000	6 000	31 020	25 020	25 020	**85 520**
Fine-tuning reverse operations	–	–	–	–	–	–	–	–	–	–	–	**–**
Structural reverse operations	–	–	–	–	–	–	–	–	–	–	–	**–**
Marginal lending facility	–	–	–	–	–	–	–	–	–	–	–	**–**
Credits related to margin calls	–	–	–	–	–	–	–	–	–	–	–	**–**
Other claims on euro area credit institutions denominated in euro	96 756	1 849	441	43	3 993	5 135	4 520	3 140	7 012	272	159	**4 475**
Securities of euro area residents denominated in euro	1 120 904	1 121 695	1 133 267	1 103 249	1 096 098	1 101 978	1 106 183	1 096 094	1 103 926	1 102 667	1 100 613	**1 095 446**
Intra-Eurosystem claims	3 147 247	3 150 455	4 156 075	3 134 622	3 155 656	3 158 223	3 214 495	3 221 943	3 242 033	3 266 917	3 281 333	**3 393 275**
Participating interest in the ECB	72 330	115 082	115 082	115 082	115 082	115 082	115 082	115 082	115 082	115 082	115 082	**115 082**
Claims equivalent to the transfer of foreign reserves to the ECB	163 480	163 480	163 480	163 480	163 480	163 480	163 480	163 480	163 480	163 480	163 480	**163 480**
Claims related to TARGET2 and national central bank correspondent accounts (net)	37 036	23 240	–	3 790	–	–	–	–	–	–	–	**–**
Claims related to other operational requirements within the Eurosystem	2 874 401	2 848 653	3 877 513	2 852 270	2 877 094	2 879 661	2 935 933	2 943 381	2 963 471	2 988 355	3 002 771	**3 114 713**
Items in course of settlement	–	–	–	–	–	2	4	5	11	18	–	**–**
Other assets	102 013	130 579	104 879	117 497	110 399	116 974	116 739	118 520	120 985	138 724	143 998	**92 455**

Appendix 2 (cont.)

(at the end of the month; in thousands of euro)

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	**XII**
LIABILITIES	7 701 444	7 610 698	8 629 114	7 592 859	7 662 568	7 649 086	7 733 149	7 748 225	7 857 588	7 832 872	7 824 098	**8 024 508**
Banknotes in circulation	3 669 722	3 626 377	3 615 783	3 636 033	3 643 900	3 650 758	3 679 987	3 684 765	3 684 262	3 697 532	3 718 256	**3 849 170**
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	2 052 289	2 178 020	2 136 753	1 956 244	2 039 528	1 008 646	745 919	702 156	838 857	626 070	792 423	**2 423 356**
Current accounts (covering the minimum reserve system)	1 417 289	1 218 907	1 191 753	1 206 244	999 528	1 008 646	745 919	702 156	838 857	626 070	792 423	**2 073 356**
Deposit facility	–	–	–	–	–	–	–	–	–	–	–	**350 000**
Fixed-term deposits	635 000	959 113	945 000	750 000	1 040 000	–	–	–	–	–	–	**–**
Fine-tuning reverse operations	–	–	–	–	–	–	–	–	–	–	–	**–**
Deposits related to margin calls	–	–	–	–	–	–	–	–	–	–	–	**–**
Other liabilities to euro area credit institutions denominated in euro	–	–	–	–	–	–	–	–	–	–	4 430	**540**
Liabilities to other euro area residents denominated in euro	1 179 153	1 059 283	641 695	1 265 062	557 329	119 504	129 106	146 956	135 932	166 381	180 235	**126 919**
General government	1 153 855	1 033 403	606 650	1 219 614	514 027	68 558	69 151	76 967	67 907	87 246	103 716	**50 900**
Other liabilities	25 298	25 880	35 045	45 448	43 302	50 946	59 955	69 989	68 025	79 135	76 519	**76 019**
Liabilities to non-euro area residents denominated in euro	46 520	19 836	3 349	27 471	62 030	9 271	5 157	28 893	5 427	23 155	73 672	**23 986**
Liabilities to euro area residents denominated in foreign currency	138 383	136 229	136 255	136 502	137 387	137 734	138 609	139 342	142 638	143 940	142 180	**144 579**
Liabilities to non-euro area residents denominated in foreign currency	–	652	–	946	–	–	–	–	–	–	–	**–**
Intra-Eurosystem liabilities	–	–	475 013	–	618 048	2 137 902	2 429 588	2 429 837	2 395 055	2 548 672	2 304 542	**796 980**
Liabilities related to TARGET2 and national central bank correspondent accounts (net)	–	–	475 013	–	618 048	2 137 902	2 429 588	2 429 837	2 395 055	2 548 672	2 304 542	**796 980**
Liabilities related to other operational requirements within the Eurosystem	–	–	–	–	–	–	–	–	–	–	–	**–**
Items in course of settlement	–	–	–	–	–	–	–	–	–	–	–	**–**
Other liabilities	141 812	112 972	1 149 442	123 028	141 634	121 493	141 038	143 583	179 325	143 193	117 908	**180 089**
Capital and reserves	473 565	477 329	470 824	447 573	462 712	463 778	463 745	472 693	476 092	483 929	490 452	**478 889**

Appendix 3

ORGANISATIONAL UNITS OF LATVIJAS BANKA AT THE END OF 2014

1. ACCOUNTING DEPARTMENT
(Head of Department, Chief Accountant of Latvijas Banka – Jānis Caune; Deputy Head of Department, Deputy Chief Accountant of Latvijas Banka – Iveta Medne)
1.1 Financial Statements and Accounting Policy Division (Head of Division – Gatis Gersons)
1.2 Internal Banking Operations Division (Head of Division – Anita Jakāne)

2. CASH DEPARTMENT
(Head of Department – Jānis Blūms; Deputy Heads of Department – Veneranda Kausa, Vilnis Kepe)
2.1 Cash Operations Division (Head of Division – Ģirts Jansons)
2.2 Coin Division (Head of Division – Maruta Brūkle)
2.3 Cash Technology Division (Head of Division – Andris Tauriņš)
2.4 Riga Branch (Branch Manager – Jānis Strēlnieks)
2.5 Liepāja Branch (Branch Manager – Gundars Lazdāns)

3. FINANCIAL STABILITY DEPARTMENT
(Head of Department – Elmārs Zakulis; Deputy Head of Department – Andris Ņikitins)
3.1 Financial Stability Division (Head of Division – Kārlis Grīnbergs)

4. GOVERNOR'S OFFICE
(Head of Office – Guntis Valujevs)

5. INFORMATION SYSTEMS DEPARTMENT
(Head of Department – Harijs Ozols; Deputy Head of Department – Krišs Rauhvargers)
5.1 System Design and Programming Division (Head of Division – Ilgvars Apinis)
5.2 Computer Network and Server Systems Division (Head of Division – Uldis Kristapsons)
5.3 Bank Information System Maintenance and Development Division (Head of Division, Deputy Head of Department – Valdis Spūlis)
5.4 Information Systems Security Division (Head of Division – Ilona Etmane)
5.5 Information Systems Quality Assurance Division (Head of Division – Askolds Kālis)
5.6 Systems Maintenance Division (Head of Division – Valērijs Kondratjevs)

6. INTERNAL AUDIT DEPARTMENT
(Head of Department – Leo Ašmanis; Deputy Heads of Department – Jānis Stražinskis, Juris Ziediņš)

7. INTERNATIONAL RELATIONS AND COMMUNICATION DEPARTMENT
(Head of Department – Juris Kravalis)
7.1 Document Management and Library Division (Head of Division – Ineta Strade)
7.2 Publications Division (Head of Division, Deputy Head of Department – Aina Raņķe)
7.3 Public Relations Division (Head of Division, Deputy Head of Department – Kristaps Otersons)
7.4 International Relations and Protocol Division (Head of Division, Deputy Head of Department – Aleksandra Bambale)

8. LEGAL DEPARTMENT
(Head of Department – Ilze Posuma; Deputy Heads of Department – Maija Āboliņa, Iveta Krastiņa)

9. MARKET OPERATIONS DEPARTMENT
(Head of Department – Raivo Vanags)

Appendix 3 (cont.)

9.1 Trading and Investment Division (Head of Division – Vadims Zaicevs)
9.2 Risk Management Division (Head of Division, Deputy Head of Department – Daira Brunere)

10. MONETARY POLICY DEPARTMENT
(Head of Department – Mārtiņš Bitāns)
10.1 Macroeconomic Analysis Division (Head of Division – Santa Bērziņa)
10.2 Financial Market Analysis Division (Head of Division – Gunārs Bērziņš)
10.3 Monetary Research and Forecasting Division (Head of Division – Konstantīns Beņkovskis)

11. PAYMENT SYSTEMS DEPARTMENT
(Head of Department – Egons Gailītis; Deputy Heads of Department – Agnija Jēkabsone, Irēna Krūmane)
11.1 Payment Systems Policy Division (Head of Division – Anda Zalmane)
11.2 Payment Systems Operations Division (Head of Division – Natālija Popova)
11.3 Payment and Settlement Division (Head of Division – Una Ruka)
11.4 Credit Register Division (Head of Division – Laura Ausekle)

12. PERSONNEL DEPARTMENT
(Head of Department – Liene Glāzniece; Deputy Head of Department – Vineta Veikmane)

13. SECURITY DEPARTMENT
(Head of Department – Romualds Namnieks; Deputy Heads of Department – Imants Kravals, Sandis Mackēvičs)
13.1 Analytical Unit (Head of Unit – Māris Dzelme)
13.2 Armament Unit (Head of Unit – Juris Kušķis)
13.3 Central Division (Head of Division – Ivars Geriņš)
13.4 Riga Division (Head of Division – Igo Peičs)
13.5 Liepāja Division (Head of Division – Gints Liepiņš)

14. STATISTICS DEPARTMENT
(Head of Department – Agris Caune; Deputy Head of Department – Ilmārs Skarbnieks)
14.1 Financial Market and Monetary Statistics Division (Head of Division – Zigrīda Aušta)
14.2 Balance-of-Payments Statistics Division (Head of Division – Daiga Gaigala-Ližbovska)
14.3 General Economic and Financial Statistics Division (Head of Division – Iveta Salmiņa)

15. TECHNICAL SUPPORT DEPARTMENT
(Head of Department – Reinis Jakovļevs)
15.1 General Service Division (Head of Division – Einārs Cišs)
15.2 Building Systems Division (Head of Division, Deputy Head of Department – Jānis Kreicbergs)
15.3 Security Systems Division (Head of Division – Viesturs Balodis)

16. TRAINING CENTRE
(Head of Centre – Zaiga Blūma)

Appendix 4

PARTICIPATION OF LATVIJAS BANKA IN THE EUROPEAN SYSTEM OF CENTRAL BANKS

Governing Council of the ECB
Ilmārs Rimšēvičs, Governor of Latvijas Banka

General Council of the ECB
Ilmārs Rimšēvičs, Governor of Latvijas Banka

Supervisory Board of the ECB
Zoja Razmusa, Deputy Governor of Latvijas Banka (banking supervisory institution is represented by Kristaps Zakulis, Chairman of the Council of the FCMC)

Accounting and Monetary Income Committee (AMICO)
Jānis Caune, Member of the Board of Latvijas Banka, Chief Accountant of Latvijas Banka, Head of Accounting Department
Gatis Gersons, Head of Financial Statements and Accounting Policy Division, Accounting Department

Banknote Committee (BANCO)
Jānis Blūms, Member of the Board of Latvijas Banka, Head of Cash Department
Veneranda Kausa, Deputy Head of Cash Department

Budget Committee (BUCOM)
Jānis Caune, Member of the Board of Latvijas Banka, Chief Accountant of Latvijas Banka, Head of Accounting Department

Committee on Controlling (COMCO)
Iveta Medne, Deputy Chief Accountant of Latvijas Banka, Deputy Head of Accounting Department

Financial Stability Committee (FSC)
Elmārs Zakulis, Head of Financial Stability Department

Eurosystem/ESCB Communications Committee (ECCO)
Kristaps Otersons, Deputy Head of International Relations and Communication Department, Head of Public Relations Division
Varis Vagotiņš-Vagulis, Chief Communication Project Manager of Public Relations Division, International Relations and Communication Department

Eurosystem IT Steering Committee (EISC)
Arvils Sautiņš, Member of the Council of Latvijas Banka

Human Resources Conference (HRC)
Liene Glāzniece, Head of Personnel Department

Information Technology Committee (ITC)
Harijs Ozols, Member of the Board of Latvijas Banka, Head of Information Systems Department
Valdis Spūlis, Deputy Head of Information Systems Department, Head of Bank Information System Maintenance and Development Division

Internal Auditors Committee (IAC)
Leo Ašmanis, Head of Internal Audit Department
Juris Ziediņš, Deputy Head of Internal Audit Department

Appendix 4 (cont.)

International Relations Committee (IRC)
Juris Kravalis, Head of International Relations and Communication Department
Andris Strazds, Adviser to International Relations and Communication Department

Legal Committee (LEGCO)
Ilze Posuma, Deputy Chairperson of the Board of Latvijas Banka, Head of Legal Department
Iveta Krastiņa, Deputy Head of Legal Department

Market Operations Committee (MOC)
Raivo Vanags, Member of the Board of Latvijas Banka, Head of Market Operations Department
Harijs Zuļģis, Chief Analyst of Financial Market Operations, Market Operations Department

Monetary Policy Committee (MPC)
Mārtiņš Bitāns, Head of Monetary Policy Department
Gundars Dāvidsons, Adviser to Monetary Policy Department

Organisational Development Committee (ODC)
Jānis Caune, Member of the Board of Latvijas Banka, Chief Accountant of Latvijas Banka, Head of Accounting Department
Igors Fleitmanis, Business Continuity Manager of Latvijas Banka[1]

Payment and Settlement Systems Committee (PSSC)
Egons Gailītis, Head of Payment Systems Department
Agnija Jēkabsone, Deputy Head of Payment Systems Department

Risk Management Committee (RMC)
Daira Brunere, Deputy Head of Market Operations Department, Head of Risk Management Division

Statistics Committee (STC)
Agris Caune, Head of Statistics Department
Ilmārs Skarbnieks, Deputy Head of Statistics Department

[1] As of 1 February 2015 – Operational Risk Manager of Latvijas Banka.

Appendix 5

REPRESENTATION OF LATVIJAS BANKA IN INTERNATIONAL ORGANISATIONS

EUROPEAN UNION

ESRB
Ilmārs Rimšēvičs, Governor of Latvijas Banka (banking supervisory institution is represented by Kristaps Zakulis, Chairman of the FCMC)

Advisory Technical Committee of the ESRB
Elmārs Zakulis, Head of Financial Stability Department (banking supervisory institution is represented by Ludmila Vojevoda, Member of the Council of the FCMC)

Economic and Financial Committee for the Council of the EU (EFC)
Juris Kravalis, Head of International Relations and Communication Department
Santa Bērziņa, Head of Macroeconomic Analysis Division, Monetary Policy Department (Alternate)

EFC's Euro Coin Sub-Committee (ECSC)
Maruta Brūkle, Head of Coin Division, Cash Department

EFC's Sub-Committee on IMF and Related Issues (SCIMF)
Aleksandra Bambale, Deputy Head of International Relations and Communication Department, Head of International Relations and Protocol Division

Board of Supervisors of the EBA
Vita Pilsuma, Member of the Council of Latvijas Banka (banking supervisory institution is represented by Kristaps Zakulis, Chairman of the FCMC)

Permanent Representation of Latvia to the EU
Inese Allika, Counsellor of Latvijas Banka at the Permanent Representation of Latvia to the EU

ESCB and ESSC Joint Committee on Monetary, Financial and Balance of Payments Statistics (CMFB)
Agris Caune, Head of Statistics Department
Ilmārs Skarbnieks, Deputy Head of Statistics Department

EC Public Administration Network (PAN II)
Antra Trenko, Senior Economist of International Relations and Protocol Division, International Relations and Communication Department

INTERNATIONAL MONETARY FUND

Board of Governors
Ilmārs Rimšēvičs, Governor of Latvijas Banka

Nordic-Baltic Monetary and Financial Committee (NBMFC)
Zoja Razmusa, Deputy Governor of Latvijas Banka

Nordic-Baltic Monetary and Financial Committee, Group of Alternates (NBMFC Alternates)
Juris Kravalis, Head of International Relations and Communication Department

Nordic-Baltic IMF Office in Washington
Uldis Rutkaste, Senior Advisor to the Executive Director of the Nordic-Baltic Constituency of the IMF, Latvia's representative in IMF

Appendix 6

LATVIJAS BANKA PUBLICATIONS AND MAJOR PUBLICATIONS BY THE EXPERTS OF LATVIJAS BANKA IN 2014

The following Latvijas Banka publications are available on Latvijas Banka website (www.bank.lv). Annual Reports of Latvijas Banka prepared in print until 2014 are available free of charge both at Latvijas Banka and by mail (if a sufficient number of copies are available) by sending a request to the address indicated on page 2 of this publication or by e-mailing to: info@bank.lv.

REGULAR PUBLICATIONS AND SERIAL PUBLICATIONS

Financial Stability Report (2013/2014)
Latvijas Banka: Annual Report 2013
Latvijas Maksājumu Bilance. Latvia's Balance of Payments. 2013
Macroeconomic Developments Report (January, March, June and December; No. 17–20, 2014)
Payment and Securities Settlement System Oversight Carried out by Latvijas Banka in 2013

WORKING PAPERS

AJEVSKIS, Viktors (2014) – *Semi-Global Solutions to DSGE Models: Perturbation around a Deterministic Path*. Latvijas Banka Working Paper, No. 1.
BUŠS, Ginters (2014) – *Financial Frictions in a DSGE Model of Latvia*. Latvijas Banka Working Paper, No. 2.
BEŅKOVSKIS, Konstantīns, WÖRZ, Julia (2014) – *What Drives the Market Share Changes?* Price versus Non-Price Factors. Latvijas Banka Working Paper, No. 3.
BEŅKOVSKIS, Konstantīns, WÖRZ, Julia (2014) – *"Made in China" – How Does It Affect Measures of Competitiveness?* Latvijas Banka Working Paper, No. 4.
FADEJEVA, Ludmila, FELDKIRCHER, Martin, REININGER, Thomas (2014) – *International Transmission of Credit Shocks: Evidence from Global Vector Autoregression Model*. Latvijas Banka Working Paper, No. 5.
CHRISTODOULOPOULOU, Styliani, TKAČEVS, Oļegs (2014) – *Measuring the Effectiveness of Cost and Price Competitiveness in External Rebalancing of Euro Area Countries: What Do Alternative HCIs Tell Us?* Latvijas Banka Working Paper, No. 6.

DISCUSSION PAPERS

ĀRIŅŠ, Mikus, SIŅENKO, Nadežda, LAUBE, Laura (2014) – S*urvey-Based Assessment of Household Borrowers' Financial Vulnerability*. Latvijas Banka Discussion Paper, No. 1.
BEŅKOVSKIS, Konstantīns, PASTUŠENKO, Jūlija, WÖRZ, Julia (2014) – *Assessing the Extent of EU–Russia Trade Integration in the Presence of Global Value Chains*. Latvijas Banka Discussion Paper, No. 2.
MEĻIHOVS, Aleksejs (2014) – *Forecasting Natural Population Change: Case of Latvia*. Latvijas Banka Discussion Paper, No. 3.

PUBLICATIONS

AJEVSKIS, Viktors, RIMGAILAITE, Ramune, RUTKASTE, Uldis, TKAČEVS Oļegs (2014) – The Equilibrium Real Exchange Rate: Pros and Cons of Different Approaches with Application to Latvia. *Baltic Journal of Economics*, vol. 14, issue 1–2, pp. 101–123.
BENKOVSKIS, Konstantins, FADEJEVA, Ludmila (2014) – The Effect of VAT Rate on Inflation in Latvia: Evidence from CPI Microdata. *Applied Economics*, vol. 46, issue 21, April, pp. 2520–2533.
BEŅKOVSKIS, Konstantīns, PASTUŠENKO, Jūlija, WÖRZ, Julia (2014) – Assessing

the Full Extent of Trade Integration between the EU and Russia – A Global Value Chain Perspective. *Focus on European Economic Integration*, No. Q3/14, pp. 31–47.
BENKOVSKIS, Konstantins, SILGONER, Maria, STEINER, Katharina, WÖRZ, Julia (2014) – *Mapping Competitive Pressure between China and EU Countries*. European Central Bank, CompNet Policy Brief, No. 4, January. 12 p.
BENKOVSKIS, Konstantins, WÖRZ, Julia (2014) – *What Drives the Market Share Changes? Price versus Non-Price Factors*. European Central Bank Working Paper Series, No. 1640, February. 46 p.
BENKOVSKIS, Konstantins, WÖRZ, Julia (2014) – *"Made in China" – How Does It Affect Measures of Competitiveness?* Oesterreichische Nationalbank Working Paper, No. 193, May. 47 p.
BENKOVSKIS, Konstantins, WÖRZ, Julia (2014) – How Does Taste and Quality Impact on Import Prices? *Review of World Economics*, vol. 150, issue 4, November, pp. 665–691.
CHRISTODOULOPOULOU, Styliani, TKAČEVS, Olegs (2014) – *Measuring the Effectiveness of Cost and Price Competitiveness in External Rebalancing of Euro Area Countries*. European Central Bank Working Paper Series, No. 1736, September. 36 p.

Appendix 7

HIGHLIGHTS OF EUROSYSTEM MONETARY POLICY AND OTHER IMPORTANT TASKS IN 2014

On 3 January, the Governing Council of the ECB approved the updated "Framework for the assessment of securities settlement systems and links to determine their eligibility for use in Eurosystem credit operations".

On 8 January, the Governing Council of the ECB decided to gradually reduce its offering of US dollar liquidity-providing operations.

On 9 January, the Governing Council of the ECB decided that the key interest rates used in Eurosystem monetary policy operations (hereinafter, the key ECB interest rates) would remain unchanged.

On 23 January, the Governing Council of the ECB adopted Recommendation ECB/2014/2 on the statistical reporting requirements of the European Central Bank in the field of external statistics.

On 30 January, the Governing Council of the ECB endorsed the "Assessment guide for the security of internet payments" developed by the European Forum on the Security of Retail Payments (SecuRe Pay).

On 31 January, the Governing Council of the ECB adopted Decision ECB/2014/5 on the close cooperation with the national competent authorities of participating Member States whose currency is not the euro.

On 3 February, the Governing Council of the ECB adopted a draft ECB Regulation establishing the framework for cooperation within the Single Supervisory Mechanism between the ECB and national competent authorities and with national designated authorities (SSM Framework Regulation) and decided to launch a one-month public consultation on the draft SSM Framework Regulation.

On 4 February, the Governing Council of the ECB adopted Decision ECB/2014/3 identifying the credit institutions that are subject to the comprehensive assessment (to be carried out by 3 November 2014).

On 6 February, the Governing Council of the ECB decided that the key ECB interest rates would remain unchanged.

On 13 February, the Governing Council of the ECB approved a report on the assessment of all securities settlement systems (SSSs) and the links that are currently being used to collateralise Eurosystem credit operations and approved new links as eligible for use in Eurosystem credit operations.

On 20 February, the Governing Council of the ECB adopted Guideline ECB/2014/9 on domestic asset and liability management operations by the national central banks and Decision ECB/2014/8 on the prohibition of monetary financing and the remuneration of government deposits by national central banks.

On 24 February, the Governing Council of the ECB adopted Decision ECB/2014/6 on the organisation of preparatory measures for the collection of granular credit data by the European System of Central Banks, and Recommendation ECB/2014/7 on the organisation of preparatory measures for the collection of granular credit data by the European System of Central Banks.

On 6 March, the Governing Council of the ECB decided that the key ECB interest rates would remain unchanged.

Appendix 7 (cont.)

On 12 March, the Governing Council of the ECB adopted the following documents:
1) Guideline ECB/2014/10 amending Guideline ECB/2011/14 on monetary policy instruments and procedures of the Eurosystem;
2) Decision ECB/2014/11 amending Decision ECB/2013/35 on additional measures relating to Eurosystem refinancing operations and eligibility of collateral;
3) Guideline ECB/2014/12 amending Guideline ECB/2013/4 on additional temporary measures relating to Eurosystem refinancing operations and eligibility of collateral and amending Guideline ECB/2007/9.

On 19 March, the Governing Council of the ECB considered the state of progress of the TARGET2-Securities programme and approved a revised User Requirements Document.

On 20 March, the Governing Council of the ECB approved the annual assessment of the availability and quality of the various kinds of statistics that are compiled by the Eurosystem on the basis of an ECB legal act.

On 21 March, the Governing Council of the ECB adopted Recommendation ECB/2014/13 for a Council Regulation amending Regulation (EC) No. 2533/98 concerning the collection of statistical information by the European Central Bank (in relation to the use of statistical information necessary for the SSM).

On 27 March, the Governing Council of the ECB adopted Recommendation ECB/2014/14 concerning the common rules and minimum standards to protect the confidentiality of the statistical information collected by the European Central Bank assisted by the national central banks.

On 3 April, the Governing Council of the ECB decided that the key ECB interest rates would remain unchanged.

On 4 April, the Governing Council of the ECB adopted Guideline ECB/2014/15 on monetary and financial statistics (recast; repeals Guideline ECB/2007/9).

On 16 April, the Governing Council of the ECB adopted Regulation (EU) No. 468/2014 establishing the framework for cooperation within the Single Supervisory Mechanism between the European Central Bank and national competent authorities and with national designated authorities (SSM Framework Regulation).

On 2 May, the Governing Council of the ECB approved the recommendations set out in the report on the measures adopted to safeguard the confidentiality of the statistical information referred to in Council Regulation (EC) No. 2533/98 of 23 November 1998 concerning the collection of statistical information by the European Central Bank (as amended by Council Regulation (EC) No. 951/2009).

On 8 May, the Governing Council of the ECB decided that the key ECB interest rates would remain unchanged.

On 30 May, the Governing Council of the ECB decided to continue offering seven-day US dollar liquidity-providing operations.

On 5 June, the Governing Council of the ECB decided on the change of the key ECB interest rates and on monetary policy measures to enhance the functioning of the monetary policy transmission mechanism. The decisions taken were as follows:
1) to cut the interest rates on the deposit facility and main refinancing operations by 10 basis points (to –0.10% (with effect from 11 June 2014) and 0.15% (starting from the operation to be settled on 11 June 2014) respectively, and to reduce the interest rate on the marginal lending facility by 35 basis points (to 0.40%; with effect from 11 June 2014);

Appendix 7 (cont.)

2) to continue conducting the Eurosystem's main refinancing operations as fixed rate tender procedures with full allotment for as long as necessary, and at least until the end of the Eurosystem's reserve maintenance period ending in December 2016;
3) to conduct three-month LTROs as fixed rate tender procedures with full allotment until the end of the Eurosystem's reserve maintenance period ending in December 2016;
4) to discontinue the Eurosystem's special-term refinancing operations with a maturity of one reserve maintenance period, following the operation to be allotted on 10 June 2014;
5) to suspend the weekly fine-tuning operation sterilising the liquidity injected under the Securities Markets Programme, following the operation to be allotted on 10 June 2014;
6) to conduct a series of TLTROs aimed at improving bank lending to the euro area non-financial private sector, excluding loans to households for house purchase;
7) to intensify preparatory work related to outright purchases of asset-backed securities;
8) adopted Decision ECB/2014/23 on the remuneration of deposits, balances and holdings of excess reserves.

On 3 July, the Governing Council of the ECB decided:
1) that the key ECB interest rates would remain unchanged;
2) to change the frequency of its meetings dedicated to monetary policy to a six-week cycle from 1 January 2015. It was also decided to extend reserve maintenance periods (to six weeks to match the new schedule) and to publish accounts of its monetary policy meetings on a regular basis;
3) on further technical details in relation to several TLTROs announced on 5 June 2014.

On 8 July, the Governing Council of the ECB adopted Regulation (EU) No. 756/2014 amending Regulation (EU) No. 1072/2013 (ECB/2013/34) concerning statistics on interest rates applied by monetary financial institutions.

On 23 July, the Governing Council of the ECB announced that on the same day the EU Council formally approved the accession of Lithuania to the euro area on 1 January 2015 and determined the euro conversion rate of the Lithuanian litas at 3.45280 litas to 1 euro (coinciding with the level of the central rate of the Lithuanian litas in the ERM II). At the same time, the ECB informed about an agreement with Lietuvos bankas to monitor developments in the foreign exchange market of the Lithuanian litas against the euro until 1 January 2015, and that the ECB would take over direct supervision of the biggest Lithuanian banks in January 2015 as Lithuania would also join the SSM.

On 29 July, the Governing Council of the ECB adopted Decision ECB/2014/34 on measures relating to targeted longer-term refinancing operations.

On 1 August, the ECB marked a major milestone in the integration of retail payments in Europe. After 15 years of work, the SEPA was successfully implemented for credit transfers and direct debits in the euro area.

On 7 August, the Governing Council of the ECB decided that the key ECB interest rates would remain unchanged.

On 21 August, the ECB identified four key payment systems (TARGET2, EURO1, STEP2-T and CORE(FR) regulated by ECB Regulation (EU) No. 795/2014 of 3 July 2014 on oversight requirements for systemically important payment systems.

On 4 September, the Governing Council of the ECB decided:
1) to continue the reduction of the key ECB interest rates by 10 basis points. Thus, starting from the operation to be settled on 10 September 2014, the interest rate on the main refinancing operations was set at 0.05%, on the marginal lending facility – 0.30% and on the deposit facility – –0.20% (the last two interest rates with effect from 10 September 2014);

Appendix 7 (cont.)

2) to purchase a broad portfolio of simple and transparent asset-backed securities (ABSs) with underlying assets consisting of claims against the euro area non-financial private sector under an asset-backed securities purchase programme (ABSPP);
3) that the Eurosystem would purchase a broad portfolio of euro-denominated covered bonds issued by MFIs domiciled in the euro area under a new covered bond purchase programme (CBPP3).

On 4 September, the ECB published a document "The list of significant supervised entities and the list of less significant institutions", also comprising three significant supervised credit institutions and 19 less significant ones based in Latvia. On 28 August 2014 and 1 September 2014, the Governing Council of the ECB approved the list of credit institutions which it considered to be significant and which would thus be subject to direct ECB supervision as of 4 November 2014.

On 17 September, the Governing Council of the ECB adopted Decision ECB/2014/39 on the implementation of separation between the monetary policy and supervision functions of the ECB.

On 17 September, the Governing Council of the ECB took note of the final ranking of euro area countries and the allocation of governors of the Eurosystem's central banks into voting groups 1 and 2, as foreseen by the Statute of the ECBS and of the ECB. The Governing Council decided on the starting point for the rotation order for each group based on a random draw.

On 2 October, the Governing Council of the ECB decided:
1) that the key ECB interest rates would remain unchanged;
2) to approve the asset-backed securities purchase programme and covered bond purchase programmes. The programmes will last at least two years and aim at enhancing the transmission of monetary policy and supporting the provision of credit to the euro area economy.

On 15 October, the Governing Council of the ECB adopted Decision ECB/2014/40 on the implementation of the third covered bond purchase programme.

On 20 October, the ECB announced that it would step up cooperation with the EBA to increase the security of retail payments. The ECB and EBA agreed to use the technical work developed in the European Forum for the Security of Retail Payments as a basis for their cooperation.

On 26 October, the ECB published the results of a thorough year-long examination of the resilience and positions of the 130 largest banks (including three Latvian credit institutions) in the euro area as of 31 December 2013, noting that credit institutions should take further steps to improve their operation.

On 3 November, the ECB published a "Guide to banking supervision". It explains how the SSM functions and gives guidance on the SSM supervisory practices. However, it does not substitute the legal requirements laid down in the relevant applicable EU law.

On 4 November, the ECB assumed responsibility for the supervision of euro area banks and launched a new website, www.bankingsupervision.europa.eu to reflect issues in relation to the operation of the SSM.

On 6 November, the Governing Council of the ECB decided that the key ECB interest rates would remain unchanged.

On 6 November, the Governing Council of the ECB adopted Guideline ECB/2014/43 amending Guideline ECB/2014/15 on monetary and financial statistics. The amendments relate to the compilation of statistics on the issuance of securities and the reporting requirements for payment transactions involving non-MFIs.

On 13 November, the Governing Council of the ECB approved the publication of two guides for the assessment against the relevant oversight standards of the SEPA credit transfer and direct debit schemes run by the European Payments Council (EPC). The assessments will be coordinated by the ECB as lead overseer.

On 19 November, the Governing Council of the ECB adopted Decision ECB/2014/45 on the implementation of the asset-backed securities purchase programme.

On 26 November, the Governing Council of the ECB adopted Regulation (EU) No. 1333/2014 concerning statistics on the money markets.

On 28 November, the Governing Council of the ECB adopted Regulation (EU) No. 1374/2014 on statistical reporting requirements for insurance corporations.

On 1 December, the Euro Retail Payments Board chaired by the ECB decided to step up work on the topics of instant payments in euro, person-to-person mobile payments and contactless payments. Taking stock of the advantage of integration already achieved with SEPA, the Board also adopted a set of recommendations focusing on the outstanding aspects of the SEPA credit transfer and direct debit schemes to avoid the development of a fragmented market in Europe.

On 4 December, the Governing Council of the ECB decided that the key ECB interest rates would remain unchanged.

On 16 December, the Governing Council of the ECB decided to publish regular accounts of its monetary policy discussions, starting with the meeting on 22 January 2015. In accordance with the decision taken by the Governing Council of the ECB on 3 July 2014 concerning the new six-week cycle for monetary policy meetings, the ECB will henceforth, starting from January 2015, publish the Economic Bulletin, which will replace the Monthly Bulletin, two weeks after each meeting.

On 17 December, the Governing Council of the ECB approved an updated brochure entitled "Correspondent central banking model (CCBM) – procedures for Eurosystem counterparties" and also approved the transfer of detailed technical information from the CCBM brochure to a new document entitled "CCBM information for counterparties – summary of legal instruments used in the euro area".

Appendix 8

2014 HIGHLIGHTS OF REGULATORY DOCUMENTS ADOPTED IN PURSUIT OF THE MAIN TASKS OF LATVIJAS BANKA

Regulatory document	No.	Date of adoption (effective date)	Title of the regulatory document adopted by the Council of Latvijas Banka
Regulation	131	13.03.2014 (01.07.2014)	"Regulation for Compiling Credit Institution, Electronic Money Institution and Payment Institution Payment Statistics Report"
Procedure	221/1	27.03.2014 (01.04.2014)	"Amendments to Procedure No. 217/1 'Participation Procedure in the Eurosystem Monetary Policy Operations Organised by Latvijas Banka' of the Council of Latvijas Banka of 12 December 2013"
Regulation	132	16.05.2014 (01.12.2014)	"Regulation for Compiling the 'Monthly Financial Position Report' of Monetary Financial Institutions"
Regulation	133	16.05.2014 (01.12.2014)	"Regulation for Compiling Interest Rate Reports of Monetary Financial Institutions"
Regulation	134	16.05.2014 (01.12.2014)	"Regulation for Compiling the 'Report on Adjustments in Respect of Write-Offs/Write-Downs of Loans and Price Revaluations of Securities'"
Regulation	135	16.05.2014 (01.12.2014)	"Amendments to Regulation No. 109 'Regulation for Preparing the 'Calculation of the Reserve Base and Reserve Requirement' ' of Latvijas Banka of 11 July 2013"
Regulation	136	16.05.2014 (01.12.2014)	"Regulation for Compiling Reports on Securities"
Regulation	137	16.05.2014 (01.12.2014)	"Amendments to Regulation No. 115 'Regulation for Compiling Reports on Long-Term Foreign Debt of Credit Institutions' of Latvijas Banka of 11 July 2013"
Regulation	138	16.05.2014 (01.07.2014)	"Amendment to Regulation No. 131 'Regulation for Compiling Credit Institution, Electronic Money Institution and Payment Institution Payment Statistics Report' of Latvijas Banka of 13 March 2014"
Regulation	139	16.05.2014 (22.05.2014)	"Amendments to Regulation No. 93 'Regulation for the Credit Register' of Latvijas Banka of 13 September 2012"
Regulation	140	16.05.2014 (01.07.2014)	"Amendments to Regulation No. 130 'Regulation for Electronic Information Exchange with Latvijas Banka' of Latvijas Banka of 12 December 2013"
Procedure	225/2	10.07.2014 (11.07.2014)	"Amendments to Procedure No. 217/1 'Participation Procedure in the Eurosystem Monetary Policy Operations Organised by Latvijas Banka' of the Council of Latvijas Banka of 12 December 2013"
Procedure	225/3	10.07.2014 (11.07.2014)	"Amendments to Procedure No. 186/4 'Participation Procedure in TARGET2-Latvija' of the Council of Latvijas Banka of 4 November 2010"
Procedure	225/4	10.07.2014 (11.07.2014)	"Amendment to Procedure No. 213/9 'On the Regulation for Servicing of Customer Accounts of Latvijas Banka' of the Council of Latvijas Banka of 16 September 2013"
Procedure	226/2	15.09.2014 (06.10.2014)	"Amendments to Procedure No. 183/3 'Participation Procedure in the Electronic Clearing System of Latvijas Banka' of the Council of Latvijas Banka of 9 September 2010"
Procedure	226/3	15.09.2014 (01.10.2014)	"Amendments to Procedure No. 213/12 'Participation Procedure in Cash Transactions at Latvijas Banka' of the Council of Latvijas Banka of 16 September 2013"
Regulation	141	15.09.2014 (16.09.2014)	"Requirements for the Prevention of Laundering the Proceeds Derived from Criminal Activity and of Terrorist Financing upon Purchasing and Selling Cash Foreign Currencies"
Procedure	227/2	13.11.2014 (01.01.2015)	"Amendment to Procedure No. 183/3 'Participation Procedure in the Electronic Clearing System of Latvijas Banka' of the Council of Latvijas Banka of 9 September 2010"
Procedure	227/3	13.11.2014 (21.11.2014)	"Amendment to Procedure No. 213/9 No. 'On the Regulation for Servicing of Customer Accounts of Latvijas Banka' of the Council of Latvijas Banka of 16 September 2013"

Appendix 8 (cont.)

Regulatory document	No.	Date of adoption (effective date)	Title of the regulatory document adopted by the Council of Latvijas Banka
Procedure	227/21	13.11.2014 (14.11.2014)	"Amendments to Procedure No. 213/12 'Participation Procedure in Cash Transactions at Latvijas Banka' of the Council of Latvijas Banka of 16 September 2013"
Procedure	228/1	27.11.2014 (15.12.2014)	"Amendments to Procedure No. 217/1 'Participation Procedure in the Eurosystem Monetary Policy Operations Organised by Latvijas Banka' of the Council of Latvijas Banka of 12 December 2013"

Appendix 9

GLOSSARY

Asset-backed securities purchase programme (ABSPP): a programme under which the Eurosystem purchases eligible asset-backed securities.

Balance of payments: a statistical report that reflects Latvia's economic transactions with the rest of the world within a specific period. This report includes the transactions related to goods, services, income and transfers, and such net transactions that result in financial claims ("Assets") or financial obligations ("Liabilities") to the rest of the world.

Bank for International Settlements (BIS): an international financial organisation, founded in May 1930, to facilitate international monetary and financial cooperation. The BIS acts as a bank for central banks.

Banking union: a framework for closer EU economic integration, which is composed of four pillars: a single rulebook, SSM, single bank resolution mechanism and harmonised deposit protection. Euro area countries and those EU countries outside the euro area opting to participate in the banking union are members of the banking union.

Central government: public institutional units, including ministries, embassies, representative offices, agencies, councils, educational, healthcare, law enforcement, cultural and other public institutions whose competence covers the whole economic territory of the country. The list of the institutional units of the Latvian central government is prepared by the CSB.

Clearing: the process of transmitting, processing and reconciling payment documents or securities transfer orders prior to settlement, resulting in establishment of the net position of each settlement participant by netting all payment documents submitted by the settlement participants, i.e. establishing net cash liabilities to or claims on other settlement participants.

Collateral: assets that are pledged or otherwise transferred to secure repayment of a loan, as well as those sold under repurchase agreements. The collateral used in the Eurosystem's reverse transactions should meet certain eligibility criteria.

Council of the EU (EU Council): the institution representing the governments of EU countries. The ministers of EU countries meet in the EU Council to adopt legislative acts and coordinate policies. The EU Council is an essential EU decision-maker. It is a single legal entity, but it meets in 10 different configurations, depending on the subject being discussed. The most significant tasks of the EU Council include negotiating and adopting legislative acts, developing common foreign and security policy of the EU, signing international agreements on behalf of the EU as well as adopting the EU budget together with the European Parliament.

Covered bond purchase programme (CBPP): a programme under which the Eurosystem purchases eligible covered bonds.

Credit institutions: capital companies whose business is to receive deposits or other repayable funds from the public and to grant credits on its own account and provide other financial services.

Debt security: a promise on the part of the issuer (i.e. the borrower) to make one or more payments to the holder of the securities (the lender) at a specified future date or dates. Such securities usually carry a specific rate of interest (the coupon) or are sold at a discount to the amount that will be repaid at maturity.

Appendix 9 (cont.)

Deposit facility: a standing facility of the Eurosystem which credit institutions registered in the Republic of Latvia and branches, registered in Latvia, of credit institutions registered in other countries may use to make overnight deposits with Latvijas Banka at a pre-specified interest rate.

Deposits: funds placed on the accounts of MFIs for a specified or unspecified period of time, with or without earning interest.

Deposits redeemable at notice: funds deposited with an MFI without any specified maturity, with the possibility of withdrawing on demand either subject to notifying the MFI within an agreed period of notice or subject to payment of a substantial penalty.

Direct investment: investment (net transactions and outstanding amounts) made by a foreign investor (direct investor) directly or indirectly (through subsidiaries or associated companies) in order to obtain a lasting interest (ownership of at least 10% of the ordinary shares or voting power) in a Latvian commercial company (direct investment company; direct investment in Latvia) or by a Latvian investor in a foreign company (direct investment abroad). The components of direct investment are equity capital, reinvested earnings and debt instruments. Direct investment implies long-term relationship between a direct investor and direct investment company. Direct investor can be either a natural or legal person.

EBA Clearing (EBA Clearing S.A.S. à capital variable): a capital company established by the major European and international banks, which provides pan-European payment infrastructure solutions, offering clearing and settlement services for both high-value and low-value euro payments to a wide community of banks in the EU.

Economic and Financial Affairs Council (ECOFIN): comprises ministers of finance and economics of all EU countries. ECOFIN adopts decisions on the EU policy in the following three major areas: economic policy, taxation issues and the regulation of financial services.

Economic and Financial Committee (EFC): a counselling body set up to promote economic and financial policy coordination among the EU countries. In its fields of competence, the EFC delivers opinions at the request of the EU Council or the EC, as well as provides framework for the dialogue between the EU Council and the ECB and contributes to the preparation of the work of the EU Council. The EFC is composed of representatives of the governments (usually Ministries of Finance) and central banks of the EU Member States as well as representatives of the EC and ECB.

Economic and Monetary Union (EMU): an agreement between the EU Member States on a significant economic integration, involving the coordination of economic and fiscal policies, a single monetary policy and a single currency, the euro. Whilst all EU countries take part in the economic union, some countries have taken integration further and adopted the euro. Together, these countries make up the euro area.

Electronic Clearing System of Latvijas Banka (EKS): net settlement system of Latvijas Banka ensuring the processing of retail payment orders and the settlement of net positions.

EONIA (euro overnight index average): a measure of the effective interest rate prevailing in the euro interbank overnight market. It is calculated as a weighted average of the interest rates on unsecured overnight loans denominated in euro, as reported by a panel of contributing banks.

Equities: securities representing ownership of a stake in a commercial company. They comprise shares traded on stock exchanges (quoted shares), unquoted shares and other forms of equity. Equities usually produce income in the form of dividends.

Appendix 9 (cont.)

EURIBOR (euro interbank offered rate): the interest rate at which a prime bank is willing to lend funds to another prime bank, as reported by a panel of contributing banks, computed daily for interbank deposits with different maturities of up to 12 months.

Euro area: EU countries which have adopted the euro as their single currency in accordance with the Treaty on the Functioning of the European Union and in which a single monetary policy is conducted under the responsibility of the Governing Council of the ECB. As at the end of 2014, the euro area comprised Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia and Spain (Lithuania joined the euro area on 1 January 2015).

Eurogroup: an informal gathering of the ministers of economics and finance of the euro area member countries, at which they discuss issues connected with their shared responsibilities in respect of the euro. The main task of the Eurogroup is to ensure close coordination of economic policies in the euro area and promote conditions for stronger economic growth.

European Banking Authority (EBA): an EU body with legal personality which forms part of the ESFS. The objective of the EBA is to protect the public interest by contributing to the short-, medium- and long-term stability of the financial system and effectiveness for the EU economy, its citizens and businesses. One of the key tasks of the EBA is to develop and maintain a European Single Rulebook which sets out supervisory methodology and best practice in relation to the supervision of financial institutions across the EU. The EBA comprises a Board of Supervisors, a Management Board, a Chairperson, an Executive Director and a Board of Appeal.

European Central Bank (ECB): the central institution of the ESCB and the Eurosystem having a legal personality under the EU law. The ECB implements the tasks conferred upon the Eurosystem and the ESCB pursuant to the Statute of the ESCB and the ECB in cooperation with the national central banks of the EU Member States. The ECB is governed by the Governing Council and the Executive Board, and, within the ESCB, by a third decision-making body, the General Council, which will be dissolved once all EU countries have introduced the euro.

European Council: an EU institution defining the EU's overall political direction and priorities. It is comprised of the heads of state or government of the EU Member States, the President of the European Council and the President of the EC.

European Systemic Risk Board (ESRB): an independent body of the EU which forms part of the ESFS. The ESRB is responsible for the macro-prudential oversight of the financial system within the EU in order to contribute to the prevention or mitigation of systemic risks to financial stability in the EU that arise within the financial system, taking into account macroeconomic developments, so as to avoid periods of widespread financial distress. It contributes to the smooth functioning of the internal market and thereby ensures a sustainable contribution of the financial sector to economic growth. The ESRB has a General Board, a Steering Committee, a Secretariat, an Advisory Scientific Committee and an Advisory Technical Committee.

European System of Central Banks (ESCB): includes the ECB and the national central banks of the EU Member States. The national central banks of those EU countries that have not yet adopted the euro implement an independent monetary policy according to their national law and are thus not involved in the conduct of the monetary policy of the Eurosystem.

Appendix 9 (cont.)

European System of Financial Supervision (ESFS): comprises ESRB, EBA, European Insurance and Occupational Pensions Authority, European Securities and Markets Authority, Joint Committee of the European Supervisory Authorities and the national supervisory authorities of the EU Member States. The main objective of the ESFS is to ensure that the rules applicable to the financial sector are adequately implemented to preserve financial stability and thus to ensure confidence in the financial system as a whole and sufficient protection for the customers of financial services.

Eurosystem: comprises the ECB and the national central banks of the euro area countries. The decision-making bodies of the Eurosystem are the Governing Council and the Executive Board of the ECB.

Exchange rate mechanism II (ERM II): the exchange rate mechanism that ensures the framework for exchange rate policy cooperation between the euro area countries and the non-euro-area EU countries. ERM II is a multilateral agreement on fixed, albeit adjustable central rates with a standard fluctuation band of ±15%. The decisions on the central rates and fluctuation bands are taken by an agreement between the respective EU Member State, euro area countries, the ECB and other EU Member States participating in the mechanism. Participation in the ERM II is a pre-condition for an EU country to become a fully-fledged member of the EMU and introduce the euro. As at the end of 2014, Denmark (the fluctuation band for the Danish krone is set at ±2.25%) and Lithuania were members of the ERM II (with the introduction of the euro on 1 January 2015, Lithuania ceased to participate in the ERM II).

Financial stability: the condition in which the financial system – comprising financial intermediaries, markets and market infrastructures – is capable of withstanding shocks, thereby mitigating the likelihood of disruptions in the financial intermediation process which could impair the allocation of savings and investment opportunities.

Fine-tuning operation: an open market operation executed by the Eurosystem in order to deal with unexpected liquidity fluctuations in the market. The frequency and maturity of these operations are not standardised.

Fixed rate instrument: a financial instrument for which the coupon is fixed throughout the life of the instrument.

General Council of the ECB: one of the decision-making bodies of the ECB, comprising the President and the Vice-President of the ECB and the Governors of the central banks of all EU countries.

General government: public institutional units, engaged in production of non-market goods or provision of services intended for individual or collective consumption, or public institutions engaged in redistribution of national income or wealth, primarily financed from the contributions (taxes and duties) imposed on economic agents. General government in the Republic of Latvia includes central government, social security funds and local government. The list of the institutional units of the general government in Latvia is prepared by the CSB.

Gross settlement system: a transfer system in which the settlement concerning each cash or securities transfer order occurs on an instruction-by-instruction basis in the order of receipt.

Household: a natural person or group of natural persons in the capacity of a consumer and producer of goods and a provider of non-financial services for exclusively own final use; a sole proprietor engaged in its professional practice or working at its farm (fishery) with the aim of gaining income or benefits, without employing any other person and without registering its activity with the Commercial Register of the Enterprise Register of the Republic of Latvia.

Interbank Automated Payment System of Latvijas Banka (SAMS): real-time gross settlement system of Latvijas Banka used for settlements concerning Latvijas Banka's monetary policy operations, large-value interbank transfers and other payments in lats until the end of 2013.

International Monetary Fund (IMF): an international organisation, conceived in July 1944, to facilitate international monetary cooperation, exchange rate stability, national economic growth and employment growth, and provide short-term financial assistance to IMF member countries for balancing the payment flow.

Key ECB interest rates: the interest rates on the main refinancing operations, on the marginal lending facility and on the deposit facility, set by the Governing Council of the ECB.

Local government: institutional units of the local public administration, whose competence covers only a local economic territory. The list of the institutional units of the Latvian central government is prepared by the CSB.

Longer-term refinancing operation (LTRO): an open market operation with a maturity of over one week executed by the Eurosystem in the form of a reverse transaction. The regular monthly operations are conducted with a maturity of three months; the maturity of the supplementary operations initiated at varying frequency in August 2007 may vary from one reserve maintenance period to 36 months.

M1: a narrow monetary aggregate comprising currency in circulation and overnight deposits held with MFIs by euro area residents.

M2: an intermediate monetary aggregate comprising M1 and deposits held with MFIs by euro area residents and redeemable at a period of notice of up to and including 3 months (i.e. short-term savings deposits) and those with an agreed maturity of up to and including 2 years (i.e. short-term time deposits).

M3: a broad monetary aggregate comprising M2 and 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 MFIs.

Main refinancing operation: a regular open market operation executed by the Eurosystem in the form of reverse transactions. Such operations are carried out through weekly standard tender procedures and normally have a maturity of one week.

Marginal lending facility: a standing facility, offered by the Eurosystem, which credit institutions registered in the Republic of Latvia and branches, registered in Latvia, of credit institutions registered in other countries may use to receive overnight credit from Latvijas Banka at a pre-specified interest rate against eligible assets.

Market risk: the risk related to fluctuations of the fair value or cash flow of financial instruments on account of movements in market prices. Market risk reflects the interest rate risk, currency risk and price risk.

Monetary base (base money): currency (banknotes and coins) in circulation, the minimum reserves credit institutions are required to hold with the Eurosystem as well as any excess reserves they may hold under the Eurosystem's deposit facility or as other liabilities related to the monetary policy operations.

Monetary financial institution (MFI): a central bank, credit institution, credit union, money market fund and other financial institution whose business is to receive deposits or close substitutes for deposits from customers other than MFIs and, on their own account, to grant credits and invest in securities, as well as an electronic money institution whose core business is to issue electronic money. Latvijas Banka sets up, maintains and regularly updates the List of Monetary Financial Institutions of the Republic of Latvia (see section Statistics on Latvijas Banka's website www.bank.lv). The list is also available on the ECB website where the ECB publishes the list of MFIs of the EU Member States on a regular basis. As at the end of 2014, there were 62 MFIs in Latvia.

Monetary income: income accruing to the national central banks of the euro area in the process of the Eurosystem's monetary policy implementation, derived from assets earmarked in accordance with guidelines established by the Governing Council and held against banknotes in circulation and credit institutions' deposits with central banks of the euro area.

Non-financial corporation: an institutional unit whose core business is producing goods or providing non-financial services, including an individual merchant registered with the Commercial Register of the Enterprise Register of the Republic of Latvia.

Non-standard measures: temporary measures taken by the Governing Council of the ECB to support the effectiveness and transmission of interest rate decisions to the wider euro area economy in the context of a dysfunctional situation in some financial market segments and the financial system more broadly.

Open market operation: an operation executed in the financial market on the initiative of a central bank. With regard to their aims, regularity and procedures, Eurosystem's open market operations can be divided into four categories: main refinancing operations, longer-term refinancing operations, fine-tuning operations and structural operations.

Outright transactions: open market operations where the Eurosystem purchases or sells eligible assets outright in the market. Outright transactions are executed only for structural purposes.

Price stability: the maintenance of price stability is the primary objective of the Eurosystem. The Governing Council of the ECB has defined price stability as a year-on-year increase in the HICP for the euro area that is below 2%. The Governing Council has also stated that, in the pursuit of price stability, it aims to maintain inflation rates below, but close to, 2%.

Real-Time Gross Settlement (RTGS) system: a settlement system in which processing of cash or securities transfer orders and settlement takes place on an individual basis and in a consecutive order (without netting) in real time.

Reference value for M3 growth: the annual growth rate of M3 over the medium term that is consistent with the objective of maintaining price stability. In 2014, this value was 4.5%.

Reserve requirement: a requirement for credit institutions and credit unions to hold their minimum reserves with the national central bank over the reserve maintenance period. Compliance with the requirement is determined on the basis of the average end-of-day balance on the reserve account over the reserve maintenance period.

Residual maturity: time remaining until the maturity date of a debt instrument or a loan or time remaining until the final date of any other financial operation.

Appendix 9 (cont.)

Reverse transaction: a transaction whereby the Eurosystem buys or sells assets under a repurchase agreement or conducts credit operations against collateral.

Securities markets programme (SMP): a programme for conducting interventions in public and private debt securities markets with the objective to restore appropriate monetary policy transmission mechanism. The securities markets programme continued until 6 September 2012.

Securities settlement system: an agreement between at least three participants, apart from the operator of the system, on the execution of securities' transfer orders between those participants in accordance with uniform regulations and standardised procedures.

Single Euro Payments Area (SEPA): a project proposed by the European banks and supported by the Eurosystem and the EC to harmonise the way retail payments in euro are made, making payments in euro across European countries as fast, secure and effective as domestic payments. SEPA enables consumers, businesses and other economic agents to make both domestic and cross-border payments in euro on the same main terms and conditions, with the same rights and obligations, regardless of their location. As at the end of 2014, SEPA encompassed all EU Member States, Iceland, Liechtenstein, Monaco, Norway, San Marino and Switzerland.

Single Supervisory Mechanism (SSM): an EU-level framework for a prudential supervision of credit institutions in the euro area countries and in those EU countries outside the euro area opting to participate in the mechanism. The SSM is one of the central pillars of the banking union, comprising the ECB as the final responsible supervisory authority and the relevant national competent authorities of the EU countries.

STEP2: a payment system maintained by the EBA Clearing for the processing of retail payments in euro. STEP2 is a Pan-European Automated Clearing House (PE-ACH) system that fully complies with the requirements for SEPA clearing and settlement infrastructures set out by the European Payments Council, and is the sole system providing reachability of all EU credit institutions within SEPA.

Structural operations: open market operations executed by the Eurosystem on a regular or non-regular basis whenever the ECB wishes to adjust the structural liquidity position of the Eurosystem vis-à-vis the financial sector.

Systemic risk: the risk that the inability of one participant to meet its obligations in a system will cause other participants to be unable to meet their obligations when they become due, potentially with spillover effects threatening the stability of or confidence in the financial system. That inability to meet obligations can be caused by operational or financial problems.

TARGET (Trans-European Automated Real-time Gross settlement Express Transfer system): the Eurosystem's real-time gross settlement system for the euro. The first generation TARGET system was replaced by TARGET2 in May 2008.

TARGET2: the second-generation TARGET system. It settles payments in euro in central bank money and functions on the basis of a single IT platform, to which all payment orders are submitted for processing.

TARGET2-Latvija: a component system of TARGET2 in Latvia. Its operation is ensured by Latvijas Banka in conjunction with the national central banks of the ESCB participating in TARGET2.

TARGET2-Securities (T2S): the Eurosystem's single technical platform enabling central securities depositories and national central banks to provide borderless and neutral core securities settlement services in the central bank money in Europe.

Targeted longer-term refinancing operations (TLTROs): liquidity providing reverse operations executed in the Eurosystem through standard tenders, over a window of two years, by way of fixed-rate tender procedures, aiming to promote lending to households and non-financial corporations by credit institutions in euro area countries.