

LATVIJAS BANKA: ANNUAL REPORT 2020



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; 0.0 magnitude less than half of the unit employed.*

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ABBREVIATIONS

AML/CFT	anti-money laundering and combating the financing of terrorism and proliferation
AS	joint stock company
BIS	Bank for International Settlements
CSB	Central Statistical Bureau of Latvia
CSDR	European Union Central Securities Depositories Regulation
EBA	European Banking Authority
EC	European Commission
ECB	European Central Bank
ECMS	Eurosystem Collateral Management System
EFC	Economic and Financial Committee
EKS	Latvijas Banka's electronic clearing system
ESCB	European System of Central Banks
ESRB	European Systemic Risk Board
EU	European Union
Eurostat	statistical office of the European Union
FCMC	Financial and Capital Market Commission
GDP	Gross Domestic Product
HICP	Harmonised Index of Consumer Prices
IMF	International Monetary Fund
LTRO	longer-term refinancing operations
MFI	Monetary Financial Institution
OECD	Organisation for Economic Co-operation and Development
OPEC	Organization of Petroleum Exporting Countries
OPEC+	OPEC Member States and the Republic of Azerbaijan, the Kingdom of Bahrain, Brunei Darussalam, the Republic of Kazakhstan, Malaysia, the United Mexican States, the Sultanate of Oman, the Russian Federation, the Republic of South Sudan, and the Republic of Sudan
PEPP	Pandemic Emergency Purchase Programme
PSPP	public sector asset purchase programme
SDDS Plus	Special Data Dissemination Standard Plus
SEPA	Single Euro Payments Area
SIA	limited liability company
SSM	single supervisory mechanism
TLTRO	targeted longer-term refinancing operations
UK	United Kingdom
US	United States of America



2020 was a very difficult year. The global pandemic weighed on economic activity, restricted travel, heightened the uncertainty surrounding the future, significantly reshaped the work habits and daily lives of all of us. Despite that, we have implemented some major and really important projects. Covid-19 has already changed and is still going to change a lot of what we are doing and the ways of doing it. Many changes to our daily routines remain yet to be seen. A new normal or a new standard is being born.

The pandemic is far from over, despite the successful development of the Covid-19 vaccines in record time underpinning a more optimistic future outlook. We will clearly be dealing with the fallout from Covid-19 for at least several years. The virus has also brought sweeping and permanent changes to many areas of our lives such as education and work environment, the importance of digital solutions, travelling habits and health considerations.

Addressing the economic effects of the Covid-19 pandemic required a strong and coordinated response, and central banks provided swift and crucial assistance to national governments, businesses and society at large by implementing accommodative monetary policies and safeguarding financial stability. The record-low interest rates maintained by central banks encouraged governments to provide unprecedented crisis support to households and businesses. Accommodative monetary policies helped the global economy to steer confidently through this raging storm.

Latvia was also able to very directly appreciate the positive effects of its past geopolitical choices of joining the European Union and the euro area. Common economic and monetary policies have meant that, for the first time in its history, Latvia has been able to counter the crisis independently, like a grown-up: we can make our own decisions and define our economic policy preferences, we enjoy free access to financial markets at very good prices, benefiting from the favourable financing conditions.

Central banks, including Latvijas Banka, underwent further operational changes in 2020, increasingly focusing on their role of working for the benefit of the society. Central banks are broadening the scope of their policies from merely pursuing the price stability objective in its traditionally narrow interpretation to a wider perspective encompassing sustainability and climate change aspects that are important to deliver an effective monetary policy as well as to improve the population's quality of life.

The modern world has changed the ways in which the population can both learn about the monetary policy decisions and influence them. Central banks increasingly listen to

the views of the general public; the monetary policy strategy review, to which Latvijas Banka is an active contributor, is an excellent tool in this process in the euro area.

As to the developments concerning Latvijas Banka, this Report will provide a detailed insight into the institution's accomplishments in various areas: in providing the infrastructure for cash and non-cash payments, reliable financial statistics and Credit Register data, contributing to innovations and the development of modern payment solutions and supporting the government with economic analysis in these challenging circumstances. I would like to stress that we are highly appreciated by Latvia's society because of our high quality work based on analysis and objective argumentation. This is confirmed by the very high demand for our analytical involvement, considerably exceeding our current capacity. We intend to continue developing this area.

I would like to draw particular attention to the changes in Latvijas Banka's operational strategy, highlighting the near-term priorities and most significant tasks. Our objective is to become one of the most powerful central banks in Northern Europe acting in Latvia's public interest and contributing to the development of the Eurosystem. We are a transparent, efficient and cooperative institution, and we are implementing a culture of innovation. Latvijas Banka's priorities are effective and active participation in shaping and implementation of the Eurosystem's monetary policy and being Latvia's leading economic and financial competence centre, contributing to analysis-based decisions aimed at sustainable economic development and safeguarding the stability of the financial system. We are building and supporting a reliable, effective and innovative payments infrastructure, strengthening the economic and financial literacy of the public, we are a modern, transparent and efficient national central bank.

Despite being difficult, last year was also a successful year. For that, I would primarily like to thank my colleagues who quickly adapted to the new circumstances without losing their passion for work and energy. I am also extremely grateful to their families whose understanding and support helped us work successfully, achieve and even exceed the defined targets.

Let us preserve this dedication and make it even stronger! The coming years are likely to be eventful as usual, with many challenges and opportunities for both the Latvian economy in general and Latvijas Banka in particular, also considering the upcoming merger with the FCMC. This will result in a fully integrated institution that will build a stronger and more powerful backbone of Latvia's financial sector.



Mārtiņš Kazāks
Governor of Latvijas Banka
Riga, 26 April 2021

VISION, MISSION AND VALUES OF LATVIJAS BANKA

VISION

Latvijas Banka is an **influential central bank in Northern Europe** acting in Latvia's public interest and contributing to the development of the Eurosystem.

MISSION

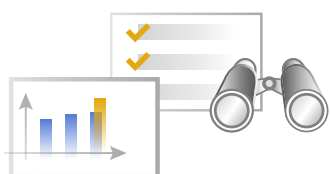
Latvijas Banka's mission is to promote sustainable economic development. Price stability, modern and reliable payments infrastructure as well as a sound financial system are prerequisites for Latvia's economic growth and prosperity of its people.

VALUES

- Competence
- Responsibility
- Result-orientation

Latvijas Banka is a **transparent** and **cooperative** institution, active in voicing and explaining its views.

LATVIJAS BANKA'S PRIORITIES



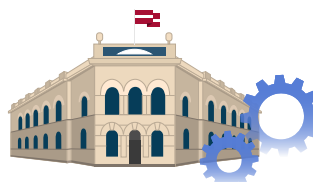
Economic analysis and research



Economic and financial literacy of the public



Reliable, effective and innovative payments infrastructure



Modern, transparent, innovative and efficient institution

2020 IN FIGURES

in Latvia and the euro area

ECONOMIC GROWTH

 *in Latvia*
-3.6%

The Covid-19 pandemic was weighing on economic growth


 *in the euro area*
-6.6%



EXPORTS

 *in Latvia*
-2.7%

Individual commodity groups supported the resilience of exports against uneven external demand

 *in the euro area*
-9.4%



INFLATION

 *in Latvia*
0.1%

The decline in economic activity was also reflected in price changes

 *in the euro area*
0.3%



WAGE BILL

 *in Latvia*
1.5%

While employment was declining, higher wages and low inflation maintained the purchasing power

 *in the euro area*
-2.2%



UNEMPLOYMENT

 *in Latvia*
8.1%

Government support measures were holding down unemployment growth

 *in the euro area*
7.8%
(estimate)



LENDING

 *in Latvia*
-1.8%*

Both banks and borrowers became more cautious

 *in the euro area*
4.3%



* Taking into account the structural changes in the credit institution sector.

MONETARY POLICY

Interest rate on new loans to non-financial corporations

 *in Latvia*
3.0%

Significant monetary policy support ensured low interest rates

 *in the euro area*
1.4%



FISCAL POLICY

Government deficit

 *in Latvia*
-4.5%
of GDP

Accommodative fiscal policy supported businesses and household income

 *in the euro area*
-7.2%
of GDP
(estimate)



Sources: Latvijas Banka, ECB, CSB and Eurostat.

LATVIJAS BANKA IN 2020

BACKBONE OF LATVIA'S PAYMENT SYSTEM

The daily average processed
via Latvijas Banka's systems:

345 600
payments
+49%
compared to 2019

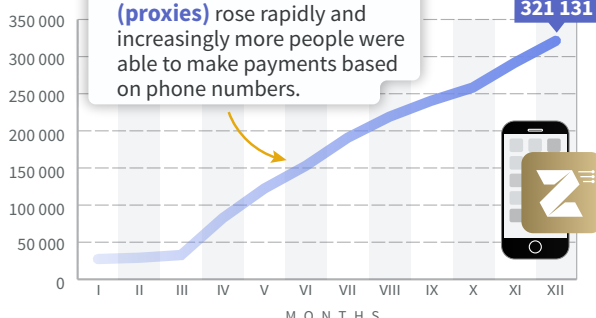


totalling
1.59 billion
euro
+37%
compared to 2019



The volume of payments processed via **the instant payment service** increased 1.9 times to stand at 11.8 million in 2020 overall and their value increased 2.1 times to 2.5 billion euro.

The number of instant links (proxies) rose rapidly and increasingly more people were able to make payments based on phone numbers.



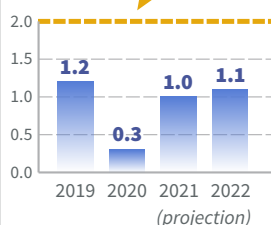
EURO - SECURE MONEY

931 euro counterfeits were identified in Latvia. This is 12% less than in 2019.



EURO AREA INFLATION (%)

Eurosystem's medium-term objective: below, but close to 2%



ECONOMIC ANALYSIS



Participation in drafting proposals on mitigating the consequences of the Covid-19 pandemic, financial sector development and other areas. Analysis of topical economic issues, inter alia government debt sustainability and Latvia's competitiveness.

PUBLIC ENGAGEMENT



As part of the monetary policy strategy review, Latvijas Banka heard opinions of 15 leading non-governmental organisations in Latvia. Active collaboration with the financial sector, business organisations and other partners.

ECONOMIC AND FINANCIAL LITERACY



The production of the digital teaching aid "Mana ekonomika" ("My Economics") for schools.

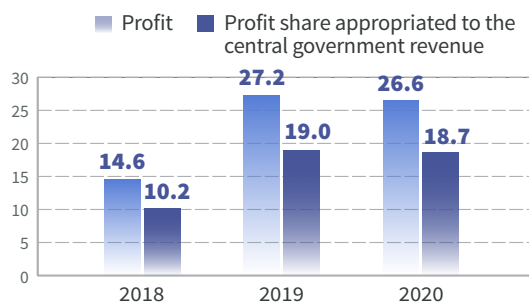
670 interactive exercises

REDUCING THE BURDEN



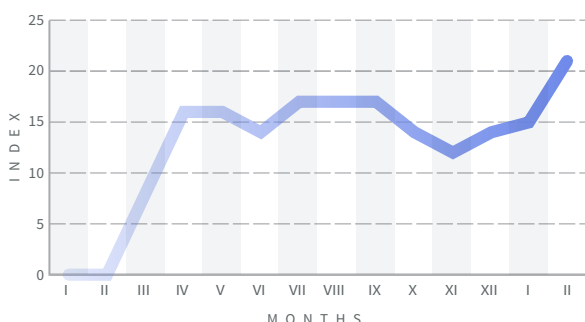
In cooperation with partners, legislative amendments were approved **releasing thousands of people from their hopeless mortgage obligations** which arose during the 2008 crisis and enabling them to become active participants in the economy.

PROFIT SHARE (in millions of euro)



Over the last five years, the profit totalled **104.0 million euro**, of which **71.0 million euro** appropriated to the central government revenue.

PUBLIC CONFIDENCE



Source: SIA "Latvijas Fakti".

EFFICIENCY

Virtual assistant **Mona** has joined the team.



6300 queries submitted by **3368** users were resolved

38 queries per day on average

Operating expenses



Operating expenses were 4 million euro or **11% lower than in the previous year**. Despite the expanding range of the provided services, the number of employees has decreased by more than 12% (from 479 to 421 in 2020).

GLOBAL ECONOMIC DEVELOPMENTS

The Covid-19 pandemic shock significantly affected the global economy in 2020

Covid-19 was spreading at an alarmingly rapid pace and created a considerable pressure on health care systems worldwide revealing the low preparedness of countries in their fight against public health threats of this type and magnitude. To contain the spread of the virus, countries were forced to implement social distancing measures and mobility restrictions. Thus, a large share of the global economy became idle. The services sectors providing services in person were hit particularly hard as their options to continue their operation in a social distancing environment were limited.

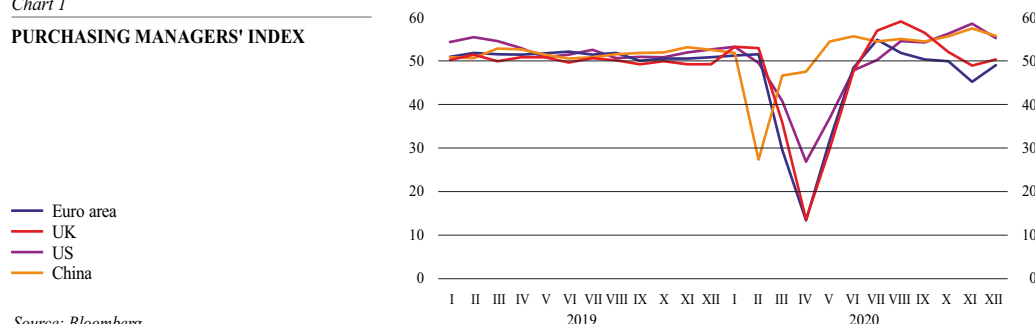
Central banks provided decisive and sizeable monetary policy support to the global economy resulting in lower volatility and uncertainty in the financial markets, thus maintaining favourable financing conditions. With financial markets continuing to function successfully even under high stress, businesses were able to attract the funds necessary to continue operations. Governments around the world had the opportunity to increase fiscal support. Channelling government financial resources towards health care systems facilitated effective implementation of preventive measures to contain the spread of the virus and helped reduce the damage to public health. Furthermore, government support measures partly offset the decline in household income caused by the Covid-19 pandemic crisis, thus also easing social tensions, as well as provided support to businesses in the form of guarantees, loans, grants, tax holidays and loan payment moratoriums.

Political disagreements and tensions as well as unrests in several countries created additional uncertainty and instability in both the real economy and the financial markets

Despite the sizeable support provided by central banks and governments, uncertainty remained high. The global scale of the pandemic, unrests, protests and the hype around the presidential elections in the US, Brexit, disagreements among EU countries regarding the recovery plan, the war in the Nagorno-Karabakh region, the controversial National Security Law of Hong Kong as well as other events have created unfavourable conditions for international trade, investment and the overall economic activity in various regions of the world (for the Purchasing Managers' Index, see Chart 1).

Chart 1

PURCHASING MANAGERS' INDEX



Source: Bloomberg.

The fall in the global economic activity also affected demand for various commodities. The negative demand shock was so sudden and strong that e.g. oil prices declined to record lows in the first half of the year. Concerned about the options to find the necessary oil storage facilities, several oil market participants were temporarily prepared to pay the buyer for the purchase of oil. With global demand rebounding in the second half of the year, largely on account of an effective containment of the virus in China, accommodative national fiscal policies and more targeted restriction strategies, an upward trend in commodity prices was also observed.

The pandemic-induced changes and shocks also affected financial markets. The panic in financial markets reached its peak in spring resulting in a sharp sell-off of risky assets and a significant drop in stock prices. In search of safe investment opportunities, investors increasingly chose to invest their funds in government debt securities of developed and stable countries, and the US dollar reached its annual high. However, against the backdrop of a sharp cut of the Federal Reserve base rates and higher central government spending, the spreads between the real interest rates in the US and the euro area shrank and the relative attractiveness of the US dollar in comparison with the euro also declined.

The vaccination roll-out gives hope for further normalisation of the situation

Although at the end of 2020 the Covid-19 morbidity and mortality rates remained high and the news of the spread of new virus variants gives rise to concerns over further tightening of restrictions, the approval of vaccines and their roll-out imply that people may gradually return to their normal daily lives. Moreover, the intention of the new US President to increase the fiscal support even further, expectations of funds absorption from the European Recovery and Resilience Facility, the EU-UK agreement on their post-Brexit relations reached in December and the strong economic recovery in China reinforce the hope for further recovery of the global economy. This is also confirmed by the optimism in the global capital markets where the stock prices of non-financial corporations have risen to the levels observed prior to the first wave of the Covid-19 pandemic, and their upward trend continues.

EURO AREA ECONOMY AND EUROSISTEM'S MONETARY POLICY

A record-steep decline in growth, sizeable support measures and hopes for a solution to the pandemic

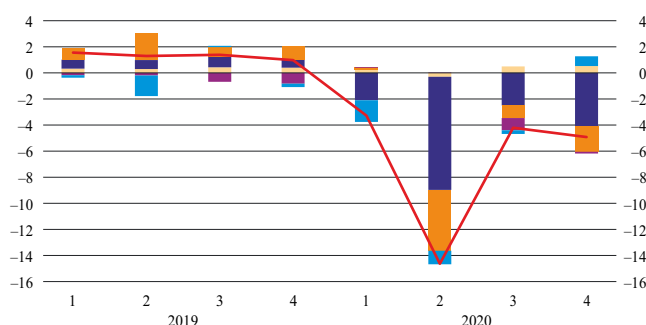
The Covid-19 pandemic became the main factor behind dramatic changes in the economic development of the euro area, with its economic activity decreasing rapidly and the uncertainty about the future growing. Faced with Covid-19, the infectious virus still little known at that time, in the first half of the year almost all euro area countries introduced strict measures which brought the activity in several economic sectors to a halt. In the second half of 2020, the economy shrank at a pace unseen since World War II and GDP declined by 14.6% year-on-year (see Chart 2). With the spread of Covid-19 slowing down in the summer months, restrictions were eased, which lead to a resumption of economic activity. However, with the onset of the second wave of the Covid-19 pandemic at the end of the year, the Member States resumed their fight against the spread of Covid-19. Thus, the economic recovery, which had just started, came to a halt. In 2020 overall, the euro area economy shrank by 6.6% year-on-year. Despite the fact that the Covid-19 pandemic was spreading in all euro area Member States, the impact on their economic activity varied due to the differences in their economic structures and sector contributions

Chart 2

EURO AREA GDP

(year-on-year, seasonally and calendar adjusted data;
%; percentage point contributions)

- Government consumption
- Private consumption
- Investment
- Changes in inventories
- Net exports
- GDP



Source: Eurostat.

to their economic growth. The vaccine solutions and vaccination roll-outs represent an important corner stone in solving the current health crisis and inspire optimism in a gradual economic recovery, with the mobility restrictions being eased and households and businesses returning to their usual habits and activities.

The economic decline was reflected in lower private consumption and shrinking investment. Meanwhile, government consumption supported the economy, and the implemented support measures dampened the negative impact of the crisis on the labour market

Both forced and precautionary savings increased due to social distancing and mobility restrictions as people were deterred from spending or their spending was restricted. In 2020, during the period of the tightest restrictions, the level of savings reached up to 24.6% of disposable income compared to an average of 12.4% of disposable income in 2010–2019. The fall in private consumption by 4.3% was the main factor having a downward impact on GDP. Moreover, restrictions and uncertainty over the future economic development also negatively affected investment which decreased by 1.8% in 2020. At the same time, the support measures implemented by the euro area governments helped mitigate the consequences of the crisis by supporting businesses and households. Therefore, unemployment only grew by less than one percentage point, i.e. from 7.4% in December 2019 to 8.1% in December 2020.

The impact of the government restrictions on various economic sectors has varied notably. During the first and second waves of the Covid-19 pandemic, the retail trade sector (wearing apparel and footwear in particular) and the services sector (accommodation and food service activities in particular) were hit the hardest. At the same time, the experience and knowledge gained during the first wave of Covid-19 allowed for the introduction of more targeted restrictions at the onset of the second wave. Thus, the recovery rate of foreign trade and production did not slow down in the last months of 2020, which helped to reduce the economic losses.

The fall in the economic activity was also reflected in the price level, with the euro area experiencing a brief period of deflation. Euro area inflation declined from 1.2% in 2019 to 0.3% in 2020. The fall in inflation was most likely driven by the global oil price dynamics as well as restricted demand for services. A positive contribution to inflation came from an increase in food prices driven by resilient demand and a gradual rise in global food prices.

In its fight against the Covid-19 crisis, the ECB provided significant monetary policy support

While the ECB kept all its key interest rates unchanged, it eased its monetary policy stance several times throughout the year by employing several unconventional monetary policy instruments. In response to the shock effects on the real economy and the financial markets caused by the Covid-19 pandemic crisis, the Governing Council of the ECB decided to launch a new PEPP. The programme will run until the end of March 2022, with its total envelope amounting to 1850 billion euro. The PEPP provided considerable support to stabilise the financial market and contributed to particularly favourable monetary policy conditions. Furthermore, the traditional asset purchase programme was expanded by another 120 billion euro in 2020, while also retaining the previous monthly pace of the net asset purchases of 20 billion euro per month. Besides, measures were taken and LTRO and TLTRO III conditions were improved to ensure immediate liquidity support to the euro area financial system and to facilitate lending. These and other ECB measures have played a key role in mitigating the downside risks and the negative impact on the economy and in ensuring the financial market stability.

In 2020, a sizeable review of the ECB's monetary policy strategy was initiated, covering the quantitative formulation of price stability, a set of monetary policy instruments, economic and monetary analysis and the practice of communication. The review analyses the interrelationship between monetary policy and fiscal policy, financial stability, employment and environmental sustainability. As part of its strategy review, the ECB organises listening events intended for the general public as well as representatives of civil society organisations and academia to express their views on the future of monetary policy. According to the plan, the results of the strategy review will be presented in the second half of 2021.

ECONOMIC DEVELOPMENT OF LATVIA

FINANCIAL CONDITIONS AND MONEY SUPPLY

Ample liquidity surplus in the banking system and further monetary policy accommodation in the euro area effectively eased the financial market tensions caused by the Covid-19 pandemic

Interest rates in Latvia's financial market remained low overall, although the lending rates in some segments increased. Covid-19-related caution and restrictions were reflected in a significant rise in deposits, whereas lending remained muted as before, with no significant decline in the loan portfolio size or deterioration of its quality.

Latvia's actions to contain the Covid-19 spread and the significant measures to support the economy were also highly appreciated by the rating agencies. At the beginning of the year, the international rating agency S&P Global Ratings upgraded Latvia's sovereign credit rating from A to A+ on expectations of a fall in its public debt and in appreciation of its progress in the field of AML/CFT/CFP, and, during the Covid-19 crisis, all leading rating agencies maintained Latvia's credit ratings unchanged.

The high liquidity level resulted in a progressing decline in the role of the money market financing: the value of money market transactions involving Latvia's credit institutions decreased, with a minor rise only observed in domestic transactions in foreign currencies.

The significant Eurosystem's monetary policy support helped to preserve favourable financing conditions and enabled the Latvian government to launch bonds at low yields on international markets in a very short time, thereby providing access to additional financing for stimulating the economy hit by the Covid-19 crisis

The Latvian government sold 3-year and 6-year bonds in the total amount of 1.55 billion euro on external markets in March and April. It also successfully issued 2-year, 5-year and 7-year bonds on the domestic market, with the yield on the 5-year bonds decreasing from 0.09% in December 2019 to -0.07% in July 2020 and the yields on government securities on the secondary market overall sinking to their historical lows. At the same time, the optimistic outlook and progress in containing the virus spread facilitated a 9.7% rise in Latvia's share index OMXR and even a 11.3% increase in Baltic share index OMXBBI towards the end of the year.

The demand for foreign exchange transactions decreased as a result of the Covid-19 containment measures. A decline was observed in all categories of foreign exchange instruments, with spot transactions recording the most significant fall. Foreign exchange transactions in cash were particularly strongly affected by the pandemic: in April and May, the value of those transactions decreased by 80% in comparison with the same

months of the previous year. At the end of summer and in autumn, along with the easing of the pandemic-related restrictions and the pick-up in economic activity, the foreign exchange business also recovered, albeit overall remaining below the levels seen in the previous years. The bulk of cash transactions were carried out in US dollars and British pounds sterling.

In the pandemic circumstances, banks pursued cautious lending policies, business and consumer sentiment deteriorated and the propensity to borrow decreased

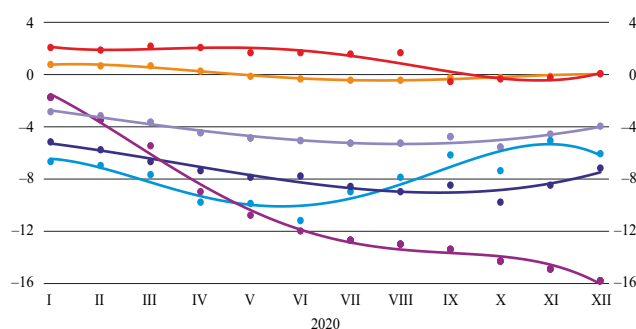
Not all sectors were affected by the crisis. Lending to energy and water supply sectors implementing infrastructural projects increased significantly. Loans to domestic customers (excluding the government) decreased by 4.0% in 2020 (see Chart 3). Even looking past the impact of restructuring of the credit institution sector, the loan portfolio overall contracted by 1.8% in the course of the year, including a 2.8% decline in loans to non-financial corporations. A notable fall by 15.8% was recorded for consumer credit. Overall, new loans totalled 1.8 billion euro in 2020, falling by 5.0% in comparison with the previous year.

Chart 3

DOMESTIC LOANS

(outstanding amounts; annual percentage changes)

- Financial institutions
- Non-financial corporations
- Households
- Loans for house purchase
- Consumer credit
- Total (excluding government).



Source: Latvijas Banka.

The announced moratorium on principal repayments and the individual borrower relief measures implemented by banks helped to prevent lending from contracting even more significantly. At the end of December, loans with an effective moratorium on principal repayments and individual relief measures constituted about 10% of the aggregate loan portfolio of credit institutions.

Interest rates on new corporate loans in euro remained broadly unchanged in 2020 (3.0%)

Credit terms and conditions, including interest rates, were tightened in the first half of 2020 on account of the uncertainty surrounding the economic development due to the Covid-19 pandemic. In the second half of the year, when the first wave of Covid-19 was over, the credit terms and conditions were eased, including a reduction in interest rates. A significant role was played by the government support measures, while, at the beginning of the Covid-19 crisis, households were actively using the loan repayment deferral option, and the interest rates on renegotiated loans remained unchanged. Overall, the interest rate on loans to households for house purchase declined by 0.1 percentage point in 2020 (to 2.6%), whereas the consumer credit rate edged down by 0.3 percentage point (to 14.8%). At the same time, in the corporate segment, a growing difference was observed between the costs of finance of large enterprises and small and medium-sized enterprises whose credit risk is considered higher and who might find it more difficult to fight the consequences of the pandemic (see Chart 4).

Chart 4

INTEREST RATES ON NEW EURO LOANS
(annual average; flow-weighted; %)

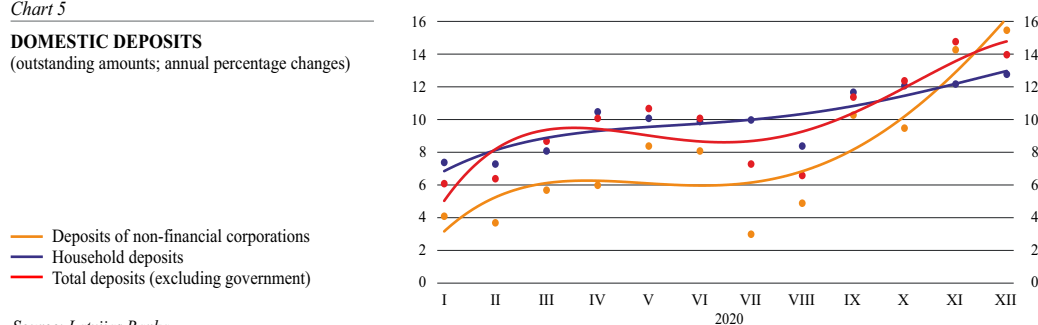
Source: Latvijas Banka.

Despite the sharp economic downturn, due to the conservative approach to lending pursued over the most recent years, the quality of loans did not deteriorate significantly in 2020

Nevertheless, the implemented measures deferring obligations (for example, moratoriums on loan repayments or tax holidays) mask potential financial problems of the borrowers. For most of non-financial corporations, the moratorium expired at the end of 2020, whereas for the majority of households it will expire at the end of the first half of 2021. Considering the expiry of the announced moratoriums on principal repayments and the government support measures in the course of 2021, banks may have to build additional provisions if the quality of their loan portfolios deteriorates.

In 2020, the uncertainty caused by the new circumstances and restrictions on entertainment and travel contributed to an increase in both precautionary and forced savings of households. At the same time, the corporate cash flows were bolstered by the export opportunities and the provided government support. As a result, domestic deposits with credit institutions grew significantly by 14.0%, which is almost twice as much as in the respective period of the previous year and the highest rate since 2007 (see Chart 5). Due to the low interest rates and high uncertainty, demand deposits were the sole contributors to the overall deposit growth.

Chart 5

DOMESTIC DEPOSITS
(outstanding amounts; annual percentage changes)

Source: Latvijas Banka.

The interest rates on demand deposits both for households and businesses have been close to zero already for several years. Also, the interest rates on new fixed-term corporate deposits in euro have been almost zero for a long time. The interest rates on new fixed-term deposits by household went down from 0.5% in 2019 to 0.4% in 2020.

The high level of capitalisation and liquidity enabled credit institutions¹ to successfully absorb the shocks caused by the first wave of the Covid-19 pandemic

At the end of 2020, the total capital ratio of credit institutions was 25.7% as compared

¹ 16 credit institutions, including three branches of foreign credit institutions, were registered in the Republic of Latvia at the end of 2020. The credit institution statistics were significantly affected by the cancelling of the AS PNB Banka licence as of 18 February 2020.

to the EU average of 19.7%¹, whereas the liquidity coverage ratio was 371%, with the EU average being 173%. The high ratio levels were ensured by restrictions on dividend pay-outs, the long-term financing provided by the ECB (TLTRO III) as well as the previous structural changes implemented in the banking sector.

The weakening of the economic activity was also reflected by the falling credit institution profit. Moreover, credit institutions built higher provisions for their loan portfolios. Nevertheless, return on equity in credit institutions remained higher than in the EU overall (5.2%; EU average was 2.0%). Credit institutions also fully substituted the parent bank financing by domestic customer deposits, and the ratio of loans to domestic customers to deposits from domestic customers reached a historical low at 73.8%.

MACROECONOMIC DEVELOPMENTS

In 2020, the global economic growth outlook and that of Latvia were significantly influenced by the Covid-19 pandemic developments

A fall in the freight volumes transported through ports and by railway, observed already since the beginning of the year, as well as the intensified spread of the Covid-19 pandemic in March caused an economic slump. The Covid-19 containment measures, precautionary considerations and income losses were significant supply and demand shocks causing a deep economic contraction in the second quarter (7.0% quarter-on-quarter), with the hospitality and entertainment sectors suffering the most serious consequences. Relatively successful containment of the first wave of the Covid-19 pandemic enabled easing of the restrictions in summer, thereby supporting growth and resulting in a fast economic recovery. The rebound in the economic activity, however, lost momentum with the start of the second wave of the pandemic, when due to a gradual deterioration of the epidemiological circumstances restrictions were renewed towards the end of the year. As many companies had managed to adapt to the new conditions, the economy was overall resilient to the negative impact of the second wave of the pandemic and continued to grow. At the same time, the year-end growth was uneven, as there was an increase in the productive sectors, especially in the exporting ones, and another fall in the services sectors. Although the fiscal policy support measures helped to ease the pressures on businesses and households, Latvia's economy contracted by 3.6% in 2020.

The global epidemiological challenges resulted in a lower external demand for Latvia, yet the competitiveness of Latvia's goods remained robust

Latvia's main trade partners fought the crisis with various success. Nevertheless, their economic activity was overall more resilient compared to the rest of the world. Among the most significant partners, the most dramatic fall in external demand was observed in the United Kingdom and Russia. Nevertheless, as the demand for Latvia's major exports of goods remained relatively high and also on account of individual supply-side factors, the overall exports of goods remained resilient. This resilience was largely achieved by the wood industry and agriculture with its record-high grain harvest as well as the demand for food products. The transition to remote work also boosted the exports of electrical equipment and machinery. Latvia's export market shares in both global imports and the EU market increased in 2020. Regardless of an even slightly weaker cost competitiveness, this increase in the market shares could be partly explained by the narrowing of the global trade in mineral products and capital goods which are not dominant in Latvia's exports. The imposed restrictions resulted in a steep decline in Latvia's exports of services, contributing to a 2.7% decrease in total exports. Mostly because of the restrictions, travel and transportation services were the components of

¹ Hereinafter in this Section the data published by the EBA are used.

services exports that suffered the most severe losses, whereas the exports of construction, computer and business services even expanded.

Domestic demand contracted under the impact of the imposed domestic restrictions, income losses and the high uncertainty delaying consumption and investment decisions

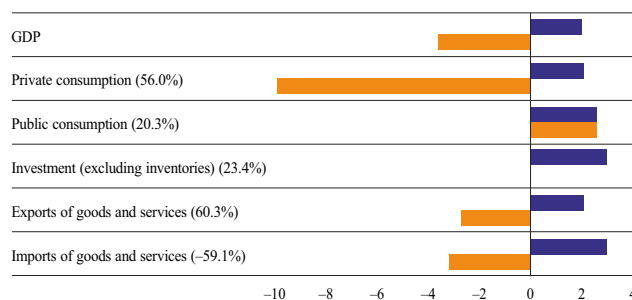
Private consumption plunged by 9.9%. This development was largely driven by the implemented Covid-19 containment measures, making some spending (primarily, on services, including travel, cultural, sports and other events) impossible. Cautiousness in spending, particularly in the second half of the year due to renewed concerns about another surge in the Covid-19 infections, was also reflected in a significant upsurge in precautionary savings. Moreover, restrictions on business resulted in income losses for a part of households (particularly, in low-income population groups), limiting consumption. Despite the high uncertainty causing businesses to evaluate their labour cost reduction options, the average wage continued to grow at an annual rate of 6.2%. This was partly attributable to the rapid fall in employment in sectors where the average wage was below the national average already before the crisis and where low-skilled employees were laid off more often. Nevertheless, a minor increase of 1.5% was retained also in the wage bill. In combination with the low inflation, it supported the purchasing power of the population. The crisis support provided by the government in the form of furlough benefits, wage subsidies and other benefits also helped to stabilise the income level.

Investment was the only component of the gross domestic product that remained unchanged in comparison with 2019 (see Chart 6). Due to the high uncertainty, private sector investors were cautious in their investment decisions and partly postponed them. The investment decisions made by the government were based on its resolution to grant additional financing for road infrastructure upgrades with a view to cushioning the fall in economic activity caused by the crisis. In the crisis circumstances, production capacity was also sustained by measures like loan holiday guarantees and working capital loans granted to businesses affected by the Covid-19 pandemic by AS Attīstības finanšu institūcija Altum. In 2021, investment in further development will be provided by means of loans and guarantees to large and medium-sized businesses as well as via the investment fund set up to support large enterprises. The pandemic had little effect on the foreign direct investment inflows into Latvia (2.6% of GDP). Investment into equity continued, including via reinvested earnings, as the crisis impact on major foreign companies was negligible. At the same time, due to the cautious behaviour of credit institutions and borrowers, credit resources were mostly allocated to only individual sectors implementing infrastructural projects as well as lending to households. New loans initially decreased, particularly during the first wave of the pandemic, followed by a rise and stabilisation in the second half of the year. External liabilities of the corporate sector also decreased.

Chart 6

GDP
(expenditure components; annual percentage changes;
seasonally and calendar adjusted data)

■ 2019
■ 2020



Source: CSB.

Note. Component contributions are provided in brackets (% of nominal GDP).

Weaker domestic demand due to the pandemic was reflected in lower imports of goods and services

The most significant decline in imports of goods was observed in the segments of intermediate consumption and capital goods rather than consumer goods. Consumption contracted notably primarily on account of lower consumption of services. The 3.2% decline in imports, combined with more resilient exports, resulted in a small surplus of goods and services account, which together with the income account surplus translated into a surplus in the current account of the balance of payments (3.0% of GDP). External liabilities of financial institutions and non-financial corporations continued to contract, whereas the public sector's external debt increased on account of the government borrowing as well as Latvijas Banka's participation in the Eurosystem's monetary policy operations. In addition to the shrinking of the external debt of the private sector, foreign assets of financial institutions also contributed to the declining net external debt. As a consequence, Latvia's gross external debt increased to 124.2% of GDP, while its net debt contracted to 14.3% of GDP.

Due to the pandemic, businesses had to adapt to living in the circumstances of necessary caution and the restrictions implemented by the national governments in 2020, yet the effects were uneven across sectors

Initially, the Covid-19 pandemic caused supply chain disruptions, and, with the crisis dragging on, income losses and precautionary considerations also had a downward effect on demand. Yet the most significant factor weighing on economic growth was the direct business restrictions introduced to limit gathering and social contacts. This made the consumption of some services impossible.

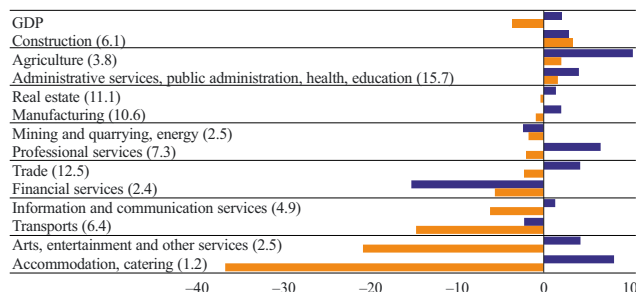
Accommodation and catering services as well as arts, recreation and entertainment services were the sectors most severely hit by the pandemic (see Chart 7). These sectors suffered the most direct negative consequences of the restrictions on gathering and movement. Although the lifting of the restrictions during the summer months and the resulting surge in travellers from the Baltic neighbour states led to some recovery of tourism, the activity remained far below the level of the previous year, and the number of foreign visitors in Latvia's tourist accommodations was the lowest in the last decade. The high season of the entertainment sector, however, coincided with the first and the second waves of the pandemic and the related restrictions, weighing on the sector's growth.

Chart 7

GDP

(value added; annual percentage changes; seasonally and calendar adjusted data)

■ 2019
■ 2020



Source: CSB and Eurostat data; Latvijas Banka's estimates.
Sectoral contributions are provided in brackets (% of nominal GDP).

A steep fall was also recorded in the transport sector, where the downward trend in Russia's transit freight flows through ports and by rail which was observed already before the pandemic continued. Another factor was the negative effect of the Covid-19 containment measures on the performance of road transport and air transport. The temporary production chain disruptions and logistics problems during the first wave of the Covid-19 pandemic as well as lower demand limited the freight turnover in international road transport.

Following a good performance at the beginning of the year, air transport was severely affected by the imposed restrictions. When part of the restrictions was eased in summer, the number of passengers carried by air slightly increased. Nevertheless, with new infections growing, national governments tightened the containment measures, resulting in a steep dive in the number of passengers transported by air.

Manufacturing and trade performed relatively better in 2020. The former was less affected by the second wave of the pandemic towards the end of the year. That can be explained by better adjusted production and supply processes following the first shock in spring and a good year for the wood industry. Because of a recovery in demand and prices as well as less damage from forest infestation, it had managed to progressively increase its output since spring. Wholesale trade was negatively affected by deceleration of the global trade flows, while the effect of social restrictions on retail trade was highly uneven, with trading in basic goods being affected to a lesser extent. Although the government's support measures helped to partly stabilise the level of consumer income, the trade of non-food items was negatively affected by both restrictions on face-to-face business and the cautiousness of households postponing their purchases in the circumstances of prolonged uncertainty.

The Covid-19 pandemic had a little effect on agriculture and forestry where growth was underpinned by the record-high grain harvest and increasing logging volumes. Construction development was stabilised by the government investment in infrastructural construction works as well as favourable weather conditions at the beginning of the year and the ability to continue working also in the pandemic circumstances, particularly outdoors. Further growth was also observed in public services sectors like health care, public administration and education.

Plunging oil prices and weak domestic demand caused by the crisis resulted in a very low inflation

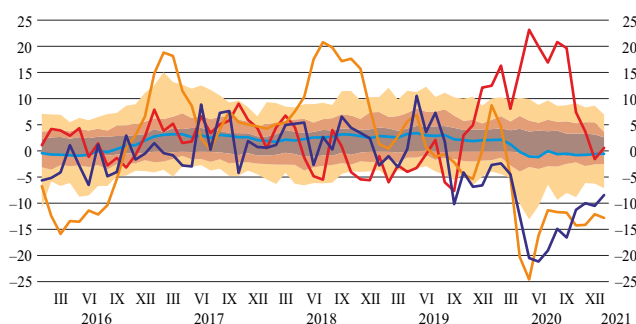
The annual rate of change in consumer prices was mostly negative since April 2020, and the annual consumer price inflation (HICP) was only 0.1% in 2020 (see Chart 8). The prices of some products and services (for example, fuel, accommodation) contracted sharply, while those of 3/4 of products comprised in the consumer price index were growing faster than the headline inflation.

Chart 8

HICP

(percentage distribution of 12-month changes;
163 product groups)

- 90% of products
- 75% of products
- 50% of products
- HICP
- Fruit
- Fuel
- Accommodation services



Source: Eurostat.

Oil prices decreased significantly in the first four months of 2020. This was on account of the negative impact of the spread of Covid-19 on the global economic development and the failure of Saudi Arabia and Russia to agree on oil production cuts. In later months, against the background of positive news about the Covid-19 vaccine development and the new OPEC+ agreement on further oil production cuts, oil prices gradually improved. The pass-through of oil prices to fuel prices took a few weeks and to heating and gas prices – several months. Global food prices increased in the second half of the year, following a decline at the beginning of the year. A weaker domestic demand was manifested most

notably in a generally smaller rise of service prices. At the same time, a further increase was observed in the prices of some services, since the implemented Covid-19 pandemic containment measures and lower customer flows pushed up their costs per customer.

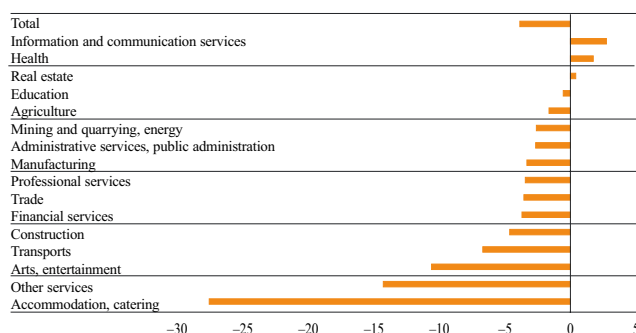
The negative effects of the Covid-19 pandemic on the labour market were partly offset by the government support measures

During the period of shrinking business incomes, employment was sustained by government support provided through furlough benefits and, towards the end of the year, also wage subsidies. The largest decrease in occupied posts was observed in the services sub-sectors most directly affected by restrictions (accommodation and catering, transport, arts, entertainment and recreation) as well as in travel agencies and tour operator business. Employment in other sectors remained relatively stable (see Chart 9 for numbers of employees). At the same time, the number of hours worked decreased more than employment. This was partly reflecting the government support to idle businesses, helping to preserve employment in the months to follow. Unemployment increased moderately during the first wave of the pandemic, followed by a reversal on account of recovering business activity. During the second wave of the pandemic at the turn of the year, the government reintroduced a better tailored employment support framework, and the annual unemployment rate averaged 8.1% in 2020.

Chart 9

NUMBER OF EMPLOYEES

(annual percentage changes; full-time units)



Source: CSB.

The government provided financial support to businesses and households to reduce the fallout from crisis, but tax revenue also contracted

The government deficit reached 4.5% of GDP in 2020, which is the highest level since the previous crisis of 2009. The difference is that the EU fiscal rules were relaxed during the present crisis. This allowed national governments to use their budgets flexibly and increase fiscal deficits in addressing the crisis consequences, to the extent that it did not undermine the sustainability of public finances. The Latvian government had access to borrowing during the present crisis, and the accommodative monetary policy of the ECB ensured very favourable financing conditions. This enabled the government to provide significant support to the economy. The Treasury of the Republic of Latvia issued securities on both international financial markets and the domestic securities market in 2020. As a consequence, the government debt expanded to 12.7 billion euro or 43.5% of GDP at the end of 2020.

The 8.1% rise in the government spending reflects the support provided to various sector businesses and population. Expenditure on current transfers, subsidies and also social benefits increased. The budgeted wages raises for medical and teaching staff as well as additional financing for purchasing equipment to counter the crisis in the health sector and individual means of protection also contributed to higher government consumption. Government investment grew at a moderate rate. The deceleration of the economic activity was reflected in a 0.6% drop in tax revenue, with the fall in business transactions

depleting the revenue from the value added tax. Although the average wage was growing, social insurance contributions were only slightly above the previous year's level, as employment decreased. At the same time, the personal income tax revenue contracted on account of higher tax relief applied since the beginning of the year. The government's crisis support measure of providing an option to postpone tax payments for a period of up to three years also had a downward effect on tax revenue.

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

Latvijas Banka is the central bank of the Republic of Latvia and a member of the ESCB and the Eurosystem.

In its activities, Latvijas Banka complies with the Republic of Latvia and EU legislation, including ECB legal acts in accordance 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 (the Statute of the ESCB and ECB).

Pursuant to the Law on Latvijas Banka, the primary goal of Latvijas Banka is to maintain price stability. Latvijas Banka has the following main tasks:

- participate in defining and implementing the Eurosystem's monetary policy;
- manage the foreign reserves and other financial investments;
- ensure currency circulation in Latvia and participate in ensuring the 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 countries 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 and the Cabinet of Ministers of the Republic of Latvia on monetary policy issues and other issues related to the performance 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;
- implement the functions of the National Analysis Centre and the Coin National Analysis Centre, ensuring efficient analysis of currency counterfeits.

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.

In 2020, efforts were made to ensure the implementation of the amendments to the Law on Latvijas Banka. The amendments were adopted by the Saeima of the Republic of Latvia on 21 November 2019. The amendments tasked the Cabinet of Ministers with submitting to the Saeima a draft Law on Latvijas Banka stipulating its governance framework and operation and providing for the incorporation of the FCMC into Latvijas Banka, respecting the independence of its monetary policy functions and the functions of the finance and capital market supervisor and resolution authority. At the same time, in accordance with the task of the Budget and Finance (Taxation) Committee of the Saeima¹, the Ministry of Finance, Latvijas Banka and the FCMC performed the following activities related to the incorporation of the FCMC into Latvijas Banka: carried out the benefit and risk assessment and the estimation of the financial impact, provided a description of decision-making competences, the macro-prudential policy and the mechanism for

¹ The Minutes of the meeting of the Budget and Finance (Taxation) Committee of the Saeima held on 11 September 2019 lay down the task for the Ministry of Finance to submit, in cooperation with Latvijas Banka and the FCMC, the assessment of the foreseen incorporation of the FCMC into Latvijas Banka by 30 June 2020.

ensuring independence of supervisory and resolution functions. The Budget and Finance (Taxation) Committee of the Saeima, following the examination of the above assessment, decided¹ to pursue work on the draft law.

In light of the above, Latvijas Banka and the FCMC, in cooperation with the Ministry of Finance and other public institutions, drafted the Law on Latvijas Banka in 2020. It regulates operation of Latvijas Banka in its capacity as the central bank and supervisor of the financial market and stipulates that the integrated institution will commence work on 1 January 2023.

In 2020, 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 Eurosystem's monetary policy and decision-making related to the tasks of the Eurosystem and the ESCB.

The representative of Latvijas Banka, in cooperation with the FCMC, participated in the work of the Supervisory Board of the ECB, ensuring the fulfilment of the ECB tasks relating to the supervision of credit institutions and preparing the respective draft decisions to be submitted to the Governing Council of the ECB according to the non-objection procedure.

Representatives of Latvijas Banka participated in the Eurosystem/ESCB committees (see Appendix 6) and working groups, dealing with issues related to monetary policy, market operations, financial stability, payment systems, euro banknotes, statistics, international relations, communication, financial accounting and other issues.

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, representatives of Latvijas Banka regularly participated in the preparation of decisions concerning the economic development and financial stability of the EU, the development of the EU economic policy strategy and improvement of crisis instruments with a particular focus on building close economic cooperation with the post-Brexit UK, on EU-level measures to overcome the crisis caused by the Covid-19 pandemic, on facilitating economic resilience and sustainable development, taking account of the opportunities and challenges resulting from both digitalisation and climate change.

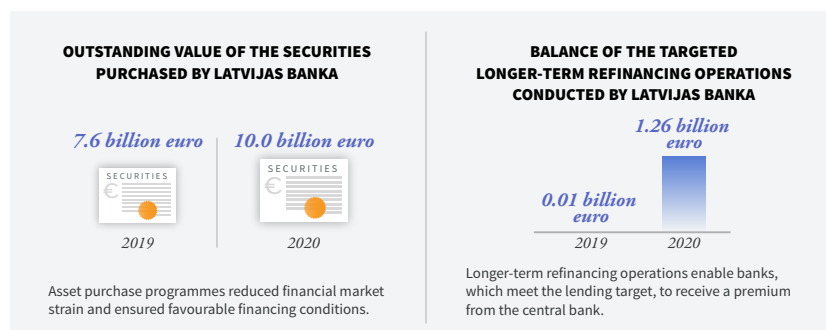
Representatives of Latvijas Banka participated in the EC and Eurostat working groups, focusing on issues related to euro coins, economic forecasting and statistics.

In 2020, Latvijas Banka participated in the work of the ESRB which made decisions on the issues related to the EU macroprudential policy. Representatives of Latvijas Banka also engaged in the work of the Advisory Technical Committee of the ESRB and its working groups.

With the FCMC's consent, a representative of Latvijas Banka also participated in the work of the Board of Supervisors of the EBA whose general objective is to maintain financial stability and to safeguard the integrity, efficiency and orderly functioning of the banking sector.

¹ The decision of the meeting of the Budget and Finance (Taxation) Committee of the Saeima held on 2 June 2020.

IMPLEMENTATION OF EUROSISTEM MONETARY POLICY IN LATVIA



The Eurosystem continued to implement an accommodative monetary policy, thus providing an opportunity for its counterparts in Latvia to use a record number of monetary policy instruments.

Latvijas Banka participated in the PSPP in 2020 and also in the PEPP (since March) to mitigate the tension and the adverse effects on the economy caused by Covid-19. Latvijas Banka also reinvested the principal amounts of securities of the above programmes. Over the year, Latvijas Banka's balance sheet item "Securities held for monetary policy purposes" grew from 7.6 billion euro to 10.0 billion euro¹. In March, the Eurosystem included short-term commercial papers of non-financial corporations in the assets purchase programme, but in April Member States eased the collateral framework temporarily and extended the opportunities for using several types of collateral. Assets of that type are additional credit claims, which can be employed as collateral in the Eurosystem's credit operations on a temporarily basis. Additional credit claims may also include loans to households as well as similar loan pools made up of, e.g. loans, consumer credit and mortgage loans to non-financial corporations as well as small and medium-sized enterprises. In the case of additional credit claims compared to the regular ones, lower quality of loans is permissible along with the application of a higher valuation haircut.

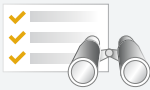


Overall, the Eurosystem's holding of the Latvian government securities totalled 2.8 billion euro² at the end of 2020 (2.4 billion euro at the end of 2019).

The excess liquidity of Latvian credit institutions' settlement accounts opened with Latvijas Banka increased from the average of 5228 million euro in December 2019 to the average of 5412 million euro in December 2020. The minimum reserve requirements for credit institutions expanded from 156 million euro at the end of 2019 to 168 million euro at the end of 2020. The large excess liquidity usually does not generate interest of credit institutions in Eurosystem credit operations. However, the outstanding amount of LTROs at Latvijas Banka was 1260.0 million euro at the end of 2020, rising from the average of 30.0 million euro in 2019 to the average of 637.7 million in 2020. The particularly favourable TLTRO conditions during the Covid-19 crisis contributed to such an increase in demand, since the interest rate for counterparties, whose eligible net lending reached a certain level of lending indicators, was reduced from June 2020 to June 2021, providing that it would be 50 basis points below the average rate on deposit facility. This enabled several credit institutions to receive credit resources at very favourable rates and use them for lending to the economy.

Latvian credit institutions also used the main refinancing operations and the marginal lending facility, albeit in insignificant volumes. The Eurosystem also introduced pandemic emergency longer-term refinancing operations, but Latvian credit institutions did not make use of them.

¹ <https://www.bank.lv/en/about-us/reports/lb-monthly-balance-sheet>

² <https://www.ecb.europa.eu/mopo/implement/omt/html/index.en.html>.

PRIORITY DIRECTIONS IN 2020	PUBLICATIONS	PRESENTATION OF RESEARCH RESULTS
 <p>Research activities continued in three priority directions:</p> <ul style="list-style-type: none"> ▪ monetary policy transmission; ▪ fiscal policy, including the assessment of the support measures associated with Covid-19; ▪ long-term growth and competitiveness. 	 <p>The analysis by Latvijas Banka's researchers has been used in the Eurosystem's monetary policy strategy review; in mitigation of economic consequences resulting from Covid-19 and in other areas.</p>	 <p>In 2020, papers by researchers were presented at conferences, seminars and working groups – the academic ones and those organised by other institutions. Seminars, to which highly qualified experts from other countries were invited to present their research results, were organised.</p>

Economic analysis and research are important areas of Latvijas Banka's operation. They deal with the latest economic developments in Latvia and the euro area as well as project future development trends. Analysis-based understanding of the current developments is an essential precondition for defining quality economic policy decisions. This becomes particularly topical in periods of economic downturns and amid heightened uncertainty which describe the tension caused by the Covid-19 pandemic in 2020 rather precisely.


The pandemic and the related response of economic policies both in Europe and Latvia also made Latvijas Banka review its research priorities fundamentally and adapt the macroeconomic forecasting process.

Macroeconomic forecasting was organised four times at Latvijas Banka in 2020. In June and December, it was carried out within the framework of the Eurosystem forecasting cycle by developing macroeconomic forecasts for the Latvian economy and taking part in the discussions of forecasting outcomes of other euro area countries in the Eurosystem/ ESCB Monetary Policy Committee and its Working Group on Forecasting. In addition, macroeconomic forecasts by Latvijas Banka's experts were developed and published in March and September. Unlike other years, forecasts in 2020 were developed for several alternative development scenarios, which included different assumptions concerning the progress made towards Covid-19 containment, thus increasing substantially the resources used for forecasting. A reinforced focus was on modelling and assessment of the effects of economic policy counter-measures.

Analytical work is no less important than forecasting and, in cooperation with other euro area national central banks, it is carried out in the Eurosystem/ESCB Monetary Policy Committee and its three Working Groups on Econometric Modelling, on Forecasting and on Public Finance wherein substantiated discussions form the basis for the Eurosystem's monetary policy decisions. In 2020, the focus of monetary policy makers and the Eurosystem's research activities was on the Eurosystem's monetary policy strategy review. Experts of Latvijas Banka were also actively engaged in the strategy review's work streams.

In 2020, Latvijas Banka organised research activities in three priority directions: 1) monetary policy transmission, 2) fiscal policy and public debt sustainability and 3) long-term growth and competitiveness. In 2020, Latvijas Banka published six working papers and one discussion paper on its website (see Appendix 8).

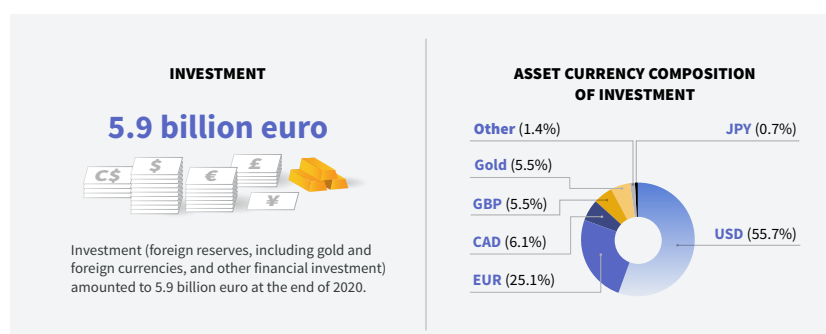
Quality research activities are impossible without continuous improvement of staff qualifications and thorough assessment of the results achieved. External reviewers from national central banks and academia of other countries are involved in assessing working papers to ensure their high quality. The publication of employees' working papers in internationally refereed journals is also supported. Seven such studies were published in 2020.

<p>WORKING PAPER NO. 1/2020</p> <p>The paper shows the pass-through of domestic labour costs, global food commodity prices and crude oil prices to consumer prices in Latvia. It concludes that the forecasting performance of the short-term inflation projections (STIP) model significantly outweighs the simple benchmark model in statistical terms in real time.</p>	<p>WORKING PAPER NO. 2/2020</p> <p>The paper compares the forecasting performance of the dynamic factor model (DFM) and autoregressive (AR) benchmark models, focusing on a possible asymmetry of the business cycle. It concludes that the widespread practice of relying on full sample forecast evaluation metrics may not be ideal, i.e. full sample error metrics systematically over-estimates performance in expansionary subsamples and under-estimates it in recessionary subsamples in at least two thirds of all 216 macroeconomic indicators.</p>
<p>WORKING PAPER NO. 3/2020</p> <p>The net wealth distribution in Western EU countries is consistent with the life cycle hypothesis, while in Eastern EU countries, the wealth distribution is skewed towards younger ages. The paper analyses the characteristics of EU countries leading to differences in the net wealth distribution by age and evaluates the impact of these differences on the transmission of monetary policy. The paper concludes that the structure of net wealth distribution by age has an important bearing on the effectiveness and hence the implementation of monetary policy.</p>	<p>WORKING PAPER NO. 4/2020</p> <p>The paper investigates the impact of national fiscal rules on government capital investment policy. It suggests that loosening fiscal rules does not solve the problem of underinvestment; however, properly designed rules can help to protect public capital stock to some extent.</p>
<p>WORKING PAPER NO. 5/2020</p> <p>The paper develops and describes the fiscal dynamic stochastic general equilibrium (DSGE) model of Latvia, depicting a small and open economy in a monetary union. The fiscal sector comprises government investment, government consumption, transfers, unemployment benefits, government debt, fiscal rules and other indicators describing government finances. The model is appropriate for the analysis of scenarios involving fiscal policy changes.</p>	<p>WORKING PAPER NO. 6/2020</p> <p>The paper, using an empirical euro area model, assesses transmission of negative interest rates, set by the central bank, to the overall demand and inflation. The paper concludes that monetary policy still continues to provide considerable support to the overall demand in the euro area even when interest rates are in negative territory; the effects on inflation are, however, much less pronounced compared to the period when interest rates are changed in positive territory.</p>
<p>DISCUSSION PAPER NO. 1/2020</p> <p>The paper analyses the results of the Household Finance and Consumption Survey 2017 conducted by the ECB, reflecting the financial situation of Latvian households before the Covid-19 crisis. The survey provides a detailed insight into households' balance sheet indicators, including household income, assets, liabilities and spending. This allows drawing conclusions about household wealth. The results of the survey conducted in 2017 vis-à-vis that conducted in 2014 suggest that net wealth has overall increased, although it ranks among the lowest ones in the euro area.</p>	

To raise researchers' qualifications and promote research work, presentation of papers by Latvijas Banka's researchers at international conferences and seminars is enhanced on an annual basis. In 2020, however, the Covid-19 containment measures significantly affected arrangement of academic conferences, i.e. researchers of Latvijas Banka presented their papers only at 14 conferences and seminars – the academic ones and those organised by Eurosystem/ESCB institutions. To enable employees of Latvijas Banka to familiarise themselves with recent papers by their foreign colleagues and strengthen international cooperation, Latvijas Banka also organises regular seminars to which highly qualified experts are invited to present their research results. In 2020, eight such seminars were organised, and interested parties from other institutions were also invited to participate.

Latvijas Banka also disseminates research findings to the public at large by explaining conclusions of working and discussion papers via articles and blogs published on www.macroecomics.lv and other popular websites.

INVESTMENT MANAGEMENT



Latvijas Banka's investments (foreign reserves of gold and foreign currencies as well as other financial investments) amounted to 5.9 billion euro at the end of 2020.

Latvijas Banka manages its investments in compliance with the guidelines adopted by the Council of Latvijas Banka. Latvijas Banka invests its financial assets in safe and liquid financial instruments, basically in debt securities issued by the governments of EU countries and the US government, their agencies and international organisations, highly rated bank and corporate debt securities and asset-backed debt securities as well as stocks of the companies included in the developed markets equity index. The major share of Latvijas Banka's financial assets was managed relative to the weighted index of 1–3 year government securities of the US and Canada and that of 1–10 year government securities of euro area countries and the UK. The benchmark currency is the euro, and the benchmark assets are composed of 55% US dollar-denominated, 21% euro-denominated, 14% British pound sterling-denominated and 10% Canadian dollar-denominated assets. Interest rate futures are used to manage the duration and to implement yield curve strategies on the interest rate market, whereas both currency futures and forward exchange rate contracts ensure the optimal currency composition of financial assets.

When managing the investment portfolio, the focus was on interest rates of 2, 5 and 10-year government bonds. In 2020, all markets saw interest rates drop significantly (see Table 1).

Table 1

**CHANGES IN GOVERNMENT BOND
YIELDS**
(%)

Country	2-year government bond yield		5-year government bond yield		10-year government bond yield	
	2019	2020	2019	2020	2019	2020
Germany	-0.60	-0.70	-0.47	-0.74	-0.19	-0.57
UK	0.55	-0.16	0.60	-0.08	0.82	0.20
US	1.57	0.12	1.69	0.36	1.92	0.91
Canada	1.70	0.20	1.69	0.39	1.70	1.68

Source: Bloomberg.

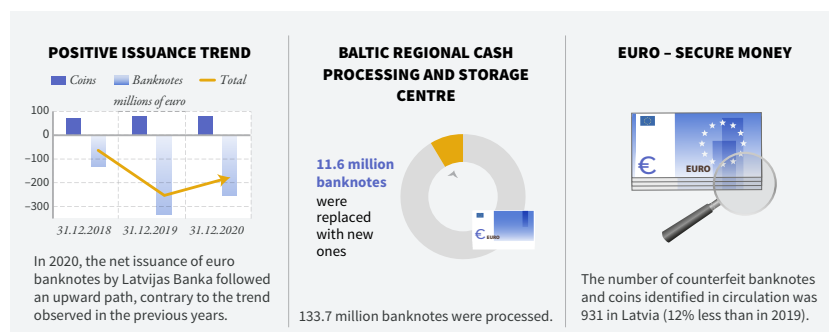
The gold reserves of Latvijas Banka are stored in the Bank of England.

Latvijas Banka uses the services provided by eight external managers. They manage a portion of Latvijas Banka's financial assets in compliance with the guidelines adopted by the Council of Latvijas Banka to further diversify financial assets and increase income generation on risk adjusted basis over the medium and longer term. To enhance that objective, Latvijas Banka continued to increase investment in equities in 2020.

Risk management and control is an integral part of investment management. The investment portfolio's compliance with the guidelines and the risk allocation in accordance with investment decisions is monitored and controlled on a daily basis.

Together with Oesterreichische Nationalbank, Latvijas Banka manages the foreign reserve assets in Japanese yen transferred to the ECB.

CURRENCY IN CIRCULATION



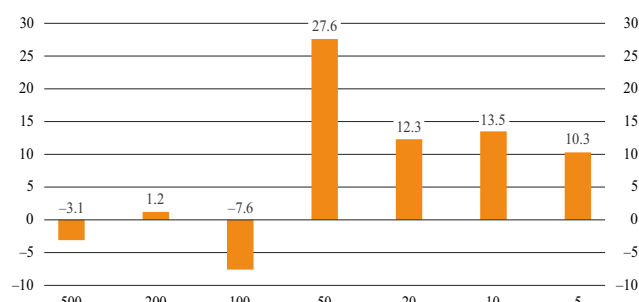
The net issuance of euro banknotes by Latvijas Banka followed an upward path in 2020, i.e. from –332.7 million euro in 2019 to –255.0 million euro in 2020; however, it remained in negative territory. Meanwhile, the issuance of euro coins by Latvijas Banka picked up from 79.5 million euro in 2019 to 79.7 million euro in 2020. Thus, the net issuance of euro banknotes and coins by Latvijas Banka was –175.4 million euro at the end of 2020.

The net issuance of banknotes by Latvijas Banka in terms of number grew by 10.3% (to 54.2 million banknotes) during 2020. It is the net issuance of 50 euro and 10 euro banknotes by Latvijas Banka that predominated over other denominations in the period lasting from the euro changeover in January 2014 until the end of 2020 (27.6 million and 13.5 million banknotes respectively; see Chart 10).

Chart 10

EURO BANKNOTES ISSUED BY LATVIJAS BANKA IN NET TERMS

(by face value; 2014–2020; number in millions)



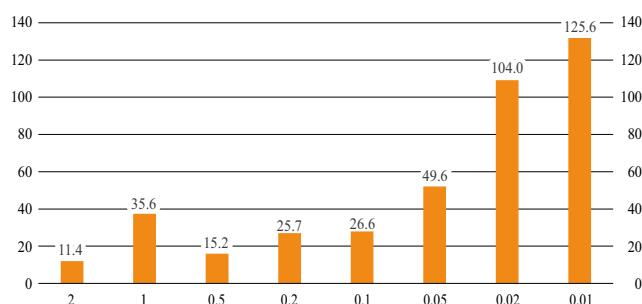
Source: Latvijas Banka.

Meanwhile, the net issuance of coins by Latvijas Banka in terms of number augmented by 5.8% (to 393.7 million coins). It is the 1 cent and 2 cent coins that accounted for a major portion of the net issuance of coins by Latvijas Banka during the period starting from the euro changeover day in January 2014 and ending in late 2020 (125.6 million and 104.0 million coins respectively; see Chart 11).

Chart 11

EURO COINS ISSUED BY LATVIJAS BANKA IN NET TERMS

(by face value; 2014–2020; number in millions)



Source: Latvijas Banka.

The cash received from credit institutions is checked for fitness and authenticity by automated cash processing systems of Latvijas Banka. They processed 133.7 million banknotes in 2020, i.e. 12.2% less than in 2019. 8.7% (11.6 million) of the processed banknotes were identified as unfit for circulation and destroyed.

In 2020, the banknote packaging equipment NOTAPACK, which automatically packs the processed banknote packages, was installed at Latvijas Banka within the framework of automation of banknote processing.

In 2020, Latvijas Banka continued to register merchants, engaged in handling and recirculating of euro banknotes and coins, and to monitor their operation. A merchant is entitled to handle and recirculate euro banknotes and coins in the Republic of Latvia upon registering with Latvijas Banka as a cash handling institution. At the end of 2020, 49 cash processing institutions were registered in Latvia. Latvijas Banka conducted inspections of cash handlers and assessed the compliance of their operation with the requirements of laws and regulations governing cash handling. In 2020, three inspections of operation of cash processing institutions were carried out.

In 2020, the National Analysis Centre and the Coin National Analysis Centre received and identified 1140 counterfeits (889 banknotes and 251 coins). Counterfeits of euro banknotes and coins constituted 93% of the counterfeits, but those of lats banknotes and coins – 2%. Counterfeits of US dollars (3%), UK and Chinese currencies (totalling 1%) were identified relatively seldom.

In 2020, the number of counterfeit banknotes and coins identified in circulation was 931 (706 and 225 respectively), and their total nominal value stood at 30.8 thousand euro (in 2019 – 42.4 thousand euro). As compared to 2019, the total number of counterfeits in circulation decreased by 12.4%, with the number of counterfeit coins moving down by 37%. The 50 euro and 20 euro banknotes (81% of counterfeits of euro banknotes identified in circulation) and 2 euro coins were the most counterfeited denominations.

In 2020, withdrawal of lats banknotes and coins from circulation continued. In 2020, the lats banknotes and coins received from circulation by Latvijas Banka totalled 0.9 million lats (0.8 million lats were in banknotes and 0.1 million lats in coins). Lats banknotes and coins worth 41.0 million lats and 44.0 million lats respectively were in circulation at the end of 2020. In late December 2020, the 5 lats and 20 lats banknotes (1.7 million and 0.8 million respectively) and the 1 santims and 2 santims coins (149.6 million and 89.7 million respectively) accounted for the majority of banknotes and coins in circulation in terms of number.

In 2020, to mark significant cultural and historic events as well as to highlight other topics relevant to society, Latvijas Banka issued collector coins "Modernism in Latvia. The 1960s" (issued on 6 October 2020), "Linden leaf" (issued on 3 November 2020), "Ventastega" (issued on 24 November 2020) and "Personal freedom" (issued on 11 December 2020). In 2020, Latvijas Banka issued a 2 euro commemorative coin "Latgalian Ceramics" (in circulation as of 5 June 2020).

In 2020, at the competition Coin of the Year Awards organised by Active Interest Media (AIM, US), the collector coin "Honey Coin" issued by Latvijas Banka in 2018 was announced the Coin of the Year (it was the second time a coin issued by Latvijas Banka received this award). The "Honey Coin" was also awarded the first place in the category "Most Artistic Coin of the Year".

In 2020, several coins issued in 2019 were submitted for participation in international contests, and they were among winners. In 2020, two collector coins issued in 2019 received recognition at the international Coin Constellation Contest organised by Watermark, Russian Numismatic Publishing House, i.e. the coin "Niklāvs Strunke" won the first place in the category "Most Artistic Coin" and the coin "Freedom Fights (1918–1920)" – the first place in the category "Classical Coin".

2 EURO COMMEMORATIVE COIN



LATGALIAN CERAMICS

Struck in 2020 by UAB Lietuvos monetų kalykla (Lithuania)
 Artists of the national side of the coin: Gundega Rancāne (graphic design) and Jānis Strupulis (plaster model)
 The national side features a candelabra – a typical Latgalian ceramic candle holder.

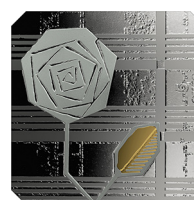
Weight: 8.50 g; diameter: 25.75 mm; thickness: 2.20 mm
 Shape: round; colour: outer part silver, inner part gold
 Composition: outer part – copper-nickel (Cu, Ni), inner part – three layers: nickel, copper and zinc; nickel; nickel, copper and zinc (Ni, Cu, Zn; Ni; Ni, Cu, Zn)
 The edge of the coin bears the inscription "DIEVS * SVĒTĪ * LATVIJU *" (God, Bless Latvia).
 The common side artist Luc Luyckx

5 EURO COLLECTOR COINS

MODERNISM IN LATVIA.

THE 1960S

Weight: 26.25 g; shape: a square (32.00 mm × 32.00 mm; with cut corners)
 Metal: silver of fineness .925; quality: proof; with frosting of different intensity and gold plated details
 Struck in 2020 by UAB Lietuvos monetų kalykla (Lithuania)
 Artists: Sandra Krastiņa (graphic design) and Jānis Strupulis (plaster model)



LINDEN LEAF

Weight: 18.13 g; shape: irregular; distance from the base of the leaf to the tip: 32.00 mm
 Metal: silver of fineness .925; quality: proof
 Struck in 2020 by Koninklijke Nederlandse Munt (the Netherlands)
 Artists: Mārcis Kalniņš (graphic design) and Līgita Franckeviča (plaster model)

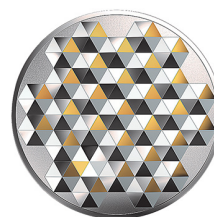
VENTASTEGA

Weight: 22.00 g; diameter: 35.00 mm
 Metal: silver of fineness .925; quality: proof; with frosting of different intensity on the obverse and reverse and photo luminescent print on the obverse
 Struck in 2020 by Koninklijke Nederlandse Munt (the Netherlands)
 Artist: Ivars Drulle (graphic design and plaster model)

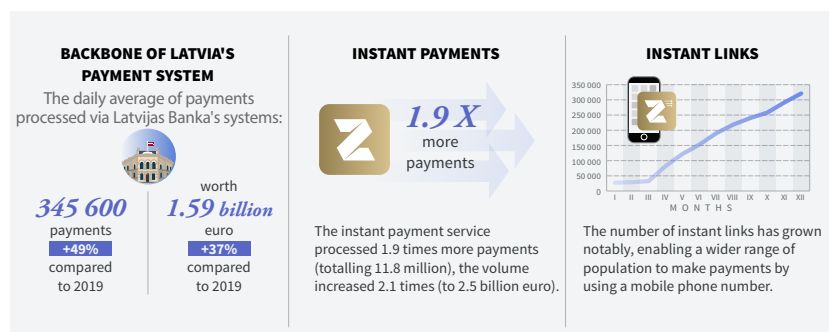


PERSONAL FREEDOM

Weight: 22.00 g; diameter: 35.00 mm
 Metal: silver of fineness .925; quality: proof with frosting of different intensity and black colour print, gold plating and mirror surface on the obverse and reverse
 Struck in 2020 by Mennica Polska S.A. (Poland)
 Artist: Beate Šņuka (graphic design and plaster model)



PAYMENT AND SETTLEMENT SYSTEMS



INNOVATION OF PAYMENT INFRASTRUCTURES

Latvijas Banka continued to develop an efficient, safe and innovative payment infrastructure, which is a prerequisite for ensuring currency circulation in the interests of society as a whole. Latvijas Banka informed the public (through articles, commentaries, discussions at conferences, lectures at universities) about technological innovation in the financial field and development of innovative payment services, thus facilitating the uptake of innovation in payment services and a wider use of modern payment services.

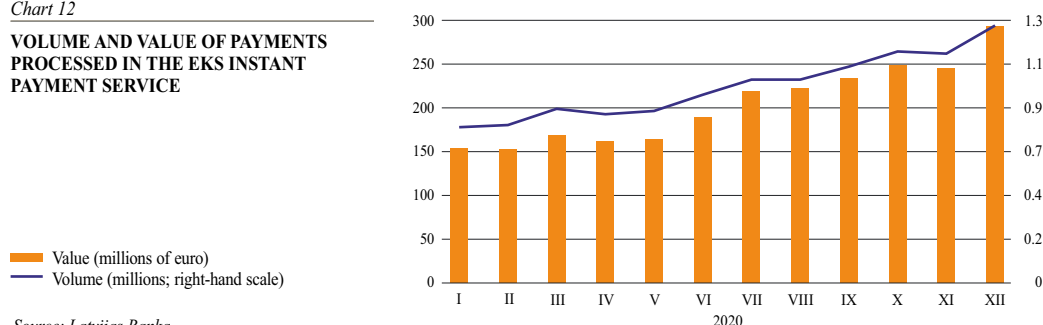


In 2020, Latvijas Banka contributed to an increasingly widespread utilisation of instant payments in Latvia. In addition to Latvijas Banka and three credit institutions (AS Citadele banka, AS SEB banka and Swedbank AS), which already provided instant payments before 2020, instant payments were also introduced by Signet Bank AS and AS BlueOrange Bank when they started to use Latvijas Banka's EKS instant payment service in 2020. Overall, instant payments were available to 90% of Latvia's population.

The EKS instant payment service provided a very high degree (99.96%) of availability in 2020. It processed twice as many instant payments as a year ago both in terms of volume and value (11.8 million and 2.5 billion euro respectively; see Chart 12). The instant payment service processed up to 64 thousand instant payments on certain days.

Chart 12

VOLUME AND VALUE OF PAYMENTS PROCESSED IN THE EKS INSTANT PAYMENT SERVICE



Source: Latvijas Banka.



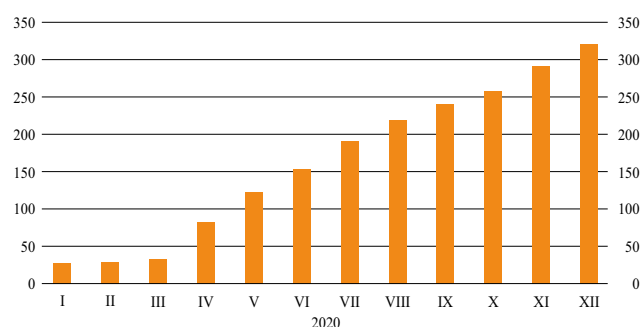
Latvijas Banka ensured the operation of the Proxy Registry "Instant Links", enabling credit institution customers to make instant and other payments in an even more

convenient and fast manner, just indicating the payee's mobile phone number in the payment order.

At the end of 2020, 321 thousand instant links were registered with the Proxy Registry "Instant Links", i.e. 13 times more than at the end of 2019 (see Chart 13). The Proxy Registry received 3.7 million requests, 215 times more than in 2019. As a result of the active engagement of Latvijas Banka, practically all largest Latvian and Estonian credit institutions embarked on a widespread use of the Proxy Registry "Instant Links". In 2020, Latvijas Banka provided 100% availability of the Proxy Registry.

Chart 13

DYNAMICS OF INSTANT LINKS IN 2020
(thousands)



Source: Latvijas Banka.



ZIBPRASĪJUMU SERVISS

NODROŠINA: LATVIJAS BANKA

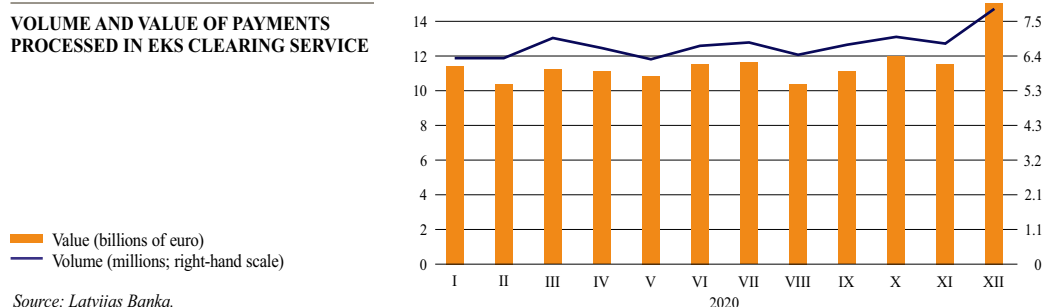
In 2020, Latvijas Banka commenced development of a new and innovative instant payment request service expected to be in place in the second half of 2021. The instant payment request service will be an interbank solution enabling an instant sending of a request to the payer who will only have to approve the request for the initiator of the instant request to receive the payment immediately. The new service will ensure more user-friendly payments between individuals, while businesses and public institutions will enjoy sending, e.g. payment requests containing billing information for direct approval (payment) without entering the payment details. This will increase the efficiency of the payment process, reduce the potential for errors and speed up the payment of bills in Latvia.

More widespread use of instant payments and development of instant payment requests were incorporated into the Latvian Digital Transformation Guidelines of the Ministry of Environmental Protection and Regional Development as a significant contribution to development of the Latvian economy over the next six years.

The EKS maintained by Latvijas Banka supports the digital transformation through maintaining and developing the instant payment service, and it also maintains the clearing service. The clearing service continued to ensure payments from one customer account held with a credit institution to a customer account of another credit institution within a few hours on business days, accepting, processing and executing interbank settlement seven times a day. At the end of 2020, the EKS clearing service comprised the following direct participants: 12 credit institutions, the Treasury and Latvijas Banka.

The EKS clearing service continued to ensure customer payments in euro within SEPA for Latvian and Estonian credit institutions and the Treasury. The availability of the EKS clearing service accounted for 99.94% in 2020, and it processed 1.5 times more payments than a year ago, with the total volume increasing 1.6 times (see Chart 14). The volume and value of the customer SEPA credit transfers processed by the clearing service on a daily basis was 313 thousand and 537 million euro respectively.

Chart 14

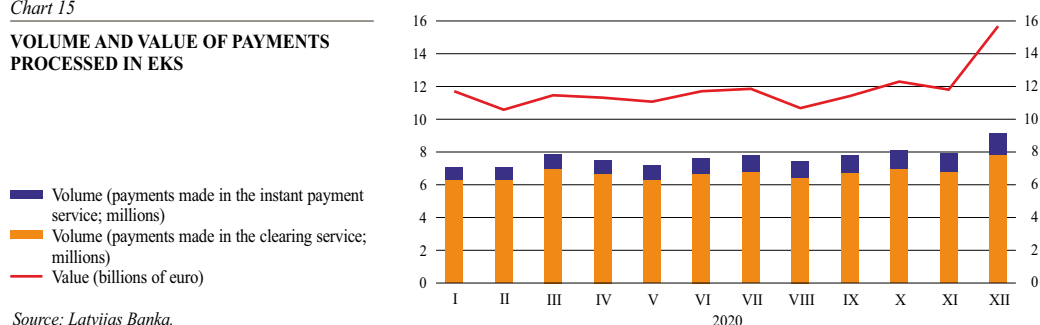
VOLUME AND VALUE OF PAYMENTS PROCESSED IN EKS CLEARING SERVICE

Source: Latvijas Banka.

In 2020, Latvijas Banka continued to develop the EKS system to prepare for the use of the new settlement model (Continuous Gross Settlement) of the STEP2 system maintained by EBA clearing.

In 2020, 92.5 million SEPA credit transfers totalling 141.0 billion euro were executed in the EKS (see Chart 15; in the instant payment service and the clearing service combined). The volume of payments executed in the EKS increased 1.5 times, but their value – 1.6 times year-on-year, since the volume and value of payments of Baltic branches of EKS participants' credit institutions followed an upward path.

Chart 15

VOLUME AND VALUE OF PAYMENTS PROCESSED IN EKS

Source: Latvijas Banka.

For over a year now, Latvijas Banka provides an innovative cooperation platform – the Instant Payment Laboratory ZibLab++ which was used in 2020 to inform market participants about the most important events related to the development of the EKS instant payment service, the Proxy Registry "Instant Links" and the Instant Payment Request Registry.

In 2020, Latvijas Banka participated in the Eurosystem's activities aimed at exploring technological feasibility of the introduction of the digital euro as well as its impact on the application of monetary policy and the financial system as a whole. Within the Eurosystem framework, Latvijas Banka commenced experiments related to the introduction of a digital euro, focusing on the simulation of on-site interface (purchases made in a shop using the digital wallet).

TARGET2-LATVIJA OPERATION

In 2020, Latvijas Banka continued to provide the operation of TARGET2-Latvija – one of the component systems of TARGET2, which is the third largest payment system in the world.

In 2020, Latvijas Banka together with other Eurosystem central banks continued the implementation of TARGET2 and TARGET2-Securities consolidation project by which a new payment system TARGET is being developed using technologies of the TARGET2-Securities platform. The T2 service of this system will replace the TARGET2 system on 21 November 2022. The T2 service will use modern infrastructure and high cyber security

standards to provide a wider range of opportunities for liquidity management of credit institutions and interbank settlements, utilising central bank money in compliance with ISO 20022 standard. Latvijas Banka completed its assessment regarding the impact of the T2 service on Latvijas Banka's operation as well as continued to coordinate the progress of the project in Latvia, providing information to credit institutions and other market participants about topical issues and changes in the context of the project on a regular basis. Within the framework of enhancement of TARGET2-Latvija cyber security, Latvijas Banka coordinated the submission of statements by system participants acknowledging the compliance with TARGET2 security requirements and those of TARGET2 network service provider's end-user.

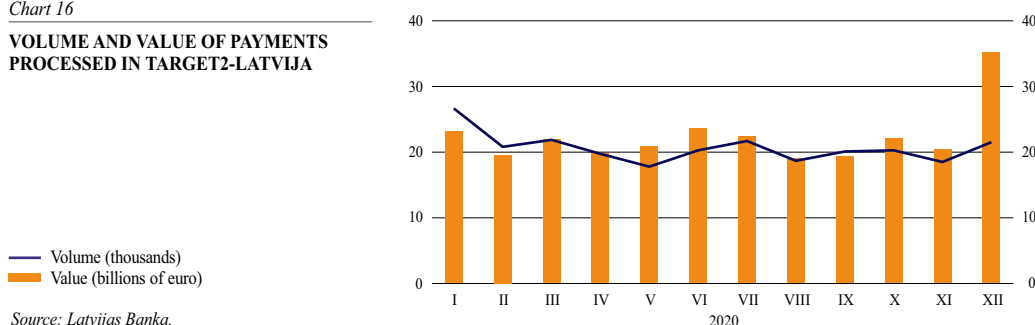
Latvijas Banka continued work on the ECMS implementation project by commencing the assessment of the project's impact on Latvijas Banka and Latvian credit institutions. The ECMS will replace the existing local systems used for collateral management in 19 Eurosystem central banks, harmonising the procedures for collateral management in monetary policy operations and integrating these procedures in the new TARGET system. It has been planned to launch the ECMS in November 2023.

In 2020, Latvijas Banka, within the Eurosystem framework, developed solutions to ensure reachability of the TARGET Instant Payment Settlement (TIPS) service across Europe and offer an opportunity to European instant payment systems to improve their mutual settlements 24/7/365. Thus, the EKS instant payment service will be transferred to the TIPS platform at the end of 2021. Latvijas Banka will continue to provide reachability of the EKS instant payment service participants both in the RT1 system maintained by EBA CLEARING and TIPS.

In 2020, the availability of TARGET2, including TARGET2-Latvija, was 99.67%. The volume and value of the processed payments constituted 1.0 thousand and 1.0 billion euro respectively (see Chart 16). The total volume of payments decreased by 47.0%, while their total value increased by 28.2% year-on-year.

Chart 16

**VOLUME AND VALUE OF PAYMENTS
PROCESSED IN TARGET2-LATVIJA**



Source: Latvijas Banka.

At the end of 2020, 15 credit institutions, one investment brokerage firm, the Treasury and Latvijas Banka were the participants of TARGET2-Latvija. TARGET2-Latvija also provided interbank settlement in euro of the EKS maintained by Latvijas Banka and of the card settlement system Worldline Latvia CSM maintained by SIA Worldline Latvia.

Latvijas Banka also ensured the execution of payments in euro to the institutions whose settlement accounts were opened with Latvijas Banka, but which were not direct participants of Latvijas Banka's payment systems, i.e. the FCMC, Latvian, foreign and international financial institutions. In 2020, such customer payments executed by Latvijas Banka amounted to 2.7 billion euro.

PAYMENT SYSTEM OVERSIGHT

In 2020, with a view to enhance the development of the Latvian financial ecosystem, Latvijas Banka contributed to the elaboration of the Financial Sector Development Plan

2021–2023. This work involved both drawing up proposals for shaping an ecosystem that supports innovation and ensuring the availability of innovation-supportive infrastructure.

In 2020, Latvijas Banka participated in oversight of retail payment systems of 43 European countries, thus facilitating development of efficient and safe payments. Latvijas Banka also participated in the assessment of compliance of five European systematically important payment systems (TARGET2, EURO1, STEP2-T, CORE(FR)) with amendments to Regulation of the European Central Bank (EU) No 795/2014 of 3 July 2014 on oversight requirements for systemically important payment systems (ECB/2014/28) and CROE, including an agreement with operators of the assessed systems on action plans to rectify certain deficiencies and following the implementation of these plans. In 2020, the Eurosystem recognised the Mastercard Clearing Management System (MCMS) as the fifth systematically important payment system in Europe and started its oversight.

Latvijas Banka executed day-to-day oversight of the EKS, analysing the system's technical and operational functions, compiling its statistical data and making sure that the EKS operation and development provide a secure and efficient interbank payment environment in Latvia.

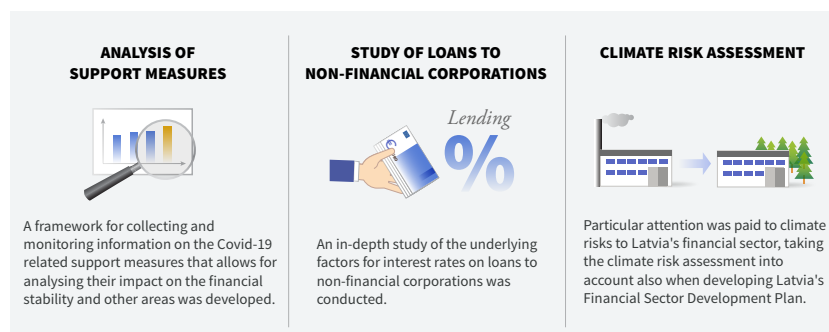
Latvijas Banka participated in the preparation of the PISA oversight framework (Oversight framework for electronic payment instruments, payment schemes and payment arrangements), which is currently undergoing public consultations. It has also been intended to extend the PISA oversight framework, along with payment instruments and payment schemes, to payment solutions that support the use of electronic payment instruments (e.g. payment initiation services or digital wallets). The latest regulatory, technological and market development has been taken into account in its elaboration.

When performing the oversight of development of the payment instruments used in Latvia, Latvijas Banka regularly (on a semi-annual basis) compiled and analysed data on customer payments made in Latvia, publishing reports on the website of Latvijas Banka. Payment data are compiled in compliance with a uniform ECB statistical methodology.

OVERSIGHT OF THE SECURITIES SETTLEMENT SYSTEMS

In 2020, Latvijas Banka performed oversight of Nasdaq CSD SE, assessing the expansion of its operation in Iceland and the takeover of the Icelandic securities settlement system. Representing the Eurosystem – the central bank issuing euro – Latvijas Banka performed an annual review of Nasdaq CSD SE operation and assessed the compliance of Nasdaq CSD SE with the CSDR requirements important for the Eurosystem. Nasdaq CSD SE was assessed as compliant with the requirements. At the same time, some recommendations were made for improvement of certain processes. Latvijas Banka continues to follow the implementation of these recommendations.

In 2020, Latvijas Banka together with other central banks of the Eurosystem carried out the oversight of the TARGET2-Securities platform as well as participated in the joint oversight (conducted by the Eurosystem) of 17 securities settlement systems maintained by European central securities depositories.



In 2020, Latvijas Banka, in line with the ESRB recommendations¹, developed a framework for collecting and monitoring information on the support measures related to the Covid-19 pandemic, also enhancing the exchange of data with AS Attīstības finanšu institūcija Altum and thus improving the possibility to follow the implementation of the government support programmes, to make a comparison with other countries as well as to analyse the impact of the support measures on the financial stability and other areas.

The above framework improves Latvijas Banka's capability to provide advice to the Latvian government and other public institutions. With the role of the government support measures growing, Latvijas Banka's participation in drafting various legislative initiatives and other legal acts also increased significantly.

In 2020, Latvijas Banka continued its close cooperation with public institutions in the prevention of money laundering and financing of terrorism (AML/CFT) and the enforcement of sanctions by improving the regulatory framework, preparing Latvia's position regarding the EU's course of action in the field of AML/CFT, preparing the National Report on Money Laundering and Terrorism Financing Risk Assessment and participating in the development of the scope of assessment in the area of the regional Baltic and Nordic AML/CFT.

In 2020, Latvijas Banka paid particular attention to climate risks to Latvia's financial sector. An article on this topic examining international initiatives and frameworks in this regard, their development and impact on Latvia's financial sector as well as assessing the exposure of the portfolio of loans granted to non-financial corporations by credit institutions to climate risks and providing recommendations was published in the Financial Stability Report². This publication was taken into account when developing Latvia's Financial Sector Development Plan.

In 2020, Latvijas Banka conducted an in-depth study of the underlying factors for interest rates on loans to domestic non-financial corporations, analysing the Credit Register granular data with the help of econometric models. The outcomes of research were presented in the forum of central bank governors of the Baltic States and discussed with the experts of the Finance Latvia Association.

In 2020, the IMF continued to conduct the assessment of Latvia's financial sector as part of the Financial Sector Assessment Program, and at the beginning of the year, representatives of Latvijas Banka were actively involved in providing informative and analytical support necessary for the IMF to conduct the assessment, particularly as regards the stress tests and financial stability analysis, the macroprudential policy and financial crisis management.

¹ https://www.esrb.europa.eu/pub/pdf/recommendations/esrb.recommendation200608_on_monitoring_financial_implications_of_fiscal_support_measures_in_response_to_the_COVID-19_pandemic_3~c745d54b59.en.pdf?35a81a46f32f9b8d233f3c3d59812675

² https://datnes.latvijaskbanka.lv/fsp/FSP_2020.pdf

Latvijas Banka participates in the work of the Financial Stability Committee comprising representatives of the ECB, national central banks and supervisory authorities and the relevant groups by providing contribution to the assessment of systemic risks to financial stability in the euro area, the development of financial stability analysis tools and the evaluation of macroprudential policy instruments. In parallel with the above euro area working groups, Latvijas Banka engaged in the work of the ESRB Advisory Technical Committee and its working groups and contributed to drafting ESRB policy and analysis documents and defining opinion.

Latvijas Banka continued to engage in the work of the Nordic-Baltic Macro-prudential Forum, where it shared experience in introducing the Covid-19 pandemic containment measures and taking macro-prudential measures to reduce the impact of the pandemic on financial stability. The sustainability of pension funds and insurance companies was also thoroughly analysed.

STATISTICS

<p>28 TYPES OF STATISTICS</p>  <p>A full range of statistics was provided also during the Covid-19 pandemic in 2020, and additional tasks were also carried out.</p>	<p>COOPERATION WITH RESPONDENTS</p>  <p><i>"The Respondent of the Year"</i></p> <p>The Respondent of the Year event was organised for the first time in 2020, inviting 100 respondents from different economic sectors.</p>	<p>HOUSEHOLD FINANCE ASSESSMENT</p>  <p>The 2020–2022 Household Finance and Consumption Survey was launched. This is already the third survey of its kind in Latvia.</p>
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Latvijas Banka collects and compiles a wide range of statistics and ensures the operation of the Credit Register in pursuit of its tasks, including those of the ESCB. Latvijas Banka employs statistical data to perform financial and macroeconomic analyses, assess financial stability 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 the Eurosystem's monetary statistics and the relevant euro area statistical data as well as to discharge its other tasks.

To reflect its activities in the field of statistics, Latvijas Banka publishes an annual statistical programme and a medium-term statistical work programme for the period of three years on a regular basis. The above programmes provide transparent information on statistical activities planned by Latvijas Banka both with regard to the most important new tasks and the types of statistical data Latvijas Banka compiles and publishes. The Statistical Programme of Latvijas Banka for 2020 was implemented, except for individual tasks where their deadlines were changed at the ESCB level due to the deceleration of the process of drafting the ECB legal acts in conditions of the Covid-19 pandemic. The tasks requiring the implementation of amendments to the requirements for payments statistics and MFI balance sheet statistics as well as the conducting of a costs survey on changes in the requirements of investment fund statistics were postponed to 2021.

In the circumstances of the Covid-19 pandemic, Latvijas Banka continued to provide a full range of statistics, in total 28 types of statistics, while also carrying out additional tasks. In the context of the Covid-19 pandemic, faster compilation of individual data was required for the purposes of monetary and macro-prudential policies, financial stability and market operations. Therefore, for the needs of Latvijas Banka and the ECB, data on holdings of securities were compiled in a shorter period of time and the effectiveness of the compilation of the monthly balance of payments was increased by processing the data sources used in the compilation of the quarterly balance of payments at a faster pace to

obtain best possible flash estimates of the quarterly balance of payments. An additional block of questions about the impact of the Covid-19 pandemic on household finances and employment was added to the Household Finance and Consumption Survey, and a new survey technique CATI (Computer Assisted Telephone Interviewing), i.e. interviewing by telephone, was also introduced. The "new normal" also prompted the expansion of the range of data available from the Credit Register to comply with the requirement to provide information on the types of the support measures provided in relation to the Covid-19 outbreak. In view of the fact that the CSB travellers' survey data were not available in this extraordinary situation, another data source (SIA Worldline Latvia) had to be sought and used for the balance of payments purposes by supplementing it with administrative data on the estimates of the number of people crossing the border and the expert judgement based on the historical data analysis.

The Respondent of the Year event and the non-bank statistics system (eSTAT system) user survey, which were organised for the first time in 2020, provided evidence that activities of Latvijas Banka in the field of statistics were highly appreciated by its cooperation partners.

To strengthen cooperation with respondents and enhance the openness and availability of Latvijas Banka to the public, reporting agents met for the first time in person with the representatives of the management of Latvijas Banka and the employees of the Statistics Department at the Respondent of the Year event in February 2020. A hundred randomly selected respondents who had submitted high-quality reports (without any corrections) in due time (without reminder) in 2019 were invited to the above meeting. The event brought together representatives of different economic sectors such as the financial, electricity supply, software programming, manufacturing of veneer sheets and wood panels, wireless telecommunications, railway transport, forestry, cargo loading and cargo unloading sectors. Respondents' better understanding of the rationale behind Latvijas Banka's data requirements, the uses of the reported statistical data by Latvijas Banka, the networking opportunities that allow for informal discussions on the process of preparing and submitting reports and on topical issues, as well as better further cooperation are the main gains provided by such a meeting, as emphasised by the participants of the event in their positive references.

In July and August 2020, Latvijas Banka conducted a survey on the data submission process using the eSTAT system where 7.6 thousand active users are registered. Overall, 3.9 thousand unique (i.e. the user registered with a business or group connection in the eSTAT system has completed the survey once) survey questionnaires were received, and the average score on a five point scale was 4.5, with 70% of the survey participants assigning the highest score – 5 points. In response to some of the received suggestions, Latvijas Banka provided information on the eSTAT system's existing functionalities, while other suggestions were taken on board for planning the improvement of the eSTAT system in the future.

Latvijas Banka continued regular transmission of statistical data to the ECB, BIS, Eurostat, OECD, World Bank and IMF as well as provided statistical information to other data users in Latvia and abroad. To provide a wide range of data users with timely information, Latvijas Banka disseminated statistics via its regular publications and website and compiled statistical data for publishing in the ECB publications and the ECB Statistical Data Warehouse as well as in IMF publications and within the framework of the IMF Special Data Dissemination Standard (SDDS Plus). Latvijas Banka continued to perform the tasks of the coordinating institution in Latvia within the framework of SDDS Plus.

To ensure a more convenient access to the range of data available in Latvijas Banka's internet statistical database INTS, a new database functionality that allows data users to access a link to the created data table in the selected format and to use this link for

automated access to data or multiple access to the data table has been introduced. With the publication of the statistical data on foreign currency purchases and sales launched, the expansion of the range of data published in Latvijas Banka's internet statistical database INTS also continued.

FINANCIAL AND GENERAL ECONOMIC STATISTICS

In 2020, Latvijas Banka participated actively in the development of new ESCB requirements in the field of statistics, expanded the range of compiled statistics, ensured the process of conducting the household finance and consumption survey and the availability of its data, harmonised financial account statistics with government finance statistics as well as granted exemptions to respondents in the field of investment fund statistics.

The development of new ESCB requirements continued in the area of MFI statistics and payment statistics. The activities in the field of MFI statistics were pursued in two main directions, which included, first, the drafting of the recast version of Regulation (EU) No 1071/2013 of the European Central Bank of 24 September 2013 concerning the balance sheet of the monetary financial institutions sector (ECB/2013/33), and, second, the establishment of the ESCB Integrated Reporting Framework to ensure data acquisition and the provision of granular data by their type from credit institutions' information systems, using the Banks' Integrated Reporting Dictionary and a data exchange standard. The recast version of the above Regulation also includes changes in the scope of the MFI definition providing that investment brokerage firms whose value of the consolidated assets equals or exceeds 30 billion euro are credit institutions pursuant to Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013. At the same time, a costs survey was launched in 2020 to assess the potential costs and gains in relation to the introduction of the ESCB Integrated Reporting Framework.

The work on drafting amendments to the respective Regulation of the ECB was completed in the field of payment statistics, and Regulation (EU) No 2020/2011 of the European Central Bank of 1 December 2020 amending Regulation (EU) No 1409/2013 on payments statistics (ECB/2013/43) (ECB/2020/59) was adopted to expand the range of data necessary for overseeing the operation of payment systems and for more accurate presentation of certain indicators in balance of payments statistics.

Latvijas Banka continued to expand the range of compiled and transmitted statistics. Regulation (EU) No 2018/231 of the European Central Bank of 26 January 2018 on statistical reporting requirements for pension funds (ECB/2018/2) was implemented, thus at the euro area level ensuring harmonised statistical data for the purposes of monetary and financial analysis. Likewise, Latvijas Banka started reporting information that characterises Latvia's pension plans managed by private pension funds and investment plans of the state-funded pension scheme to the ECB Register of Institutions and Affiliates Database (RIAD) for the purpose of maintaining the List of Pension Funds of the EU Member States. According to the OECD requirements, transmission of more detailed financial account statistics to the OECD was commenced. Moreover, harmonisation of financial account statistics with government finance statistics was carried out, and, starting with the data of the first quarter of 2004, revised time series of financial accounts were published.

Latvijas Banka launched the 2020–2022 Household Finance and Consumption Survey. This is already the third survey of its kind in Latvia, and in accordance with the ECB requirements, it is conducted every three years to obtain data on the real and financial assets, credit liabilities, income, spending and consumption of households. In 2020, in cooperation with the CSB, the survey sample was created and the sampled households were interviewed. Moreover, Latvijas Banka expanded the range of anonymised data

obtained via the Household Finance and Consumption Survey and available upon request for research purposes with the results of the 2017–2019 survey, and the descriptions of files containing anonymised data available for research purposes and the data request were published in the Statistics section of Latvijas Banka's website. The availability of the anonymised data of two consecutive surveys ensures the possibility of analysing the dynamics of the household sector development.

Decision (EU) No 2020/1100 of the Governing Council of the ECB of 17 July 2020 amending Decision (EU) No 2015/32 concerning derogations that may be granted under Regulation (EU) No 1073/2013 (ECB/2020/33) was a significant event in the field of investment fund statistics. According to the above Decision, Latvia's alternative investment funds are included in the list of those investment fund categories to which the national central banks have the discretion to grant derogations. Latvijas Banka granted the said derogation, i.e. the possibility to report data on an annual basis pursuant to Regulation (EU) No 1073/2013, to alternative investment fund managers.

EXTERNAL STATISTICS

In 2020, Latvijas Banka updated the methodology used in the compilation of external statistics.

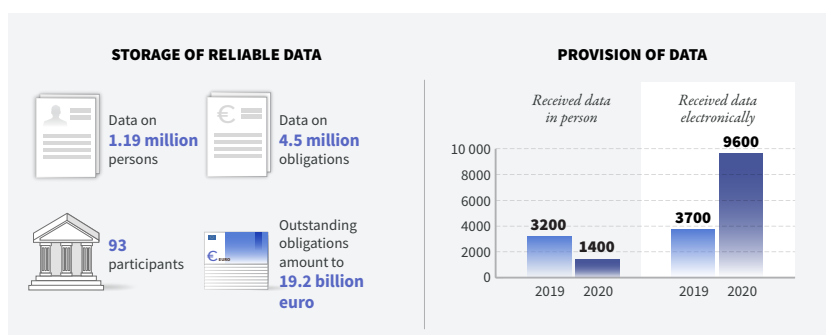
In view of the fact that certain types of statistics compiled by Latvijas Banka are a data source for the CSB data on Latvia's Gross National Income used for the formation of the EU general budget and that the EC checks the data sources and methods used in the calculation of the Gross National Income on a regular basis, Latvijas Banka provided additional data and explanations of the methodology used as well as improved the data compilation methods. For the purposes of providing the said additional data, a survey of credit institutions was conducted to obtain information on the composition of other ordinary income and other ordinary expenditure, enabling the CSB to verify the use of data provided by Latvijas Banka. Moreover, an additional source of information on used cars imported by individuals was introduced to account for these cars in imports of goods.

In order to ensure comparability of the balance of payments with the government sector statistics in respect of reporting of EU policy instruments and projects co-financed by other foreign financial assistance (EU funds), the principle of accounting was changed from the cash flow principle to the accrual principle, i.e. EU funds are reported in the period when expenditure from the Latvian central government budget is effected. An additional data source on investment in real estate was introduced in the compilation of data on direct investment made abroad, thus enabling a more accurate evaluation of the foreign assets of households.

To obtain the best possible flash estimates of the quarterly balance of payments, which is a sum of the data for the relevant months, in the process of compiling the monthly balance of payments, Latvijas Banka introduced a practice to revise the data for the first two months of the relevant quarter along with the compilation of the data for the third month of the quarter.

CREDIT REGISTER AND ANACREDIT STATISTICS

In 2020, Latvijas Banka continued to maintain and develop the Credit Register by collecting and storing data on borrowers and borrowers' guarantors, as well as their loans, received guarantees and delayed payments from its participants (credit institutions, credit institutions' subsidiaries (leasing companies), other companies having close links with credit institutions, credit unions, insurers and AS Attīstības finanšu institūcija Altum) and the Treasury.



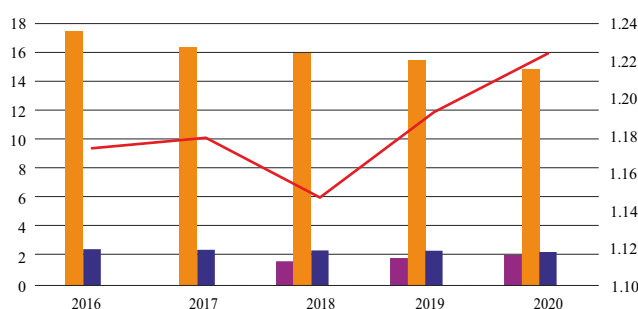
By using the Credit Register data, Latvijas Banka continued to report the Credit Register data to AnaCredit on a monthly and quarterly basis in accordance with the requirements of Regulation (EU) No 2016/867 of the ECB of 18 May 2016 on the collection of granular credit and credit risk data (ECB/2016/13) in 2020. AnaCredit brings together the data provided by the euro area central banks on loans granted to legal entities into a single system with the aim to improve the availability of detailed lending information for statistical needs, monetary policy analysis and decision-making as well as the financial stability analysis and risk assessment.

At the end of 2020, the Credit Register comprised 93 participants (including the Treasury). The Credit Register contained data on 4.5 million obligations pertaining to 1.19 million persons. The total outstanding obligations of the Credit Register participants amounted to 19.2 billion euro, while the granted and unused amount of the obligations was 4.3 billion euro (see Chart 17). Meanwhile, data on 14.8 thousand loans (on average) granted to legal entities and credit exposures between the credit institutions and the central bank with the total outstanding obligations amounting to 14.5 billion euro were reported to AnaCredit on a monthly basis.

Chart 17

OUTSTANDING OBLIGATIONS OF CREDIT REGISTER PARTICIPANTS AND NUMBER OF CURRENT OBLIGATIONS

- Treasury and AS Attīstības finanšu institūcija Altum (billions of euro)
- Credit institutions (billions of euro)
- Associated companies (billions of euro)
- Number of current obligations (millions; right-hand scale)



Source: Latvijas Banka.

Latvijas Banka continued to provide for any person a possibility to receive the Credit Register data pertaining to them free of charge. In 2020, the spread of Covid-19 and the related restrictions accelerated digitalisation of the Credit Register data receipt as the number of data issued in person decreased by approximately 55%, while the electronic receipt of data (through the website servicing persons electronically (<https://manidati.kreg.lv>) or to the person's official electronic address (e-address)) increased approximately 2.6 times. At the same time, the website (<https://manidati.kreg.lv>) was improved by automating the processing of the requests of the representatives of legal entities if the representative of the legal person had the right to represent this person individually. Thus, the representative of the legal entity receives the data immediately, and the employees of Latvijas Banka are not involved in the processing of such requests. In 2020, the possibility to receive data electronically via e-address was used 700 times also by authorities authorised to request data on the obligations of persons pursuant to the Law on Credit Register (including insolvency administrators, bodies performing operational activities, courts, etc.).

In 2020, Credit Register participants submitted 14.5 million requests (15.9 million requests in 2019) to the Credit Register for the purpose of assessing the creditworthiness of their current or potential borrowers and borrowers' guarantors. Following the development of technologies and encouraging electronic information exchange among persons (potential borrowers and potential borrowers' guarantors) and financial services providers (the Credit Register participants), amendments to the Law on Credit Register stipulating the rights of the Credit Register participants to request the Credit Register data on persons by using broader remote identification opportunities as well as the rights to also request data on the persons who are the beneficial owners of the current and potential borrowers and the borrowers' guarantors were made. Meanwhile, the cooperation between the systems of the Credit Register and the Population Register was initiated in 2020, thus providing for linkages between identity codes to ensure the full provision of data on the credit history of a person if the person has changed the identity code.

As of 1 April 2020, the list of the types of obligations has been supplemented with the categories "Study loan" and "Student loan" (state-guaranteed loans), and the implementation of the ESRB recommendation of 31 October 2016 on closing real estate data gaps (ESRB/2016/14) was commenced to include detailed types of purpose. As of 6 May 2020, new data, which refer to the Covid-19-related support measures, have been entered in the Credit Register. The data are available to the Credit Register participants and the Treasury to allow for an objective and fair assessment of the creditworthiness of a person, to Latvijas Banka and the FCMC for performing their tasks, as well as to persons where they receive the Credit Register data about themselves.

In 2020, Latvijas Banka continued to take care of the quality of the data contained in the Credit Register and the rationale behind the requests by checking activities undertaken by Credit Register participants on a regular basis and by enhancing cooperation with the Credit Register participants on issues regarding the quality of the data contained in the Credit Register and AnaCredit.

PROVIDING FINANCIAL SERVICES TO THE GOVERNMENT

In order to facilitate efficient and safe budgetary payments of Latvia, the management of the Treasury's settlement accounts in euro and foreign currencies opened with Latvijas Banka was ensured by Latvijas Banka in 2020. The Treasury used the payment services provided by Latvijas Banka for effecting settlement and participated in TARGET2-Latvija and the EKS as a direct participant. In 2020, in addition to payments of the Treasury processed by payment systems, Latvijas Banka settled 421 payments of the Treasury in euro and foreign currencies totalling 9.7 billion euro (900 payments accounting for 5.8 billion euro in 2019).

ADVICE ON MATTERS WITHIN LATVIJAS BANKA'S COMPETENCE

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 aspects of economic policy associated with Latvia's participation in the euro area as well as other issues related to the performance of the tasks of Latvijas Banka.

In 2020, officials of Latvijas Banka and its employees held regular meetings with the representatives of the Saeima and the government of the Republic of Latvia, inter alia, participated in meetings of the committees of the Saeima and the Cabinet of Ministers of the Republic of Latvia and in the work of several committees and working groups established by the government, providing opinion on the financial and economic development. In 2020, when analysing Latvia's economic growth prospects, Latvijas Banka focused on analysing the impact of the Covid-19 pandemic on the economy

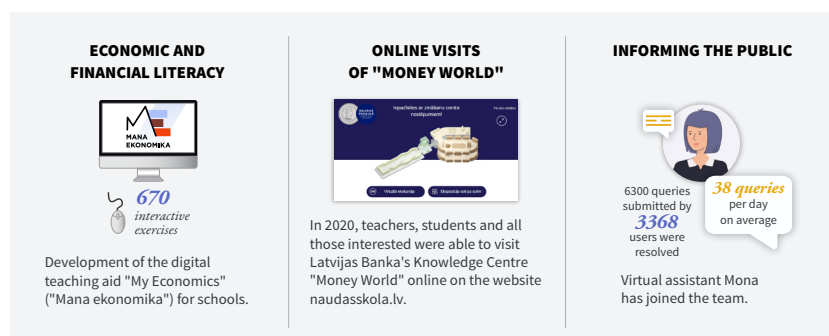
and drafting proposals on improving the government support instruments to mitigate the consequences of the crisis as well as the issues related to taxes, social security and education policy. Latvijas Banka also continued to analyse the role of Latvia's financial sector in the economy by starting an in-depth discussion with financial sector participants on lending trends, their underlying factors and the future development in Latvia. Likewise, Latvijas Banka continued to analyse the potential impact of Brexit on Latvia's economy.

Employees of Latvijas Banka contributed to the promotion of Latvia's economic development by participating in different working groups and professional organisations, sharing experience and providing advice and support to them, including in the fields of economic forecasts, the government expenditure and the programming and uptake of EU funds, the financial sector and financial (including payment) services development and the AML/CFT as well as in other areas and in the process of drafting legal acts and their amendments regulating the above areas.

Employees of Latvijas Banka continued to participate in the Working Group for the Preparation of the Notification of the General Government Budget Deficit and Debt chaired by the CSB by compiling the notification data of the general government budget deficit and debt in 2019 and dealing with the methodological issues related to accounting of the general government budget deficit and debt.

Experts of Latvijas Banka provided support to the government enabling Latvia to take an active part in the EU and the OECD as well as ensured the provision of information to the international rating agencies and information exchange.

INFORMATION AND EDUCATIONAL FACILITIES PROVIDED TO THE PUBLIC



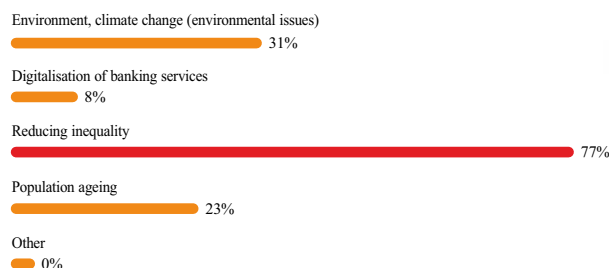
In 2020, the most important factors affecting institutional communication were similar across countries, population groups and economic sectors. Research worldwide suggests significant lack of trust in institutions and their leaders and policy makers. Therefore, institutions need to address this problem by finding the appropriate message, form and tone in their communication. The Covid-19 pandemic and the necessary restrictions first had a direct impact on the interaction and communication between the public and institutions, not only making certain activities impossible but also facilitating some forms of digital communication, and second – institutions themselves became an integral part of communication.

These factors may have been even more important for Latvijas Banka than any other institutions. First, Latvijas Banka needed to regain public trust after experiencing a fairly dramatic drop in 2018–2019. Second, in view of its mission to provide highly competent expert opinions for both the decision-making in the Eurosystem and the economic policy-making in Latvia, Latvijas Banka had to quickly incorporate the pandemic impact in its analytical framework and the respective communication. Third, the new conditions reinforced the need for innovative solutions for both work organisation

and communication with the public; moreover, they also had an impact on long-term educational programmes. It should be noted that in the midst of this broad-based crisis Latvijas Banka's focus on promoting the economic literacy of the public became even more relevant for the people and the education system.

Chart 18

IN YOUR OPINION, WHICH SUSTAINABLE DEVELOPMENT ISSUES SHOULD BE THE FOCUS OF A CENTRAL BANK?



Source: the votes cast on the Sli.do platform for the online discussion "My opinion for the future economy" held by Latvijas Banka on 5 November 2020 within the framework of the euro area monetary strategy review.

During this period, the ECB and the national central banks of the Eurosystem are conducting the strategic review of their main task, i.e. the adoption and implementation of the monetary policy with the aim of maintaining price stability. The most important part of the process was completed in 2020 by holding broad consultations with academics and professionals in the economic and financial sectors as well as with the civil society. Latvijas Banka, together with the Civic Alliance – Latvia, engaged Latvia's leading civil society organisations and experts in a discussion on the economic and financial environment in Latvia, the pandemic crisis and sustainable development opportunities in view of the monetary policy impact on these developments and the welfare of the population. The result of the exchange of ideas will form part of the basis for the discussion in the Governing Council of the ECB. Furthermore, one specific result with a long-term impact on Latvijas Banka's communication is the commitment of the involved parties and Latvijas Banka to continue to practice two-way communication and active listening and to further the dialog between the policy-shaping institution and the civil society.

To improve the understanding of the latest economic developments in Latvia, in September 2020 Latvijas Banka started a practice whereby the macroeconomic forecast announcement is followed by a discussion involving economic analysts and journalists with expertise in the given subject. This allows improving not only the quality of forecasting but also the overall quality of the economic dialogue in Latvia.

For these purposes, Latvijas Banka established contacts with diaspora researchers in Europe and worldwide, meeting with them in Riga and Brussels before the Covid-19 pandemic crisis. The aim was to build a stronger foundation for quality research in Latvia, inter alia, to map out, together with the partners, the discussion on the opportunities for using the EU aid in Latvia. A high-level conference on security of payments and development of digital money in Latvia was held, and several conversations outlining the future of the global, European and Latvian economies took place at Lampa Conversation Festival, etc.

As the household income shrank and savings, return on investment and a significant need for the use of credit gained importance during the crisis, the public interest in economic and financial issues increased. Meanwhile, these subjects were promoted in schools as part of the gradual implementation of the project Skola2030, based on the teachers' need for study materials that would be appropriate in terms of their content and methodology, with their approach focussed on the new realities, the practical application as well as the understanding of the "larger playing field". Moreover, the remote learning process accelerated the development of technologies and reinforced the students' habits of communicating and finding information in a digital format. Therefore, Latvijas Banka's

principal objective in promoting economic literacy was to support the public and schools in their needs in the most explicit and up-to-date way possible.



On its economic education website "Money School", Latvijas Banka started to publish a digital teaching aid "My Economics" ("Mana Ekonomika") in September 2020. The content and methodology included in the teaching aid are intended for the social science teachers (1–12 grades) covering the subject of economics in general education schools. By the end of the year, half of the social sciences and economics teachers had used this opportunity more or less. Moreover, Latvijas Banka received a lot of positive feedback as well as recommendations for further

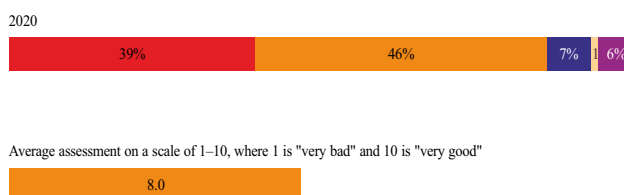
improvement of the teaching aid (see Chart 19). "My Economics" is an adaptable set of materials that can be adjusted according to the changes in the economy and education. The result – the knowledge of students and the public in the long run – depends on the knowledge and skills of teachers. Furthermore, the teachers themselves have indicated suitable courses on methodology and content as their second most important priority, with quality study materials being the first. In light of these considerations, already in 2021 Latvijas Banka, together with the National Centre for Education, will start building a learning and experience exchange platform for economics and finance teachers – seminars based on "My Economics". In addition to the above, in 2020 teachers, students and all those interested were able to visit Latvijas Banka's Knowledge Centre "Money World" online on the website "Money School". Given the continuation of the pandemic and the long-term needs of teachers associated with the remote learning process, in 2021 the Knowledge Centre will also offer options of remote visits and lectures.

Chart 19

SOCIAL SCIENCES AND ECONOMICS TEACHERS' ASSESSMENT OF LATVIJAS BANKA'S SUPPORT. HOW DO YOU ASSESS LATVIJAS BANKA'S ROLE IN FACILITATING ECONOMIC EDUCATION AND FINANCIAL LITERACY?

- Good (9 + 10)
- Rather good (6 + 7 + 8)
- Rather bad (3 + 4)
- Bad (1 + 2)
- Difficult to say / NA

Source: SIA LATVIJAS FAKTI, 2020.



The above online formats are used to implement financial literacy projects and, for Latvijas Banka, they are an essential, albeit not the only, means of communicating with the public and organisations in the new environment in an innovative and technology-based manner. The annual economic conference organised by Latvijas Banka was one of the first events of such scale in the ESCB or even in Latvia which took place completely remotely, was technically flawlessly conducted and even provided for the opportunity to engage the participants. To provide the necessary information to Latvijas Banka's customers or the general public, Latvijas Banka's website offers a virtual assistant Mona which is available 24/7/365 and ensures an effective use of resources.

Overall, Latvijas Banka was more open and actively engaged in addressing issues important to the public and, thus, has regained the public trust, with the share of the population positively disposed towards Latvijas Banka returning to 60% in April 2020 and remaining within the 54%–60% range despite the economic and social shocks caused by the pandemic.

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 2020, 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 the developments in the global economy and the financial system. In 2020, the IMF focused particularly on the crisis caused by the Covid-19 pandemic and the provision of the financial assistance to more than 80 countries in the world. The financial assistance instruments were improved for this purpose, including to reduce the burden of debt servicing costs for poor countries. The development of a comprehensive strategy was launched to support emerging market economies, given their high debt levels. Discussions also continued on IMF resources, climate change related challenges and inequality.

Latvia's interests in the IMF were represented by the Nordic-Baltic Constituency that includes Denmark, Estonia, Iceland, Latvia, Lithuania, Norway, Finland and Sweden. One Executive Director represented this constituency on the IMF Executive Board, with a total of 3.3% votes.

In 2020, cooperation with the IMF, based on consultations under Article IV of the IMF Articles of Agreement, continued.

In 2020, Latvijas Banka continued its membership in the BIS. At the beginning of 2020, Latvijas Banka actively participated in the Innovation Expert Working Group, which prepared the Eurosystem's application for establishing the BIS Innovation Hub. Latvijas Banka participated in consultations and discussions on current achievements in innovation advancement and the possibilities to host the new BIS Innovation Hub centre in Europe. On 30 June, the BIS approved the Eurosystem's application and announced the establishment of the BIS Innovation Hub centre in two locations (Frankfurt and Paris). Latvijas Banka will continue its participation in the central bank innovation area.

In early 2020 before the introduction of the Covid-19 related containment measures, Latvijas Banka organised several events with the participation of the experts of the national central banks of different countries and the ECB, including research and training workshops, in Riga.

Cooperation between the central banks of the Nordic and Baltic countries also continued to be the case, including the discussion on topical issues in central banking. As part of the long-term cooperation between the central banks of the Baltic States, seminars and high-level meetings for experts were organised in Riga.

ACTIONS TAKEN IN THE AREA OF SUSTAINABILITY

The issues of sustainability increasingly appear also on the agenda of central banks. In 2020, Christine Lagarde, President of the ECB, stressed that addressing climate change will remain high on the list of the ECB's future actions: "Through our strategy review, we will determine where and how the issue of climate change and the fight against climate change can actually have an impact on our policies."

The ECB has defined that it takes actions in four main areas of competence in the fight against climate change: economic analysis, banking supervision, monetary policy and investment portfolios and financial stability.¹

In 2020, Latvijas Banka started to actively form its opinion on the green economy and sustainability issues by participating in discussions of various formats and by establishing an internal working group for coordinating sustainability issues at Latvijas Banka.

A discussion "The European Green Deal and Economic Recovery after the Covid-19 Crisis" was held at Lampa Conversation Festival in September 2020 with the participation of Valdis Dombrovskis, Vice-President of the EC, Juris Pūce, Minister of Environmental Protection and Regional Development, Līga Meņģelsone, Director General of Employers' Confederation of Latvia, and Mārtiņš Kazāks, Governor of Latvijas Banka.²

The participants debated about the framework and significance of the European Green Deal and Economic Recovery Plan as well as its impact on Latvia's economic development, about how to raise public awareness of the European and Latvian climate and crisis management policies and how to use the opportunity to participate in achieving climate neutrality and establishing a green economy.

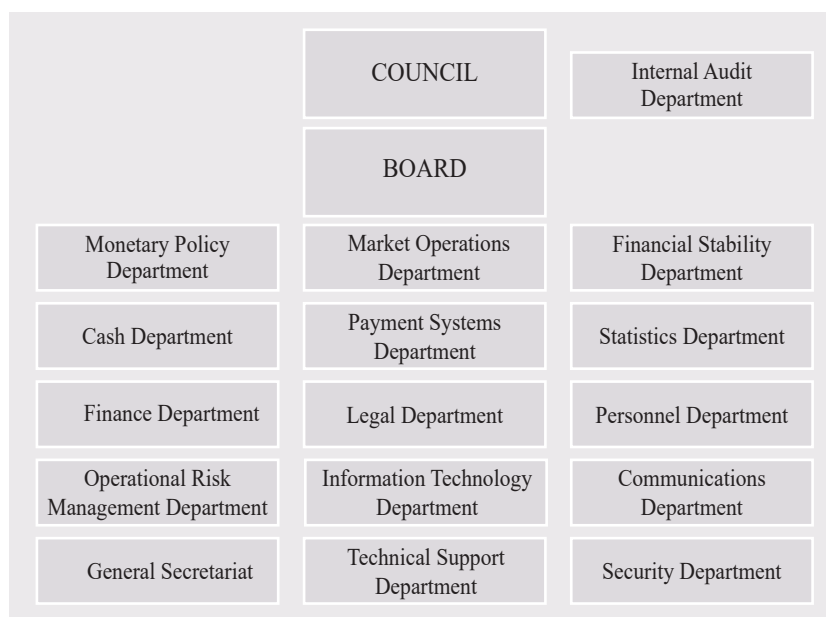
In 2020, Latvijas Banka joined the Network of Central Banks and Supervisors for Greening the Financial System (NGFS) – the forum bringing together national central banks committed to study the effects of climate change on the economy and the financial sector and to search for solutions and best practices.

The sustainability and the green economy will be topical issues on the agenda of Latvijas Banka in the coming years. Latvijas Banka's analytical capacity and long-term vision of the economy allow it to become a respectable opinion leader in this area.

¹ <https://www.ecb.europa.eu/ecb/orga/climate/html/index.en.html>.

² <https://festivalslampa.lv/en/video-archive/1387>.

ORGANISATIONAL STRUCTURE OF LATVIJAS BANKA



THE COUNCIL OF LATVIJAS BANKA

The Council of Latvijas Banka takes decisions on behalf of Latvijas Banka. The term of office of Governor, Deputy Governor and Members of the Council of Latvijas Banka is five years. The current Members of the Council of Latvijas Banka shall continue to hold office by the end of the six-year term of office. Zoja Razmusa held office as Deputy Governor of Latvijas Banka until 12 March 2020, the expiration date of her term of office. Vita Pilsuma, Member of the Council of Latvijas Banka, left her office at the Council of Latvijas Banka on 30 September 2020. On 5 March 2020, the Saeima of the Republic of Latvia approved Māris Kālis, the Chairman of the Board of Latvijas Banka, as the Deputy Governor of Latvijas Banka; he took office on 13 March 2020. In 2020, the Saeima of the Republic of Latvia elected two new Members of the Council of Latvijas Banka: Zita Zariņa was elected on 5 March 2020 and she took office on 15 April 2020, and Andris Vilks was elected on 1 October 2020 and he took office on 16 November 2020. The composition of the Council of Latvijas Banka, as at the end of 2020, was as follows:

- Governor **Mārtiņš Kazāks;**
- Deputy Governor **Māris Kālis;**
- Members of the Council: **Arvils Sautiņš,**
Aivars Skopiņš,
Andris Vilks,
Zita Zariņa.

Meetings of the Council of Latvijas Banka are held as appropriate, but at least once a quarter. In 2020, the Council of Latvijas Banka held 22 meetings where decisions were taken on the use of monetary policy instruments, investment management, provision of currency in circulation, compiling statistical data, operation and oversight of the payment and securities settlement systems, operation of the Credit Register, licensing and supervising of purchase and sale of foreign currency, and other issues pertaining to the operation, management and organisation of Latvijas Banka.

THE BOARD OF LATVIJAS BANKA

To carry out and efficiently manage day-to-day activities of Latvijas Banka, the Council of Latvijas Banka has established the Board of Latvijas Banka that performs activities on a continuous basis.

In view of the fact that Māris Kālis, the former Chairman of the Board of Latvijas Banka, was elected the Deputy Governor of Latvijas Banka, as from 13 March 2020 Ilze Posuma, Deputy Chairperson of the Board of Latvijas Banka, is simultaneously also performing the duties of the Chairperson of the Board of Latvijas Banka.

Pursuant to the amendments to the Law on Latvijas Banka adopted by the Saeima of the Republic of Latvia on 21 November 2019, the number of Members of the Board of Latvijas Banka has been reduced from six to four Members as from 1 March 2020. The composition of the Board of Latvijas Banka, as at the end of 2020, was as follows:

- acting Chairperson of the Board of Latvijas Banka, Deputy Chairperson of the Board of Latvijas Banka **Ilze Posuma;**
- Members of the Board: **Jānis Caune,**
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 and by implementing decisions of the Council of Latvijas Banka.

EMPLOYEES OF LATVIJAS BANKA

At the end of 2020, the number of Latvijas Banka employees was 421, of which 9 had fixed-term employment contracts (compared with 479 and 10 employees at the end of 2019, respectively). At the end of 2020, 59% of Latvijas Banka's staff were male and 41% were female. The Counsellor of Latvijas Banka worked at the Permanent Representation of the Republic of Latvia to the EU in 2020.

Structural improvements continued at Latvijas Banka in 2020.

On 1 June 2020, the Credit Register Division of the Payment Systems Department was included in the Statistics Department, which is functionally and structurally more appropriate, and was renamed the Register Division.

With the advancement of engineering and technical security systems, their functioning increasingly relies on information technologies. In light of the above, on 1 June 2020 the Security Systems Division of the Technical Support Department was included in the Information Technology Department and was renamed the Engineering and Technical Security Systems Division.

On 1 July 2020, the International Relations and Communication Department was divided into two separate structural units – the General Secretariat and the Communications Department.

COMMISSIONS AND COMMITTEES OF LATVIJAS BANKA

Audit Committee of Latvijas Banka	Investment Committee of Latvijas Banka
Budget Committee of Latvijas Banka	Licensing Committee of Latvijas Banka
Coin Design Commission of Latvijas Banka	Security Oversight Commission of Latvijas Banka
Commission for Evaluation of Gifts and Disposal and Write-off of Movable Assets of Latvijas Banka	Standing Commission for Procurement of Latvijas Banka
Commission for Management of Banknotes and Coins of Latvijas Banka	Strategic Development and Innovation Management Committee of Latvijas Banka
Ethics Committee of Latvijas Banka	

In order to ensure quality performance of Latvijas Banka's tasks, several committees, commissions and working groups approved by the Council of Latvijas Banka, Governor of Latvijas Banka or the Board of Latvijas Banka continued their work in 2020.

The Commission for the Management of Banknotes and Coins of Latvijas Banka made decisions on the replacement of damaged euro and lats banknotes and circulation coins, exercised control over identification, accounting, storage and destruction of banknotes and coins with signs of counterfeiting and counterfeits, registered cash processing institutions and cancelled their registration, and controlled the operation of cash processing institutions. To ensure the fulfilment of the requirements specified for purchasing and selling foreign currency as a financial service, the Licensing Committee of Latvijas Banka issued, re-registered and rewrote the licences of capital companies for purchasing and selling foreign currency as a commercial activity and controlled the operation of the licensed capital companies.

The Security Oversight Commission of Latvijas Banka supervised the management process of operational risks, including physical security risks.

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

The Budget Committee of Latvijas Banka contributed to an efficient use of Latvijas Banka's financial resources during the process of management of Latvijas Banka's budget. The Standing Commission for Procurement of Latvijas Banka implemented this objective in the area of procurements organised by Latvijas Banka. The Investment Committee of Latvijas Banka developed and defined a strategy for and made tactical decisions on managing financial assets and gold.

The Audit Committee of Latvijas Banka, authorised by the Council of Latvijas Banka, carried out the oversight of the internal audit function, activities of the external auditors of Latvijas Banka and the preparation of financial statements; it also enhanced the functioning of the internal control system of Latvijas Banka.

On 1 June 2020, a new committee, i.e. the Strategic Development and Innovation Management Committee of Latvijas Banka, was formed with the aim to coordinate the strategic planning and management as well as to facilitate Latvijas Banka's uptake of innovation.

MANAGEMENT PRINCIPLES AND DEVELOPMENT

Management of Latvijas Banka ensures quality performance of the tasks stipulated in the Law on Latvijas Banka and other legal acts. The management model of Latvijas Banka provides an opportunity to detect gaps in the areas of management and leadership with respect to strategies, resources, staff and processes as well as to measure the results achieved vis-à-vis customers, employees and the general public.

Commissioned by the Saeima of the Republic of Latvia, in 2020 the Cabinet of Ministers endorsed the draft laws on the incorporation of the FCMC into Latvijas Banka prepared by the Ministry of Finance in cooperation with Latvijas Banka and the FCMC.

The endorsed draft laws as well as 24 supporting draft laws will be sent to the ECB. Upon receipt of the ECB's opinion, the draft laws will be submitted to the State Chancellery for their further processing by the Saeima.

According to the plan, the integrated institution will commence its work on 1 January 2023.

In 2020, Latvijas Banka's operational management largely focussed on its work organisation, considering the conditions during the Covid-19 pandemic.

The vision, mission and values of Latvijas Banka and its priority objectives underlie the operation and development planning. Progress towards achieving the set objectives is measured annually. At the same time, the execution of functions and processes is monitored daily, and the fulfilment of work plans is reviewed on a regular basis.

RESOURCE MANAGEMENT

HUMAN RESOURCES

In 2020, Latvijas Banka continued to pursue its key principles of human resources policy of hiring qualified and professional employees by way of an effective staff recruitment process and establishing long-term employment relationships, creating a motivating working environment and enhancing professional development opportunities.

Like in previous years, Latvijas Banka used staff rotation and promotion to foster personnel development and career.

Latvijas Banka participated in the Schuman programme designed to provide ESCB and SSM staff members with multi-directional, project-based external work experience. Within the framework of the programme, an expert from the Cash Department and an expert from the Information Systems Department took part in the project of *Nationale Bank van België/Banque Nationale de Belgique*. The employee of Latvijas Banka appointed as the Adviser to the Executive Director of the Nordic-Baltic Constituency of the IMF in 2018 continued her work.

In 2020, inter alia, considering the Covid-19 restrictions and actively making use of remote learning opportunities, the staff of Latvijas Banka continued to broaden their professional expertise in the fields of monetary policy, financial stability, macroeconomics, econometrics, financial market, financial institution supervision, statistics, financial accounting, internal audit, personnel management, law, risk management, securities operations, cash processing supervision and information technologies. Several employees of Latvijas Banka further developed their professional knowledge by participating in international professional certification programmes.

Latvijas Banka's staff training costs amounted to 0.5% of the total expenses on remuneration (1.3% in 2019).

FINANCIAL RESOURCES

The financial management system of Latvijas Banka has been developed to ensure support to decision making, financial risk management and efficient use of financial resources.

Latvijas Banka finances its operation primarily from the income generated from managing financial investments and from monetary policy operations. Latvijas Banka does not receive any financing from the state budget. Instead, it transfers 70% of the profit made during the reporting year to the state budget. In 2020, Latvijas Banka recorded profits of 26.7 million euro, of which 18.7 million euro are to be transferred to the state budget. Over the last five years, Latvijas Banka's profit totalled 104.0 million euro, of which an amount of 71.0 million euro was transferred to the state budget.

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 in the

medium term within the framework of acceptable risk standards without contradicting the monetary policy implemented by the Eurosystem. Meanwhile, the 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 Latvijas Banka's financial transactions, financial risks and their management as well as its performance results, Latvijas Banka 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 laws and 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 as well as other financial information, which is also available on the website of Latvijas Banka. Latvijas Banka's integrated information system ensures a standardised, automated, secure 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 the changes in assets and liabilities as well as those in income and expenses of Latvijas Banka, paying particular attention to both 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 and planning 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 ensure the independence of internal audit function, the Council of Latvijas Banka also approves the expenditure plan for the Internal Audit Department.

The Budget Committee, set up by the Council of Latvijas Banka, evaluates the draft budget prepared by the Board of Latvijas Banka and oversees the budget execution. The Board of Latvijas Banka, together with the heads of the relevant structural units of Latvijas Banka, draws up the draft budget and submits it to the Budget Committee and the Council of Latvijas Banka as well as controls the budget execution on a regular basis.

INFRASTRUCTURE RESOURCES

Engineering and technical infrastructure resources

Latvijas Banka provides and maintains the infrastructure necessary for its operation. Construction works necessary for the maintenance of buildings were carried out in the buildings of Latvijas Banka.

In 2020, the central entrance of the building at K. Valdemāra iela 2A, Riga, was reconstructed, and the double flooring was renovated in some rooms of the Riga Branch building.

Information technologies

The technological modernisation of the advanced security system, widely used when exchanging the Credit Register information, payment systems information as well as

statistical and other information with credit institutions and other market participants, was performed in 2020.

The Banking Information System T24 was upgraded, thus ensuring additional functionalities and options as well as compliance with the latest technological requirements.

Several information systems and services of Latvijas Banka were improved both by introducing important extra functionalities and by introducing technological enhancements, inter alia, by improving the infrastructure and security necessary for effective remote work.

Engineering and technical security systems solutions were enhanced by increasing the security of important components, by ensuring a higher level of integration and efficiency and, overall, by including them into the unified information technologies infrastructure.

Cyber security testing of the Credit Register and the systems infrastructure has been conducted and significant additional security solutions and procedures were introduced to mitigate the risks associated with information security, cyber security and the latest technological threats.

Environmental resources

Latvijas Banka is an environmentally friendly institution taking care of an efficient use of environmental resources.

Over time, a number of measures have been taken to reduce the use of paper and, consequently, also resources required for its production. Electronic circulation of documents has been fully provided within Latvijas Banka and, to the extent possible, also between Latvijas Banka and its external cooperation partners, thus substantially reducing the need for document printing and, at the same time, speeding up the document circulation. Waste paper is recycled.

Efficient printer mode is used to ensure lower consumption of materials (toner, ink and paper) and smaller amount of required paper (by applying duplex printing). The employees are encouraged to choose a more efficient printing mode and assess the necessity of printing (colour printing in particular).

As regards energy efficiency, Latvijas Banka also takes into account the energy consumption of new equipment when implementing projects in relation to technical modernisation of equipment. The energy efficiency ratio is considered when upgrading hardware and other technical equipment as well as when improving lighting solutions.

RISK MANAGEMENT

Latvijas Banka manages strategic, financial and operational risks. Latvijas Banka's risk management goal and basic principles are set out in the "Risk Management Policy of Latvijas Banka" adopted by the Council of Latvijas Banka.

Risk management at Latvijas Banka is carried out as part of a systematic process identifying, analysing and assessing risks, developing and implementing relevant risk mitigation measures, and overseeing and reviewing risks on a regular basis. This allows to identify in advance, assess and efficiently manage risks that are likely to have a negative effect on:

- Latvijas Banka's financial position and financial performance;
- Latvijas Banka's capability to perform in a quality and efficient manner the tasks set out in the legislative acts, inter alia, to participate in the implementation of the ESCB functions.

Financial risks are managed to mitigate any potential negative impact on Latvijas Banka's financial position and financial performance that might arise from adverse changes in financial market factors or a counterparty default. When managing financial risks, including market risk (price, interest rate and currency risks), credit risk and liquidity risk, acceptable risk limits and risk parameters are taken into consideration to preserve the value of investments ensuring the required liquidity and income earning in the long term.

Financial risks related to Latvijas Banka's investment are managed in accordance with the "Procedure for Managing Financial Assets and Gold of Latvijas Banka" adopted by the Council of Latvijas Banka.

Latvijas Banka's investments are managed by classifying them into different investment portfolios. The parameters for a benchmark reflecting the acceptable levels of financial risks and return are set out for each investment portfolio and the Risk Management Division of the Market Operations Department monitors 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 managers. The Investment Committee of Latvijas Banka reviews the investment strategy on a quarterly basis, and on a weekly basis receives and reviews reports and forecasts for the developments in the financial markets prepared by portfolio managers, and reports by financial risk managers, and decides on the investment management tactic for the forthcoming week. The Market Operations Department regularly informs the Council and the Board of Latvijas Banka about the results of investment management.

Operational risks of Latvijas Banka are managed to mitigate any potential negative impact on Latvijas Banka's operation, reputation or financial position and financial performance, resulting from inadequate or defective performance of Latvijas Banka's processes, an act or omission by an employee or unavailability of staff, as well as by inadequate operation or unavailability of Latvijas Banka's information systems, information systems infrastructure, or other infrastructure, or by external events.

Latvijas Banka's operational risks are managed under a uniform operational risk management framework, with the major operational risks being compliance risks (inter alia, in preventing conflict of interests, anti-corruption control, personal data protection, anti-money laundering and combating the financing of terrorism and proliferation, and ensuring workplace environment protection), risks related to business continuity, physical security, information security and information systems (including cyber security). Latvijas Banka's operational risks are managed through processes and projects by identifying and assessing risks and, depending on the risk assessment, defining and implementing the most appropriate actions.

Compliance risks are managed to ensure compliance of Latvijas Banka's operation, inter alia, that of activities of Latvijas Banka's officials and employees, with legislative acts.

Risks related to the business continuity of Latvijas Banka are managed to mitigate any potential negative impact on the execution of critical processes where their discontinuity may cause negative consequences for the Latvian financial system or adversely affect the implementation of Latvijas Banka's tasks. The risks are managed, inter alia, by ensuring continuity of the critical processes or their recovery as soon as possible and to a full extent in the event of their disruption or failure, as well as efficient incident management.

Risks related to physical security, including risks associated with fire safety and civil protection are managed to mitigate any potential negative impact on the physical security of persons present on the premises of Latvijas Banka, the premises of Latvijas

Banka and valuables therein, transportation of its valuables and the events organised by Latvijas Banka.

Risks related to information security are managed to prevent unauthorised disclosure or use of confidential information, classifying it by its degree of confidentiality and ensuring appropriate protection, at the same time taking care that the protective measures do not prevent Latvijas Banka from providing non-classified information to its cooperation partners and general public.

Risks related to information systems, including cyber security risks are managed to prevent a potential negative impact on availability, security and integrity of the information systems and infrastructure of Latvijas Banka. The information systems of Latvijas Banka are classified based on their importance for implementing Latvijas Banka's tasks and on the basis of the confidentiality, integrity and availability requirements for the data to be processed, establishing appropriate physical and logical protection for each level of classification.

In 2020, the main focus of operational risk management was on managing risks related to the Covid-19 pandemic and remote working. The state of emergency declared due to the rapid spread of the Covid-19 infection, inter alia, the imposed restrictions, have not affected Latvijas Banka's operation, and Latvijas Banka has ensured continuous and complete execution of its functions.

Latvijas Banka ensures risk management training for its employees and inter alia, conducts, on a regular basis, training sessions and tests for employees to maintain appropriate level of their know-how and skills.

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, control system and processes and advises on improvements in Latvijas Banka's operation. The internal audit at Latvijas Banka is conducted by the Internal Audit Department.

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 the Internal Audit Department. It is carried out in line with the "Core Principles for the Professional Practice of Internal Auditing", "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 is also assessed by an external assessor every five years. In 2020, the external assessment was carried out by PricewaterhouseCoopers SIA. The assessment confirmed compliance of the internal audit activities with the above standards and the "Code of Ethics".

The internal audit covers all business areas of Latvijas Banka. Internal audits are planned and conducted using a risk-based approach. The Head of the Internal Audit Department reports the outcomes of each internal audit to the Council and the Board of Latvijas Banka. The Internal Audit Department submits a report on the performance of the approved annual plan of internal audits, the accomplished internal audits, their results and identified findings, the status of the follow-up of the previously reported audit findings and other relevant information to the Audit Committee of Latvijas Banka 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 of the Eurosystem/ESCB/SSM Internal Auditors Committee. In 2020, the Internal Audit Department performed four such internal audits at Latvijas Banka. The staff of the Internal Audit Department also engage in the fulfilment of other Eurosystem/ESCB/SSM internal audit tasks. In 2020, the staff of the Internal Audit Department participated in three working groups responsible for the Eurosystem/ESCB/SSM internal audit planning and implementation and work organisation.

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 Council of the EU. SIA "ERNST & YOUNG BALTIC", a commercial company of certified auditors, has been approved as the external auditor of Latvijas Banka's financial statements for 2020–2024.

Activities of the Internal Audit Department of Latvijas Banka and the external auditor auditing Latvijas Banka's financial statements are overseen by the Audit Committee of Latvijas Banka.

FINANCIAL STATEMENTS OF LATVIJAS BANKA

FOR THE YEAR ENDED 31 DECEMBER 2020

BALANCE SHEET

	(at the end of the year; in thousands of euro)		
	Note ¹	2020	2019
ASSETS			
Gold and gold receivables	6	330 139	289 043
Claims on non-euro area residents denominated in foreign currency	7	3 970 780	3 688 972
Receivables from the International Monetary Fund		142 411	149 082
Balances with banks and security investments, external loans and other external assets		3 828 369	3 539 890
Claims on euro area residents denominated in foreign currency	8	333 706	460 415
Claims on non-euro area residents denominated in euro	9	119 143	90 139
Lending to euro area credit institutions related to monetary policy operations denominated in euro	10	1 260 000	12 250
Longer-term refinancing operations		1 260 000	12 250
Other claims on euro area credit institutions denominated in euro	11	120	8
Securities of euro area residents denominated in euro	12	11 129 440	8 721 137
Securities held for monetary policy purposes		10 008 456	7 636 472
Other securities		1 120 984	1 084 665
Intra-Eurosystem claims	13	5 673 974	5 277 483
Participating interest in the European Central Bank		114 095	114 108
Claims equivalent to the transfer of foreign reserves		157 202	158 264
Other claims within the Eurosystem		5 402 677	5 005 111
Other assets	14	228 440	206 062
TOTAL ASSETS		23 045 742	18 745 509

¹ The accompanying Notes set out on pages 61 to 107 are an integral part of these financial statements.

<i>(cont.)</i>	(at the end of the year; in thousands of euro)		
	Note	2020	2019
LIABILITIES			
Banknotes in circulation	15	5 142 726	4 666 799
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	16	6 053 812	5 660 676
Current accounts (covering the minimum reserve system)		6 053 812	5 660 676
Other liabilities to euro area credit institutions denominated in euro	17	577 746	11 871
Liabilities to other euro area residents denominated in euro	18	3 012 014	1 506 709
General government		1 588 192	442 044
Other liabilities		1 423 822	1 064 665
Liabilities to non-euro area residents denominated in euro	19	238 737	307 239
Liabilities to euro area residents denominated in foreign currency	20	615 986	153 351
Liabilities to non-euro area residents denominated in foreign currency	21	1 364 010	1 642 368
Intra-Eurosystem liabilities	13	4 837 613	3 833 540
Liabilities related to TARGET2 and correspondent accounts (net)		4 809 553	3 826 452
Liabilities related to other operational requirements within the Eurosystem		28 060	7 088
Other liabilities	22	409 700	329 326
Capital and reserves	23	793 398	633 630
TOTAL LIABILITIES		23 045 742	18 745 509

PROFIT AND LOSS STATEMENT

		(in thousands of euro)	
	Note	2020	2019
Net interest income	33	139 537	95 946
Interest income		190 313	198 804
Interest expense		-50 776	-102 858
Net result of financial operations, recognition of revaluation result in profit and loss statement and financial risk provisions		-68 947	-37 821
Realised gains arising from financial operations	34	44 471	46 253
Recognition of revaluation result on financial assets and positions in profit and loss statement	23, 35	-35 237	-3 856
Provisions for market risk and credit risk	36	-78 181	-80 218
Net expense from fees and commissions		-3 394	-3 607
Fees and commissions income		949	811
Fees and commissions expense		-4 343	-4 418
Income from equity securities and participating interest	37	18 605	14 884
Net result of pooling of monetary income	38	-27 701	-6 801
Other operating income	39	1 268	1 300
NET INCOME		59 368	63 901
Remuneration	40	-16 867	-17 660
Social security costs and solidarity tax	40	-3 764	-3 941
Banknote and coin acquisition costs	41	-1 546	-1 791
Depreciation of fixed assets and amortisation of intangible assets	14	-3 851	-4 129
Other operating expenses	42	-6 694	-9 225
PROFIT OF THE REPORTING YEAR		26 646	27 155

STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

		(in thousands of euro)	
	Note	2020	2019
Profit of the reporting year		26 646	27 155
Revaluation	23	140 950	169 433
Realisation of the accumulated revaluation result	23	-24 056	-6 986
Recognition of revaluation result on financial assets and positions in profit and loss statement	23, 35	35 237	3 856
Total changes in the valuation account	23	152 131	166 303
TOTAL		178 777	193 458

The financial statements set out on pages 57 to 107 were authorised by the Board of Latvijas Banka on 9 March 2021.

THIS DOCUMENT HAS BEEN ELECTRONICALLY SIGNED WITH A SECURE ELECTRONIC SIGNATURE CONTAINING A TIMESTAMP.

Acting Chairperson of the Board	Ilze Posuma
Member of the Board	Jānis Caune
Member of the Board	Raivo 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 legislation of the Republic of Latvia and the EU, inter alia, ECB legal acts, in compliance with the Treaty on the Functioning of the European Union and the Statute of the ESCB and of the ECB.

Pursuant to the Law on Latvijas Banka, the primary goal of Latvijas Banka is to maintain price stability. Latvijas Banka has the following main tasks:

- participate in the formulation and implementation of the Eurosystem's monetary policy;
- manage foreign reserves and other financial investments;
- ensure cash currency circulation in Latvia and contribute to ensuring cash currency circulation in the euro area;
- participate in promoting the 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 the Latvian 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 Latvijas Banka's tasks;
- 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;
- perform the function of the National Analysis Centre and the Coin National Analysis Centre, ensuring efficient analysis of currency counterfeits.

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's execution of operating activities is mainly financed from income received from its investment management and monetary policy operations.

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 branch in Riga.

2. PRINCIPAL ACCOUNTING POLICIES

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

2.1 BASIS OF PREPARATION

These financial statements have been prepared in accordance with the Guideline of the ECB of 3 November 2016 on the legal framework for accounting and financial reporting in the European System of Central Banks (recast) (ECB/2016/34), Financial Accounting Policy of Latvijas Banka approved by Latvijas Banka's Council, and the requirements of the Law on Latvijas Banka governing financial reporting.

2.2 BASIS OF MEASUREMENT

Gold, securities (except held-to-maturity debt securities and securities held for monetary policy purposes that are measured at amortised cost), 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 2.15. The comparison of the book value and fair value of these instruments is provided in Note 5. Other assets and liabilities are measured in accordance with the historical cost basis of accounting.

2.3 FAIR VALUE OF FINANCIAL ASSETS AND FINANCIAL LIABILITIES

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

The 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, except for the fair value of the BIS shares: the method of its estimation is 70% of the BIS net asset value (see also Note 14.2). The discounted cash flows are modelled using money market interest rates. The breakdown of assets measured at fair value as well as of financial instruments that have not been measured at their fair value but whose estimated fair value is different from their book value, taking into account the hierarchy of fair value determination, is provided in Note 5.

2.4 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 quoted gold market price in US dollars and the exchange rate of the US dollar against the euro published by the ECB. The exchange rate of the SDR is set on the basis of the weights of currencies in the SDR basket 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 prevailing 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 prevailing on the day of the transaction.

Transactions in foreign currencies are included in the calculation of net foreign currency position of the respective currency. The transactions in foreign currencies that reduce the respective currency position result in realised gains or losses. Any gain or loss arising from the revaluation of transactions in foreign currencies and of foreign currency positions is credited or charged to the profit and loss statement or the balance sheet item "Capital and reserves" as the foreign currency revaluation reserve ("Revaluation account") in accordance with the principles referred to in Note 2.23. The principles referred to herein and in Note 2.23 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 2020 and the year ended 31 December 2019 are as follows:

	(at the end of the year)		
	2020	2019	Changes (%)
US dollar (USD)	1.2271	1.1234	9.2
Japanese yen (JPY)	126.49	121.94	3.7
Canadian dollar (CAD)	1.5633	1.4598	7.1
British pound sterling (GBP)	0.8990	0.85080	5.7
Gold (XAU)	1543.884	1354.104	14.0

2.5 RECOGNITION AND DERECOGNITION OF FINANCIAL ASSETS AND FINANCIAL 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 the 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.

2.6 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.

2.7 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: the accounting policy for securities held to maturity (see Note 2.9), the useful life of fixed assets and intangible assets (see Notes 2.17 and 2.18), impairment of assets (see Note 2.19), the exchange probability of those lats banknotes and coins that have not been yet exchanged for euro banknotes and coins (see Note 2.20), the repurchasing probability of collector coins (see Note 2.21), provisions for market risk and credit risk (see Notes 2.22 and 36), the breakdown of fair value determination (see Note 5), the method for establishing the fair value of the BIS shares (see Note 14.2), and the method of recognising a part of the initial revaluation account balance in the profit and loss statement (see Note 23).

2.8 GOLD AND GOLD RECEIVABLES

Gold is stated at market value in the balance sheet in accordance with the principles described in Note 2.4.

Gold swap arrangements are treated as repurchase agreements (see also Notes 2.11 and 2.15).

Gains or losses arising from the revaluation of gold reserves is credited or charged to the profit and loss statement or the balance sheet item "Capital and reserves" as the foreign currency and gold revaluation reserve in accordance with the principles described in Note 2.23.

2.9 DEBT SECURITIES

Debt securities are stated at fair value in the balance sheet, except those held to maturity and securities held for monetary policy purposes, measured at amortised cost subject to impairment. Securities held to maturity are securities with fixed or determinable payments and fixed maturity which Latvijas Banka intends to hold to maturity.

Interest on securities, including premium and discount, is recognised in the profit and loss statement as interest income (see also Note 2.24).

Gains or losses arising from transactions in debt securities and the revaluation of the debt securities stated at fair value are credited or charged to the profit and loss statement

or the balance sheet item "Capital and reserves" as the securities revaluation reserve in accordance with the principles referred to in Note 2.23.

2.10 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.

2.11 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. The 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.

2.12 SECURITIES LENDING

Securities lent under automated security 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.

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

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

2.14 EQUITY SECURITIES AND PARTICIPATING INTEREST

Equity securities consist of investments in marketable equity instruments made as part of Latvijas Banka's investment management activities.

Participating interest includes permanent investments of Latvijas Banka in the equity of other entities. Latvijas Banka has no control or significant influence over any institution, therefore participating interest is not accounted for as an investment in a subsidiary or an associate.

Equity securities and participating interest 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 the fair value of participating interest is reported under the balance sheet item "Capital and reserves" as the revaluation reserve.

2.15 DERIVATIVE FINANCIAL INSTRUMENTS

Latvijas Banka enters into commitments involving forward exchange rate contracts, currency, gold 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, except gold swap arrangements that are treated as repurchase agreements and related claims and liabilities are reported on the balance sheet of Latvijas Banka. 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 prevailing 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 the fair value of interest rate and currency future contracts as well as OTC interest rate swap arrangements is included in the profit and loss statement taking into account the settlement. Any gain or loss arising from a change in the fair value of other derivative financial instruments is credited or charged to the profit and loss statement or the balance sheet item "Capital and reserves" as the revaluation reserve in accordance with the principles referred to in Note 2.23.

2.16 ACCRUED INTEREST INCOME AND EXPENSE

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

2.17 FIXED ASSETS

Fixed assets are tangible long-term assets with the useful life of over one year. The capitalisation limit of fixed assets is 150 euro, except for 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. Fixed assets are used in the provision of services as well as in the maintenance of other fixed assets and to ensure the 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 for by separate components, with individual useful life set for each such component.

In 2020, the useful lives set for fixed assets were not changed. In 2020 and 2019, the useful lives set for fixed assets were as follows:

	(years)	
	2020	2019
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 telecommunications equipment	2–5	2–5
Other fixed assets	5–15	5–15

In accordance with the 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 the development of the respective fixed assets.

2.18 INTANGIBLE ASSETS

Intangible assets are long-term assets without physical substance with a useful life of over one year. The 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.

2.19 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 impairment allowances for the respective asset are made. Such impairment allowances are recognised in the profit and loss statement with a respective reduction in the asset's carrying amount.

The ECB carries out impairment assessment of securities held for monetary policy purposes, identifying any potential changes in future cash flows and any other factors encumbering the fulfilment of the liabilities by the securities issuer. Assets are impaired when the carrying amount of securities held for monetary policy purposes exceeds their recoverable amount. The latter is defined as the present value of a future cash flow estimate. The Governing Council of the ECB approves the results of the asset impairment assessment carried out by the ECB (see Note 36).

2.20 CURRENCY IN CIRCULATION

In view of the fact that euro banknotes are issued by all euro area NCBs and the ECB, they report a certain share of the total amount of euro banknotes issued by the Eurosystem on their balance sheets. The ECB's share is 8% of the total amount of euro banknotes issued by the Eurosystem; the remaining 92% are allocated to the Eurosystem NCBs in proportion to their respective shares 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 net amount of euro banknotes it has issued (see Note 15); consequently, claims on the ECB related to the allocation of banknotes within the Eurosystem are reported under the balance sheet item "Intra-Eurosystem claims".

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.

The lats banknotes and coins issued by Latvijas Banka which have not been yet exchanged for the euro banknotes and coins are recognised in the balance sheet as liabilities considering the exchange probability of such lats banknotes and coins within 20 years from the euro changeover. The exchange probability of the lats banknotes and coins is assessed annually on the basis of the actual exchange data of the above banknotes and coins (see Note 22.1).

Euro coins and the lats banknotes and coins in circulation issued by Latvijas Banka that have been recognised as liabilities by Latvijas Banka, except collector coins (see also Note 2.21), are reported under the balance sheet item "Other liabilities" at nominal value.

2.21 COLLECTOR COINS

Collector coins sold are not included in the balance sheet as liabilities since the probability that the coins will be sold back to Latvijas Banka at their nominal value is low (e.g. 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.

2.22 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.

In addition, on the basis of reasonable risk estimates and in accordance with the legal framework for accounting and financial reporting in the ESCB, Latvijas Banka's Council takes decisions on making provisions for market risk (price, interest rate and currency risks) and credit risk associated with Latvijas Banka's investment management and other financial transactions (see also Note 36) as well as the use of these provisions should the above risks materialise.

2.23 RECOGNITION OF GAINS AND LOSSES ON FINANCIAL INSTRUMENTS, FOREIGN CURRENCY AND GOLD POSITION

Gains and losses on financial instruments, foreign currency and 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 item "Capital and reserves" as the revaluation reserve;
- (c) unrealised losses recognised in the balance sheet item "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 another financial instrument, foreign currency or gold position.

The average cost method shall be used to calculate the realised and unrealised gains and losses arising from a financial instrument, foreign currency or gold position. The average cost of a 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.

2.24 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 placed, loans granted, forward exchange rate contracts, currency and interest rate swap arrangements, and intra-Eurosystem claims, as well as negative interest on deposits received. Interest on securities also includes premium and discount, which are 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, interest on forward exchange rate contracts, currency and interest rate swap arrangements and intra-Eurosystem liabilities, as well as negative interest on securities, loans granted and deposits placed.

In the profit and loss statement received negative interest is reported as interest income; paid negative interest is reported as interest expense. Accrued negative interest on balance sheet liabilities is reported under the balance sheet item "Other assets"; accrued negative interest on balance sheet assets is reported under the balance sheet item "Other liabilities".

2.25 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 the disposal of the 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.

2.26 INCOME FROM EQUITY SECURITIES AND PARTICIPATING INTEREST

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

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

In recognising income from equity securities, the income recognition principles established by the ECB legal framework for accounting and financial reporting are applied to the investment portfolio rather than individual securities where externally managed investments in equity securities replicate the structure of an index-linked equity fund.

Pursuant to the decision of the Governing Council of the ECB, the income gained by the ECB on the claims related to the allocation of banknotes within the Eurosystem, and from the Securities Markets Programme, the asset-backed securities purchase programme, the third covered bond purchase programme, the PSPP and the PEPP shall be distributed as interim profit for the reporting year in which it accrues. The Governing Council of the ECB decides on the interim profit distribution 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 ECB's interim profit distribution, as well as in the event the Governing Council of the ECB decides to establish provisions for financial 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; the deductions may not exceed income on the claims related to the allocation of banknotes within the Eurosystem.

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

Income from equity securities and participating interest is reported under the profit and loss statement item "Income from equity securities and participating interest".

2.27 NET RESULT OF POOLING OF MONETARY INCOME

Pursuant to the Statute of the ESCB and of the ECB, euro area NCBs 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 after an NCB has joined the Eurosystem, the euro area NCB's monetary income is adjusted in compliance with a definite coefficient to avoid significant euro area 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. The 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 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.

2.28 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.

2.29 OTHER EXPENSES AND INCOME

Latvijas Banka's other operating expenses and income are recognised in the profit and loss statement on an accrual basis. The amount of accrued expenses 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 2020, Latvijas Banka's assets grew by 4300.2 million euro.

In 2020, the balance sheet item "Securities held for monetary policy purposes" increased by 2372.0 million euro. In March 2020, the Governing Council of the ECB decided to launch a new securities purchase programme PEPP providing for securities purchases in the Eurosystem to a total of 1850.0 billion euro; the PEPP will be continued until the impact of the COVID-19 pandemic on the economy decreases. At the end of 2020, asset purchases under the PEPP by Latvijas Banka amounted to 1690.9 million euro. Along with the PEPP, the previously launched asset purchase programme continued, under which the balance of this balance sheet item increased by 681.1 million euro.

In 2020, the amount of loans granted to credit institutions by Latvijas Banka as a result of longer-term refinancing operations increased by 1247.8 million euro (see also Note 10.2).

Other claims related to other operational requirements within the Eurosystem grew by 397.6 million euro, mostly due to a rise in claims on banknote allocation in the Eurosystem (see also Note 13.4).

In 2020, banknotes in circulation increased by 475.9 million euro, in line with the pickup in the overall amount of banknotes in circulation of the euro area NCBs.

The increases of 565.9 million euro and 462.6 million euro under balance sheet items "Other liabilities to euro area credit institutions denominated in euro" and "Liabilities to euro area residents denominated in foreign currency" respectively, as well as a decrease of 278.4 million euro under the balance sheet item "Liabilities to non-euro area residents denominated in foreign currency" are mostly related to repurchase agreements and gold swaps arrangements concluded in 2020 to reduce the costs for hedging currency risks and increase return on financial investments.

In 2020, demand deposits in euro from Latvian Government grew by 1146.1 million euro, as reported under the balance sheet item "Liabilities to general government".

At the end of 2020, credit institution deposits, reported under the balance sheet item "Liabilities to euro area credit institutions related to monetary policy operations denominated in euro", increased by 393.1 million euro. As a result of cross-border payments, liabilities to the ECB for the settlement result in TARGET2, reported under the balance sheet item "Intra-Eurosystem liabilities", increased by 983.1 million euro.

The capital and reserves of Latvijas Banka increased by 159.8 million euro due to net

changes in the "Revaluation account" balance (152.1 million euro) and the profits earned in 2020 (26.6 million euro), while the share of profits earned in 2019 and remitted to the state budget revenue (19.0 million euro) had a decreasing effect.

3.2 FINANCIAL PERFORMANCE

In 2020, Latvijas Banka's profit amounted to 26.6 million euro (27.2 million euro in 2019).

Net interest income in 2020 grew by 43.6 million euro as compared to 2019 and reached the amount of 139.5 million euro. This mainly resulted from a 52.1 million euro decrease in interest expense on account of lower costs of hedging currency risks.

The realised result from financial operations was positive (44.5 million euro; 46.3 million euro in 2019), while the recognition of the negative revaluation result on financial assets and positions in the profit and loss statement increased to stand at 35.2 million euro (3.9 million euro in 2019), mostly on account of depreciation of the US dollar vis-à-vis the euro (see also Notes 34 and 35).

In 2020, additional provisions in the amount of 78.2 million euro were established for market risk and credit risk (80.2 million in 2019).

Income from equity securities and participating interest amounted to 18.6 million euro (14.9 million euro in 2019), the increase resulting from higher dividends due to the equity securities portfolio growth.

Pursuant to the Statute of the ESCB and of the 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 2019, Latvijas Banka's net result of pooling of monetary income was negative (27.7 million euro; negative at 6.8 million euro in 2019).

Other operating income stood at 1.3 million euro (1.3 million euro in 2019).

The total recognised financial result, including changes in the "Revaluation account" balance, decreased by 14.7 million euro in comparison with 2019 and reached 178.8 million euro on account of a decrease of 45.6 million euro in the positive result of revaluation and a 31.4 million euro rise in the negative result on revaluation of financial assets and positions in the profit and loss statement, while the profit for the reporting year was 0.5 million euro lower than in 2019.

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

During the reporting year, the COVID-19 pandemic had no material effect on Latvijas Banka's operating income and expenses, except net interest income related to conducting monetary policy operations. The restrictions imposed to limit the spread of the pandemic in Latvia in the reporting year had no significant impact on the performance of Latvijas Banka's functions and provision of services.

4. FINANCIAL INVESTMENT POLICY

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

Investments include assets reported under the balance sheet items "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 "Other securities", as well as accrued income on debt securities reported under the balance sheet item of other assets "Accrued interest on other securities" and derivative financial instruments and spot exchange rate contracts whose book value is reported under relevant balance sheet items of other assets or other liabilities.

Investments are managed by classifying them into different investment portfolios by investment strategy and source of funding. The portfolio of borrowed funds includes investments which correspond to Latvijas Banka's liabilities in foreign currencies to government or government deposits. Investments that are not included in the portfolio of borrowed funds are included in the portfolios of 1–10 year fixed income securities, mortgage-backed securities, long-term fixed income securities, equity securities, Latvian government securities, and gold. The equity securities portfolio, part of the investments included in the 1–10 year fixed income securities portfolios and the mortgage-backed securities portfolios are managed by external managers.

The parameters for a benchmark reflecting the acceptable level of financial risks and expected return are set out for the 1–10 year fixed income securities portfolios, mortgage-backed securities portfolios, the portfolio of borrowed funds, and the equity securities portfolio.

The breakdown of investments by type of investment portfolio at the end of 2020 and 2019 was as follows:

	Book value (in thousands of euro)		Proportion (%)	
	2020	2019	2020	2019
1–10 year fixed income securities portfolios	3 445 980	3 535 151	58.2	62.5
Mortgage-backed securities portfolios	1 211 775	1 175 059	20.5	20.8
Equity securities portfolio	573 316	289 428	9.7	5.1
Gold portfolio	330 139	289 043	5.6	5.1
Long-term fixed income securities portfolio	168 173	168 099	2.8	3.0
The portfolio of borrowed funds	143 350	153 351	2.4	2.7
Latvian government securities portfolio	47 025	47 912	0.8	0.8
Total	5 919 758	5 658 043	100.0	100.0

The 1–10 year fixed income securities portfolio benchmark comprised the weighted 1–10 year government securities index of the UK and euro area countries, and the 1–3 year government securities index of the US and Canada.

The mortgage-backed securities portfolio benchmark is the US mortgage-backed securities index.

The equity securities portfolio benchmark is the equity securities index comprised of issuers from developed countries.

The gold portfolio comprises the gold of Latvijas Banka and the related financial instruments.

The long-term fixed income securities portfolio comprises euro area government securities denominated in euro, with term to maturity of 10 years at the time of acquisition.

The benchmark for the portfolio of borrowed funds is formed in compliance with the parameters of respective liabilities.

The Latvian government securities portfolio comprises euro denominated Latvian government bonds with term to maturity of 5–10 years at the time of acquisition.

The benchmark currency of Latvijas Banka's investment portfolios is the euro, except for the portfolio of borrowed funds, the equity securities portfolio and the gold portfolio, thus limiting the currency risk. For the portfolio of borrowed funds, the benchmark currency structure is formed considering the currency of the respective liabilities.

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

BALANCE SHEET NOTES

5. FAIR VALUE MEASUREMENT

The fair value of Latvijas Banka's assets is determined using the following hierarchy (see also Note 2.3):

- quoted market price. The fair value is determined using quoted prices for identical financial instruments in active markets;
- observable data. The 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. The fair value is determined using a model where significant inputs are non-observable.

At the end of 2020 and 2019, Latvijas Banka's assets carried at fair value were generally valued on the basis of a quoted market price.

At the end of 2020 and 2019, the participating interest in the BIS was assessed using non-observable data. The assessment was conducted using the 70% net asset value method (see also Note 14.2).

At the end of 2020 and 2019, the breakdown of financial instruments and gold carried at fair value and of the financial instruments whose fair value is different from their book value, according to the fair value hierarchy, was as follows:

					(in thousands of euro)	
	Book value	Fair value			Total fair value	Difference between fair value and book value
		Quoted market price	Observable data	Non-observable data		
As at 31 December 2019						
Gold	289 043	289 043	–	–	289 043	–
Securities in investment portfolios	5 151 246	4 552 682	610 900	–	5 163 582	12 336
Forward exchange rate contracts	24 649	–	24 043	–	24 043	–606
Interest rate swap arrangements	–533	–533	–	–	–533	–
Securities held for monetary policy purposes	7 703 471	8 155 588	–	–	8 155 588	452 117
Participating interest in the Bank for International Settlements	34 341	–	–	34 341	34 341	–
Total	13 202 217	12 996 780	634 943	34 341	13 666 064	463 847
As at 31 December 2020						
Gold	330 139	330 139	–	–	330 139	–
Securities in investment portfolios	5 362 253	4 842 019	541 405	–	5 383 424	21 171
Forward exchange rate contracts	25 613	–	25 063	–	25 063	–550
Interest rate swap arrangements	1	1	–	–	1	–
Securities held for monetary policy purposes	10 082 251	10 897 433	–	–	10 897 433	815 182
Participating interest in the Bank for International Settlements	35 960	–	–	35 960	35 960	–
Total	15 836 217	16 069 592	566 468	35 960	16 672 020	835 803

The securities, including accrued interest on the above securities, are reported under the balance sheet items "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", "Other assets" and "Other liabilities".

The book value of forward exchange rate contracts is reported under the balance sheet items "Other assets" or "Other liabilities", while the present Note discloses the total net book value.

The average market prices on the last trading day of the reporting year are obtained from the electronic information systems Bloomberg and Refinitiv (quoted market price if the market of the respective financial instrument is active; observable data if the market is inactive). Where the above quoted price for a financial instrument is absent in the electronic information systems and the market for the financial instrument is inactive, the price provided by a market participant or the discounted cash flow is used for evaluating the financial instrument (observable data).

6. GOLD AND GOLD RECEIVABLES

	Troy ounces	In thousands of euro
As at 31 December 2018	213 384	239 195
During 2019		
Increase in gold market value	x	49 749
Net change resulting from gold swaps arrangements	73	99
As at 31 December 2019	213 457	289 043
During 2020		
Increase in gold market value	x	40 511
Net change resulting from gold swaps arrangements	379	585
As at 31 December 2020	213 836	330 139

The revaluation result of gold is recognised under the balance sheet item "Capital and reserves" as the revaluation reserve.

At the end of 2020, all gold in the amount of 330 139 thousand euro (289 043 thousand euro at the end of 2019) had been involved in gold swaps arrangements (see also Notes 21 and 44).

At the end of 2020 and 2019, 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 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 2020, the receivables from the IMF in SDR as recorded on Latvijas Banka's balance sheet were equivalent to 142 411 thousand euro (149 082 thousand euro at the end of 2019), whereas the liabilities to the IMF are made up of funds at the disposal of the IMF in the amount of 983 thousand euro (1035 thousand euro at the end of 2019) held on its Accounts No. 1 and No. 2 (see also Note 19).

At the end of 2020 and 2019, Latvia's net receivables from the IMF were as follows:

	(in thousands of euro)		(in thousands of SDR)	
	2020	2019	2020	2019
Latvia's quota in the International Monetary Fund	391 649	410 025	332 300	332 300
International Monetary Fund holdings in euro	-391 588	-409 967	-332 249	-332 253
Promissory note of the Latvian government	-390 605	-408 932	-331 414	-331 414
Account No. 1	-979	-1 025	-831	-831
Account No. 2	-4	-10	-4	-8
Reserve position in the International Monetary Fund	65	68	55	55
SDR	142 411	149 082	120 830	120 822
General allocation	-110 786	-115 984	-93 998	-93 998
Special allocation	-31 615	-33 098	-26 824	-26 824
Latvia's net receivables from the International Monetary Fund	75	68	63	55

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)	
	2020	2019
Securities	3 783 432	3 501 497
Demand deposits	44 920	38 375
Foreign currency in cash	17	18
Total	3 828 369	3 539 890

8. CLAIMS ON EURO AREA RESIDENTS DENOMINATED IN FOREIGN CURRENCY

	(in thousands of euro)	
	2020	2019
Securities	332 969	460 047
Demand deposits	737	368
Total	333 706	460 415

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

	(in thousands of euro)	
	2020	2019
Securities	105 509	84 352
Demand deposits	13 634	5 787
Total	119 143	90 139

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

At the end of 2020, the total amount of Eurosystem loans in monetary policy operations reached 1 793 194 million euro (624 233 million euro at the end of 2019), including 1260 million euro (12.3 million euro at the end of 2019) of loans granted by Latvijas Banka. Pursuant to the Statute of the ESCB and of the ECB, the 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 (see Note 2.27). Losses from Eurosystem lending related to monetary policy operations might only be incurred where the counterparty defaults on its obligations and the funds recovered as a result of the disposal of the collateral provided by the counterparty are not sufficient (see also Note 25.1.2).

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 2020 and 2019, Latvijas Banka had granted no loans in main refinancing operations.

10.2 LONGER-TERM REFINANCING OPERATIONS

Longer-term refinancing operations are open market operations, executed through reverse transactions with the aim to provide credit institutions with additional longer-term refinancing. Such operations are conducted through monthly standard tenders with maturities between 3 and 48 months. In addition, following the decision of the Governing Council of the ECB, TLTROs were launched in 2014. They are liquidity providing reverse operations providing longer-term liquidity to credit institutions on attractive terms, so that they can continue easing the terms and conditions of lending to the private sector and to encourage their lending to the real economy. In 2016, the Governing Council of the ECB introduced a new series of four targeted longer-term refinancing operations (TLTRO II). These operations have a four-year maturity, with a possibility of early repayment after two years. In 2019, the Governing Council of the ECB introduced a new series of seven targeted longer-term refinancing operations (TLTRO III). These operations have a three-year maturity, with a possibility of early repayment after two years. In 2020, the Governing Council of the ECB added three further operations to this series, which will be conducted in 2021, and have a three-year maturity, with a possibility of early repayment. According to the initial decisions, the interest rate applicable to TLTRO III operations could be as low as the average interest rate on the deposit facility. In response to the impact of the COVID-19 pandemic, in 2020 the Governing Council of the ECB decided to lower this rate, establishing that for the period between 24 June 2020 and 23 June 2022 the interest rate applicable can be as low as 50 basis points below the average interest rate on the deposit facility, but in any case may not become less negative than -1%. Additionally, in April 2020, the Governing Council of the ECB decided to conduct a new series of seven additional longer-term refinancing operations (maturing at the third quarter of 2021) called pandemic emergency longer-term refinancing operations (PELTROs). These operations provide further liquidity support after the expiry of the bridge longer-term refinancing operations (LTROs) that have been conducted since March 2020. In 2020, Latvijas Banka granted loans in the amount of 1 260 000 thousand euro to Latvian credit institutions at TLTRO III auctions and received 12 250 thousand euro as repayment of loans granted to credit institutions. At the end of 2020, the balance of the TLTROs conducted by Latvijas Banka stood at 1 260 000 thousand euro; these operations will mature in 2023 (at the end of 2019, the balance was 12 250 thousand euro).

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

Other claims on euro area credit institutions denominated in euro mostly include Latvijas Banka's demand deposits in euro with euro area credit institutions (120 thousand euro at the end of 2020; 8 thousand euro at the end of 2019).

12. SECURITIES OF EURO AREA RESIDENTS DENOMINATED IN EURO

At the end of 2020, the amount of securities held by the Eurosystem for monetary policy purposes totalled 3695 billion euro (2632 billion euro at the end of 2019). Of them, Latvijas Banka held 10 008 million euro (7636 million euro at the end of 2019). Pursuant to the Statute of the ESCB and of the ECB, any income and losses, if any materialise, are allocated among euro area NCBs in proportion to their share in the ECB's capital, except any risks associated with the purchases of government securities carried out by Latvijas Banka and other euro area NCBs under the PSPP and PEPP. Of the total amount of securities held by the Eurosystem for monetary policy purposes, at the end of 2020, the amount of government securities purchased by the euro area NCBs under the PSPP totalled 1872 billion euro (1681 billion euro at the end of 2019); of them, Latvijas Banka held Latvian government securities in the amount of 1848 million euro (1448 million euro at the end of 2019). At the end of 2020, the amount of government securities purchased by the euro area NCBs under the PEPP totalled 586 913 million euro (0 euro at the end of 2019); of them, the amount of Latvian government securities held by Latvijas Banka was 749 million euro.

Between the end of 2018 and October 2019, only the principal payments from the purchased and matured securities were fully reinvested. As of 1 November 2019, the Governing Council of the ECB decided to restart its net purchases of securities under the APP at a monthly pace of 20 billion euro. In March 2020, the Governing Council of the ECB made a decision on additional temporary net asset purchases in the amount of 120 billion euro until the end of 2020. The Governing Council of the ECB expects them to run for as long as necessary to reinforce the accommodative impact of its monetary policy rates, and to end shortly before the ECB starts raising the key ECB interest rates. In response to the COVID-19 pandemic and the related potential risks to the monetary policy transmission mechanism and the euro area economic outlook, in March 2020, the Governing Council of the ECB launched a new asset purchase programme, the PEPP, with an overall envelope of 750 billion euro. In June and December 2020, the Governing Council of the ECB decided to increase the initial PEPP envelope by 600 billion euro and 500 billion euro respectively; thus, the total PEPP envelope reached 1850 billion euro at the end of 2020. The purchase period of the net assets was also extended to at least March 2022 or until the crisis caused by the COVID-19 pandemic is over.

Securities held for monetary policy purposes and securities held to maturity are measured at amortised cost subject to impairment. The comparison of the book value and fair value of the above securities is represented in Note 5. Other securities are accounted for at fair value.

(in thousands of euro)		
	Book value	
	2020	2019
Securities held for monetary policy purposes	10 008 456	7 636 472
Latvian government securities	2 596 791	1 447 653
PSPP government securities	1 848 233	1 447 653
PEPP government securities	748 558	0
Debt securities issued by international institutions	7 411 665	6 188 819
PSPP debt securities issued by international institutions	6 469 341	6 118 819
PEPP debt securities issued by international institutions	942 324	0
Other securities	1 120 984	1 084 665
Securities not held to maturity	952 811	916 566
Securities held to maturity	168 173	168 099
Total	11 129 440	8 721 137

13. INTRA-EUROSISTEM CLAIMS/LIABILITIES (–)

(in thousands of euro)			
	Note	2020	2019
Participating interest in the European Central Bank	13.1	114 095	114 108
Claims in respect of foreign reserves transferred to the European Central Bank	13.2	157 202	158 264
Claims related to the allocation of banknotes in the Eurosystem	13.4	5 397 767	4 999 497
Claims related to other operational requirements within the Eurosystem	13.5	4 910	5 614
Total intra-Eurosystem claims		5 673 974	5 277 483
Liabilities related to TARGET2 and national central bank correspondent accounts (net)	13.3	–4 809 553	–3 826 452
Other liabilities within the Eurosystem	13.5	–28 060	–7 088
Total intra-Eurosystem liabilities		–4 837 613	–3 833 540
Intra-Eurosystem claims/liabilities (–) (net)		836 361	1 443 943

13.1 PARTICIPATING INTEREST IN THE EUROPEAN CENTRAL BANK

With Latvia's accession to the EU, Latvijas Banka became a subscriber to the capital of the ECB. In accordance with the Statute of the ESCB and of the ECB, the weighting assigned to Latvijas Banka in the ECB capital subscription key is calculated on the basis of the share of Latvia's population and gross domestic product in the EU. The weightings assigned to the NCBs in the ECB's capital subscription key are adjusted every five years or at shorter intervals depending on changes in the number of the EU NCBs that contribute to the ECB's capital. Since 1 January 2014, Latvijas Banka's weighting in the ECB's capital key was 0.2821%, equivalent to 30 537 thousand euro; however, on 1 January 2019, the weightings of the NCBs in the ECB's capital subscription key were adjusted, therefore Latvijas Banka's weighting in the ECB capital subscription key slightly decreased to 0.2731%, equivalent to 29 563 thousand euro. As a result of the departure of the United Kingdom from the European Union and the subsequent withdrawal of the Bank of England from the ESCB, the weightings assigned to the remaining NCBs in the key for subscription to the ECB's capital were adjusted in 2020. The Bank of England's share in the ECB's subscribed capital (14.3374%) was reallocated among other NCBs; hence the capital key of Latvijas Banka increased from 0.2731% to 0.3169%, equivalent to 34 304 thousand euro.

The Statute of the ESCB and of the ECB stipulates that a euro area NCB shall pay up its subscribed share in the ECB's capital in full, as well as contribute to the ECB's reserve capital, to those provisions equivalent to reserves and to the revaluation account for financial instruments in proportion to its share in the ECB's capital. After Latvijas Banka's weighting in the ECB capital subscription key changed in 2020, and in line with the decisions of the Governing Council of the ECB regarding the paying up of the ECB's capital following the withdrawal of the United Kingdom from the EU, the paid-up share in the ECB's capital decreased by 13 thousand euro, and claims equivalent to the transfer of foreign reserves to the ECB shrank by 1062 thousand euro (see also Note 13.2). At the end of 2020, the participating interest in the ECB consisted of the paid-up shares in the amount of 29 550 thousand euro in the ECB's capital, transfers to the financial instrument revaluation account amounted to 42 752 thousand euro and the difference between the market value of the foreign reserves transferred to the ECB and the value of the corresponding euro-denominated claim amounted to 41 793 thousand euro (see also Note 13.2).

The 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.

	(in thousands of euro)	
	2020	2019
Total amount of the European Central Bank's subscribed capital	10 825 007	10 825 007
The subscribed share of Latvijas Banka in the European Central Bank's capital	34 304	29 563
The paid-up share of Latvijas Banka in the European Central Bank's capital	29 550	29 563
The percentage share of Latvijas Banka in the European Central Bank's capital (capital key; %)	0.3169	0.2731

At the end of 2020 and 2019, the percentage shares of NCBs in the ECB's capital (capital key) were as follows:

	(%)	
	2020	2019
Nationale Bank van België/Banque Nationale de Belgique	2.9630	2.5280
Deutsche Bundesbank	21.4394	18.3670
Eesti Pank	0.2291	0.1968
Banc Ceannais na hÉireann/Central Bank of Ireland	1.3772	1.1754
Bank of Greece	2.0117	1.7292
Banco de España	9.6981	8.3391
Banque de France	16.6108	14.2061
Banca d'Italia	13.8165	11.8023
Central Bank of Cyprus	0.1750	0.1503
Latvijas Banka	0.3169	0.2731
Lietuvos bankas	0.4707	0.4059
Banque centrale du Luxembourg	0.2679	0.2270
Bank Ċentrali ta' Malta/Central Bank of Malta	0.0853	0.0732
De Nederlandsche Bank	4.7662	4.0677
Oesterreichische Nationalbank	2.3804	2.0325
Banco de Portugal	1.9035	1.6367
Banka Slovenije	0.3916	0.3361
Národná banka Slovenska	0.9314	0.8004
Suomen Pankki – Finlands Bank	1.4939	1.2708
Subtotal for euro area NCBs	81.3286	69.6176
Българска народна банка (Bulgarian National Bank)	0.9832	0.8511
Česká národní banka	1.8794	1.6172
Danmarks Nationalbank	1.7591	1.4986
Hrvatska narodna banka	0.6595	0.5673
Magyar Nemzeti Bank	1.5488	1.3348
Narodowy Bank Polski	6.0335	5.2068
Banca Națională a României	2.8289	2.4470
Sveriges Riksbank	2.9790	2.5222
Bank of England	0.0000	14.3374
Subtotal for non-euro area NCBs	18.6714	30.3824
Total	100.0000	100.0000

In 2020, the subscribed capital of the ECB remained unchanged at 10 825 million euro; therefore, the share of Latvijas Banka in the ECB's subscribed capital increased by 4741 thousand euro, to 34 304 thousand euro. When the Bank of England left the ESCB, the total amount of the ECB's capital to be paid up increased by 1221 million euro due to the overall increase in the weightings of the euro area NCBs (with fully paid-up subscription) in the ECB's subscribed capital and the equivalent decrease in the weightings of non-euro area NCBs (which have only paid up 3.75% of their subscriptions) in the ECB's subscribed capital. The Governing Council of the ECB decided that the euro area NCBs would pay up in full their increased subscriptions in two instalments: at the end of 2021 and 2022 respectively.

The subscribed and paid-up NCB shares in the ECB's capital at the end of 2020 and 2019 were as follows:

(in thousands of euro)

	Subscribed capital		Paid-up capital	
	2020	2019	2020	2019
Nationale Bank van België/ Banque Nationale de Belgique	320 745	273 656	276 291	273 656
Deutsche Bundesbank	2 320 817	1 988 229	1 999 160	1 988 229
Eesti Pank	24 800	21 304	21 363	21 304
Banc Ceannais na hÉireann/Central Bank of Ireland	149 082	127 237	128 420	127 237
Bank of Greece	217 767	187 186	187 585	187 186
Banco de España	1 049 820	902 708	904 319	902 708
Banque de France	1 798 120	1 537 811	1 548 908	1 537 811
Banca d'Italia	1 495 637	1 277 600	1 288 347	1 277 600
Central Bank of Cyprus	18 944	16 270	16 318	16 270
Latvijas Banka	34 304	29 563	29 550	29 563
Lietuvos bankas	50 953	43 939	43 891	43 939
Banque centrale du Luxembourg	29 000	24 573	24 981	24 573
Bank Ċentrali ta' Malta/Central Bank of Malta	9 234	7 924	7 954	7 924
De Nederlandsche Bank	515 941	440 329	444 434	440 329
Oesterreichische Nationalbank	257 678	220 018	221 965	220 018
Banco de Portugal	206 054	177 173	177 496	177 173
Banka Slovenije	42 391	36 383	36 516	36 383
Národná banka Slovenska	100 824	86 643	86 850	86 643
Suomen Pankki – Finlands Bank	161 715	137 564	139 302	137 564
Subtotal for euro area NCBs	8 803 827	7 536 110	7 583 649	7 536 110
Българска народна банка (Bulgarian National Bank)	106 431	92 132	3 991	3 455
Česká národní banka	203 445	175 062	7 629	6 565
Danmarks Nationalbank	190 423	162 224	7 141	6 083
Hrvatska narodna banka	71 391	61 410	2 677	2 303
Magyar Nemzeti Bank	167 658	144 492	6 287	5 418
Narodowy Bank Polski	653 127	563 636	24 492	21 136
Banca Națională a României	306 229	264 888	11 484	9 933
Sveriges Riksbank	322 477	273 028	12 093	10 239
Bank of England	0	1 552 025	0	58 201
Subtotal for non-euro area NCBs	2 021 182	3 288 897	75 794	123 334
Total ¹	10 825 007	10 825 007	7 659 444	7 659 444

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

Pursuant to the Statute of the ESCB and of 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 capital key weighting of each euro area NCB in the ECB's capital. For the foreign reserves transferred to the ECB,

¹ The total amount and the sum of the components may differ due to rounding.

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. After Latvijas Banka's weighting in the ECB's capital subscription key changed in 2020, this claim decreased to the amount of 157 202 thousand euro. 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). The interest rate on the main refinancing operations set by the ECB is applied to the claims equivalent to the transfer of foreign reserves to the ECB (see also Note 33).

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

TARGET2 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 central bank money. The above settlements result in bilateral claims and liabilities in the TARGET2 accounts held by NCBs. 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 2020, the 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 Latvijas Banka.

The interest rate on the main refinancing operations set by the ECB is applied to the above claims and liabilities.

13.4 CLAIMS RELATED TO THE ALLOCATION OF BANKNOTES WITHIN THE EUROSISTEM

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. Of the total amount of euro banknotes issued, the share allocated to Latvijas Banka is larger than the net 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".

13.5 CLAIMS/LIABILITIES RELATED TO OTHER OPERATIONAL REQUIREMENTS WITHIN THE EUROSISTEM

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 the ECB's interim profit distribution.

Monetary income to be pooled by Latvijas Banka in 2020 was higher than monetary income to be received. This resulted in a liability to the ECB associated with the net result of pooling of monetary income, standing at 28 060 thousand euro at the end of 2020 (7088 thousand euro claim at the end of 2019; see also Notes 2.27 and 38).

Claims for the ECB's interim profit distribution in the amount of 4910 thousand euro are set as per Latvijas Banka's percentage share in the ECB's capital (5614 thousand euro at the end of 2019; see also Notes 2.26 and 37).

14. OTHER ASSETS

(in thousands of euro)

	Note	2020	2019
Accrued interest on securities held for monetary policy purposes		73 795	66 999
Participating interest in the Bank for International Settlements	14.2	35 960	34 341
OTC financial derivative contracts	24	34 169	32 492
Fixed assets	14.1	33 590	35 319
Claims on collateral for the use of the instant payment service	17	26 306	11 581
Accrued interest on other securities		18 196	20 146
Intangible assets	14.1	2 160	2 263
Other accrued income		2 660	1 491
Prepaid expenses		1 030	951
Other		574	479
Total		228 440	206 062

14.1 FIXED ASSETS AND INTANGIBLE ASSETS

(in thousands of euro)

	Buildings, improvement of territory, and land	Furniture and office equipment	Computer and telecom- munication equipment	Cash processing and storage equipment	Transport vehicles	Other fixed assets	Total
As at 31 December 2018							
Cost	61 349	6 315	4 595	7 046	9 910	89 215	7 800
Accumulated depreciation/amortisation	-30 871	-4 098	-3 472	-5 684	-7 300	-51 425	-5 394
Net book value	30 478	2 217	1 123	1 362	2 610	37 790	2 406
During 2019							
Additions	616	35	431	1 540	202	2 824	387
Change in classification	-3	-	-	-	3	-	-
Disposals and write-offs	-3 664	-119	-259	-3 253	-285	-7 580	-77
Net change in cost	-3 051	-84	172	-1 713	-80	-4 756	310
Depreciation/amortisation charge	-1 982	-264	-564	-310	-479	-3 599	-530
Change in classification	3	-	-	-	-3	-	-
Accumulated depreciation/amortisation on disposals and write-offs	2 269	116	258	2 963	278	5 884	77
Net change in accumulated depreciation/ amortisation	290	-148	-306	2 653	-204	2 285	-453
As at 31 December 2019							
Cost	58 298	6 231	4 767	5 333	9 830	84 459	8 110
Accumulated depreciation/amortisation	-30 581	-4 246	-3 778	-3 031	-7 504	-49 140	-5 847
Net book value	27 717	1 985	989	2 302	2 326	35 319	2 263
During 2020							
Additions	346	48	430	673	165	1 662	457
Change in classification	-1	-6	6	-	-24	-25	25
Disposals and write-offs	-	-146	-154	-86	-1 483	-1 869	-
Net change in cost	345	-104	282	587	-1 342	-232	482

(cont.)

(in thousands of euro)

	Buildings, improvement of territory, and land	Furniture and office equipment	Computer and telecom- munication equipment	Cash processing and storage equipment	Transport vehicles	Other fixed assets	Total
Depreciation/amortisation charge	-1 917	-252	-444	-251	-427	-3 291	-560
Change in classification	1	6	-6	-	24	25	-25
Accumulated depreciation/amortisation on disposals and write-offs	-	144	153	86	1 386	1 769	-
Net change in accumulated depreciation/ amortisation	-1 916	-102	-297	-165	983	-1 497	-585
As at 31 December 2020							
Cost	58 643	6 127	5 049	5 920	8 488	84 227	8 592
Accumulated depreciation/amortisation	-32 497	-4 348	-4 075	-3 196	-6 521	-50 637	-6 432
Net book value	26 146	1 779	974	2 724	1 967	33 590	2 160

At the end of 2020, Latvijas Banka's contractual commitments related to acquisition of fixed assets were 24 thousand euro (11 thousand euro at the end of 2019).

14.2 PARTICIPATING INTEREST IN THE BANK FOR INTERNATIONAL SETTLEMENTS

At the end of 2020 and 2019, Latvijas Banka owned 1070 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 SDR 5350 thousand (the nominal value per share is SDR 5 thousand), paid up in the amount of SDR 1338 thousand or 25% (see also Note 46). At the end of 2020 and 2019, 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, 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 published financial statements of the BIS. The BIS applied this valuation method for calculating the issue price of its shares; the International Court of Justice 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 2020, the estimated fair value of BIS shares was 35 960 thousand euro (34 341 thousand euro at the end of 2019).

15. BANKNOTES IN CIRCULATION

(in thousands of euro)

	2020	2019
Euro banknotes	5 142 726	4 666 799
Net issuance of euro banknotes by Latvijas Banka	-255 041	-332 698
Adjustment for banknote allocation in the Eurosystem	5 397 767	4 99 497
Total	5 142 726	4 666 799

The euro coins issued by Latvijas Banka are reported under the balance sheet item "Other liabilities" (see also Note 22).

Cross-border flows of euro banknotes in 2020 decreased, reducing the difference between the amount of banknotes deposited with Latvijas Banka and the amount of banknotes withdrawn from Latvijas Banka; consequently, the negative net issuance of euro banknotes by Latvijas Banka reached 255 041 thousand euro. At the end of 2020, the total amount of euro banknotes in circulation in the Eurosystem grew to 1435 billion euro (1293 billion

euro at the end of 2019); as a result, an increase in the adjustment for banknote allocation in the Eurosystem was reported on the balance sheet of Latvijas Banka.

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. The latest available interest rate used by the Eurosystem in its tenders for main refinancing operations is applied to the balances held on those accounts within the framework of the reserve requirements. Since June 2014, the lower rate of either 0% or the ECB's deposit facility rate has been applied to the reserves held in excess of the minimum requirements. On 12 September 2019, the Governing Council of the ECB decided to introduce a two-tier system for reserve remuneration, which exempts part of credit institutions' excess liquidity holdings (i.e. reserve holdings in excess of minimum reserve requirements) from the negative remuneration rate applicable on the deposit facility.

At the end of 2020, the balance on the current accounts with Latvijas Banka was 6 053 812 thousand euro (5 660 676 thousand euro at the end of 2019), including the minimum reserves in the amount of 168 154 thousand euro (156 304 thousand euro at the end of 2019).

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. No such deposits were placed with Latvijas Banka at the end of 2020 and 2019.

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

	(in thousands of euro)	
	2020	2019
Liabilities for repurchase agreements	551 537	–
Collateral received for the use of the instant payment service	26 209	11 871
Total	577 746	11 871

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).

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

Liabilities to other financial institutions mostly comprise funds received under repurchase agreements concluded in 2020.

	(in thousands of euro)	
	2020	2019
Other financial institutions	237 744	306 195
International Monetary Fund	983	1 035
European Commission	9	9
Total	238 737	307 239

20. LIABILITIES TO EURO AREA RESIDENTS DENOMINATED IN FOREIGN CURRENCY

	(in thousands of euro)	
	2020	2019
Liabilities for repurchase agreements	472 636	–
Demand deposits of the Latvian government	143 350	153 351
Total	615 986	153 351

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

	(in thousands of euro)	
	2020	2019
Liabilities for repurchase agreements	1 042 015	1 363 337
Liabilities for gold swap arrangements	321 995	279 031
Total	1 364 010	1 642 368

22. OTHER LIABILITIES

		(in thousands of euro)	
	Note	2020	2019
Provisions for market risk and credit risk	36	281 723	203 900
Euro coins in circulation	22.1	79 690	79 496
Lats banknotes in circulation	22.1	22 584	23 719
Accrued expense and similar liabilities		13 637	9 805
OTC financial derivative contracts and spot exchange rate contracts	24	7 479	7 837
Lats coins in circulation	22.1	2 750	2 855
Tax liabilities	22.2	19	13
Other		1 818	1 701
Total		409 700	329 326

22.1 BANKNOTES AND COINS IN CIRCULATION

Apart from the lats and euro circulation coins issued by Latvijas Banka and recognised on the balance sheet, euro collector coins, lats collector coins and precious metal circulation coins were also in circulation with the total nominal value of 7034 thousand euro at the end of 2020 (6960 thousand euro at the end of 2019). The above coins in circulation have not been reported under the balance sheet item "Other liabilities" (see also Notes 2.21 and 46).

Issued lats banknotes and coins with a low probability of exchange in the amount of 95 600 thousand euro, including lats banknotes in the amount of 35 791 thousand euro and lats coins in the amount of 59 809 thousand euro at the end of 2019) have not been reported as a liability on the balance sheet at the end of 2020 and 2019 (see also Note 46).

22.2 TAX LIABILITIES

At the end of 2020 and 2019, tax liabilities of Latvijas Banka were as follows:

	(in thousands of euro)						
	Personal income tax	State compulsory social security contributions and ST (by employer)	State compulsory social security contributions and ST (by employee)	Tax on real estate	Value added tax	Other taxes and duties	Total
Liabilities as at 31 December 2018	–	–	–	–	65	1	66
During 2019							
Calculated	3 076	3 941	1 843	225	1 349	1	10 435
Increase in deferred liabilities	–	101	–	–	–	–	101
Paid	–3 076	–4 042	–1 843	–225	–1 401	–2	–10 589
Liabilities as at 31 December 2019	–	–	–	–	13	–	13
During 2020							
Calculated	2 999	3 764	1 790	220	1 156	3	9 932
Increase in deferred liabilities	–	40	–	–	–	–	40
Paid	–2 999	–3 802	–1 789	–220	–1 154	–2	–9 966
Liabilities as at 31 December 2020	–	2	1	–	15	1	19

In addition to the tax payments indicated herein, in 2020, Latvijas Banka transferred to the state budget 70% of the profit for the previous year (19 009 thousand euro in 2020; 10 196 thousand euro in 2019; 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	Revaluation account	Profit for the year	Capital and reserves
As at 31 December 2018	100 000	236 363	99 439	14 566	450 368
During 2019					
Net result of revaluation, realisation, and revaluation result recognition in profit and loss statement	x	x	166 303	x	166 303
Profit appropriated to the state budget	x	x	x	–10 196	–10 196
Profit transferred to the reserve capital	x	4 370	x	–4 370	–
Profit for the year	x	x	x	27 155	27 155
As at 31 December 2019	100 000	240 733	265 742	27 155	633 630
During 2020					
Net result of revaluation, realisation, and revaluation result recognition in profit and loss statement	x	x	152 131	x	152 131
Profit appropriated to the state budget	x	x	x	–19 009	–19 009
Profit transferred to the reserve capital	x	8 146	x	–8 146	–
Profit for the year	x	x	x	26 646	26 646
As at 31 December 2020	100 000	248 879	417 873	26 646	793 398

The capital and reserves of Latvijas Banka comprises the nominal capital, reserve capital and the revaluation account, as well as the undistributed profit for the reporting year.

The legal framework 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 of the ECB and the Law on Latvijas Banka. The implementation of the monetary policy as well as exposure to 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 has historically been comprised of the state-allotted resources, transfers from the reserve capital and Latvijas Banka's profit allocations.

The Law on Latvijas Banka establishes that a part of Latvijas Banka's profit for the reporting year, calculated by applying the same percentage as the corporate income tax rate set by the Law on Corporate Income Tax, together with a payment in the amount of 50% of the profit for the reporting year for the usage of state capital shall be transferred to the state budget. Furthermore, 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 2020 and 2019, the corporate income tax rate was 20%. Therefore, unless the Council of Latvijas Banka decides otherwise, 70% of Latvijas Banka's profit for the reporting year or 18 652 thousand euro shall be transferred to the state budget within 15 days following the approval of the Annual Report of 2020 by the Council of Latvijas Banka.

After making the above deductions, the remaining profit of Latvijas Banka 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 revaluation 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 item "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 2020 and 2019, the changes in the revaluation account were as follows:

(in thousands of euro)

	2020	Recognition in profit and loss statement	Revaluation	Realisation	2019
Revaluation reserve for participating interest	33 451	–	1 619	–	31 832
Result on revaluation of foreign currencies and gold	131 683	28 642	11 622	–	91 419
Result on revaluation of interest rate swap arrangements	–	296	–296	–62	62
Result on revaluation of securities	252 739	6 299	128 005	–23 994	142 429
Total	417 873	35 237	140 950	–24 056	265 742

	2019	Recognition in profit and loss statement	Revaluation	Realisation	2018
Initial revaluation account	–	x	x	–2 859	2 859
Revaluation reserve for participating interest	31 832	–	3 020	–	28 812
Result on revaluation of foreign currencies and gold	91 419	145	45 994	–	45 280
Result on revaluation of interest rate swap arrangements	62	431	–369	–	–
Result on revaluation of securities	142 429	3 280	120 788	–4 127	22 488
Total	265 742	3 856	169 433	–6 986	99 439

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 revaluation account. The initial revaluation 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 revaluation 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 revaluation 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. In 2019, the above six-year transition period following the date Latvijas Banka joined the Eurosystem expired.

The revaluation reserve for participating interest has been established to account for the result on revaluation of the BIS shares. The result on revaluation of the BIS shares is not recognised in the profit and loss statement.

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, forward transactions in securities, and interest rate and currency future contracts in order to manage interest rate and currency risks associated with Latvijas Banka's investments. At the end of 2020 and 2019, the contract or notional amounts and book value of the above transactions were as follows:

	Contract or notional amount		Assets		Book value	
	2020	2019	2020	2019	2020	2019
OTC financial derivative and spot exchange rate contracts						
Forward exchange rate contracts and currency swap arrangements	2 487 071	2 524 378	31 971	31 570	5 004	6 477
Spot exchange rate contracts	409 272	396 631	–	–	1 354	444
Forward transactions in securities	1 186 202	788 442	2 197	843	812	304
Interest rate swap arrangements	24 366	36 229	1	79	309	612
Total	x	x	34 169	32 492	7 479	7 837
Derivative OTC gold swap arrangements	321 995	279 031	330 139	289 043	322 104	279 419
Traded financial derivative contracts						
Interest rate future contracts	912 276	1 374 836	x	x	x	x
Currency future contracts	100 000	100 000	x	x	x	x

The book value of the OTC financial derivative contracts and spot exchange rate contracts is reported under the balance sheet items "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 item.

To reduce the costs for hedging currency risks and increase return on financial investments, Latvijas Banka engages in gold swap arrangements (see also Notes 6 and 21).

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. Latvijas Banka's risk management is organised and implemented according to the Risk Management Policy of Latvijas Banka approved by the Council of Latvijas Banka.

Risk management at Latvijas Banka is carried out as part of a systemic process that includes identifying, analysing and assessing risks, developing and implementing relevant risk mitigating measures, and overseeing and reviewing risks on a regular basis. This allows to identify in advance, assess and efficiently manage risks that are likely to have a negative effect on Latvijas Banka's financial position and financial performance, and on Latvijas Banka's capability to perform in a quality and efficient manner the tasks set out in the legislation, including participation in the implementation of the ESCB functions.

The risk management process is organised in compliance with the international principles of best practice in risk management, in view of the aims and tasks of Latvijas Banka and the external environment developments, as well as in compliance with the requirements of the ECB.

25.1 FINANCIAL RISKS

Market risk (price, interest rate and currency risks), credit risk and liquidity risk are the most significant financial risks Latvijas Banka is exposed to in its daily activities. Financial risks are managed to mitigate a potential negative impact on Latvijas Banka's financial position and financial performance that might arise from adverse changes in financial market factors or a counterparty default. When managing financial risks, acceptable types of risks and their parameters are taken into consideration to preserve the value of investments ensuring the required liquidity and income earning in the long term.

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 the investment policy are described in Note 4. Investments are managed by classifying them into different investment portfolios. The parameters for a benchmark reflecting the acceptable level of financial risks and expected return are set out for each financial instrument portfolio. The Risk Management Division of the Market Operations Department monitors the compliance of investments with the established requirements and in case of any departure from the provisions of the Procedure duly notifies the Council and the Board of Latvijas Banka.

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 the developments in financial markets prepared by financial investment portfolio managers, receives and reviews reports by financial risk managers, and approves the investment management tactical decisions for the forthcoming week. The Market Operations Department informs the Council and the Board of Latvijas Banka about the results of investment management on a regular basis.

Latvijas Banka purchases assets under the PSPP and PEPP in accordance with the decisions of the Governing Council of the ECB. Latvijas Banka makes the purchases and manages financial risks in line with the guidelines of the Governing Council of the ECB and the procedure adopted by the Board of Latvijas Banka. Financial risks arising from the implementation of monetary policy are shared among the euro area NCBs in proportion to their shares in the ECB's capital, except risks associated with the purchases of Latvian government securities carried out by Latvijas Banka under the PSPP.

25.1.1 MARKET RISK

Market risk is the exposure to losses due to adverse changes in financial markets.

Latvijas Banka is exposed to interest rate risk due to investing in foreign debt securities and interest rate derivatives that are subject to interest rate fluctuations and have been purchased within the course of investment management. Latvijas Banka manages interest rate risk by using the effective duration and deviation limits set individually for each investment portfolio.

Latvijas Banka's exposure to currency risk is determined by its investment structure. Latvijas Banka manages currency risk by establishing that the benchmark currency is the euro, thus hedging the currency risk (except for the gold portfolio and the equity securities portfolio, where investments are made in the stock denomination currencies of the respective equity securities index), and using tracking error limits in relation to the respective benchmark. 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 risk of 1–10 year fixed income securities portfolios, mortgage-backed securities portfolios, and the equity securities portfolio (see Note 4) is managed by determining the tracking error limit. The tracking error in 2020 and 2019 is disclosed in Note 28.

The equity securities portfolio is exposed to the market price risk (the risk that the value of an investment might decrease due to price changes). As the equity securities portfolio is highly diversified, it is mostly exposed to the risk of systematic share price movements.

For investment portfolios, except for the portfolio of borrowed funds, the equity securities portfolio, and the gold portfolio, the benchmark currency is the euro. For the portfolio 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 set 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 effective duration, tracking error, and open currency positions with the Procedure adopted by the Council of Latvijas Banka and the related resolutions passed by the Investment Committee of Latvijas Banka.

Latvijas Banka's exposure to market risk (as at the end of 2020 and 2019) is disclosed in Notes 26–28.

25.1.2 CREDIT RISK

Credit risk is the exposure to losses resulting from a counterparty default. Latvijas Banka's exposure to credit risk results mainly from investments in foreign financial instruments and from monetary policy operations. Pursuant to the Statute of the ESCB and of the ECB, the risks associated with the implementation of monetary policy (if any materialise) are shared among the euro area NCBs in proportion to their share in the ECB's capital, except for the risks associated with the purchases of Latvian government securities carried out by Latvijas Banka under the PSPP.

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, Standard & Poor's, and DBRS. 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. To hedge the credit risk associated with the counterparties of repurchase agreements and reverse repurchase agreements, Latvijas Banka and the respective counterparties enter into Global Master Repurchase Agreements of Securities Industry and Financial Markets Association (SIFMA) and International Capital Market Association (ICMA), whereas the external managers of mortgage-backed securities portfolios 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 the compliance with the Procedure adopted by the Council of Latvijas Banka.

In 2020 and 2019, loans granted to credit institutions in monetary policy operations were secured by securities collateral in compliance with the ECB requirements. The Market Operations Department monitors the adequacy of collateral of the respective loans and its eligibility and compliance with the ECB's requirements on a regular basis, as well as maintains a list of securities eligible for monetary policy operations issued and held in the Republic of Latvia.

Latvijas Banka's exposure to market risk (as at the end of 2020 and 2019) is disclosed in Notes 30–32.

25.1.3 LIQUIDITY RISK

Liquidity risk is associated with a failure to dispose of investments in a short time and at a competitive market price. Since Latvia joined the euro area, the need for liquidity and the risk associated with a failure to meet liabilities in a timely manner have considerably decreased. In compliance with its investment strategy, Latvijas Banka manages liquidity risk by investing a certain amount of its investments in liquid debt securities issued by international institutions, foreign governments and the corporate sector, in short-term

deposits with foreign financial institutions and in other financial instruments. The liquidity structure of Latvijas Banka's assets and liabilities as at the end of 2020 and 2019 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 risks are managed to ensure that processes are implemented in a continuous, adequate and safe manner and that the processes and projects are completed efficiently and to a high standard in order to mitigate any potential negative impact on Latvijas Banka's financial performance, financial position, reputation or capability to accomplish its tasks. Such impact could be triggered by inadequate or defective performance of Latvijas Banka's processes, an act or omission by an employee or unavailability of staff, as well as by inadequate operation or unavailability of Latvijas Banka's information systems, information systems infrastructure or other infrastructure, or by external events.

Latvijas Banka's operational risks are managed under a uniform operational risk management framework, with the major operational risks being compliance risks (inter alia in preventing conflicts of interest, anti-corruption control, personal data protection, prevention of money laundering and terrorism financing, and ensuring workplace environment protection), risks related to business continuity, physical security, information security and information systems (including cyber security).

Latvijas Banka's operational risks are managed through processes and projects by classifying the processes and risks, evaluating the impact of risks on the results of the processes or projects and, depending on the risk classification, defining and implementing the most appropriate actions to ensure adequate risk management. The Operational Risk Management Department is in charge of maintaining a common operational risk management framework, organising incident management as well as providing regular information on operational risk management pursuant to the legal acts of Latvijas Banka. The improved risk management process is based on the best practice in the field of risk management and concentrates the resources allocated to operational risk management, thereby increasing the effectiveness of this management model. In 2020, operational risk management was overseen by the Security Oversight Commission of Latvijas Banka.

Compliance risks are managed to ensure the compliance of Latvijas Banka's operation with legislative acts.

The risks related to Latvijas Banka's business continuity are managed to mitigate a potential negative impact on the execution of critical processes, where their discontinuity may cause negative consequences for the Latvian financial system or adversely affect the implementation of Latvijas Banka's tasks. The risks are managed, inter alia, by ensuring efficient incident management and the continuity or recovery of the critical processes as soon as possible and to a full extent in the event of a disruption or failure.

Risks related to physical security, inter alia, risks associated with fire safety and civil protection are managed to mitigate a potential negative impact on the physical security of persons, the premises of Latvijas Banka, the transportation of its valuables and the events organised by Latvijas Banka, with a priority focus on protecting the life and health of individuals.

Risks related to information security are managed to prevent unauthorised disclosure or use of confidential information, classifying it by its degree of confidentiality and ensuring appropriate protection, at the same time taking care that the protective measures do not prevent Latvijas Banka from providing non-classified information to its cooperation partners and general public.

Risks related to information systems, including cyber security risks are managed to prevent a potential negative impact on the availability, security and integrity of the information systems and infrastructure of Latvijas Banka. Information systems at Latvijas Banka are classified based on their importance for implementing Latvijas Banka's tasks and on the basis of the confidentiality, integrity and availability requirements for the data to be processed, establishing appropriate physical and logical protection for each level of classification.

Latvijas Banka ensures risk management training for its employees, inter alia, to maintain appropriate level of their know-how and skills, and conducts, on a regular basis, training sessions and tests in risk management for employees.

As part of the framework for operational risk mitigation measures, Latvijas Banka is insured against a possible impact of certain types of operational risks.

In 2020, the main focus of operational risk management was on managing risks related to the COVID 19 pandemic and remote working. Operational risks were appropriately managed in 2020, and the risk mitigation measures limit those risks to acceptable levels.

26. CURRENCY STRUCTURE

(in thousands of euro)

	EUR	USD	CAD	GBP	Gold	Other	Total
As at 31 December 2020							
Total assets	18 443 448	3 400 387	367 842	348 093	330 139	155 833	23 045 742
Total liabilities	21 108 390	1 445 139	337 486	127 662	–	27 065	23 045 742
Net position on balance sheet	–2 664 942	1 955 248	30 356	220 431	330 139	128 768	0
Net position on financial instruments' off-balance sheet accounts	1 842 451	–1 575 561	–10 287	–195 983	–	–33 930	26 690
Net position on balance sheet and off-balance sheet accounts	–822 491	379 687	20 069	24 448	330 139	94 838	26 690
Net position on balance sheet and off-balance sheet accounts to total assets (%)	–3.5	1.6	0.1	0.1	1.4	0.4	0.1
As at 31 December 2019							
Total assets	14 338 668	3 264 840	386 768	360 716	289 043	105 474	18 745 509
Total liabilities	16 986 997	1 274 718	346 416	109 526	–	27 852	18 745 509
Net position on balance sheet	–2 648 329	1 990 122	40 352	251 190	289 043	77 622	0
Net position on financial instruments' off-balance sheet accounts	2 131 383	–1 811 033	–28 960	–235 321	–	–31 414	24 655
Net position on balance sheet and off-balance sheet accounts	–516 946	179 089	11 392	15 869	289 043	46 208	24 655
Net position on balance sheet and off-balance sheet accounts to total assets (%)	–2.8	1.0	0.1	0.1	1.5	0.2	0.1

27. REPRICING MATURITY

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

	(in thousands of euro)						
	Up to 3 months	3–12 months	1–3 years	3–5 years	Over 5 years	Non-interest bearing items	Total
As at 31 December 2020							
Gold and gold receivables	–	–	–	–	–	330 139	330 139
Claims on non-euro area residents denominated in foreign currency	201 815	163 406	119 098	653 618	2 137 144	695 699	3 970 780
Claims on euro area residents denominated in foreign currency	–	–	95 974	112 328	115 143	10 261	333 706
Claims on non-euro area residents denominated in euro	–	–	205	6 908	97 408	14 622	119 143
Lending to euro area credit institutions related to monetary policy operations denominated in euro	–	–	1 260 000	–	–	–	1 260 000
Other claims on euro area credit institutions denominated in euro	–	–	–	–	–	120	120
Securities of euro area residents denominated in euro	–	–	247 995	193 961	10 687 484	–	11 129 440
Intra-Eurosystem claims	–	–	–	–	–	5 673 974	5 673 974
Other assets	192	4	1 433	4 029	86 166	136 616	228 440
Total assets	202 007	163 410	1 724 705	970 844	13 123 345	6 861 431	23 045 742
Banknotes in circulation	–	–	–	–	–	5 142 726	5 142 726
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	6 053 812	–	–	–	–	–	6 053 812
Other liabilities to euro area credit institutions denominated in euro	574 869	–	–	–	–	2 877	577 746
Liabilities to other euro area residents denominated in euro	3 012 014	–	–	–	–	–	3 012 014
Liabilities to non-euro area residents denominated in euro	232 019	–	–	–	–	6 718	238 737
Liabilities to euro area residents denominated in foreign currency	615 986	–	–	–	–	–	615 986
Liabilities to non-euro area residents denominated in foreign currency	1 364 010	–	–	–	–	–	1 364 010
Intra-Eurosystem liabilities	4 809 553	–	–	–	–	28 060	4 837 613
Other liabilities	463	–	–	–	–	409 237	409 700
Capital and reserves	–	–	–	–	–	793 398	793 398
Total liabilities	16 662 726	–	–	–	–	6 383 016	23 045 742
Net position on balance sheet	–16 460 719	163 410	1 724 705	970 844	13 123 345	478 415	–
Assets on financial instruments' off-balance sheet accounts	3 464 812	16 299	417 896	4 700	789 748	–	4 693 455
Liabilities on financial instruments' off-balance sheet accounts	4 201 209	31 782	60 328	98 688	274 758	–	4 666 765
Net position on balance sheet and off-balance sheet accounts	–17 197 116	147 927	2 082 273	876 856	13 638 335	478 415	26 690

(cont.)

(in thousands of euro)

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	Up to 3 months	3–12 months	1–3 years	3–5 years	Over 5 years	Non-interest bearing items	Total
As at 31 December 2019							
Gold and gold receivables	–	–	–	–	–	289 043	289 043
Claims on non-euro area residents denominated in foreign currency	31 972	24 540	125 046	746 551	2 315 288	445 575	3 688 972
Claims on euro area residents denominated in foreign currency	–	–	148 724	158 393	148 076	5 222	460 415
Claims on non-euro area residents denominated in euro	–	–	134	6 061	78 120	5 824	90 139
Lending to euro area credit institutions related to monetary policy operations denominated in euro	–	–	–	12 250	–	–	12 250
Other claims on euro area credit institutions denominated in euro	–	–	–	–	–	8	8
Securities of euro area residents denominated in euro	–	–	–	185 186	8 535 951	–	8 721 137
Intra-Eurosystem claims	–	–	–	–	–	5 277 483	5 277 483
Other assets	146	–	1 860	5 013	79 906	119 137	206 062
Total assets	32 118	24 540	275 764	1 113 454	11 157 341	6 142 292	18 745 509
Banknotes in circulation	–	–	–	–	–	4 666 799	4 666 799
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	5 660 676	–	–	–	–	–	5 660 676
Other liabilities to euro area credit institutions denominated in euro	11 871	–	–	–	–	–	11 871
Liabilities to other euro area residents denominated in euro	1 506 709	–	–	–	–	–	1 506 709
Liabilities to non-euro area residents denominated in euro	306 204	–	–	–	–	1 035	307 239
Liabilities to euro area residents denominated in foreign currency	153 351	–	–	–	–	–	153 351
Liabilities to non-euro area residents denominated in foreign currency	1 642 368	–	–	–	–	–	1 642 368
Intra-Eurosystem liabilities	3 833 540	–	–	–	–	–	3 833 540
Other liabilities	3 016	–	–	–	–	326 310	329 326
Capital and reserves	–	–	–	–	–	633 630	633 630
Total liabilities	13 117 735	–	–	–	–	5 627 774	18 745 509
Net position on balance sheet	–13 085 617	24 540	275 764	1 113 454	11 157 341	514 518	–
Assets on financial instruments' off-balance sheet accounts	3 700 161	7 922	637 084	23 431	807 984	–	5 176 582
Liabilities on financial instruments' off-balance sheet accounts	4 495 103	130 374	93 564	101 122	331 764	–	5 151 927
Net position on balance sheet and off-balance sheet accounts	–13 880 559	–97 912	819 284	1 035 763	11 633 561	514 518	24 655

28. TRACKING ERROR

The exposure to aggregate market risk and credit risk of investments, included in the 1–10 year government fixed income securities portfolios, mortgage-backed securities portfolios and the equity securities portfolio 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 2020 and 2019, the actual (ex-post) tracking error was as follows:

	(basis points)	
	2020	2019
1–10 year fixed income securities portfolios	89	30
Mortgage-backed securities portfolios	159	75
Equity securities portfolio	17	22

The expected (ex-ante) tracking error of the equity securities portfolio does not exceed 30 basis points during the year and the compliance with this limit is monitored by the respective external manager. The expected (ex-ante) tracking error in the 1–10 year government fixed income securities portfolios and mortgage-backed securities portfolios 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	100–139	140–179
During 2020						
1–10 year fixed income securities portfolios	3 445 980	51	106	45	23	26
Mortgage-backed securities portfolios	1 211 775	49	8	146	48	–
During 2019						
1–10 year fixed income securities portfolios	3 535 151	250	–	–		
Mortgage-backed securities portfolios	1 175 059	166	84	–		

29. LIQUIDITY STRUCTURE

In the liquidity structure, 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 2020				
Assets				
Gold and gold receivables	330 139	–	–	330 139
Claims on non-euro area residents denominated in foreign currency	3 970 780	–	–	3 970 780
Claims on euro area residents denominated in foreign currency	333 706	–	–	333 706
Claims on non-euro area residents denominated in euro	119 143	–	–	119 143
Lending to euro area credit institutions related to monetary policy operations denominated in euro	–	1 260 000	–	1 260 000
Other claims on euro area credit institutions denominated in euro	120	–	–	120
Securities of euro area residents denominated in euro	10 961 267	168 173	–	11 129 440
Intra-Eurosystem claims	4 910	–	5 669 064	5 673 974
Other assets	155 126	–	73 314	228 440
Total assets	15 875 191	1 428 173	5 742 378	23 045 742

(cont.)

(in thousands of euro)

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	Up to 3 months	Over 3 months	No fixed maturity	Total
Liabilities				
Banknotes in circulation	–	–	5 142 726	5 142 726
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	6 053 812	–	–	6 053 812
Other liabilities to euro area credit institutions denominated in euro	577 746	–	–	577 746
Liabilities to other euro area residents denominated in euro	3 012 014	–	–	3 012 014
Liabilities to non-euro area residents denominated in euro	238 737	–	–	238 737
Liabilities to euro area residents denominated in foreign currency	615 986	–	–	615 986
Liabilities to non-euro area residents denominated in foreign currency	1 364 010	–	–	1 364 010
Intra-Eurosystem liabilities	4 837 613	–	–	4 837 613
Other liabilities	304 655	–	105 045	409 700
Total liabilities	17 004 573	–	5 247 771	22 252 344
Net position on balance sheet	–1 129 382	1 428 173	494 607	x
As at 31 December 2019				
Assets				
Gold and gold receivables	289 043	–	–	289 043
Claims on non-euro area residents denominated in foreign currency	3 688 972	–	–	3 688 972
Claims on euro area residents denominated in foreign currency	460 415	–	–	460 415
Claims on non-euro area residents denominated in euro	90 139	–	–	90 139
Lending to euro area credit institutions related to monetary policy operations denominated in euro	–	12 250	–	12 250
Other claims on euro area credit institutions denominated in euro	8	–	–	8
Securities of euro area residents denominated in euro	8 553 038	168 099	–	8 721 137
Intra-Eurosystem claims	5 614	–	5 271 869	5 277 483
Other assets	132 709	–	73 353	206 062
Total assets	13 219 938	180 349	5 345 222	18 745 509
Liabilities				
Banknotes in circulation	–	–	4 666 799	4 666 799
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	5 660 676	–	–	5 660 676
Other liabilities to euro area credit institutions denominated in euro	11 871	–	–	11 871
Liabilities to other euro area residents denominated in euro	1 506 709	–	–	1 506 709
Liabilities to non-euro area residents denominated in euro	307 239	–	–	307 239
Liabilities to euro area residents denominated in foreign currency	153 351	–	–	153 351
Liabilities to non-euro area residents denominated in foreign currency	1 642 368	–	–	1 642 368
Intra-Eurosystem liabilities	3 833 540	–	–	3 833 540
Other liabilities	223 228	–	106 098	329 326
Total liabilities	13 338 982	–	4 772 897	18 111 879
Net position on balance sheet	–119 044	180 349	572 325	x

30. SECTORAL STRUCTURE OF ASSETS

	Amount (in thousands of euro)		Proportion (%)	
	2020	2019	2020	2019
Investment operations	5 927 237	5 665 880	25.7	30.2
Central governments and other governmental institutions	2 726 649	2 480 997	11.7	13.2
Other financial institutions	1 474 111	1 744 598	6.4	9.3
Central banks and credit institutions	710 982	638 498	3.1	3.4
Non-financial corporations	519 143	246 393	2.3	1.3
International institutions	275 804	315 024	1.2	1.7
Local governments	219 950	218 538	1.0	1.2
Unclassified assets	598	21 832	0	0.1
Monetary policy operations	11 342 251	7 715 721	49.2	41.2
International institutions	7 461 626	4 857 749	32.4	25.9
Central governments and other governmental institutions	2 620 625	2 845 722	11.3	15.2
Credit institutions	1 260 000	12 250	5.5	0.1
Other operations	5 776 254	5 363 908	25.1	28.6
Intra-Eurosystem claims	5 673 974	5 277 483	24.6	28.2
International institutions	62 266	45 922	0.3	0.2
Unclassified assets	40 014	40 503	0.2	0.2
Total	23 045 742	18 745 509	100.0	100.0

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

	Amount (in thousands of euro)		Proportion (%)	
	2020	2019	2020	2019
Investment operations	5 927 237	5 665 880	25.7	30.2
US	2 293 603	2 106 897	9.9	11.1
Euro area countries	1 441 336	1 517 175	6.2	8.1
UK	707 186	658 809	3.1	3.5
Canada	669 855	595 578	2.9	3.2
International institutions	275 804	315 024	1.2	1.7
Other EU countries	165 045	128 087	0.7	0.7
Japan	152 276	86 384	0.7	0.5
Other countries	222 132	257 926	1.0	1.4
Monetary policy operations	11 342 251	7 715 721	49.2	41.2
International institutions	7 461 626	4 857 749	32.4	25.9
Euro area countries	3 880 625	2 857 972	16.8	15.3
Other operations	5 776 254	5 363 908	25.1	28.6
Intra-Eurosystem claims	5 673 974	5 277 483	24.6	28.2
International institutions	62 266	45 922	0.3	0.2
Unclassified assets	40 014	40 503	0.2	0.2
Total	23 045 742	18 745 509	100.0	100.0

32. ASSETS BY CREDIT RATING ASSIGNED TO THE COUNTERPARTY

	Amount (in thousands of euro)		Proportion (%)	
	2020	2019	2020	2019
Investment operations	5 927 237	5 665 880	25.7	30.2
AAA	3 203 434	1 884 377	13.8	10.1
AA	1 288 025	2 706 229	5.6	14.4
A	495 629	403 832	2.2	2.2
BBB	367 665	378 991	1.6	2.0
Assets without counterparty credit rating	1 944	4 260	0	0
Assets not exposed to credit risk	570 540	288 191	2.5	1.5
Monetary policy operations	11 342 251	7 715 721	49.2	41.2
AAA	5 983 541	4 837 585	25.9	25.8
AA	1 478 085	1 401 603	6.4	7.5
A	2 620 625	1 464 283	11.4	7.8
Assets without counterparty credit rating	1 260 000	12 250	5.5	0.1
Other operations	5 776 254	5 363 908	25.1	28.6
Intra-Eurosystem claims	5 673 974	5 277 483	24.6	28.2
Unclassified assets	66 530	48 843	0.3	0.2
Assets not exposed to credit risk	35 750	37 582	0.2	0.2
Total	23 045 742	18 745 509	100.0	100.0

Based on the credit ratings assigned by international credit rating agencies Fitch Ratings, Standard & Poor's, Moody's Investors Service and DBRS to the counterparties and securities issuers, the above table shows the breakdown of Latvijas Banka's assets as at the end of the reporting period. "AAA" rating is the highest possible long-term creditworthiness rating, which indicates an extremely strong capacity of the counterparty to meet its financial commitments; "AA" rating indicates very strong capacity, while "A" rating — strong capacity. "BBB" is a medium rating considered to be the lowest level of investment-grade rating.

Assets without counterparty credit rating mostly comprise securities purchased in longer-term refinancing operations with Latvian credit institutions. Assets not exposed to credit risk mostly comprise securities in the equity securities portfolio, participating interest in the BIS, fixed assets and intangible assets.

PROFIT AND LOSS STATEMENT NOTES

33. NET INTEREST INCOME

	(in thousands of euro)	
	2020	2019
Interest income	190 313	198 804
Interest on investments	105 848	127 405
Interest on customer deposits	16 662	7 689
Interest on monetary policy operations	67 803	63 710
Interest expense	-50 776	-102 858
Interest on investments	-40 021	-100 505
Interest on monetary policy operations	-10 755	-2 353
Net interest income	139 537	95 946

Net interest income was mainly derived from debt securities investments in debt securities as well as from interest income on monetary policy operations. In 2020, net interest income increased by 43 591 thousand euro compared to 2019. This was mainly due to a decrease in both interest income and expense on investment.

In 2020, interest income on investment declined on account of lower average yields on securities. A decrease in interest expense on investment resulted from lower costs of hedging currency risk, as the money market interest rates on the US dollar and Canadian dollar declined faster than those on the euro.

In 2020, interest income on deposits received grew on account of higher negative interest on deposits from the Government and other financial institutions. The application of interest on deposits is stipulated in Guideline (EU) 2019/671 of the ECB of 9 April 2019 on domestic asset and liability management operations by the national central banks (recast) (ECB/2019/7).

In 2020, interest income on monetary policy operations grew as a result of increasing the PSPP and PEPP. A rise in interest expense on monetary policy operations in 2020 mostly resulted from granting TLTRO III and higher negative interest under the PSPP and PEPP. Interest income from and interest expense on the intra-Eurosystem claims and liabilities are remunerated by applying the ECB's interest rate on the main refinancing operations and include income from foreign reserves transferred to the ECB and claims on allocation of banknotes in the Eurosystem, as well as expense on liabilities related to TARGET2 settlements. The interest rate on the main refinancing operations set by the ECB was 0% in 2020 and 2019; therefore, Latvijas Banka had neither such interest income nor interest expense.

According to the ECB Governing Council's decision on the allocation of monetary income for the first six years following the euro changeover, the remunerable part of the euro area NCBs' claims on the banknote allocation in the Eurosystem is reduced in compliance with a definite coefficient to avoid significant income fluctuations of these NCBs. The adjustment of the reduction of the remunerable part of Latvijas Banka's claims on banknote allocation in the Eurosystem ended in 2019 and in the course of these six years was as follows:

Reporting year	Coefficient (%)
2014	100.00000
2015	86.06735
2016	70.13472
2017	53.34835
2018	35.98237
2019	18.17225
2020	–

34. REALISED GAINS/LOSSES ARISING FROM FINANCIAL OPERATIONS

	(in thousands of euro)	
	2020	2019
Debt securities	32 252	54 186
Derivative financial instruments	11 392	–19 903
Foreign exchange transactions	827	11 970
Total	44 471	46 253

The result on the disposal of debt securities increased by 21 934 thousand euro compared to 2019, mostly due to a decrease in interest rates and disposal of securities held in the long-term fixed income securities portfolio.

The result on derivative financial instruments showed an improvement of 31 295 thousand euro compared to 2019, mostly on account of the positive result on interest rate future contracts due to falling interest rates in the course of 2020, and on account of the positive result on currency future contracts concluded for the purpose of hedging currency risk exposure, affected by the US dollar depreciation against the euro. The positive result of the currency future contracts concluded for the purpose of hedging currency risk exposure is offset in an equal value by the negative revaluation result of the balance sheet items hedged for foreign currency risk.

In 2019, the realised gains on foreign exchange transactions also included the recognition of the initial revaluation account in the profit and loss statement (see also Note 23). In 2020, the realised gains on foreign exchange transactions were positively affected by the depreciation of the US dollar against the euro.

35. RECOGNITION OF REVALUATION RESULT ON FINANCIAL ASSETS AND POSITIONS IN THE PROFIT AND LOSS STATEMENT

	(in thousands of euro)	
	2020	2019
Foreign currency positions	–28 642	–145
Securities	–6 299	–3 280
Interest rate swap arrangements	–296	–431
Total	–35 237	–3 856

The revaluation result of several debt securities, foreign currency positions, and interest rate swap arrangements at the end of 2020 and 2019 was negative and has been recognised in the profit and loss statement. At the end of 2020 and 2019, the net revaluation result on the equity securities portfolio was positive and has been reported under the balance sheet item "Capital and reserves" as the securities revaluation result. The positive result on the revaluation of debt securities, foreign currency positions, and interest rate swap arrangements has been reported under the balance sheet item "Capital and reserves" as

the revaluation reserve of securities, foreign currency, and interest rate swap arrangements (see also Note 23).

The rise in the negative result on the revaluation of foreign currencies is related to an increase in the open position of the US dollar and to the depreciation of the US dollar against the euro.

36. PROVISIONS FOR MARKET RISK AND CREDIT RISK

Latvijas Banka's financial risks relate primarily to investments in financial instruments and to the implementation of the single monetary policy operations associated with Latvijas Banka's participation in the Eurosystem and sharing of the related risks and financial results. Latvijas Banka's financial assets are mostly exposed to market risk and credit risk.

The level of Latvijas Banka's financial risks for monetary policy operations and investment portfolio credit risk has been assessed in compliance with the ECB's common methodology for Eurosystem financial risk assessment, whereas for investment portfolio market risk — in compliance with the risk assessment methodology used by Latvijas Banka in its financial risk management system; in both cases, the Expected Shortfall (ES) measure with a confidence level of 99% for a risk horizon of one year is used: it describes the losses determined by the average value of 1% of the most unfavourable simulated profitability scenarios. When assessing the level of financial risks, various market risk and credit risk factors, assumptions defined by the Eurosystem/ESCB's Risk Management Committee and assumptions used in the financial risk management system are taken into account, as well as historical data and assumptions concerning the development of adverse financial market factors, e.g. an increase in interest rates, widening interest rate spreads, euro appreciation, and credit rating downgrades.

In 2020, Latvijas Banka introduced improvements to its methodology for measuring financial risks and assessed the market risk of all investment portfolios using the Expected Shortfall measure with the confidence level of 99% for a risk horizon of one year. In 2019, this methodology was only applied to the gold portfolio, long-term fixed income securities portfolio and equity securities portfolio, whereas the financial risks of other investment portfolios for the purpose of determining the targeted amount of provisions were measured according to the change in the investment portfolio value if the interest rates rise by 100 basis points. Based on the previously applied methodology, Latvijas Banka's targeted amount of provisions in 2020 would be estimated at 460.0 million euro (310.0 million euro in 2019). From 2020, the targeted amount of provisions is no longer estimated separately as it corresponds to the level of financial risks.

In 2020, the level of financial risks has been estimated at 771.9 million euro (501.1 million euro in 2019). In 2020, the level of financial risks rose on account of financial market volatility caused by the COVID-19 pandemic and an increase in the amount of equity securities portfolio and securities held for monetary policy purposes.

Provisions for market risk and credit risk are established during a longer period in the amount of 25%–75% of the positive total financial performance result included in the profit and loss statement of the reporting year before establishing provisions for financial risks, not exceeding the level of financial risks. Provisions for market risk and credit risk are used if the financial risks materialise and their negative result is not covered by other income, or the balance of the provisions considerably exceeds the level of financial risks and this excess is of permanent nature.

	(in thousands of euro)	
	2020	2019
Level of financial risks	771 900	501 100
Provisions for the market risk and credit risk	281 723	203 900
Provisions for the market risk and credit risk against the level of financial risks (%)	36	41

In 2020, due to the above-mentioned risk assessment, the Council of Latvijas Banka decided to increase the provisions for market risk and credit risk related to the financial investments managed by Latvijas Banka by 78 181 thousand euro or a percentage of the positive total financial performance result included in the profit and loss statement before establishing provisions for financial risks as laid down in the above-mentioned methodology (in 2019, the respective provisions were increased by 80 218 thousand euro). In addition, the provisions for credit risk associated with the Eurosystem monetary policy operations were reduced by 358 thousand euro (by 288 thousand euro in 2019); as a result, the total outstanding amount of provisions reached 281 723 thousand euro at the end of 2020 (203 900 thousand euro at the end of 2019).

37. INCOME FROM EQUITY SECURITIES AND PARTICIPATING INTEREST

Income from participating interest comprises dividends received from the participating interest in the BIS (in 2020, dividends from the participating interest in the BIS were not paid out; 322 thousand euro in 2019; see also Note 14.2) and income from the ECB's interim profit distribution for the reporting year, the remainder of the ECB's annual profit for the previous year, and realised gains on a decrease in the participating interest in the ECB (see also Note 13.1) in the amount of 9616 thousand euro (9910 thousand euro in 2019, see also Note 2.26).

Income from equity securities comprises the accrued and received dividends of the equity securities portfolio in the amount of 8989 thousand euro (4652 thousand euro in 2019). Income grew on account of higher dividends due to an increase in the equity securities portfolio.

38. NET RESULT OF POOLING OF MONETARY INCOME

	(in thousands of euro)	
	2020	2019
Monetary income pooled	-44 679	-51 356
Monetary income received	16 978	44 555
Net result of pooling of monetary income	-27 701	-6 801

Net result of pooling of monetary income decreased on account of smaller monetary income received, primarily due to the decisions of the Governing Council of the ECB on applying more favourable conditions to TLTRO III, and due to the redemptions of securities held for monetary policy purposes within the framework of the discontinued asset purchase programmes.

39. OTHER OPERATING INCOME

	(in thousands of euro)	
	2020	2019
Income from sale of numismatic products	613	675
Other	655	625
Total	1 268	1 300

40. REMUNERATION, SOCIAL SECURITY COSTS, AND SOLIDARITY TAX

(in thousands of euro)

	2020	2019
Remuneration		
Remuneration for performance of duties of the Council and the Board	-855	-984
Remuneration of other personnel	-16 012	-16 676
Total remuneration	-16 867	-17 660
Social security costs and solidarity tax	-3 764	-3 941
Total remuneration, social security costs, and solidarity tax	-20 631	-21 601

At the end of 2020, the number of employees was 421 (479 at the end of 2019), representing 425 full-time equivalents at the end of 2020 (465 at the end of 2019). The decrease in the number of employees is mostly related to the implementation of cost efficiency improvement measures, inter alia, upgrading the cash processing equipment of the Riga Branch and closing the Liepāja Branch of Latvijas Banka on 30 January 2020, as well as changes in the implementation of other functions.

41. BANKNOTE AND COIN ACQUISITION COSTS

(in thousands of euro)

	2020	2019
Acquisition of banknotes	-1 229	-1 140
Acquisition of collector coins	-188	-363
Acquisition of circulation coins	-129	-288
Total	-1 546	-1 791

42. OTHER OPERATING EXPENSES

(in thousands of euro)

	2020	2019
Maintenance and operation of information systems	-4 023	-3 850
Municipal services	-547	-734
Maintenance of buildings, territory and equipment	-436	-621
Risk insurance	-254	-217
Information and public relations	-231	-245
Tax on real estate	-220	-226
Telecommunication services and system maintenance	-168	-183
Acquisition of low value office supplies	-94	-225
Personnel training	-85	-225
Business travel	-66	-462
Event services	-32	-151
Transport provision	-30	-53
Disposal of material values	-30	-1 695
Other	-478	-338
Total	-6 694	-9 225

Other operating expenses also comprise remuneration in the amount of 33 thousand euro paid to SIA ERNST & YOUNG BALTIC for the audit of 2020 financial statements of Latvijas Banka (29 thousand euro in 2019 to KPMG Baltics AS). Expenses on the disposal of material values in 2019 comprise the write-off of the residual book value of capital investment in the building of Latvijas Banka's Liepāja Branch in the amount of

1401 thousand euro due to the closure of the said branch. The possession of the building of Latvijas Banka's Liepāja Branch was transferred to the Ministry of Finance of the Republic of Latvia without any compensation (see also Note 43).

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. In 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 items "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 Treasury are market-based and in line with the ECB's decisions. No commission fees are applied to transactions with the Treasury.

Pursuant to Guideline (EU) 2019/671 of the ECB of 9 April 2019 on domestic asset and liability management operations by the national central banks (recast) (ECB/2019/7), Latvijas Banka applies the euro overnight index average (EONIA) rate (it was negative at the end of both 2020 and 2019 (−0.498% and −0.446% respectively) to the amount of the Treasury's deposits in euro up to 200 million euro. As regards the total outstanding amount of the Treasury's settlement accounts in euro and foreign currencies exceeding 200 million euro, by 30 September 2019 Latvijas Banka applied the deposit facility rate set by the ECB, but as of 1 October 2019 the lower of the following rates: the ECB's deposit facility rate or the euro overnight index average (EONIA) rate (the ECB's deposit facility rate was negative at the end of both 2020 and 2019 at −0.50%).

At the end of 2020 and 2019, the breakdown of Latvijas Banka's claims and liabilities to the Latvian government was as follows:

	(in thousands of euro)	
	2020	2019
Claims		
Securities held for monetary policy purposes	2 596 790	1 447 653
Other securities	46 167	47 057
Accrued interest on debt securities	18 614	17 485
Total claims	2 661 571	1 512 195
Liabilities		
Demand deposits in euro	1 588 192	442 044
Demand deposits in foreign currencies	143 350	153 351
Tax liabilities	19	13
Total liabilities	1 731 561	595 408

In 2020 and 2019, the breakdown of Latvijas Banka's income and expense related to the Latvian government, as well as Latvijas Banka's profit for the previous reporting year appropriated to the state budget was as follows (see also Notes 22.2 and 23):

	(in thousands of euro)	
	2020	2019
Income (–)/expense and Latvijas Banka's profit appropriated to the state budget		
Interest on debt securities	–13 495	–10 381
Negative interest on government deposits	–10 400	–2 478
Taxes	9 932	10 435
Profit appropriated to the state budget	19 009	10 196
Disposal of the real estate	–	1 401
Total net expense and Latvijas Banka's profit appropriated to the state budget	5 046	9 173

Expenses on the disposal of real estate comprise the transfer of the real estate of Latvijas Banka's Liepāja Branch (the decision to close the branch was made in 2019) in the possession of the Ministry of Finance without any compensation pursuant to the Law on Public Entity's Property Disposal.

44. PLEDGED ASSETS

Debt securities, gold and other financial instruments purchased by Latvijas Banka with the market value of 2 667 712 thousand euro, as at the end of 2020 (1 977 786 thousand euro at the end of 2019), have been pledged to provide repurchase agreement deals, collateral for gold swap arrangements, forward exchange rate contracts, interest rate and currency future contracts, and to ensure the operation of payment systems. At the end of 2020, the pledged assets mostly consisted of securities pledged under repurchase agreements in the amount of 2 309 742 thousand euro (1 670 109 thousand euro at the end of 2019).

45. SECURITIES LENDING

On behalf of Latvijas Banka, its agents conclude securities lending transactions, as part of an automated security 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 above agents administer the securities lending transactions and monitor the eligibility of the securities lending transactions and related collateral. The fair value of collateral provided in securities lending transactions is higher than that of the securities lent.

To improve securities market liquidity, Latvijas Banka, simultaneously with other euro area NCBs, lends securities purchased under the PSPP and PEPP; Latvijas Banka conducts the above lending under the automated security lending programme.

At the end of 2020, the fair value of the securities lent, determined using quoted prices in an active market, was 439 thousand euro (1460 thousand euro at the end of 2019); inter alia, the fair value of securities purchased and lent under the PSPP and PEPP stood at 285 thousand euro at the end of 2020 (16 thousand euro at the end of 2019).

Foreign currency cash or securities received in the agent account of Latvijas Banka's automated security lending programme as collateral for securities lending transactions are not recognised in Latvijas Banka's balance sheet (see also Note 2.12).

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 2020, the uncalled portion of the BIS shareholding was 4012 thousand SDR (4729 thousand euro; 4012 thousand SDR (4951 thousand euro) at the end of 2019; see also Note 14.2).

At the end of 2020, Latvijas Banka had issued euro collector coins, lats collector coins and precious metal circulation coins in the nominal value of 7034 thousand euro (6960 thousand euro at the end of 2019). These coins may be represented to Latvijas Banka at a nominal value. In the opinion of Latvijas Banka's management, the probability that Latvijas Banka will be required to repurchase these coins from their holders is considered low and no provisions have been made.

At the end of 2020, Latvijas Banka had issued lats banknotes and coins with the face value of 120 934 thousand euro (122 174 thousand euro at the end of 2019), reported on the balance sheet in the amount of 25 334 thousand euro (26 574 thousand euro at the end of 2019). 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. In the opinion of Latvijas Banka's management, the probability that Latvijas Banka would be required to exchange lats banknotes and coins in the amount of 95 600 thousand euro (95 600 thousand euro at the end of 2019) at face value is low.

47. EVENTS AFTER THE REPORTING YEAR

There have been no events requiring adjustments to these financial statements or disclosure in these financial statements from the last day of the reporting year to the date of signing these financial statements.

9 March 2021

TO THE COUNCIL OF LATVIJAS BANKA¹*Opinion*

We have audited the accompanying financial statements of Latvijas Banka (the Bank) set out on pages 57 to 107, which comprise the balance sheet as at 31 December 2020 and the statement of profit and loss and the statement of total recognised gains and losses for the year then ended, and notes to the financial statements, including a summary of significant accounting policies and other explanatory notes.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of Latvijas Banka as at 31 December 2020, and of its financial performance for the year then ended in accordance with the Guideline (EU) 2016/2249 of the European Central Bank of 3 November 2016 on the legal framework for accounting and financial reporting in the European System of Central Banks (ECB/2016/34) and its amendments, the Financial Accounting Policy of Latvijas Banka approved by the Council of the Bank, and the requirements of the Law on Latvijas Banka.

Basis for Opinion

We conducted our audit in accordance with International Standards on Auditing adopted in the Republic of Latvia (ISAs). Our responsibilities under those standards are further described in the Auditor's Responsibilities for the Audit of the Financial Statements section of our report. We are independent of the Bank in accordance with the International Code of Ethics for Professional Accountants (including International Independence Standards) (IESBA Code) together with the independence requirements included in the Law on Audit Services of Republic of Latvia that are relevant to our audit of the financial statements in the Republic of Latvia. We have fulfilled our other ethical responsibilities in accordance with the Law on Audit Services of Republic of Latvia and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Responsibilities of Board and Those Charged with Governance for the Financial Statements

The Board of the Bank is responsible for the preparation of the financial statements that give a true and fair view in accordance with the Guideline (EU) 2016/2249 of the European Central Bank of 3 November 2016 on the legal framework for accounting and financial reporting in the European System of Central Banks (ECB/2016/34) and its amendments, the Financial Accounting Policy of Latvijas Banka approved by the Council of the Bank, and the requirements of the Law on Latvijas Banka. 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.

In preparing the financial statements, the Board of the Bank is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

Auditor's Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to

¹ Translation from Latvian.

issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Board of the Bank.
- Conclude on the appropriateness of Board's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

ERNST & YOUNG BALTIC SIA

Licence No. 17

Diāna Krišjāne

Chairperson of the Board

Latvian Certified Auditor

Certificate No. 124

Riga

9 March 2021

THIS DOCUMENT IS SIGNED ELECTRONICALLY WITH A SAFE ELECTRONIC SIGNATURE AND CONTAINS A TIME STAMP

Appendix 1

MONETARY INDICATORS IN 2020

(at the end of the period; 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	10 275.7	10 189.0	10 165.4	10 038.2	10 094.5	9 965.7	9 511.1	9 556.6	9 816.5	10 069.8	10 363.0	11 301.5
Currency in circulation	4 703.0	4 687.5	4 815.6	4 885.0	4 953.8	4 994.5	5 044.2	5 063.8	5 073.6	5 102.2	5 138.7	5 247.7
Current accounts (covering the minimum reserve system)	5 572.7	5 501.5	5 349.8	5 153.2	5 140.7	4 971.2	4 466.9	4 492.8	4 742.9	4 967.6	5 224.3	6 053.8
Foreign assets outside the euro area	4 264.3	4 259.4	4 356.4	4 467.6	4 333.5	4 313.0	4 265.9	4 341.6	4 421.2	4 402.3	4 342.8	4 420.1
Foreign liabilities outside the euro area	2 101.7	2 129.3	2 050.9	2 093.3	2 095.5	2 130.0	2 238.5	2 265.1	2 327.9	2 392.3	1 915.6	1 602.7
Credit	9 167.4	9 183.6	9 239.3	9 584.5	9 984.7	11 527.1	11 810.9	11 959.5	12 211.3	12 387.3	12 611.1	12 723.3
To MFIs in the euro area	326.4	305.4	297.3	295.6	307.4	1 495.3	1 457.5	1 455.2	1 530.6	1 529.6	1 522.3	1 492.8
To the general government sector in the euro area	2 230.4	2 233.7	2 281.0	2 467.1	2 660.1	2 835.9	4 342.5	4 390.1	4 429.4	4 459.9	4 531.8	4 542.0
To other euro area residents	6 610.6	6 644.5	6 661.0	6 821.8	7 017.2	7 195.9	6 010.9	6 114.2	6 251.3	6 397.8	6 557.0	6 688.5
MFI												
Overnight deposits (Latvia's contribution to M1 of the euro area)	12 899.2	12 993.2	13 380.4	13 568.6	13 916.1	13 954.4	14 268.4	14 416.0	14 616.9	14 935.6	15 240.1	15 695.0
Deposits with an agreed maturity of up to 2 years	1 547.7	1 657.9	1 573.1	1 514.3	1 481.9	1 388.3	1 373.0	1 348.4	1 329.5	1 307.0	1 288.9	1 232.2
Deposits redeemable at notice of up to 3 months	969.3	977.4	976.7	989.0	629.2	622.6	627.3	629.3	635.0	646.3	650.7	658.6
Latvia's contribution to M2 of the euro area	15 416.2	15 628.5	15 930.2	16 071.9	16 027.3	15 965.3	16 268.7	16 393.7	16 581.4	16 888.9	17 179.7	17 585.8
Money market fund shares and units	0	0	0	0	0	0	0	0	0	0	0	0
Debt securities with a maturity of up to 2 years	-9.7	-9.8	-6.1	-8.0	-7.9	-7.9	-7.6	-7.5	-7.6	-5.9	-3.3	-3.3
Latvia's contribution to M3 of the euro area	15 406.5	15 618.7	15 924.1	16 063.8	16 019.4	15 957.4	16 261.1	16 386.2	16 573.7	16 883.0	17 176.4	17 582.6
Net foreign assets outside the euro area	2 291.5	2 379.1	2 944.1	2 882.0	2 630.8	3 365.9	3 438.8	3 098.2	3 155.3	3 179.4	3 462.2	3 977.6
Credit to euro area financial institutions, non-financial corporations and households	12 945.2	12 687.0	12 591.9	12 611.9	12 719.2	12 709.3	12 663.4	12 712.1	12 746.6	12 712.5	12 727.6	12 425.9
Loans to resident financial institutions, non-financial corporations and households	11 577.5	11 487.2	11 436.3	11 389.4	11 458.5	11 371.6	11 350.4	11 403.0	11 436.7	11 387.3	11 401.8	11 214.1
Deposits by resident financial institutions, non-financial corporations and households	12 871.4	12 927.5	13 307.2	13 469.5	13 396.1	13 413.2	13 471.1	13 601.1	13 780.7	14 122.5	14 389.2	14 855.4
INTEREST RATES												
Interest rate on the main refinancing operations (at end of period; %)	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Weighted average interest rates on transactions in euro (%)												
Interbank loans	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50	-0.50
Loans to non-financial corporations and households with a floating interest rate and an initial rate fixation of up to 1 year (new business)	3.3	3.0	2.9	3.2	3.4	2.8	2.8	2.8	3.6	3.1	2.8	2.9
Time deposits by non-financial corporations and households (new business)	0.3	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1	0.1

MONTH-END BALANCE SHEETS OF LATVIJAS BANKA FOR 2020

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

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
ASSETS	18 878 793	18 882 016	19 132 105	19 545 907	19 927 545	21 462 680	21 808 678	22 027 789	22 355 374	22 520 314	22 755 585	23 045 742
Gold and gold receivables	305 420	315 324	313 566	336 857	331 757	337 654	356 833	352 033	344 133	345 030	315 962	330 139
Claims on non-euro area residents denominated in foreign currency	3 867 097	3 845 621	3 943 501	4 032 687	3 900 733	3 871 606	3 805 908	3 878 654	3 965 896	3 950 302	3 901 137	3 970 780
Receivables from the IMF	150 605	151 088	150 556	151 801	148 923	148 392	144 102	143 679	145 262	145 879	144 163	142 411
Balances with credit institutions and security investments, external loans and other external assets	3 716 492	3 694 533	3 792 945	3 880 886	3 751 810	3 723 214	3 661 806	3 734 975	3 820 634	3 804 423	3 756 974	3 828 369
Claims on euro area residents denominated in foreign currency	468 123	469 820	463 724	467 265	476 571	456 537	393 750	391 761	402 975	377 397	365 793	333 706
Claims on non-euro area residents denominated in euro	91 782	98 430	99 322	98 062	100 990	103 710	103 132	110 951	111 156	106 950	125 677	119 143
Lending to euro area credit institutions related to monetary policy operations denominated in euro	—	—	—	1 000	—	1 185 000	1 185 000	1 185 000	1 260 000	1 260 000	1 260 000	1 260 000
Main refinancing operations	—	—	—	1 000	—	—	—	—	—	—	—	—
Longer-term refinancing operations	—	—	—	—	—	1 185 000	1 185 000	1 185 000	1 260 000	1 260 000	1 260 000	1 260 000
Other claims on euro area credit institutions denominated in euro	333	1 369	2 010	1 241	416	476	628	133	1 133	399	394	120
Securities of euro area residents denominated in euro	8 698 895	8 712 387	8 773 490	9 114 979	9 507 695	9 885 047	10 231 489	10 382 660	10 547 106	10 749 506	10 984 897	11 129 440
Securities held for monetary policy purposes	7 633 747	7 671 346	7 748 978	8 096 885	8 479 799	8 847 395	9 177 134	9 326 177	9 472 973	9 658 797	9 890 210	10 008 456
Other securities	1 065 148	1 041 041	1 024 512	1 018 094	1 027 896	1 037 652	1 054 355	1 056 483	1 074 133	1 090 709	1 094 687	1 120 984
Intra-Eurosystem claims	5 271 956	5 255 523	5 345 783	5 334 822	5 401 569	5 428 035	5 474 877	5 511 701	5 541 193	5 561 625	5 592 019	5 673 974
Participating interest in the ECB	114 108	114 095	114 095	114 095	114 095	114 095	114 095	114 095	114 095	114 095	114 095	114 095
Claims equivalent to the transfer of foreign reserves to the ECB	158 264	157 202	157 202	157 202	157 202	157 202	157 202	157 202	157 202	157 202	157 202	157 202
Claims related to other operational requirements within the Eurosystem	4 999 584	4 984 226	5 074 486	5 063 525	5 130 272	5 156 738	5 203 580	5 240 404	5 269 896	5 290 328	5 320 722	5 402 677
Other assets	175 187	183 542	190 709	158 994	207 814	194 615	257 061	214 896	181 782	169 105	209 706	228 440

Appendix 2 (cont.)

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

	I	II	III	IV	V	VI	VII	VIII	IX	X	XI	XII
LIABILITIES	18 878 793	18 882 016	19 132 105	19 545 907	19 927 545	21 462 680	21 808 678	22 027 789	22 355 374	22 520 314	22 755 585	23 045 742
Banknotes in circulation	4 598 663	4 583 985	4 712 407	4 782 720	4 851 609	4 890 499	4 939 474	4 958 955	4 968 824	4 997 418	5 033 451	5 142 726
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	5 572 672	5 501 512	5 349 841	5 153 232	5 140 747	4 971 217	4 466 897	4 492 783	4 742 901	4 967 629	5 224 317	6 053 812
Current accounts (covering the minimum reserve system)	5 572 672	5 501 512	5 349 841	5 153 232	5 140 747	4 971 217	4 466 897	4 492 783	4 742 901	4 967 629	5 224 317	6 053 812
Other liabilities to euro area credit institutions denominated in euro	350 477	349 897	330 426	325 075	333 288	335 693	354 648	353 752	355 249	359 624	568 154	577 746
Liabilities to other euro area residents denominated in euro	1 341 234	1 446 424	2 100 939	4 005 700	4 092 358	3 899 858	4 252 391	4 183 340	4 181 673	4 045 110	3 997 702	3 012 014
General government	275 790	348 316	997 940	2 883 893	2 971 271	2 765 132	2 883 521	2 804 861	2 808 009	2 667 088	2 622 126	1 588 192
Other liabilities	1 065 444	1 098 108	1 102 999	1 121 807	1 121 087	1 134 726	1 368 870	1 378 479	1 373 664	1 378 022	1 375 576	1 423 822
Liabilities to non-euro area residents denominated in euro	398 275	372 390	359 049	388 086	386 530	395 610	444 060	416 926	421 247	460 793	254 626	238 737
Liabilities to euro area residents denominated in foreign currency	178 577	215 522	196 478	152 251	149 218	148 607	144 309	143 801	186 170	145 984	327 757	615 986
Liabilities to non-euro area residents denominated in foreign currency	1 703 388	1 756 922	1 691 836	1 705 259	1 708 936	1 734 404	1 794 406	1 848 130	1 906 626	1 931 547	1 660 969	1 364 010
Intra-Eurosystem liabilities	3 709 334	3 619 660	3 382 622	1 975 573	2 189 389	3 975 930	4 267 258	4 459 367	4 404 946	4 441 258	4 497 154	4 837 613
Liabilities related to TARGET2 and national central bank correspondent accounts (net)	3 709 334	3 619 660	3 382 622	1 975 573	2 189 389	3 975 930	4 267 258	4 459 367	4 404 946	4 441 258	4 497 154	4 809 553
Liabilities related to other operational requirements within the Eurosystem	—	—	—	—	—	—	—	—	—	—	—	28 060
Other liabilities	341 273	335 285	346 424	343 193	326 599	334 714	334 756	339 482	361 138	351 184	349 441	409 700
Capital and reserves	684 900	700 419	662 083	714 818	748 871	776 148	810 479	831 253	826 600	819 767	842 014	793 398

YEAR-END BALANCE SHEETS OF LATVIJAS BANKA FOR THE YEARS 2016–2020

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

	2016	2017	2018	2019	2020
ASSETS	14 772 305	17 498 642	18 247 147	18 745 509	23 045 742
Gold and gold receivables	234 305	230 856	239 195	289 043	330 139
Claims on non-euro area residents denominated in foreign currency	3 092 076	3 608 692	3 566 027	3 688 972	3 970 780
Receivables from the IMF	153 992	143 477	146 833	149 082	142 411
Balances with banks and security investments, external loans and other external assets	2 938 084	3 465 215	3 419 194	3 539 890	3 828 369
Claims on euro area residents denominated in foreign currency	358 839	355 065	326 308	460 415	333 706
Claims on non-euro area residents denominated in euro	144 564	101 333	101 837	90 139	119 143
Lending to euro area credit institutions related to monetary policy operations denominated in euro	257 160	244 660	38 750	12 250	1 260 000
Longer-term refinancing operations	257 160	244 660	38 750	12 250	1 260 000
Other claims on euro area credit institutions denominated in euro	9 071	438	488	8	120
Securities of euro area residents denominated in euro	6 319 754	8 131 197	8 813 038	8 721 137	11 129 440
Securities held for monetary policy purposes	4 357 306	6 719 984	7 423 080	7 636 472	10 008 456
Other securities	1 962 448	1 411 213	1 389 958	1 084 665	1 120 984
Intra-Eurosystem claims	4 195 918	4 604 114	4 952 780	5 277 483	5 673 974
Participating interest in the ECB	115 082	115 082	115 082	114 108	114 095
Claims equivalent to the transfer of foreign reserves to the ECB	163 480	163 480	163 480	158 264	157 202
Claims related to other operational requirements within the Eurosystem	3 917 356	4 325 552	4 674 218	5 005 111	5 402 677
Other assets	160 618	222 287	208 724	206 062	228 440

Appendix 3 (cont.)

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

	2016	2017	2018	2019	2020
LIABILITIES	14 772 305	17 498 642	18 247 147	18 745 509	23 045 742
Banknotes in circulation	4 150 106	4 314 088	4 536 729	4 666 799	5 142 726
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	4 191 147	5 712 980	5 050 101	5 660 676	6 053 812
Current accounts (covering the minimum reserve system)	4 191 147	5 712 980	5 050 101	5 660 676	6 053 812
Other liabilities to euro area credit institutions denominated in euro	720	22 610	13 847	11 871	577 746
Liabilities to other euro area residents denominated in euro	212 239	215 712	1 449 237	1 506 709	3 012 014
General government	46 710	29 516	129 113	442 044	1 588 192
Other liabilities	165 529	186 196	1 320 124	1 064 665	1 423 822
Liabilities to non-euro area residents denominated in euro	17 888	2 535	16 524	307 239	238 737
Liabilities to euro area residents denominated in foreign currency	159 844	144 324	150 535	153 351	615 986
Liabilities to non-euro area residents denominated in foreign currency	—	634	115 284	1 642 368	1 364 010
Intra-Eurosystem liabilities	5 292 395	6 339 683	6 212 645	3 833 540	4 837 613
Liabilities related to TARGET2 and national central bank correspondent accounts (net)	5 292 395	6 339 683	6 212 645	3 826 452	4 809 553
Liabilities related to other operational requirements within the Eurosystem	—	—	—	7 088	28 060
Other liabilities	294 614	305 552	251 877	329 326	409 700
Capital and reserves	453 352	440 524	450 368	633 630	793 398

PROFIT AND LOSS STATEMENTS OF LATVIJAS BANKA FOR THE YEARS 2016–2020

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

	2016	2017	2018	2019	2020
Net interest income	56 801	71 498	79 494	95 946	139 537
Interest income	102 982	138 189	180 907	198 804	190 313
Interest expense	–46 181	–66 691	–101 413	–102 858	–50 776
Net result of financial operations, recognition of revaluation result in profit and loss statement and financial risk provisions	–100 590	–28 175	–42 387	–37 821	–68 947
Realised gains arising from financial operations	38 539	33 292	–49 690	46 253	44 471
Recognition of revaluation result on financial assets and positions in profit and loss statement	–52 729	–18 791	–47 903	–3 856	–35 237
Provisions for market risk and credit risk	–86 400	–42 676	55 206	–80 218	–78 181
Net expense from fees and commissions	–2 200	–3 087	–2 783	–3 607	–3 394
Fees and commissions income	396	397	644	811	949
Fees and commissions expense	–2 596	–3 484	–3 427	–4 418	–4 343
Income from participating interest	5 242	5 258	6 922	14 884	18 605
Net result of pooling of monetary income	10 834	3 651	122	–6 801	–27 701
Other operating income	81 051	12 382	9 270	1 300	1 268
NET INCOME	51 138	61 527	50 638	63 901	59 368
Remuneration	–17 184	–17 616	–17 515	–17 660	–16 867
Social security costs and solidarity tax	–3 852	–3 962	–4 031	–3 941	–3 764
Banknote and coin acquisition costs	–7 283	–4 542	–2 104	–1 791	–1 546
Depreciation of fixed assets and amortisation of intangible assets	–3 755	–3 750	–4 189	–4 129	–3 851
Other operating expenses	–7 291	–7 773	–8 233	–9 225	–6 694
PROFIT OF THE REPORTING YEAR	11 773	23 884	14 566	27 155	26 646
Profit transferrable to the reserve capital	4 120	8 359	4 370	8 146	7 994
Profit transferrable to the state budget	7 653	15 525	10 196	19 009	18 652

ORGANISATIONAL UNITS OF LATVIJAS BANKA AT THE END OF 2020

1. CASH DEPARTMENT¹
 - 1.1 Cash Operations Division
 - 1.2 Coin Division
 - 1.3 Cash Technology Division
 - 1.4 Riga Branch
2. COMMUNICATIONS DEPARTMENT
 - 2.1 Publications Division
 - 2.2 Public Relations Division
3. FINANCE DEPARTMENT
 - 3.1 Internal Banking Operations Division
 - 3.2 Financial Statements and Accounting Policy Division
4. FINANCIAL STABILITY DEPARTMENT
 - 4.1 Financial Stability Division
5. GENERAL SECRETARIAT
 - 5.1 Records and Archive Management Division
 - 5.2 Secretariat to the Council and the Board & International Relations Division
6. INFORMATION TECHNOLOGY DEPARTMENT
 - 6.1 Bank Information System Development Division
 - 6.2 Systems Maintenance Division
 - 6.3 Computer Network and Server Systems Division
 - 6.4 Engineering and Technical Security Systems Division
 - 6.5 Cyber Security Division
 - 6.6 System Design and Programming Division
7. INTERNAL AUDIT DEPARTMENT
8. LEGAL DEPARTMENT
9. MARKET OPERATIONS DEPARTMENT
 - 9.1 Trading and Investment Division
 - 9.2 Risk Management Division
10. MONETARY POLICY DEPARTMENT²
 - 10.1 Macroeconomic Analysis Division
 - 10.2 Financial Market Analysis Division
 - 10.3 Monetary Research and Forecasting Division
11. OPERATIONAL RISK MANAGEMENT DEPARTMENT
12. PAYMENT SYSTEMS DEPARTMENT
 - 12.1 Payment Systems Policy Division
 - 12.2 Payment Systems Operations Division
 - 12.3 Payment and Settlement Division

¹ As of 1 March 2021 –
Cash Operations Division
Cash Technology Division
Riga Branch.

² As of 1 January 2021 –
Macroeconomic Analysis Division
Monetary Policy Analysis Division
Research Division.

Appendix 5 (cont.)

13. PERSONNEL DEPARTMENT

14. SECURITY DEPARTMENT

14.1 Central Division

14.2 Training and Provision Division

14.3 Riga Division

15. STATISTICS DEPARTMENT

15.1 Data Management Division

15.2 Register Division

15.3 Statistics Development Division

15.4 Statistics Compilation Division

16. TECHNICAL SUPPORT DEPARTMENT

16.1 General Service Division

16.2 Building Systems Division

**PARTICIPATION OF LATVIJAS BANKA IN THE EUROSISTEM AND
THE EUROPEAN SYSTEM OF CENTRAL BANKS**

Governing Council of the ECB

General Council of the ECB

Supervisory Board of the ECB

Accounting and Monetary Income Committee (AMICO)

Banknote Committee (BANCO)

Budget Committee (BUCOM)

Committee on Controlling (COMCO)

Eurosistem/ESCB Communications Committee (ECCO)

Financial Stability Committee (FSC)

Human Resources Conference (HRC)

Information Technology Committee (ITC)

Internal Auditors Committee (IAC)

International Relations Committee (IRC)

Legal Committee (LEGCO)

Market Infrastructure and Payments Committee (MIPC)

Market Operations Committee (MOC)

Monetary Policy Committee (MPC)

Organisational Development Committee (ODC)

Risk Management Committee (RMC)

Statistics Committee (STC)

REPRESENTATION OF LATVIJAS BANKA IN INTERNATIONAL ORGANISATIONS

EUROPEAN UNION

Advisory Technical Committee of the ESRB
Board of Supervisors of the EBA
Committee on Monetary, Financial and Balance of Payments Statistics (CMFB)
EFC's Euro Coin Sub-Committee (ECSC)
EFC's Sub-Committee on IMF and Related Issues (SCIMF)
EC Public Administration Network (PAN II)
Economic and Financial Committee for the Council of the EU (EFC)
ESRB
Permanent Representation of Latvia to the EU

INTERNATIONAL MONETARY FUND

Board of Governors
Nordic-Baltic IMF Office in Washington
Nordic-Baltic Monetary and Financial Committee (NBMFC)
Alternates of Nordic-Baltic Monetary and Financial Committee (NBMFC Alternates)

BANK FOR INTERNATIONAL SETTLEMENTS

Irving Fisher Committee on Central Bank Statistics

NETWORK FOR GREENING THE FINANCIAL SYSTEM (NGFS)

LATVIJAS BANKA PUBLICATIONS AND MAJOR PUBLICATIONS BY THE EXPERTS OF LATVIJAS BANKA IN 2020

The following Latvijas Banka publications are available on Latvijas Banka website (www.bank.lv).

REGULAR PUBLICATIONS AND SERIAL PUBLICATIONS

Financial Stability Report. 2020

Latvijas Banka: Annual Report 2019

Latvijas Maksājumu Balance. Latvia's Balance of Payments. 2019

Macroeconomic Developments Report (September; No. 31, 2020)

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BESSONOV, Andrejs, KRASNOPJOROV, Oļegs (2020). *Short-Term Inflation Projections Model and Its Assessment in Latvia.* Latvijas Banka Working Paper, No. 1. 55 p.

SILIVERSTOV, Boriss, WOCHNER, Daniel S. (2020). *Recessions as Breadwinner for Forecasters State-Dependent Evaluation of Predictive Ability: Evidence from Big Macroeconomic US Data.* Latvijas Banka Working Paper, No. 2. 46 p.

FADEJEVA, Ludmila, KANTUR, Zeynep (2020). *Wealth Distribution and Monetary Policy.* Latvijas Banka Working Paper, No. 3. 46 p.

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BUŠS, Ginters, GRÜNING, Patrick (2020). *Fiscal DSGE Model for Latvia.* Latvijas Banka Working Paper, No. 5. 60 p.

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GLOSSARY

AnaCredit (analytical credit datasets): a common Eurosystem's granular analytical credit and credit risk database collecting data on loans granted to legal entities by the credit institutions of all euro area Member States based on harmonised ECB statistical reporting requirements.

Asset Purchase Programme (APP): part of a package of non-standard monetary policy measures approved by the Governing Council of the ECB, comprising corporate sector purchase programme (CSPP), public sector purchase programme (PSPP), asset-backed securities purchase programme (ABSPP) and the third covered bond purchase programme (CBPP3).

Balance of payments: a statistical statement summarising transactions between Latvia's residents and the residents of the rest of the world. It incorporates the current account, the capital account and the financial account.

Bank for International Settlements (BIS): an international financial organisation operating to facilitate international monetary and financial cooperation. The BIS acts as a bank for central banks.

Banking union: an EU-level framework for banking supervision and resolution operating based on a single rulebook applicable in the entire EU. Euro area countries and those EU countries outside the euro area opting to participate in the banking union are members of the banking union.

Capital account: a balance sheet component reflecting gross acquisitions/disposals of non-produced non-financial assets and capital transfers between Latvia's residents and the residents of the rest of the world.

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, except for the administration of social security funds. 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 the recovery of losses in the case of counterparty default or insolvency. The collateral used in the Eurosystem's reverse operations must 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.

Credit institution: a capital company 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.

Appendix 9 (cont.)

Current account: a balance sheet component reflecting flows in goods, services, primary income and secondary income between Latvia's residents and the residents of the rest of the world.

Debt security: a security representing an obligation on the part of the issuer to make one or more payment(s) to the holder of the security at a specified future date or dates. Such security usually carries a specific rate of interest (the coupon) or is sold at a discount/premium to the amount that will be repaid at maturity.

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 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.

Deposits: funds placed on the accounts of MFIs for a specified or unspecified period of time, with or without earning interest.

Direct investment: investment by an investor (direct investor) made directly or indirectly (through subsidiaries or associated companies) to acquire a lasting interest (corresponding to at least 10% ownership of ordinary shares or voting rights) in an enterprise (direct investment enterprise). The components of direct investment are equity and debt instruments.

EBA Clearing (ABE 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 as well as instant payment services to a wide community of banks and payment service providers in the EU.

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.

Electronic Clearing System of Latvijas Banka (EKS): Latvijas Banka's payment system ensuring the processing of retail payment orders across the SEPA. The EKS provides two services: clearing service which is netting the payments and ensuring several clearing cycles per the EKS business day for settlements in euro and instant payment service which is processing payments within seconds, 24 hours a day, 7 days a week, 365 days a year.

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.

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 2020, the euro area comprised Austria, Belgium, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, the Netherlands, Portugal, Slovakia, Slovenia and Spain.

Appendix 9 (cont.)

European Banking Authority (EBA): an EU body with legal personality which forms part of the European System of Financial Supervisors and works to ensure effective and consistent prudential regulation and supervision across the European banking sector. Its overall objective is to maintain financial stability in the EU and to safeguard the integrity, efficiency and orderly functioning of the banking sector.

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.

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 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.

European Systemic Risk Board (ESRB): an independent EU body which is a part of the European System of Financial Supervision and 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 from developments 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.

Eurosystem: comprises the ECB and the national central banks of the Member States of the euro area. The decision-making bodies of the Eurosystem are the Governing Council and the Executive Board of the ECB.

Financial account: a balance sheet component reflecting financial assets and financial liabilities (direct investment, portfolio investment, financial derivatives, other investment and reserve assets) between Latvia's residents and the residents of the rest of the world.

Financial accounts: a component of the system of national accounts reflecting outstanding amounts of financial instruments, transactions, exchange rate changes, price changes and other changes broken down by sector and counterparty sector.

Financial stability: a condition of the financial system enabling it to withstand shocks, thereby mitigating the likelihood of disruptions in the financial intermediation process.

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 rate 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 goods or provision of services intended for individual or collective consumption free of charge or

Appendix 9 (cont.)

at economically insignificant prices, primarily financed from the compulsory payments (taxes and duties) imposed on economic agents, as well as institutional units engaged in redistribution of national income or wealth. General government in the Republic of Latvia includes central government, local governments and social security funds. The list of the institutional units of the Latvian central government is prepared by the CSB.

Governing Council of the ECB: the main decision-making body of the ECB. It consists of members of the Executive Board of the ECB and the governors of the national central banks of the euro area.

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 which is an economic unit established by a natural person or a group of natural persons; this natural person or group of natural persons is liable for the settlement of the obligations of the economic unit with its entire property and the unit's accounting is organised in accordance with the single-entry system.

Instant payment: execution of payments of bank and other payment service provider customers within a matter of seconds, making cash transfers 24 hours a day, 7 days a week, 365 days a year, including on holidays and weekends.

Integrated Reporting Framework (IReF): an important initiative of the ESCB providing for maximum harmonisation of data requirements for the needs of statistics and supervision of credit institutions ensuring optimal data availability on the level of both granular and aggregate data. IReF is based on data collection from credit institutions' information systems and reporting using the Bank's Integrated Reporting Dictionary (BIRD) and a data exchange standard.

International investment position: a statistical statement reflecting the value and composition of financial claims (assets) on and financial obligations (liabilities) between Latvia's residents and the residents of the rest of the world, on a specific date, as well as changes in the residual values in the respective time period.

International Monetary Fund (IMF): an international organisation operating 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, executed through reverse transactions with the aim to provide credit institutions with additional longer-term financing.

Main refinancing operation: a regular open market operation executed by the Eurosystem in the form of reverse transactions. Such operations are carried out through a weekly standard tender 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 marketable or non-marketable assets.

Appendix 9 (cont.)

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 the Statistics section of 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 2020, there were 53 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.

Net issuance of banknotes and coins: amount of euro banknotes and coins issued (difference between withdrawals and deposits of euro banknotes and coins) by the national central bank. It is estimated as at a specific date or for a specific period of time, in amounts or numbers.

Non-financial corporation: an institutional unit whose principal activity is producing goods and providing non-financial services, including an economic unit established by a natural person or a group of natural persons; this natural person or group of natural persons is liable for the settlement of the obligations of the economic unit with its entire property and the unit's accounting is organised in accordance with the single-entry system.

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.

Organisation for Economic Co-operation and Development (OECD): an intergovernmental organisation, a forum providing a platform for seeking answers to common problems, identifying good practices and coordinate domestic and stimulating policies that improve the economic and social well-being of persons.

Pandemic emergency longer-term refinancing operation (PELTRO): a non-standard monetary policy measure approved by the Governing Council of the ECB to ensure sufficient liquidity to the euro area's financial system and smooth money market conditions during the Covid-19 pandemic period.

Pandemic emergency purchase programme (PEPP): a non-standard monetary policy measure approved by the Governing Council of the ECB to counter the serious risks to the monetary policy transmission mechanism and the outlook for the euro area posed by the Covid-19 pandemic.

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%.

Proxy (instant link): a link between the customer's current account number and his/her mobile phone number or other identifier. The customers who have registered the links between their current account numbers and identifiers with the Proxy Registry "Instant Links" can also receive transfers when the payer indicates the phone number only.

Register of Institutions and Affiliates Database (RIAD): a shared central repository maintained by the ECB that holds reference data (attributes) on legal units and other statistical institutional units, the collection of which supports business processes across the Eurosystem and the performance of the tasks of the ESCB and the SSM. RIAD facilitates the integration of a variety of datasets, in particular by providing common identifiers. RIAD data are also used to prepare the official lists of monetary financial institutions, investment funds, financial vehicle corporations engaged in securitisation transactions, payment statistics relevant institutions and insurance corporations.

Request to pay: a payment request sent by the payee to the payer; the payer just has to confirm the request for the initiator of the request to receive the requested amount. It will be possible to initiate a request to pay also by indicating the payer's mobile phone number only.

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.

Reverse transaction: a transaction whereby the Eurosystem buys or sells assets under a repurchase agreement or conducts credit operations against collateral.

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 SEPA (Area): a process developed by the Eurosystem for retail payments in euro, 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 2020, SEPA encompassed all EU Member States, Andorra, Iceland, Liechtenstein, Monaco, Norway, San Marino, the United Kingdom and the Vatican City.

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 supervisory authorities of the EU countries.

Special Data Dissemination Standard Plus (SDDS Plus): the highest data dissemination standard of the IMF. Its purpose is to provide comprehensive, internationally comparable, timely, accessible, reliable and high-quality statistical data on population, financial, economic, fiscal and external sectors, including information on statistical data categories and responsible institutions in each country, as well as links to data and their clarification notes.

Appendix 9 (cont.)

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: a risk of disruptions in the financial system with the potential to have significant negative consequences for the discharge of the functions of the financial system as a whole and the real economy.

TARGET: a new payment system that is being developed within the framework of TARGET2 and TARGET2-Securities consolidation project and whose T2 service will replace TARGET2 as of 21 November 2022.

TARGET2: a multiplicity of the TARGET2 component systems of all central banks. TARGET2 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 operation is ensured by Latvijas Banka in conjunction with the national central banks of the ESCB participating in TARGET2.

TARGET2-Latvija: a component system of TARGET2 in Latvia.

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 operation (TLTRO): a reverse operation of the Eurosystem providing longer-term liquidity to credit institutions on attractive terms, so that they can continue easing the terms and conditions of lending to the private sector and to encourage their lending to the real economy. It is part of a package of non-standard monetary policy measures approved by the Governing Council of the ECB.

World Bank: the world's largest institutional investor whose primary objectives are the reduction of poverty and stimulating the economic growth of developing countries. It was founded in 1944 at the Bretton Woods (USA) conference. Currently, the World Bank Groups consists of five closely linked institutions: International Bank for Reconstruction and Development, International Development Association, International Finance Corporation, Multilateral Investment Guarantee Agency and International Center for Settlement of Investment Disputes.