

Latvijas Banka: Annual Report 2023



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Contents

Foreword	5
Latvijas Banka in 2023	7
Management and organisation	8
Mission, vision, values and strategy	8
<i>Our values</i>	8
Directions of strategic development for 2023–2026	9
Management principles and development	10
Human resources	12
Financial resources	13
Risk management	16
<i>Financial risks</i>	16
<i>Operational risks</i>	16
Sustainability	18
<i>The paramount milestones in the realm of sustainability attained in 2023</i>	20
Topics of the year	22
Economic environment and monetary policy	22
<i>Reducing inflation while sustaining potential long-term growth</i>	22
<i>In the focus of macroeconomic analysis – the response of Latvia's economy to the changes</i>	26
<i>Research: helping to make decisions based on analysis</i>	30
Security of financial services	32
<i>Critical financial services</i>	32
<i>Financial literacy</i>	34
Operational areas	37
Financial stability and macroprudential policy	37
<i>Macroprudential policy</i>	37
<i>Analytical research and publications</i>	39
<i>Cooperation with the public authorities on financial stability</i>	39
Financial sector supervision	42
<i>Licensing developments</i>	42
<i>Microprudential supervision and compliance monitoring</i>	43
<i>Supervision of sustainable finance</i>	65
<i>Supervision of information and communication technology and security risk management</i>	66
<i>Supervision of ML/FTP risk and sanctions risk</i>	68
<i>Changes in the regulatory framework</i>	70
<i>A business environment that favours innovative and secure financial services</i>	73
<i>Development of innovation and supervisory technologies (SupTech) at Latvijas Banka</i>	76
The resolution mechanism	78

Compensation schemes	81
Investment management	83
<i>Investment composition</i>	83
<i>Investment management framework</i>	84
<i>Risk management</i>	85
<i>2023 in review</i>	86
Payment and settlement systems	90
<i>Instant payments</i>	90
<i>Proxy Registry "Instant Links"</i>	90
<i>Digital euro project</i>	90
<i>Operation of the EKS</i>	91
<i>Operation of TARGET-Latvija</i>	91
<i>Oversight of the payment system</i>	92
<i>Oversight of financial instrument settlement systems</i>	92
Cash circulation	94
<i>Securing cash circulation</i>	94
<i>Execution of the functions of the National Analysis Centre and the Coin National Analysis Centre</i>	96
<i>Euro commemorative and collector coins issued by Latvijas Banka in 2023</i>	98
Data management, statistics and the Credit Register	100
<i>Data management</i>	100
<i>Latvijas Banka's statistical programmes</i>	101
<i>Development of statistical regulatory framework</i>	101
<i>Development of new experimental statistics</i>	101
<i>The launch of a new wave of the Household Finance and Consumption Survey</i>	101
<i>Improvement of the used data sources</i>	102
<i>Publication of statistical information</i>	102
<i>Credit Register</i>	102
Advice on matters that Latvijas Banka has responsibility for	104
Cooperation with international organisations and foreign central banks	106
<i>Latvijas Banka in the Eurosystem and the institutions of the European Union</i>	108
Financial Statements of Latvijas Banka for the Year Ended 31 December 2023	110
Contents	110
Independent Auditors' Report	157
Appendices	159
Appendix 1. Month-End Balance Sheets of Latvijas Banka for 2023	159
Appendix 2. Balance Sheets of Latvijas Banka for the Years 2019–2023	161
Appendix 3. Profit and Loss Statements of Latvijas Banka for the Years 2019–2023	163
Appendix 4. Latvijas Banka's Publications and Major Publications by the Experts of Latvijas Banka in 2023	164
Appendix 5. Glossary	166
Abbreviations	172



In 2023, Latvijas Banka has achieved success both domestically and internationally. The foundation has been laid for a new cycle of economic growth. The decisive monetary policy action taken by the Governing Council of the European Central Bank – specifically, the swift increase in interest rates – helped to curb inflation across the euro area. The inflation dragon has been tamed, paving the way for gradual interest rate cuts already in the near future. Low inflation coupled with reduced interest rates will foster economic growth and improve the welfare of the Latvian population.

In 2023, the integration of colleagues from the Financial and Capital Market Commission marked a significant milestone for Latvijas Banka's team, taking our collective strength and resilience to a new level. A secure and developed financial sector, improved access to financial services and a banking sector that is welcoming to its customer underscore the significant progress made so far and chart a crucial path for our future work. Commercial banks have listened to Latvijas Banka's persistent urging and have initiated proactive measures to drive positive change. We stand firm in our commitment to upholding high standards in customer service, with a strong emphasis on the importance of refraining from imposing excessive requirements on low-risk customers. Basic bank account regulation has been simplified, manuals have been revised, and efforts are currently underway to improve the availability of banking services in the regions. The low point in the relationships between commercial banks and their customers is now in the past, making 2024 a pivotal milestone where previous initiatives will start to yield tangible benefits for customers.

The financial sector plays a crucial role in fostering economic development through active engagement and robust support initiatives. Last year, a number of measures were taken to increase the participation of the financial sector in the economy. These efforts included executing an agreement initiated by Latvijas Banka and reached at the Financial Sector Development Board to remove barriers hindering the expansion of bank lending. All measures under Latvijas Banka's purview have been implemented, including reducing regulatory barriers, conducting a thorough analysis of access to finance, and ensuring regular dissemination and publication of information on loan and deposit interest rates. The Saeima backed a legislative package proposed by Latvijas Banka that streamlines the refinancing process for household mortgage loans, strengthens competition

and, according to our estimates, will reduce the collective payment burden of existing mortgage loans by 100 million euro. We are currently in the process of formulating a similar proposal aimed at loans to legal persons.

Given the current geopolitical landscape, our priority is to address security concerns and bolster the financial sector's resilience to diverse risks and crises. This entails strengthening the regulation of critical financial services and working closely with industry stakeholders to achieve tangible improvements in cash circulation and the accessibility of non-cash payments. The role of cash has been reinforced, and we will continue to build on this momentum throughout the year by actively proposing legislative changes.

Last year, Latvijas Banka developed legislative proposals aimed at enhancing the management of the second pillar pension scheme, including a proposal to reduce management fees. This initiative is expected to generate savings of over 100 million euro for pension system participants over the course of a decade. In dialogue with the FinTech sector, preparatory work has been carried out to secure access for non-bank payment service providers to central bank payment systems, once common euro area criteria have been approved. A comprehensive analysis has been conducted within the sustainability domain, empowering the Latvian financial sector to effectively prepare for future challenges. We have set the bar high with our initiative to organise sustainability breakfasts, which have become a highly anticipated event and now serve as an industry benchmark. Many significant milestones have been achieved – this list offers just a glimpse into the breadth of our work over the past year.

Latvijas Banka works for the benefit of Latvia and is highly regarded by society. We are proud of the fact that, according to sociological surveys, almost 60% of the population has confidence in Latvijas Banka. We rank among the TOP 5 institutions most trusted by the public, sharing this honour with the President of Latvia, the National Armed Forces, schools and the State Police. I would like to extend a heartfelt THANK YOU to my colleagues for their dedication and hard work! The accomplishments of the past year are a testament to our collective achievement, demonstrating the mighty contributions of a resilient and determined team.

We have set ourselves ambitious goals for 2024 as well. Our ethos is "powerful in development" – a concept I would like to extend both to my colleagues and the Latvian society overall.



Mārtiņš Kazāks


Governor of Latvijas Banka
Riga, 23 April 2024

Latvijas Banka in 2023

7




Inflation has been tamed

In the euro area, it has been reduced from **8.6%** at the beginning of the year to **2.9%** at the end of the year ( to 0.6%)



The successful integration of the FCMC has transformed Latvijas Banka into a more powerful, contemporary and efficient institution

 Number of employees **-18%** (within 4 years since the integration decision was made)



Latvijas Banka's capital and reserves increased to 730 million euro,

with reserve capital compensating 54 million euro in losses attributed to inflation containment



State budget supplemented by 58 million euro

(in interest payments to the government and taxes)



Enhanced financial sector security

- ➔ Requirements for providing critical financial services have been developed
- ➔ In cooperation with credit institutions access to cash has been provided



The financial sector has been streamlined to be welcoming for an honest customer

- ➔ Regulation for market participants has been simplified
- ➔ Banks have been tasked with eliminating excessive requirements
- ➔ Basic account solutions have been improved



Modern payments have been developed

- ➔ Value of instant payments **+42%** (to **22.4** billion euro)
- ➔ The digital euro project – the preparation stage has been commenced
- ➔ The new payment system TARGET has been introduced



Efficient and safe cash circulation has been provided

- ➔ The number of processed banknotes **+12%**
- ➔ One of the lowest counterfeit rates in Europe

Management and organisation

8



Mission, vision, values and strategy

The mission of Latvijas Banka is to work for the benefit of Latvia.

The vision of Latvijas Banka is a sound financial system, an advanced country and a prosperous nation.

Our values

Brave in addressing challenges

We are flexible in making changes and doing so in a purposeful and targeted manner. We encourage each other and people around us to be brave, to accept challenges and to look for new solutions.

United in humanity

We are very conscious of the power of teamwork, and we achieve the best results through cooperation. Our team is united by humanity. We have a deep sense of responsibility and we live up to our promises.

Powerful in development

We improve ourselves and inspire others to do the same, so that we can collectively contribute to progress in Latvia.

Directions of strategic development for 2023–2026



A secure and advanced financial sector

A favourable environment for financial market participants to provide financial services, introduce new products and run high-quality operations

Close cooperation with decision-makers to apply well-considered policy in the financial sector

Proportionate regulation and effective supervision of the financial sector



Sound economic decisions at both the state and individual levels

Enhancement of the bank's analytical and research skills both in Latvia and internationally

Promotion of financial literacy and knowledge of economics among the public and businesses

Analysis and understanding of priority topics that are important for society



Sustainability of the economy and the financial system

Implementation of the principles of sustainability in the financial sector and the economy

Construction of a regulatory environment that supports sustainability

Sustainable behaviour in the day-to-day work of the bank



An effective and innovative central bank

Skilful data management that extracts maximum value from information

Ever increasing efficiency through the use of new technologies

Development of a culture of innovation



Meaningful career opportunities for professionals

An inclusive and flexible work environment that promotes the well-being of employees

Development of employee skills and talent

Work that meets all the organisational values

Management principles and development

The management structure of Latvijas Banka comprises:

- the **Council** of Latvijas Banka, which is a collegial decision-making body that manages Latvijas Banka;
- **departments**, which are responsible for executing the functions and processes defined for the bank and achieving results in them;
- **committees** and **commissions**.

The Council of Latvijas Banka is the main decision-making body of Latvijas Banka. The term of office of the Governor, the Deputy Governors and the other members of the Council of Latvijas Banka is five years.

The membership of the Council of Latvijas Banka at the end of 2023 was:

- Governor Mārtiņš Kazāks;
- Deputy Governors Māris Kālis and Santa Purgaile;
- other members of the Council: Kristīne Černaja-Mežmale, Ilze Posuma, Andris Vilks and Zita Zariņa.



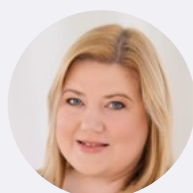
Māris Kālis



Mārtiņš Kazāks



Santa Purgaile



Kristīne Černaja-Mežmale



Ilze Posuma



Andris Vilks



Zita Zariņa

The new Law on Latvijas Banka took effect on 1 January 2023. The law was designed to modernise, enhance and advance the operation of Latvijas Banka for the benefit of the public and Latvian society. The integration into Latvijas Banka of the Financial and Capital Market Commission (FCMC) from January 2023 incorporated nine new departments into the structure of the central bank that execute the supervisory and resolution functions, and it also extended the responsibilities of several existing departments.

Under the Law on Latvijas Banka, **two new committees began operating** on 1 January 2023:

- the **Supervision Committee** of Latvijas Banka, which is responsible for taking decisions about supervising the financial market and participants in it;
- the **Resolution Committee** of Latvijas Banka, which is responsible for taking decisions about applying resolution and compensation disbursement schemes.

The **Consultative Financial Market Council of Latvijas Banka** also began operating on 1 January 2023 as a consultative body with the role of promoting engagement from the financial market participants supervised by Latvijas Banka in regulation and supervision of the financial market and participants in it, and in the application of resolution and the implementation of compensation disbursement schemes. This previously functioned under the umbrella of the FCMC, but since the change it has been composed of delegates sent by associations of the financial market participants supervised by Latvijas Banka, and three representatives of Latvijas Banka.

Meanwhile the **Sustainability Committee of Latvijas Banka was established** on 3 April 2023 with the objective of ensuring strategic management of Latvijas Banka's progress towards sustainability and monitoring the execution of measures taken to promote sustainability.

Human resources

There were 531 employees working at Latvijas Banka at the end of 2023, of whom eight had fixed-term employment contracts; there were 376 employees at the end of 2022 before the integration with the FCMC.

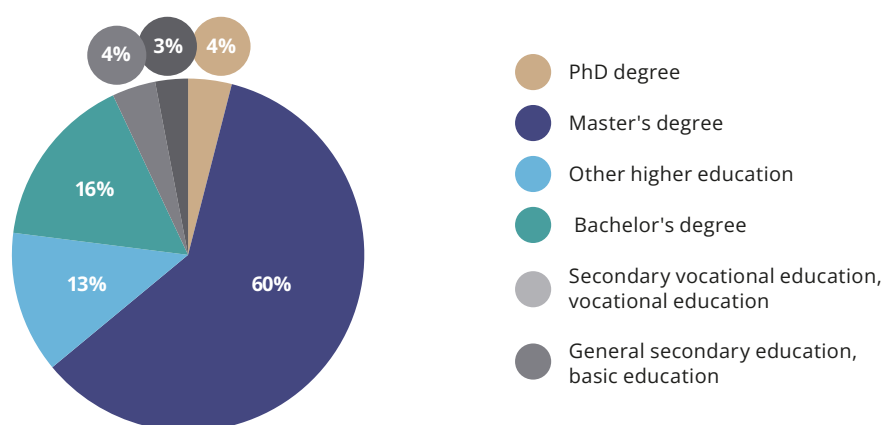
At the end of 2023, 47% of Latvijas Banka's employees were men and 53% were women, while at the end of 2022, 56% were men and 44% were women; 48% of all managers were men and 52% were women.

A Counsellor from Latvijas Banka worked at the Permanent Representation of the Republic of Latvia to the EU in 2023.

Like in previous years, Latvijas Banka ran training sessions for employees to foster their professional development and growth, while also enhancing their expertise. Staff training costs at Latvijas Banka were 1.2% of the total spending on staff remuneration in 2023, and also 1.2% in 2022.

At the end of 2023, 93% of the employees of Latvijas Banka had completed higher education, and 4% of them held a PhD degree; these figures were 88% and 5.6% in 2022.

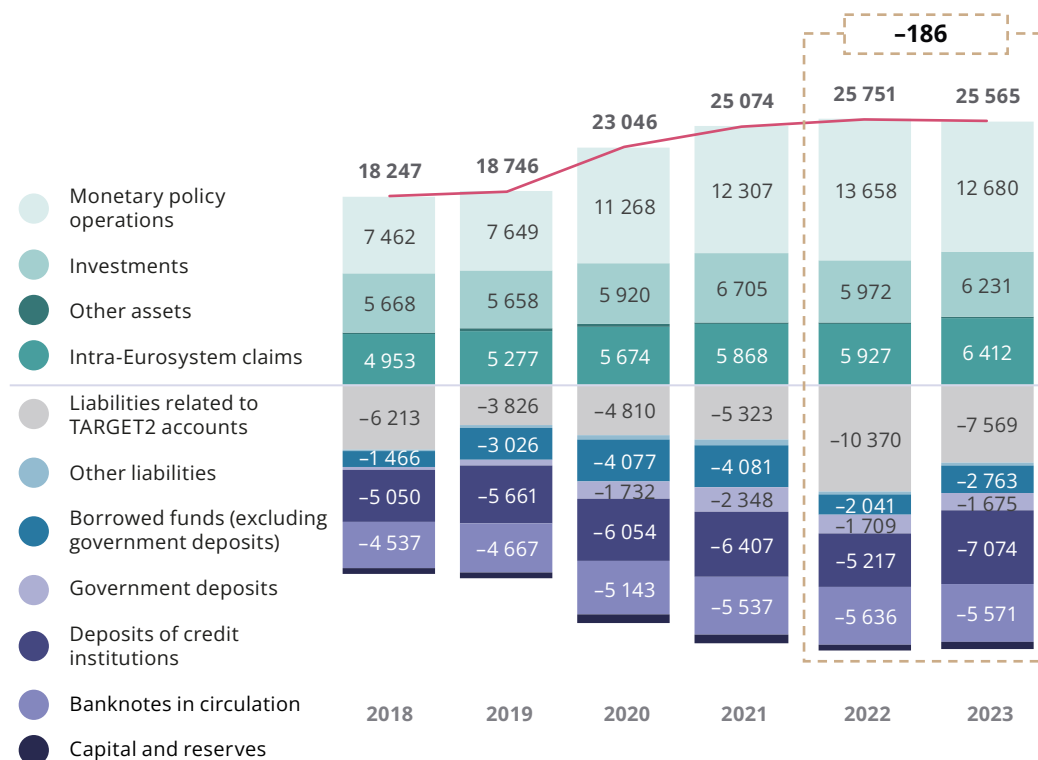
Chart 1. Education of Latvijas Banka's employees



Financial resources

The financial management system of Latvijas Banka has been developed to support decision-making processes, financial risk management and the efficient use of financial resources. The largest financial transactions made by Latvijas Banka are related to the management of financial assets and the implementation of monetary policy.

Chart 2. Balance sheet of Latvijas Banka (assets/liabilities (-); millions of euro)



The assets of Latvijas Banka declined by 186 million euro in 2023. The main changes in assets and liabilities were:

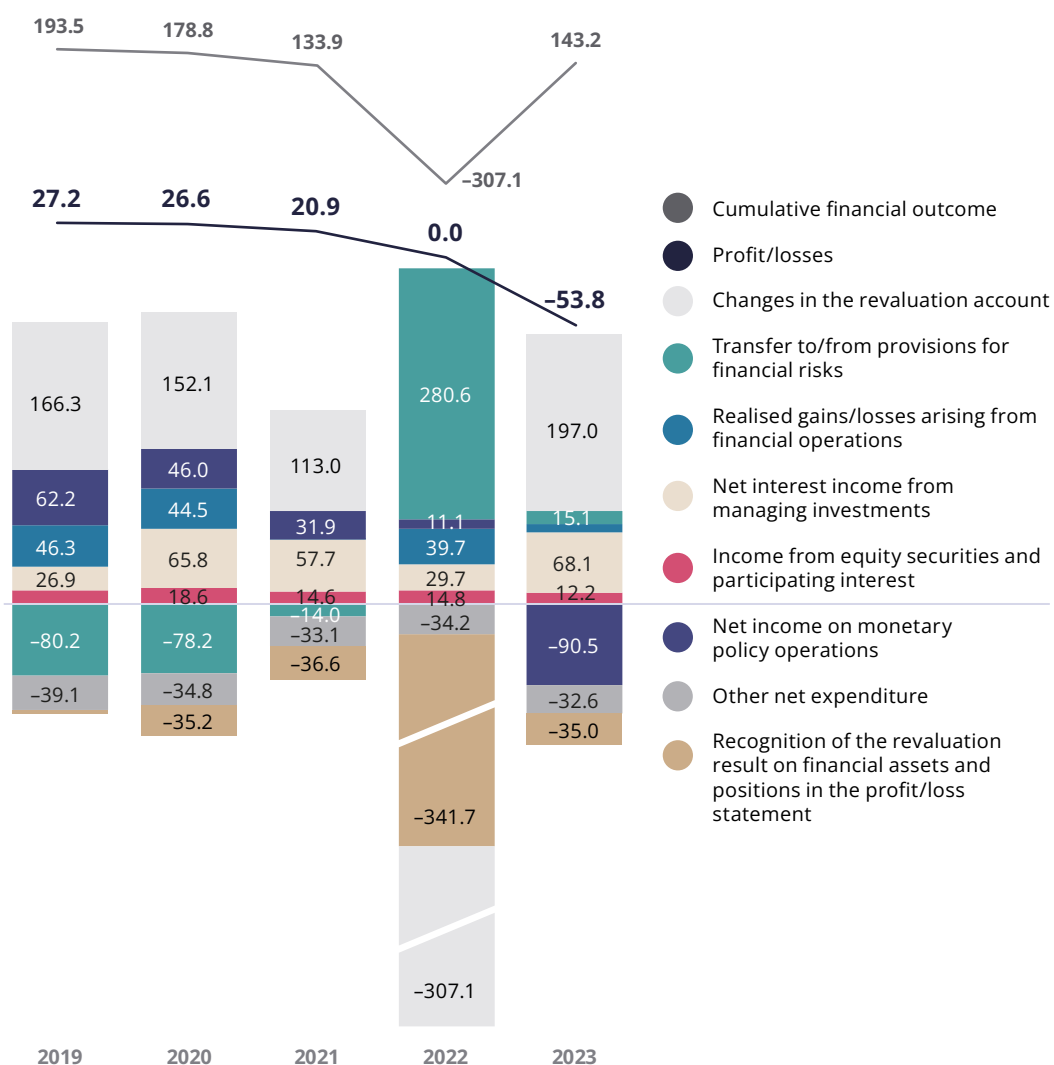
- the balance sheet item "Securities held for monetary policy purposes" decreased by 548 million euro as securities purchased by Latvijas Banka under the public sector purchase programme and the pandemic emergency purchase programme were redeemed. The value of loans granted to credit institutions by Latvijas Banka in longer-term refinancing operations dropped by 430 million euro as those loans were repaid;
- cross-border payments meant that liabilities to the ECB for the settlement result in TARGET declined by 2801 million euro;

- the value of the deposits of credit institutions mounted by 1857 million euro, mainly because credit institutions made increased use of the Eurosystem's deposit facility to make overnight deposits with Latvijas Banka at a pre-set interest rate.

Latvijas Banka finances its operations 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, but rather it transfers 70% of the profit made during the reporting year to the state budget. In addition, the financial market participants supervised by Latvijas Banka make payments to Latvijas Banka under the laws that govern their operations, and these payments cover directly or indirectly the costs to Latvijas Banka of regulating and supervising the financial market and the operation of participants in it, and of applying resolution and implementing the compensation disbursement schemes.

Against the backdrop of global geopolitical and economic developments that prompted the ECB's Governing Council to raise interest rates decisively to counter inflationary pressures within the euro area, Latvijas Banka closed 2023 with a negative result and a loss of 53.8 million euro in the profit and loss statement. The total financial result was positive at 143.2 million euro, driving Latvijas Banka's capital and reserves to a substantial year-end total of 730.1 million euro.

Chart 3. Profit of Latvijas Banka (millions of euro)



The monetary policy decisions taken by the Eurosystem to curb inflation had an adverse effect on Latvijas Banka's financial performance in 2023. Profound uncertainty has engulfed financial markets since the start of 2022, and this has been further compounded by Russia's full-scale invasion of Ukraine. This attack unleashed a particularly harmful shock to the global economy, and the ECB's Governing Council consequently raised its interest rates.

- the main refinancing operations interest rate rose from 0% in July 2022 to 2.5% at the end of 2022 and 4.5% at the end of 2023;
- the deposit facility rate rose from –0.5% in July 2022 to 2% at the end of 2022 and 4% at the end of 2023;
- the interest rate on the marginal lending facility rose from 0.25% in July 2022 to 2.75% at the end of 2022 and 4.75% at the end of 2023.

Rising interest rates meant that expenditures on monetary policy operations and the deposits of governments and other institutions surged powerfully at central banks within the Eurosystem, and Latvijas Banka was no exception to this.

The most significant changes in Latvijas Banka's operational financial results for 2023 were that:

- net income from monetary policy operations turned downwards and dropped by 102 million euro. This decline happened because the interest expenses on the deposits of Latvian credit institutions climbed to 174 million euro, while the interest expenses on Latvian government deposits also soared and peaked at 45 million euro;
 - securities yields stabilising after their rapid ascent in 2022 reduced the negative result recorded for the revaluation of financial assets and positions to 35 million euro, but the revaluation account surged to 197 million euro, mirroring the jump in the market value of financial investments.
-



Risk management

Latvijas Banka manages financial and operational risks. The goal and basic principles of risk management at Latvijas Banka are set out in the Risk Management Policy of Latvijas Banka that is approved and followed by the Council of Latvijas Banka.

Financial risks

The aim of managing financial risks at Latvijas Banka is to minimise the adverse effects they could have on Latvijas Banka's financial position and financial performance if there are adverse changes in financial market factors or a counterparty default.

Latvijas Banka manages financial risks, which are market risk from price, interest rate and currency risks, together with credit risk and liquidity risk, by following the predetermined financial risk limits and taking measures to preserve the value of investments while ensuring there is sufficient liquidity and income generation over the medium and longer term (see also the subsection [Risk management](#) of the section Investment management), and that the principles of sustainability are followed.

Given that climate change could have a long-term adverse impact on Latvijas Banka's financial results, Latvijas Banka has introduced a framework for managing climate change risks. It is expected that the disclosure of sustainability parameters will be developed over time, and that improvements will be made, particularly to indicators and data standards, and also to data quality. The current framework for managing climate change risks will also be enhanced as progress is made across the industry.

Latvijas Banka's exposure to financial risks and the magnitude of those risks are primarily determined by its investments in financial instruments and by the single monetary policy operations of the Eurosystem and the sharing of the resulting risks and financial results. Latvijas Banka's financial assets are mostly exposed to market risk and credit risk. The Council of Latvijas Banka considers reasonable risk estimates and decides on the provisions that need to be made for the financial risks associated with Latvijas Banka's investment management and other financial transactions, and on using those provisions should the risks materialise.

Operational risks

The operational risks of Latvijas Banka are managed to ensure that processes or projects efficiently achieve good-quality results within the time frame specified for them, and that the implementation of processes is continuous, appropriate and secure, and mitigates any negative impact there could be on Latvijas Banka's ability to accomplish its tasks, on its reputation, or on its financial position and

financial results. Latvijas Banka's operational risks are managed under a uniform operational risk management framework.

Major operational risks	Objective of governance
Compliance risks, including preventing conflicts of interests, anti-corruption controls, protection of personal data, prevention of money laundering and terrorism and proliferation financing, and ensuring the protection of the working environment	To ensure compliance with the requirements in the legal acts governing the operation of Latvijas Banka and its staff and their conduct in executing their official duties and responsibilities.
Business continuity risks	To mitigate any adverse effects or interruptions to the execution of critical processes where those effects could have negative consequences for the Latvian financial system or impede Latvijas Banka in its tasks. This means ensuring the uninterrupted execution of critical processes or the prompt and complete restoration of them in the event of any disruption or interruption, and the efficient management of incidents.
Physical security risks	To ensure the physical security of people on the premises of Latvijas Banka and of those actual premises, and of the transportation of valuables and of events organised by Latvijas Banka. The priority is to protect the life and health of individuals.
Information security risks	To prevent unauthorised disclosure or misuse of confidential information, classifying that information by its degree of confidentiality and ensuring appropriate protection for it. It is equally important to ensure that these protective measures do not hinder Latvijas Banka in providing non-classified information to its cooperation partners and the public.
Risks related to information systems, including cyber security risks	To prevent any negative impacts on the availability, security and integrity of the information systems and infrastructure of Latvijas Banka. Information systems at Latvijas Banka are classified by their importance for Latvijas Banka's tasks and by the confidentiality, integrity and availability requirements for the data that are to be processed, with appropriate physical and logical protection set for each level of classification.

Latvijas Banka manages operational risks across processes and projects by classifying the processes and risks and assessing how those risks could affect the outcomes of the projects or processes, and by using this classification to decide and execute the most effective actions for ensuring appropriate risk management. The Operational Risk Management Department is in charge of maintaining a common operational risk management framework, organising the processes of operational risk management and incident management, and providing regular information on operational risk management as required by law. The risk management process is based on the best practices in the field and concentrates the resources intended for operational risk management, thus creating a more efficient model for managing the process. The Operational Risk Management Committee of Latvijas Banka coordinates operational risk management at the bank.

Latvijas Banka places paramount importance on equipping employees with the education and training they need to navigate the most critical operational risks effectively, and it conducts tests on a regular basis.

Significant efforts were made in 2023 to enhance the operational risk management framework by considering evolving trends in risk management, accumulated experience, the integration of the FCMC into Latvijas Banka, and changes in the external and internal environments. Operational risks were managed appropriately in 2023, and the risk mitigation measures that were implemented limited those risks to acceptable levels.



Sustainability

The global financial system is continuously improving its processes and expanding its array of products and services to provide targeted support to make economies sustainable. The merger of Latvijas Banka and the FCMC has yielded valuable synergies in sustainability. Each level of financial sector supervision offers an opportunity to harness Latvijas Banka's analytical potential and expertise on an equal basis.

The [Sustainability Strategy](#) of Latvijas Banka defines a vision of the processes driving sustainability and how they link with the functions and tasks of Latvijas Banka, and describes the pivotal actions that Latvijas Banka takes in the interests of sustainability.

The Sustainability Committee of Latvijas Banka was set up in 2023 and marked a major step towards ensuring that measures promoting sustainability are applied effectively and systematically. It was also tasked with better integrating sustainability into the operation of Latvijas Banka.

Environmental and social objectives are currently being assessed and increased. This work encompasses initiatives to mitigate Latvijas Banka's carbon footprint and fortify diversity, equality and inclusion, and also covers the supervision of financial market participants.

Working in tandem with the Sustainability Committee of Latvijas Banka is the Green Group, which is a think tank that determinedly drives forward and promotes involvement in endeavours to advance sustainability. It serves as a platform for raising awareness at Latvijas Banka about the green transformation, and fosters dialogue with stakeholders.

The [Sustainable Governance Award](#) was bestowed on Latvian businesses in 2023 for the third consecutive year. The aim of the award is to advance the practical implementation of the Latvian [Corporate Governance Code](#) and buttress the sustainability of businesses in Latvia. By promoting operational efficiency and long-term value growth, it seeks to shine a positive public light on businesses with a sustainable governance model.



The Latvian Sustainable Governance Award 2023 presentation ceremony

To raise awareness of and spark discussions about the latest developments in sustainability and to drive policy-making, articles have been published on a range of topics:

- [financing schemes for losses](#) arising from physical climate and natural risks;
- [the impact of natural disasters on the insurance sector](#);
- [greener monetary policy](#);
- [gender equality](#);
- [the impact of fuels](#) on the environment and health;
- [energy policy](#);
- [the impact of flood risk](#) on loans and collaterals;
- [opportunities](#) for greening capital markets;
- inclusive and sustainable [economic growth](#);
- [digital inequality](#) and digitalisation;
- [greenhouse gas emissions](#) from the manufacturing and construction sectors.

Macroeconomic working papers have also been published that [explore the impact of the green transformation on the economy](#), and the stranded assets accrued by businesses as a result of decarbonisation efforts.

Latvijas Banka plays an active role in various international forums and organisations working on greening the financial system, including:

- the ECB working groups on climate change, sustainable and responsible investment in non-monetary policy portfolio management, and statistics;
- the EBA working group on sustainable finance;
- the ESMA working groups on sustainable reporting and regulation;
- inter-institutional working groups;
- the Network for Greening the Financial System (NGFS) working groups on sustainable financial investment and corporate governance, climate scenarios, research, and biodiversity. In 2023, Latvijas Banka was engaged in developing [short-term climate scenarios](#) for the NGFS to enhance understanding of the macro-financial effects of the green transition, and the physical risks from it.

The paramount milestones in the realm of sustainability attained in 2023

Macroprudential supervision	To facilitate a structural transition towards more energy-efficient housing stock, credit standards for consumer credit for purchasing energy-efficient housing have been eased. These standards include a limit of 45% on the debt service-to-income (DSTI) ratio between the borrower's loan payments and their net monthly income, and a limit of eight times for the debt-to-income (DTI) ratio of the borrower's total debt to their annual income. For other consumer credit, the limit on the DSTI is 40%, while the limit on the DTI ratio is six times. The credit standards were eased from the start of 2024.
Analysing financial stability, including stress testing, scenarios and models	A simulation was run on how natural disasters would impact the Latvian economy and the insurance sector, along with transitional period climate risk stress tests , flood risk stress tests , and an evaluation of the biodiversity/environmental risk as part of financial stability risk analysis.
Supervision of financial market participants	<p>To raise awareness of sustainable finance among financial market participants, a series of sustainability breakfast events has been launched, resulting in recommendations for ways to develop sustainability strategies.</p> <p>To monitor how well the operations of financial market participants comply with the laws and regulations and the supervisory expectations for sustainability, they were surveyed and comprehensive off-site thematic inspection spanning non-bank sectors was conducted.</p> <p>Following the precedent set in the banking sector, issues affecting sustainability have been integrated into the SREP of the non-bank sector since 2023.</p> <p>Latvijas Banka has joined an international project on environmental, social and governance (ESG) risk management in the financial sector to strengthen the skills within the bank.</p>
Climate-related data and statistics	<p>Fresh data sources have been provided to bolster sustainability analytics, with open data from other government institutions and data from the VAS Road Traffic Safety Directorate. This allows the information stored in the Credit Register on collateral from real estate and vehicle identifiers to be correlated with the open data identifying building type, the year of commissioning and the energy certificate class, or with data giving vehicle attributes such as fuel type and CO₂ emissions. This allows the contribution of financial market participants to attaining climate neutrality within the transportation sector to be assessed.</p> <p>Access to greenness data on bond issuers compiled by the ECB is provided at Latvijas Banka.</p> <p>Latvijas Banka has worked with the ECB to compile climate change statistics on physical risks, carbon emissions and the volumes of green securities.</p>
Cash and market infrastructure	<p>In 2023, Latvijas Banka negotiated transactions with the Central Bank of Ireland to exchange one, two, and 20 cent coins, laying the foundation for substantial savings in CO₂ emissions in the future. The transactions have been scheduled for 2024.</p> <p>The ongoing project to withdraw 1 and 2 cent coins from circulation promises to minimise the environmental impact from processing and minting them and from the logistics of handling them, and also save financial and labour resources.</p> <p>Banknote printing projects use joint procurement with the central banks of Germany, Lithuania and Croatia, thereby getting the lowest price possible.</p>
Foreign reserves and other non-monetary policy investment portfolios	<p>The first report on climate-related disclosures has been published.</p> <p>The integration of sustainability strategies into investment portfolios continued, and opportunities for fixed income securities portfolios were assessed.</p>

**Social responsibility
policy**

The development of a social responsibility policy strategy has commenced, and it is guided by the principles outlined in the equality, diversity and inclusion charter. This strategy will help Latvijas Banka perform better at improving the lives of the people it serves. The principles, objectives and commitments in this charter embody the fundamental rights upheld by the European Union.

Following the integration of the FCMC into Latvijas Banka, the proportion of Latvijas Banka's employees who are women increased by a significant 10% on average from the figure for 2022. The proportion of women at management level was 14% larger than in 2022. Latvijas Banka made a remarkable ascent in the OMFIF's Gender Balance Index in 2023, passing other central banks in making a substantial leap from 139th place to 34th.

Latvijas Banka remained committed to cultivating an inclusive work environment, with nearly 80% of employees engaging in discussions on organisational values and collectively committing to fostering a positive atmosphere where every individual feels accepted and included.

Several events revolving around and promoting employee well-being and social responsibility were organised in 2023.

Regular assessment of work and related issues is carried out at Latvijas Banka to cultivate feedback mechanisms and promote employee engagement. The staff of Latvijas Banka provided favourable assessments of various aspects of their work in 2023, notably highlighting "recognition and evaluation", "feedback" and "clear job tasks". Nonetheless, "workload" remains an enduring area for improvement, as it has also been in previous years.

**Knowledge
enhancement and
capacity**

Continuous and innovative initiatives aimed at enhancing employee knowledge encompassed educational seminars, campaigns and a regular intranet news column titled "Sustainability News".

Economic environment and monetary policy

Reducing inflation while sustaining potential long-term growth

The Eurosystem maintained a tighter monetary policy in 2023, though the inflationary pressures attributed to external factors continued to ease, as projected at the end of 2022.

At the same time however, the upward pressure on inflation from internal factors including wages grew stronger.

Chart 4. Changes in real wages (compensation per employee; %; annual change)



Sources: CSB, Eurostat.

The robustness of the labour market and the ability of employees to leverage it when negotiating with employers combined with the support from the government to offset gradually the decline in purchasing power caused by the Covid-19 pandemic and the surge in energy prices. This allowed companies to keep making relatively high profits and kept inflation from falling even more sharply.

Chart 5. Annual changes in the GDP deflator by component, Latvia (%) (percentage points)

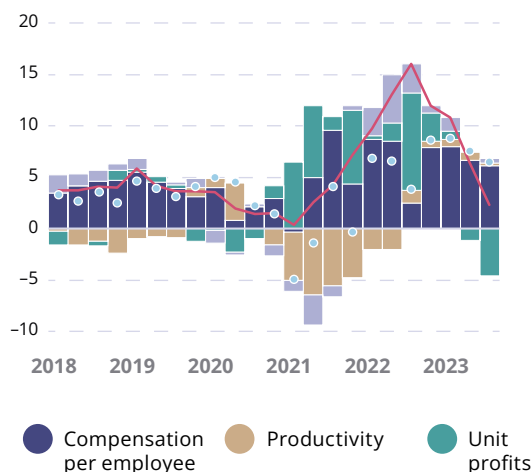
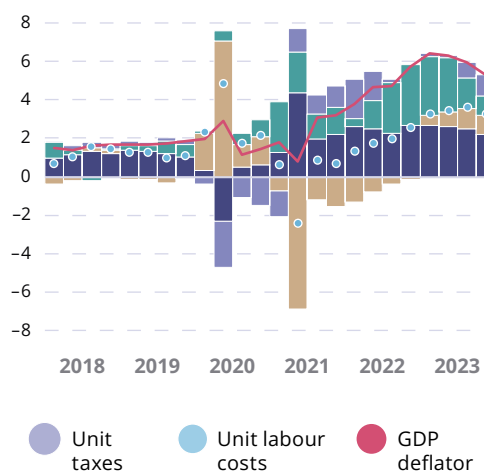


Chart 6. Annual changes in the GDP deflator by component, euro area (%) (percentage points)



Sources: CSB, Eurostat.

Latvia's economic downturn in 2023 was milder than had previously been projected, but the pace of further economic development remained highly uncertain. The high level of uncertainty also affected the direction of monetary policy, because tightening the monetary policy stance too rapidly could increase the risks of the economy cooling faster and falling into recession, while a monetary policy that was insufficiently restrictive would add to the risk that inflation might not fall far enough to reach the ECB target, contributing additionally to the risk of a further wave of inflation. To prevent this happening, an even tighter monetary policy would be needed, and that could have an adverse effect on long-term economic growth.

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Uldis Rutkaste
Head of the Monetary
Policy Department



Given the high degree of uncertainty and the dilemma of the monetary policy stance being either overly tight or insufficiently tight, the ECB dropped its forward guidance about the desired future level of interest rates on 16 March 2023 and underlined the importance of a data-based approach to the decisions taken by the Governing Council on policy rates.

Three key elements that affected the monetary policy decisions taken by the ECB in 2023 were:

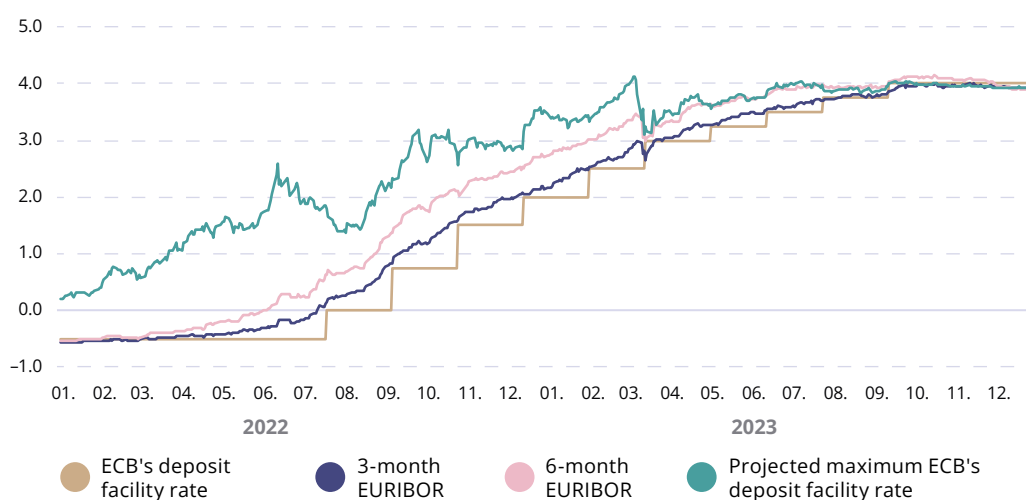
- the assessment of the inflation outlook;
- the dynamics of core inflation;
- the strength of monetary policy transmissions.

The rise in interest rates was also significant as a means to reach the inflation target and keep inflation expectations anchored while the labour market was stronger than anticipated and actual inflation in the first half of the year was surpassing forecasts. The rise also exceeded the expectations of market participants, who had forecast maximum interest rates of around 3% at the start of the year.

Interest rates have, however, stopped rising since September 2023. Reasons for this are the previously steep increase in interest rates, the effectiveness of earlier monetary policy decisions in significantly reducing inflation and helping it converge to the ECB target in the medium term, and the high level of uncertainty about how strongly the current tighter monetary policy will be transmitted over time.

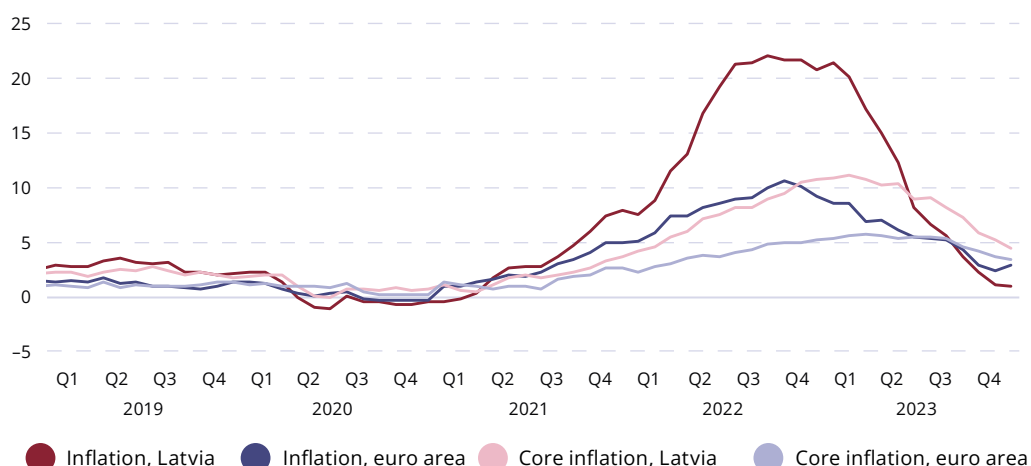
At the end of 2023, financial market participants were no longer expecting any further rises in the interest rates set by the Governing Council of the ECB. Instead, the discussion primarily focused on how long those rates would need to remain at their current level to help reach the ECB target.

Chart 7. ECB interest rates and money market rates (%)



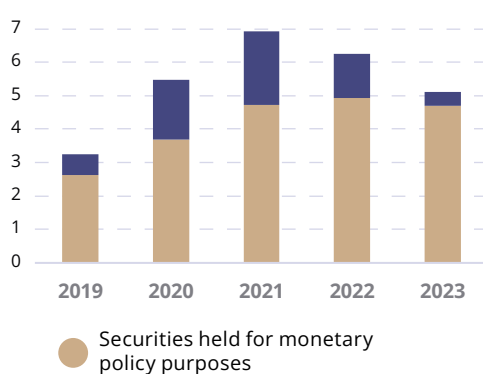
Sources: Thomson Reuters, Latvijas Banka's calculations.

Latvijas Banka's [estimates suggest](#) that higher interest rates have played an important role in reducing price pressures both in Latvia and in the euro area. Inflation in Latvia would have been at least two percentage points higher in 2023 if the Eurosystem had not reacted to the rapid rise in inflation. Interest rate rises mostly reduce price pressures in Latvia through the exchange rate channel, as a more valuable euro helps moderate the price pressures from imported goods, including energy.

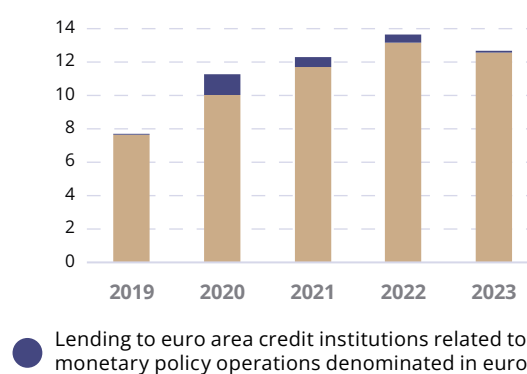
Chart 8. Inflation and core inflation in Latvia and the euro area (%; annual change)

Sources: CSB, Eurostat.

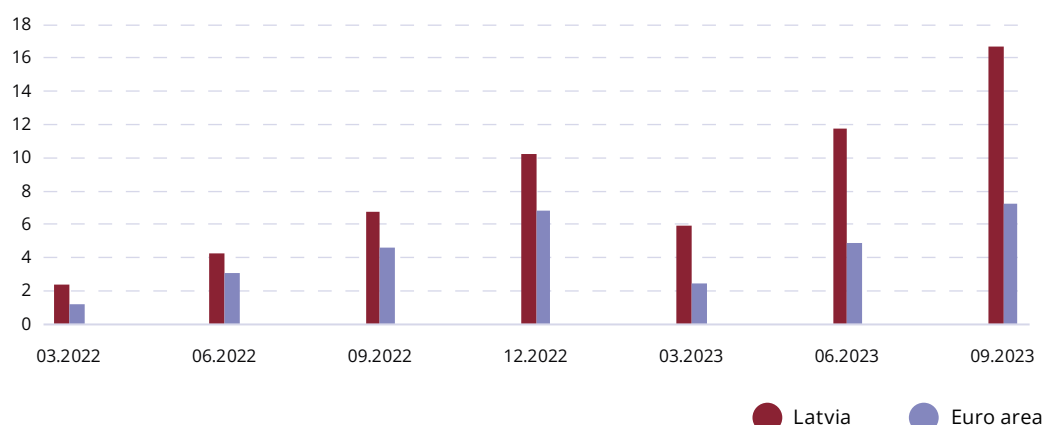
At the same time, the changing conditions that required monetary policy to be tightened also allowed the normalisation of the balance sheet of central banks to be started and the ongoing asset purchase programmes to be discontinued. The Eurosystem first acted using the policy instrument of interest rates, and only then decided to decrease the outstanding securities purchased under the asset purchase programme (APP) and the pandemic emergency purchase programme (PEPP) because interest rates were affecting financial conditions, aggregate demand and so also inflation in a more direct and faster way. The outstanding amount of securities purchased previously was reduced at a measured and predictable pace. The Eurosystem initially stopped reinvesting in full the principal payments from maturing securities, then later on ceased investing principal payments entirely. This gradual approach was necessary so that the response of the financial market could be monitored, particularly so that its capacity to absorb the new issues of securities without causing fragmentation in the securities market could be assessed.

Chart 9. Balances of the Eurosystem's monetary operations (trillions of euro)

Sources: ECB, Latvijas Banka.

Chart 10. Including the balances of Latvijas Banka's monetary operations (billions of euro)

The income of credit institutions fell as the balance of the targeted longer-term refinancing operations declined and the remuneration for minimum reserves fell, but there remained a large amount of excess liquidity in the credit institution system in Latvia even so. Meanwhile, Latvia's credit institutions saw their profits soar as the interest rates on loans surged rapidly while the expenses on deposits grew significantly more slowly, and this alleviated concerns about the financial system being weakened by the sharp rises in interest rates.

Chart 11. Banks' return on equity in Latvia and the euro area (%)

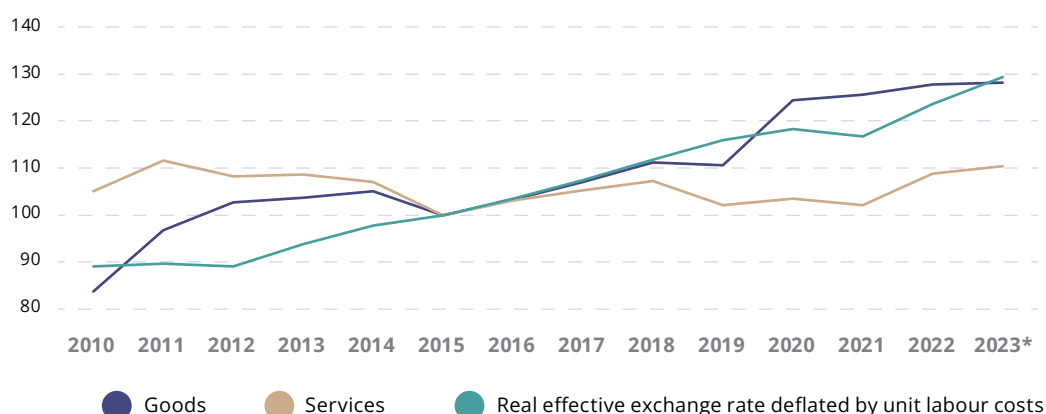
Sources: ECB, Latvijas Banka.

In the focus of macroeconomic analysis – the response of Latvia's economy to the changes

Latvia's economy was affected significantly in 2023 by various external factors:

- the consequences of rising energy prices;
- weak external demand, particularly in construction-related sectors, which impacted exports of wood products, the most important export commodity from Latvia;
- changes in trade with Russia, notably the weakening of economic ties following its full-scale invasion of Ukraine and the ensuing sanctions.

Risks to the competitiveness of exports and to economic growth come from the steady, steep climb in wages in Latvia, particularly as weak external demand intensified competition among companies vying for customers. Costs in Latvia are rising relatively faster than those in trading partners, but they remain lower in several segments than those of competitors, and export market shares may expand as foreign consumers favour Latvian products.

Chart 12. Real effective exchange rate and the share of exports of goods and services in global imports (2015 = 100)

*2023 comprises the period from the fourth quarter of 2022 to the third quarter of 2023 for market shares.

Sources: World Trade Organization, EC and Latvijas Banka's calculations.

[Discussions in the forum of experts](#) at the beginning of this year considered the economic repercussions for Latvia of Russia's full-scale invasion of Ukraine. It might be expected that the war, sanctions and ethical considerations would make companies less willing to trade with aggressor countries, but the statistics do not reflect this. Trade with Russia and Belarus persisted despite Russia's full-scale invasion of Ukraine. A fall on the imports side was only felt in early 2023, while the exports side proved much more resilient. At the same time there was a leap in exports to the countries of the Commonwealth of Independent States. The surge in energy prices that led to higher bills for heating, electricity and other utilities dealt a painful blow to Latvia's economy, causing headaches for almost every household and company.

Latvijas Banka's analysis of trade in goods under sanctions with Russia, Belarus, the Commonwealth of Independent States and other countries with close ties with Russia was used to inform the institutions responsible about the possible circumvention of sanctions, and decisions were taken to strengthen the sanctions.

The next significant drivers of economic trends in Latvia were rising interest rates and the changes in credit conditions and lending volumes that resulted from the tight monetary policy of the Eurosystem.

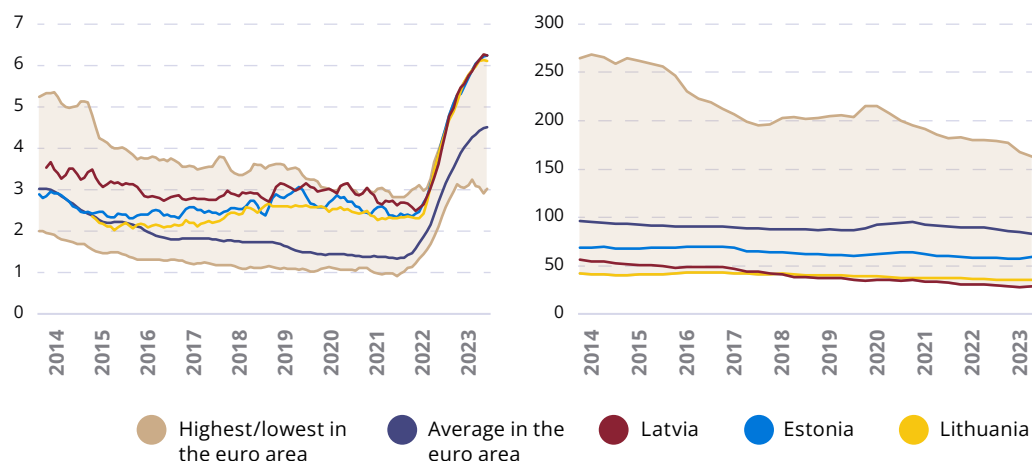
Higher interest rates affect Latvia's economy through several channels:

- **household budgets.** Since household loan payments in Latvia are mostly linked to the short-term EURIBOR, higher interest rates mean larger monthly loan payments, which put pressure on households to reduce their spending on other categories of goods and services;
- **higher costs** for bank credit and investment. The rise in interest rates makes potential investment projects more expensive, reducing new investment activity;
- **government debt servicing costs.** Higher interest rates mean borrowing is more expensive for the government and interest expenses are higher in its budget;
- **postponement of consumption.** The increase in interest rates motivates a part of the population to postpone consumption in favour of savings that earn interest. This reduces private consumption;
- **foreign demand.** The rise in interest rates also affects Latvia's trade partners, squeezing their economic activity and thus also demand for Latvia's exports.

Latvijas Banka's [calculations using the DSGE model for Latvia](#) that the most important of these channels are the weakening of economic activity in Latvia's trade partners and the consequent contraction of foreign demand, and the postponement of new investments and government spending because borrowing costs are higher.

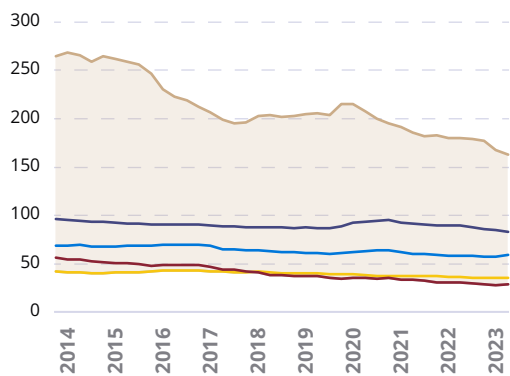
A specific focus was turned on the bank credit channel because even though money market interest rates rose evenly in all the euro area countries, the further transmission from the money market interest rates to the interest rates on loans and the dynamics of loans in the euro area varied significantly. Latvia was among the countries with the sharpest climbs in interest rates and the steepest drops in lending.

Chart 13. Interest rates on new euro-denominated loans to companies and to households for house purchase in the euro area (%) 3-month average)



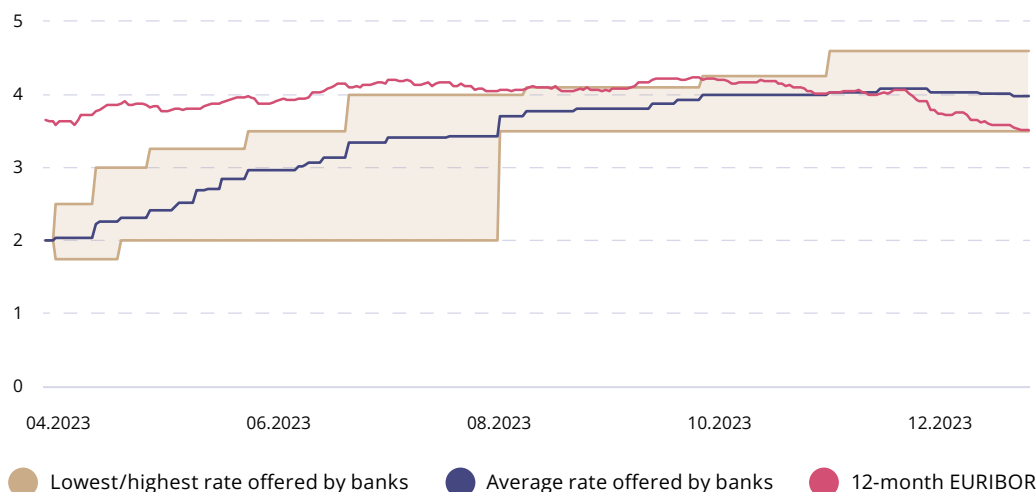
Sources: Eurostat, ECB.

Chart 14. Outstanding loans to companies and households in the euro area (% of GDP)



To help transmit the rise in the financial market interest rates to the depositors in credit institutions, Latvijas Banka began to compile and publish a regular review of the deposit rates offered by credit institutions. This is one of the measures that gave the public more comprehensive information about the services offered by credit institutions, which facilitated competition by helping clients in choosing a service provider offering more advantageous rates.

Chart 15. 12-month deposit rates offered by banks and 12-month EURIBOR (%)



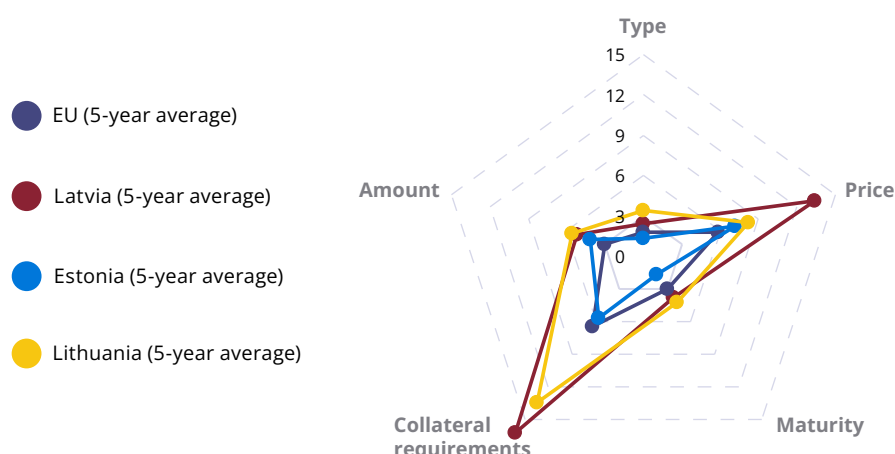
Sources: Latvijas Banka, Refinitiv.

Comparisons between the Baltic States reveal that the lack of investment correlates with lower levels of welfare in Latvia. [There are a variety of reasons why investments are more subdued in Latvia](#), some on the supply side like bureaucratic obstacles and formalities, corruption, and the shadow economy, and some on the demand side like the weak purchasing power of the population and the

low productivity of businesses, or the lack of links between science and the commercial sector. These factors are compounded by the limited availability of funding.

The factors that have limited access to financing in Latvia over the past 10–15 years were detailed in the report [Financing of the Economy 2023](#) published by Latvijas Banka. The report concluded that the decline in lending activity in the corporate segment came more from access to financing being limited than from companies being unwilling or unable to borrow. That the decrease in lending activity has been observed simultaneously with an improvement in the financial situation of companies points to the availability of loans having deteriorated.

Chart 16. Reasons for dissatisfaction with external financing (% of companies that used external financing; 2018–2022)



Sources: EIB Investment Survey Country Overview 2018/2019/2020/2021/2022: Latvia/Estonia/Lithuania.

The financial situation of households and their creditworthiness have also notably improved, but this has not been reflected in a significant expansion of lending for housing. The reasons for this lie in several structural flaws, such as bureaucratic obstacles to the construction process and the relatively high lending rates and limited availability of loans in the regions outside the capital area.

In October 2023, Latvijas Banka held an expert discussion panel on the topic "[How do we address persistent problems in financing the economy?](#)", highlighting the challenges Latvian businesses face when raising external financing. It was concluded that no quick and simple solution was feasible, and that the greatest long-term benefits would stem from competition between the banks strengthening and from other sources of external financing.

To strengthen competition between the banks, Latvijas Banka worked with other institutions to draft proposals that simplified the refinancing of housing loans. These proposals aimed to ease the restrictions on advertising and significantly reduce the costs of refinancing loans by prohibiting fees for customers leaving their current bank, abolishing Land Register duties, and limiting other costs. These changes will bring several benefits to Latvia's population:

- obstacles to active customer poaching by banks and other lenders will be removed, allowing them to offer customers more favourable terms and conditions, and more attractive services;
- loan refinancing costs will be considerably lower;
- the number of people reaping financial benefits from refinancing their loans will increase notably.

[Latvijas Banka's estimates](#) Latvijas Banka's estimates suggest that about half of all borrowers would be financially motivated to refinance their housing loans under the new regulation.

Finally, Latvijas Banka extended its analytical focus in 2023 to encompass matters relevant to the sustainability of Latvia's economy, including an examination of the impact of the tax system. [Latvijas Banka's calculations](#) from various economic models and the results of the analysis suggest that the effect of changes in the labour tax burden is not homogeneous. There are several options for changing the labour tax burden, and each of them will have a different macroeconomic impact and a different impact on the income of various social groups. Latvijas Banka used these and other calculations to produce its opinion for the tax working group organised by the Ministry of Finance.



Latvijas Banka's annual international economic conference "A Recipe for Economic Growth"

Matters related to long-term growth were also discussed at Latvijas Banka's annual conference, which brought together internationally recognised experts to discuss the reasons behind the [slowdown in global economic growth that has been observed over recent decades](#). The main conclusion was that there is no single recipe that can guide us towards swift and resilient economic growth. Instead, we should observe various principles for preventing the most frequent mistakes from hampering the [potential for growth](#), including:

- ensuring a favourable environment and opportunities for all businesses rather than selectively favouring a few under the misleading guise of industrial policy;
- introducing changes to refine current strategies and bolster development rather than constantly crafting various new visions and strategies;
- prioritising long-term goals even when there are no immediate gains.

Research: helping to make decisions based on analysis

The year 2023 proved to be a productive one for research at Latvijas Banka. Researchers from the bank delved into key issues concerning monetary policy, fiscal policy, sustainability, inflation, the labour market, and more. The results of the research have deepened insights into topics that are highly relevant for Latvia and the euro area as a whole, and have also contributed to discussions around economic policy.

- In 2023, Latvijas Banka published 10 scientific articles in the form of nine [working papers](#) and one [discussion paper](#), which was the largest number of publications within a calendar year ever.
- Latvijas Banka's employees published six articles in international scientific journals.
- Latvijas Banka's employees presented their research at 50 academic conferences and seminars.
- Eleven [research seminars](#) were held, and were attended by internationally renowned economists.

- The results of Latvijas Banka's research were presented at seminars hosted by the EC, the EIB and the IMF.
- The conference held by Latvijas Banka and the Baltic Economic Association was a resounding success.
- Several research projects were successfully launched in collaboration with international researchers.

Working papers on the latest developments in monetary policy such as [quantitative tightening](#) and [the portfolio rebalancing of quantitative easing](#) offered insights into the macroeconomic impact of the instruments on the central bank's balance sheet.

Two working papers were produced on fiscal policy that explored the effect of inflation on fiscal indicators, and the sustainability of budgetary policy. The [working paper](#) co-authored with researchers from Eesti Pank concluded that an increase of one percentage point in the inflation rate led to an improvement of around 0.7 percentage point in the primary balance. Inflation improves the primary balance both by increasing the ratio of budget revenues to GDP and by decreasing the ratio of expenditures to GDP. The [working paper](#) co-authored with researchers from the University of Lisbon also arrived at similar conclusions. Its results suggest that higher inflation rates may be used to improve fiscal sustainability.

A [working paper](#) on the effect of job retention schemes on employment in Latvia was also released. It compared similar firms that received or did not receive support from the job retention scheme. Firms that benefited from the job retention scheme displayed significantly greater resilience in employment than similar firms that did not receive such support. Moreover, the benefits of this support extended beyond its initial receipt, positively impacting firms for several months afterwards.

Improvement of the modelling toolkit for the green transition also continued in 2023. The Computable General Equilibrium model was improved by incorporating a detailed emissions block and [developing a new approach](#) to modelling the energy sector and the mutual substitution of the energy or energy products used. This model paves the way for a sector-wide exploration of the economic impacts of changes in the energy sector and of firms switching to cleaner energy sources.

Similarly, the dynamic general equilibrium model with two physical capital types, one brown and one green, and input-output sectoral linkages was developed to examine the economic impact of capital stranding. The [working paper](#) illustrates the effect of various policy instruments, including a carbon tax, on the productive capacity of capital and on aggregate economic activity.

Security of financial services

Critical financial services

The availability of financial resources is one of the key elements of public resilience in the event of a threat to national security. The National Security Law establishes that the critical financial services that must be ensured if there is a threat to national security are cash and non-cash payments provided by credit institutions, as this means that financial resources are available to people in Latvia. Under the National Security Law and the criteria established by Latvijas Banka, the banks that have been designated providers of critical financial services in Latvia are Swedbank AS, AS SEB banka, AS Citadele banka and the Latvian branch of Luminor Bank AS.

The availability of financial resources is a key part of public resilience. The critical financial services that must be ensured if there is a threat to national security are cash and non-cash payments provided by credit institutions, as this means that people in Latvia have reliable access to their money.

Ilze Posuma

Member of the Council of Latvijas Banka



The measures that ensure the availability of critical financial services are coordinated by Latvijas Banka. The role of the bank became increasingly important in 2023 following the merger with the FCMC, which brought together the expertise that each institution had developed separately by the end of 2022.

Latvijas Banka works with the financial sector, the Ministry of Finance and the Ministry of Defence to make sure that the framework of critical financial services is relevant to the current risk level and that those services remain resilient and available to the public through the best available solutions. The requirements for critical financial services were coordinated with all stakeholders across the Baltic States to keep them uniform whenever possible, and extensive consultations were held in 2023 with international and foreign institutions and organisations, including providers of global payment card services such as MasterCard and Visa, and Eesti Pank and Lietuvos bankas. This coordination resulted in a significantly upgraded framework for critical financial services, which was achieved both by finding new solutions for providing the services and by refining the procedures surrounding them.

In planning the updates to the framework of critical financial services, the following issues were assessed and taken into account:

- changes in the internal and external environment, including current scenarios for a threat to national security;
- experience gained from providing critical financial services, including that from preparing, analysing and testing the solutions for operational continuity;
- the latest available solutions for providing critical financial services, including technological developments and changes in the area of financial services.

The Council of Latvijas Banka adopted the new requirements for critical financial services on 9 October 2023 by approving Latvijas Banka's Regulation No 252 "Regulation on the Management of Critical Financial Services". The new regulation defines that providers of critical financial services are those that provide the following critical financial services:

1) non-cash payments:

- credit transfers between the providers of critical financial services, other credit institutions and the Treasury when the STEP2 system is not available. Such transfers previously only had to be ensured between the providers of critical financial services;
- offline card payments that do not access the internet allowing natural persons to purchase basic goods up to a maximum total value of 200 euro if the infrastructure for payment cards is not available. Credit institutions have until 1 January 2025 to introduce this solution. The previous rules required the execution of payments by payment cards, including online payments, to be ensured unless access to the infrastructure of international cards or settlement intermediaries was disrupted;

2) cash payments:

- the providers of critical financial services ensure that cash is continuously available in ATMs designated as critical ATMs. Latvijas Banka has worked with the providers of critical financial services to establish a network of critical ATMs that contains at least 10% of the number of ATMs operated daily by the providers of critical financial services as at the end of the previous calendar year, including one in each town. There are currently 99 ATMs in the network of critical ATMs ([the map of critical ATMs](#));
- to ensure the continuous operation of the critical ATMs and allow as many people as possible to access cash, the providers of critical financial services plan the minimum amount of cash that must be provided in the critical ATMs so that each customer using each of their payment cards issued by a financial market participant other than the operator of the ATM can withdraw 500 euro per day in cash irrespective of the number of payment cards they have or the number of payment accounts they have with the service provider;
- the new regulation introduces various requirements for critical ATMs that the provider of critical financial services needs to comply with if there is a threat to national security, while also strengthening the requirements for cash infrastructure, such as:

- the critical ATM must be available to the customer and operate during the hours of availability and operation of the ATM set for each day by the provider of critical financial services before the threat to national security emerges, and for no less than 14 hours per day;
- cash must be available in the critical ATM;
- solutions need to have been developed to ensure an uninterrupted connection between the critical ATM and the information systems, and an uninterrupted power supply to the network of critical ATMs.

The new regulation establishes that Latvijas Banka coordinates the provision of critical financial services if there is a threat to national security, and clarifies the requirements for the plans of the providers of critical financial services for continuity of operation.

A test was run in 2023 to demonstrate whether the availability of critical financial services was successfully ensured. Latvijas Banka worked with the providers of critical financial services, the economic operators involved in providing those services, the Ministry of Finance, the Ministry of Defence and the Treasury to carry out a simulation to assess whether the availability of critical financial services could be ensured in the event of a threat to national security. The lessons and conclusions drawn from the test were instrumental in shaping the new framework of critical financial services and addressing other issues related to ensuring and coordinating the availability of critical financial services.

In the second half of 2023, Latvijas Banka ran a communication campaign to inform the public about the providers of critical financial services, the financial services defined as critical, and the size of them, and also about how to respond in a crisis event. Latvijas Banka also compiled and published an information booklet [Learn about cash and other financial services in a crisis](#) that gave advice on the cash preparations everyone can make to be better prepared to deal with a crisis.

Latvijas Banka is set to improve the framework of critical financial services in 2024, primarily by introducing the solutions developed in 2023.

Financial literacy

Latvijas Banka serves as the national coordinator for financial literacy in Latvia. In 2023, Latvijas Banka strengthened its strategic approach to improving financial literacy by starting to roll out its strategy for financial literacy for 2023–2026. The objectives of the strategy are:

- to coordinate and bolster successfully national cooperation in this area and enhance the skills of the parties involved and the availability of data on the financial literacy of the population of Latvia so that financial literacy materials can be created and disseminated that strengthen financial resilience and sustainability;
- to improve the awareness and capacity of teachers by providing materials and support for teaching economics and financial literacy in Latvia's schools.

Latvijas Banka also continued to coordinate the National Strategy for Financial Literacy in Latvia 2021–2027 (the Strategy) and led the working group tasked with implementing it. The working group met several times during the year to discuss developments and thoroughly explore the priority topics for 2023 of:

- reducing financial fraud;
- making materials on financial literacy available to people with mental and physical disabilities.

The working group ran over 60 initiatives in Latvia in 2023, advancing the objectives of the Strategy notably.

During 2023, Latvijas Banka and its partners significantly broadened the array of educational materials on finance tailored to people with physical and mental disabilities and improved the availability of digital materials. To boost access to education on finance, Latvijas Banka organised meetings between the cooperation partners involved in implementing the Strategy and non-governmental organisations. Their representatives assessed whether the materials on financial services and financial education were available to people with mental or physical disabilities and explained the major financial challenges that such people face.

Towards the end of the year, Latvijas Banka held a seminar on the changing financial behaviour of the population of Latvia. The seminar aimed to promote the long-term welfare of society and focused on the people involved in implementing the Strategy. There were over 30 participants in the audience, representing more than ten public, private and non-governmental institutions.

An assessment of the financial literacy of Latvia's population was commissioned by Latvijas Banka as part of the Strategy. The results were incorporated in the report by the OECD International Network on Financial Education (INFE). This allowed the results to be analysed across 39 countries and sparked wider debates in the expert discussions held by Latvijas Banka. The level of financial literacy in Latvia was 59% of the maximum possible, while the OECD average was higher at 63%. The financial behaviour score of Latvia's population was slightly higher than that in other OECD member states but the level of financial knowledge was significantly lower, while the score for financial attitude corresponds to the OECD average.

Latvijas Banka also coordinated Financial Literacy Week in 2023, and it was held at the end of March.

During Financial Literacy Week, 22 partners ran a variety of events, with a total of 39 digital and in-person activities around the regions of Latvia. This was the most extensive array of partners and activities involved in Financial Literacy Week to date.

To promote planning for retirement and long-term savings in Latvia, Latvijas Banka also coordinated the Pension Awareness Week. Various materials were prepared, and they garnered nearly a million views online. The events were held under European Retirement Week, and the Finance Latvia Association, the Latvian Insurers Association and several financial market participants also ran their own activities as part of it.



Expert discussion "Financial Literacy and Wellness. How to Achieve a Breakthrough?"

The second half of the year marked the start of the education programme *Enhance your money management skills!*, which was developed by Latvijas Banka together with the Ministry of Education and

Science, and the project *National Coordinators for the Implementation of the European Agenda for Adult Learning in Latvia* as part of the EU programme Erasmus+. The programme's first module *Planning my personal finances* was run by 22 local governments across Latvia. Over 200 participants across Latvia have by now completed the module since it launched in October 2023. The work on the module will continue in 2024, when it will be updated with topics on financial security and the everyday use of financial services.

Latvijas Banka continued to work with teachers in Latvia, providing support for teaching economics and finance. Two seminars were held during the year that gave teachers the chance to learn more not only about economic developments, particularly the topics featured in the education programme, but also about investment. More than 400 people took part in Latvijas Banka's in-person and online seminars in 2023.

Latvijas Banka updated the contents of the financial and economic education website Money School in 2023, adding topics of financial literacy on security, loans, pensions, savings, deposits, insurance, budget planning, cash and transactions, and sustainable finances. To make information available to all the different groups in the population of Latvia, materials have also been developed in plain language, such as *Learn about cash in a crisis* and *How my pension is calculated*. In 2023, the education website Money School drew 669 thousand views and the number of unique visits grew by 144%.

Latvijas Banka's Knowledge Centre is dedicated to in-person education on economic and financial topics. It welcomed 4425 visitors in 2023, up from 3163 visitors in 2022, who included school pupils, students, and staff of businesses and organisations.

Financial stability and macroprudential policy

Latvijas Banka as the national macroprudential authority is responsible not only for financial stability analysis and analytical and advisory input into macroprudential measures, but since the merger of the FCMC and Latvijas Banka on 1 January 2023, it is also responsible for defining and implementing macroprudential policy, including the application of macroprudential tools.

Macroprudential policy

Latvijas Banka took several significant macroprudential policy decisions in 2023.

The first was that Latvijas Banka decided to follow a new approach, defined as positive neutral, to the application of the countercyclical capital buffer¹. In this approach, the countercyclical capital buffer rate is maintained at a certain base level above 0% in the standard risk environment, which is the neutral phase of the financial cycle when the cyclical systemic risk in neither heightened nor significantly low. To implement the new approach, the Council of Latvijas Banka decided to set the countercyclical buffer rate at 0.5% as of 18 December 2024 and at 1% as of 18 June 2025.



The decision on a new macroprudential policy approach to applying the countercyclical capital buffer is a forward-looking way of strengthening the resilience of banks. Given the international trends and the good financial standing of banks, resilience needs to be enhanced early. Having the capital buffer will be helpful in the event of unexpected shocks. Our targeted amendments to the borrower-based measures meanwhile aim to support sustainable changes and lending.

Elmārs Zakulis

Head of the Financial Stability and Macroprudential Policy Department

¹ See more details in [Latvijas Banka changes its approach to the application of the countercyclical capital buffer and increases the countercyclical capital buffer rate up to 1% | Latvijas Banka and Countercyclical capital buffer | Latvijas Banka](#).

International experience shows that the gradual and forward-looking accumulation of a safety buffer:

- helps to mitigate the effect of large unexpected shocks;
- reduces the uncertainty associated with timely identification of risks and their materialisation;
- provides more flexibility to the implementation of macroprudential policy throughout the financial cycle, as the countercyclical capital buffer is the macroprudential capital tool that can most easily be released in the event of a financial crisis.

Given the current good financial conditions of credit institutions, resilience buffers can be built up without any adverse pro-cyclical effects.

Changes in macroprudential regulation in 2023



Forward-looking accumulation of a resilience buffer to help banks absorb losses and continue lending in a crisis

Implementation of a positive neutral countercyclical buffer approach

gradual introduction and maintenance of a **1%** countercyclical capital buffer rate in a standard risk environment



Support for sustainable changes and lending

Easing of credit standards

a DSTI ratio of 45% and a DTI ratio of 8 for loans to purchase energy efficient housing, more flexible lending standards for buy-to-let loans

Secondly, Latvijas Banka reviewed its BBMs on 18 December 2023 and introduced amendments to the Regulation on Credit Risk Management²:

- the DSTI and DTI requirements for loans to purchase housing in a building labelled as energy efficient (class C or higher) were eased;
- a more flexible approach was introduced for buy-to-let housing loans.

The annual identification and recognition of other systemically important institutions and the recalibration of the capital buffer rates that apply to them was also carried out³.

² See more details in [Latvijas Banka Reviews Regulation on Credit Risk Management | Latvijas Banka](#) and [Borrower-Based Measures | Latvijas Banka](#). See also the section on Changes in Regulatory Requirements Framework in this Annual Report.

³ See more details in [Capital Buffer for Other Systemically Important Institutions | Latvijas Banka](#).

Analytical research and publications

Latvijas Banka analysed a very broad range of topics related to financial stability and macroprudential policy in 2023. A lot of focus was given to the factors influencing [lending](#). These include the borrower's ability to repay loans, [the financial health of businesses](#), increases in interest rates, the supply of housing, and the challenges created by negative equity.

Research placed a very strong focus on the financial sector, but also addressed climate-related risks and [insurance](#) against them, [and the impact of this on the insurance sector](#). [Climate risk stress tests](#) developed by Latvijas Banka identified flood risks as the most significant physical risks from climate change in Latvia. In addition to assessing climate change risks, Latvijas Banka launched an evaluation of the exposures of Latvian banks to biodiversity risk in the context of financial stability. An assessment was carried out to determine how dependent Latvia's commercial banks and major economic sectors are on ecosystem services and how they impact natural capital. This assessment used data from the Credit Register of Latvijas Banka and the ENCORE⁴ database. This assessment was complemented by an evaluation of country-specific environmental factors in a survey of Latvian environmental experts.

Latvijas Banka continued working on refining its credit risk stress testing methodologies by designing a GaR model for developing stress test scenarios. The methodology was also supplemented by a profit forecasting module to reflect the role of credit institutions' profit for the reporting year as a risk-absorbing factor.

The articles on [changes in Latvia's macroprudential institutional framework](#) and the [positive neutral countercyclical capital buffer approach](#) were written, and the methodology for assessing the impact of macroprudential capital tools was elaborated further.

Latvijas Banka also continued to analyse other topics of relevance to financial stability in 2023, such as the use of machine learning tools in analysing payment trends, [the potential for lowering the cap on the fixed commission fee charged by second pension pillar managers](#), [the impact of introducing the digital euro on the banking sector](#), [the impact of TLTRO funding on the balance sheets of banks in the euro area](#), and [the linkages between non-banks and the banking sector and the securitisation done by Latvia's FinTechs](#).

Cooperation with the public authorities on financial stability

Latvijas Banka conducted an assessment in 2023 of the development trends in borrower solvency and lending, which included:

- providing advice and data-based analysis on how the corporate income tax reform would impact the capitalisation of non-financial corporations;
- conducting an in-depth analysis of the initiatives to support mortgage borrowers, and presenting the results at the sittings of the Budget and Finance (Taxes) Commission of the Saeima;
- providing the Ministry of Finance with an in-depth analysis of the issues associated with non-financial corporations having negative equity.

At the 2023 meeting of the Macroprudential Council, representatives of Latvijas Banka and the Ministry of Finance discussed the most significant systemic risks to financial stability⁵. Special attention was paid to the policy measures that are required to promote financial stability. It was

⁴ ENCORE (Exploring Natural Capital Opportunities, Risks and Exposure) database contains information on 167 economic sectors and 21 ecosystem services and it sets out how the economic sectors depend and impact on the natural capital.

⁵ [The Macroprudential Council considers that the conditions are appropriate for credit institutions to build capital buffers](#), 19.07.2023.

concluded that the banking sector was financially sound and that the circumstances were appropriate for strengthening the resilience of the banking sector by introducing a positive neutral approach to the countercyclical capital buffer.

Latvijas Banka continued to work closely with representatives of the public authorities of the Republic of Latvia and managers of the state funded pension plans by proposing amendments to the Law on State Funded Pensions that would improve the method of capping the fixed component of the commission fee and supplement the regulatory framework for the variable component of the commission fee charged for managing second pillar pension assets.

International cooperation on financial stability

Latvijas Banka continued to participate actively in 2023 in the financial stability forums of the Nordic and Baltic countries.

As chair of the technical sub-stream on secure information exchange of the Nordic-Baltic Stability Group⁶ (NBSG), Latvijas Banka produced a progress report, and as a member of the NBSG sub-stream on legal impediments to information exchange, it contributed to a status report on legal impediments to information exchange between functions and institutions at the national level in the event of a possible crisis. In addition to that, work continued on preparing the 2024 crisis exercise scenario.

Since the beginning of 2023, the work stream on borrower-based measures (BBM) of the Nordic-Baltic Macroprudential Forum (NBMF) has been jointly chaired by Latvijas Banka and Lietuvos bankas. The main topics examined by the work stream are the calibration of BBM frameworks, the impact of these instruments and their practical application, and other related issues like risks and trends in lending and real estate markets. The work stream produces semi-annual reports giving the highlights of the national BBM frameworks and newly adopted measures, with thematic boxes on the latest developments like international work on BBMs in the commercial real estate segment, and the initiatives for integrating sustainability into BBMs at the EU-level and within the national BBM frameworks. Experts from Latvijas Banka are also regularly involved in the discussions of the second work stream of the NBMF on capital-based measures (CBM), addressing topics such as macroprudential instruments and how they affect banks' capital, including the calibration of them, impact assessments, national practices and other key issues.

Towards the end of 2023, [the joint project with the IMF to analyse Nordic-Baltic cross-border payment flows, money laundering threats and vulnerabilities](#) (Nordic-Baltic Technical Assistance Project – Financial Flows Analysis, AML/CFT Supervision, and Financial Stability) was approaching its final stage, and Latvijas Banka provided assistance in preparing the report, and also developed an in-house solution for a tool to identify payment flow anomalies.

Latvijas Banka contributed to the assessment of the euro area's systemic risks to financial stability and of its macroprudential policy by participating in the work of the Financial Stability Committee, which comprises representatives of the ECB and of the national central banks and supervisory authorities of the Banking Union, and its sub-groups. Latvijas Banka also participated in the Advisory Technical Committee of the ESRB and its working groups, providing input on drafting policy and analysis documents, and preparing opinions at the EU level.

Latvijas Banka shared its experience on topical macroprudential policy issues like incorporating sustainability factors into Latvia's DSTI and DTI ratios with other national central banks, when it participated in the NBMF BBM working group and the NBMF research event in Tallinn, and at the ECB and the ESRB, and an international conference in Bratislava organised by the international think tank Bruegel and Národná banka Slovenska.

⁶ A cooperation group bringing together central banks, supervisory and resolution authorities and ministries of finance of the Nordic and Baltic countries for the purpose of cross-border crises coordination, information exchange and its generation.

Latvijas Banka worked with Professor Dalvinder Singh of the University of Warwick in 2023, and the results of this collaboration were a discussion of the research on Exogenous Shocks and ECB Significant-Bank Risk Profile: Rethinking Crisis Management Frameworks, and debates about exogenous shocks and consultations on Latvia's insurance sector, while a round table discussion Exogenous Shocks and European Banks: Does Crisis Preparedness and Crisis Management Need Rethinking? was held in Warwick.

Latvijas Banka continued to participate actively in the work of the international NGFS network by helping develop the concept of short-term climate scenarios and prepare the [Conceptual Note on Short-Term Climate Scenarios](#).

Latvijas Banka's research on stress testing of flood risks was presented to the Physical Risks Group of the NGFS.



Financial sector supervision

Licensing developments

There were minor changes in the banking sector. On 10 March 2023, the ECB took the decision to withdraw the licence of Baltic International Bank SE, and after the licence was withdrawn, the bank went into liquidation. On 24 January 2024, insolvency proceedings for the bank were announced.

There were also minor changes at cooperative credit unions as the licence of the cooperative credit union AVOTS 37 was withdrawn in 2023 at the decision of the general meeting of its members.

Six new insurance brokers were registered in the insurance sector in 2023. They were SIA CREDEO, SIA Moller Auto Insurance Services, limited liability company HWCA, Inchcape Insurance Services SIA, limited liability company FIRST BROKER, and Mango Insurance SIA. The entry of SIA E-agents in the register of insurance and reinsurance brokers was cancelled in 2023. The Lithuanian insurance corporation INV L Life uždaroji akcinė draudimo bendrovė, operating in Latvia through a branch, handed over all of its insurance contracts to Gyvybes draudimo UAB SB draudimas, another insurance corporation licensed in Lithuania, on 1 December 2023. The Latvian branch of INV L Life, uždaroji akcinė draudimo bendrovė discontinued its operations as of 1 December 2023. Gyvybes draudimo UAB SB draudimas opened a branch in Latvia on 15 September 2023, and continues operations in Latvia through its branch following the transfer of the insurance contracts from INV L Life uždaroji akcinė draudimo bendrovė.

One new licence to operate as a payment institution was issued in 2023 to SIA JOOL PAY, while two payment institution licences were withdrawn. The licence of SIA Nordigen Solutions was withdrawn at the company's application, and the licence of SIA Baltic Payment Solutions was withdrawn because it had not been operating as a payment institution since September 2021, and it had no holdings of customer funds and no liabilities to customers.

A licence as an electronic money institution was issued in 2023 to SIA xpate. The licence gives it the right to issue electronic money and to provide several payment services that are set out in the licence. Registration was withdrawn for one electronic money institution, AS LatCard, at its own application requesting that its registration in the register of electronic money institutions be cancelled. AS LatCard had no liabilities to its customers, who were electronic money holders.

There were several new entrants in the investment services market. A licence was issued in 2023 to SIA Nectaro, and at the end of the year, authorisation to open a branch in Latvia was granted to UAB FMI INV L Financial Advisors. Authorisation for the operation of the AK JENSEN NORWAY AS branch in Latvia was withdrawn in 2023.

A licence to provide investment services was granted to VAIRO IPAS in 2023, while the licence of the joint stock company Rietumu Asset Management investment management company was withdrawn.

Three new alternative investment fund managers were registered in 2023, and they were SIA Merito Real Estate Management AIFP, SIGNET ASSET MANAGEMENT LATVIA IPS, and SIA ASP Asset Management AIFP. During the year, the licence of one alternative investment fund manager, SIA 2B Capital AIFP, was withdrawn. The licences of the joint stock company BIB Alternative Investment Management and the joint stock company AIFP Baltic Asset Management were also withdrawn.

SIA BALTTOMS was registered in the register of foreign exchange trading companies in 2023, while the entry of SIA VIAL in the register of foreign exchange trading companies was cancelled.

Crowdfunding service providers are a new and gradually developing sector, and an authorisation in the sector was granted to SE Capitalia in 2023. Towards the end of the year, another authorisation process was started for SIA LANDE Platform.

Microprudential supervision and compliance monitoring

Latvijas Banka had set five priorities for supervision of the financial market in 2023, which were macroeconomic and geopolitical risks, operational and financial resilience, transition risks, ML/FTP and sanction risks, and protection of consumers of financial services. The financial sector continued to face challenges in 2023 from managing the risks of sanctions circumvention while still preserving a risk-based approach. Latvijas Banka worked to ensure that the two areas were in balance and that honest customers had access to the financial services they needed



Santa Purgaile

Deputy Governor of Latvijas Banka

Supervision of credit institutions

Latvijas Banka regulates and oversees the Latvian credit institution sector in close cooperation with the ECB within the framework of the ECB's Single Supervisory Mechanism (SSM), and with European supervisory authorities following the best international practice and the fundamental principles of supervision of credit institutions.

The primary principle of supervision is that problems in the financial market or the operations of individual market participants should be identified as early as possible so that the supervisor can give their opinion and recommendations promptly or demand that the problems be resolved or mitigated.

Latvijas Banka further reinforced the supervisory framework for credit institutions in 2023 to ensure a comprehensive supervisory process and to foster the operation and development of a stable and resilient credit institution sector.

Supervisory priorities of credit institutions

Latvijas Banka performed comprehensive and consistent supervision of credit institutions in 2023. To take appropriate actions that match the supervisory priorities of Latvijas Banka while applying a risk-based approach, supervisory programmes were developed for individual market participants together with a plan for horizontal activities. Close attention was paid to the principle of proportionality and better application of it in supervisory processes.

The credit institutions sector continued to have to operate in a highly uncertain environment in 2023. The escalation of events in the Middle East meant that geopolitical risks, which had previously mainly caused by Russia's full-scale invasion of Ukraine, remained strong. Macroeconomic risks, particularly those caused by soaring inflation and rising interest rates, warranted further in-depth monitoring of the credit risk and sanctions risk faced by credit institutions and of their operational risk management. Meanwhile, the failure of two major regional credit institutions in the US financial sector drew increased attention to liquidity risk management.

The capital buffers built by credit institutions and the efforts of previous years to strengthen the sustainability of their business models, which included having reduced or initially small exposures to jurisdictions affected by the current geopolitical risks, supported the financial resilience of credit institutions and their capacity to absorb the shocks they faced. The prevailing risks appeared to have no significant effect on asset quality.

The year 2023 saw some changes in the list of participants in Latvia's credit institution sector. In addition to the tendency towards consolidation observed previously, a new market player announced its interest in joining the credit institution sector. New market entrants can be expected to strengthen competition in the credit institution sector.

Following risk assessments of credit institutions and taking account of the priorities set by the ECB and the EBA, the 2023 supervisory priorities for credit institutions were set:

- | | | | |
|---|---|---|---|
| 
1
Priority | Macroeconomic and geopolitical risks with a focus on: <ul style="list-style-type: none"> – the impact of Russia's war in Ukraine; – rising interest rates and inflation and the associated changes in asset value. | 
2
Priority | Operational and financial resilience with a focus on: <ul style="list-style-type: none"> – resilience to crises in the management of credit risk and other risks; – ICT risks; – data quality. |
| 
3
Priority | Transition risks with a focus on: <ul style="list-style-type: none"> – sustainability risks; – digital transformation; – business model change. | 
4
Priority | ML/FTP risks and sanctions risks with a focus on: <ul style="list-style-type: none"> – ML/FTP risk management; – practical application of a risk-based approach in ML/FTP risk management; – sanctions circumvention risk management. |
| 
5
Priority | Protection of the consumers of financial services with a focus on: <ul style="list-style-type: none"> – access to financial services and the protection of customer funds. | | |

The supervisory activities plan that was developed from the supervisory priorities included on-site and off-site activities both at individual credit institutions and at the level of the whole sector. Supervisory dialogues were held on fulfilling financial projections and the progress made in implementing business models, the framework for internal governance, the impact of the geopolitical and macroeconomic environment, and sustainability issues.

The potential and actual effect of **macroeconomic and geopolitical risks** on asset quality and the approach of credit institutions to integrating those risks into the most significant processes and documents came under closer scrutiny. Targeted inspections were carried out at some credit institutions where exposure to those risks had been detected, so that the impact of geopolitical and macroeconomic risks on asset quality could be assessed.

The focus in **operational and financial resilience** was on the quality of the recovery plans of credit institutions, and the quality of their ICT risk and credit risk management. The approach to the management of non-performing loans and the improvements made in it at credit institutions with large exposures to non-performing loans were discussed in focused supervisory dialogues. Latvijas Banka assessed the management and organisation of the internal audit and compliance control functions in less significant institutions within the framework of a horizontal review, and also the effectiveness of those functions and the adequacy of the resources allocated. The review identified some gaps and weaknesses as well as some examples of good practice. Following the results of the review, several supervisory expectations for the processes assessed were formulated and were discussed with the Finance Latvia Association in December 2023. On-site inspections were carried out at individual credit institutions into the regulatory compliance of their internal capital adequacy assessment process.

The focus with **transition risks** was on sustainability and the challenges of the digital transformation. Less significant credit institutions conducted a self-assessment of sustainability for the third consecutive year, tracking the progress made in integrating issues of sustainability into the operations of the credit institutions and monitoring the self-assessment of compliance with supervisory expectations. Surveys and dialogues about the digital transformation were used to identify the credit institutions that are more open to it and how they track their progress towards their objectives for it.

Latvijas Banka focused in the **protection of consumers of financial services** on the two important points of [providing critical financial services when there is a threat to national security](#), and reducing financial fraud.

The best practices for detecting and preventing financial fraud that are applied by significant credit institutions were identified, as were the risks associated with any possible gaps and weaknesses in those practices, and feedback and recommendations for improvements in preventive measures were given to credit institutions.

Focus on clear communication of the supervisory approach and supervisory expectations

In 2023, Latvijas Banka continued to improve cooperation with the institutions supervised, and to promote practices with a tighter focus on providing support and advice, and communicating the supervisory approach and expectations. The most significant work was carried out in diversity and business strategy.

Experts analysed the diversity practices of the boards and councils of credit institutions, and the best practices and gaps were identified and supervisory expectations were formulated as a result. An extensive discussion was held in November with both significant and less significant credit institutions in the sector. A summary and findings have been also published on the Latvijas Banka website under a section on [Inspection results and the best practice](#).

In 2023, recommendations were also made on the scope and quality of credit institutions' strategy documents, the process of strategy definition and its management.

Recommendations were also made in 2023 about the scope and quality of the strategy documents of credit institutions, and the process of defining and managing strategy.

With a view to improving supervisory transparency further, the practice of publishing the results of horizontal activities was introduced, which including releasing the most significant findings,

conclusions and recommendations on Latvijas Banka's website, launching the section on [Inspection results and the best practice](#), and communicating those results to market participants individually.

Supervisory Review and Evaluation Process (SREP)

Latvijas Banka conducts regular assessments of credit institutions' risks within the framework of the SREP taking a risk-based approach and applying the principle of proportionality. The risk assessment:

- analyses the quantitative indicators characterising the level of risk and their thresholds using the ECB's methodology;
- analyses the information on risk management found during on-site inspections, thematic and horizontal reviews;
- uses the information at Latvijas Banka's disposal about regulatory compliance at credit institutions, the gaps identified in internal control systems, the quality of capital and the liquidity adequacy assessment process, and the assessment of the recovery plan.

Overall, the process follows the EBA Guidelines on SREP and the ECB guidelines on SREP for credit institutions. No significant changes were made in the methodology in 2023 from the previous year, while sustainability aspects continued to be integrated into the SREP.

The supervisory priorities for 2023 and the individual supervisory programmes of credit institutions led Latvijas Banka to focus on the following risks and areas within the framework of the SREP:

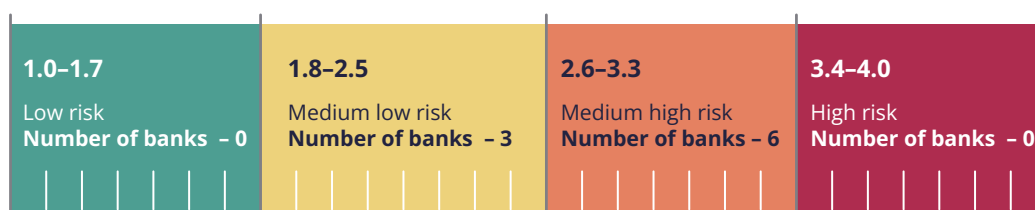
- the resilience of business models, through assessment of their viability, profitability and sustainability, given the current macroeconomic and geopolitical conditions;
- the framework for internal governance and risk management, particularly the quality of the compliance and internal audit functions;
- the level of credit risk and the measures to mitigate it, particularly where this concerned risk management practices, given the current macroeconomic and geopolitical conditions;
- liquidity risk, particularly funding concentration and risk management practices following the failure of two major regional credit institutions in the US.

In 2023, the following requirements were set for nine credit institutions, including the credit institutions under direct ECB SSM supervision, within the framework of the SREP:

- own funds requirements to cover the risks inherent or potentially inherent in their business;
- recommended capital buffer requirements (P2G).

The overall SREP score is assigned between 1 and 4, and the following risk scores were assigned to Latvia's credit institutions, including those under direct ECB SSM supervision, in 2023:

Chart 17. Risk scores within the framework of the SREP in 2023



The risk scores were broadly unchanged from the previous year. Credit risk, internal governance risks, and ICT and ML/FTP risks remain the highest risks in the credit institution sector, largely because of the geopolitical and macroeconomic risks.

In addition to the quantitative requirements, a number of qualitative requirements and recommendations were made within the framework of the SREP, and they will make a further contribution to improving the internal control systems of credit institutions and strengthen their resilience to shocks. They were mainly focused on internal governance, ensuring sustainability, credit risk management, capital adequacy planning, and operational risk management, including management of ML/FTP risk. There were 28 quantitative requirements and 40 recommendations issued to credit institutions within the framework of the SREP.

Single Supervisory Mechanism

The ninth anniversary of the establishment of the SSM, the European banking supervision system, fell on 4 November 2023. The SSM comprises the ECB and the national competent authorities of the euro area, which are the central banks and national supervisory authorities of the Eurosystem. Latvijas Banka is also a part of the SSM, and the main objectives of the SSM are:

- to ensure the safety and soundness of the European banking system;
- to increase financial integration and stability;
- to provide consistent supervision.

At the turn of 2023, there were 113 significant credit institutions under the direct supervision of the ECB, and 1956 less significant credit institutions under the direct supervision of the national competent authorities.

Three credit institutions in Latvia, Swedbank AS, AS SEB banka and AS Citadele banka, remained under the direct supervision of the ECB in 2023. Supervision of those credit institutions was carried out by the ECB and Latvijas Banka staff members working together in the Joint Supervisory Teams that are the basis for the routine supervision of significant credit institutions. Latvijas Banka staff also participated in the on-site inspections of the significant credit institutions by the ECB.

Latvijas Banka continued to supervise the less significant credit institutions in 2023 in close cooperation with the ECB and in communication with the EBA, in order to ensure consistent supervision throughout the European banking sector and promote the safety and sustainability of credit institutions and the stability of the financial system.

Experts from Latvijas Banka continued to play a part in the committees and working groups of the ECB in 2023, helping improve the ECB's common supervisory methodology and to align various regulatory frameworks within the European Banking Union.

Like other European supervisors, the ECB's SSM continued to implement supervisory processes and activities, increasing confidence in the ability of credit institutions to withstand macro-financial impacts, including the consequences of high inflation and high interest rates. The supervisors have monitored closely the evolution of the quality of credit institutions' loan portfolios and the build-up of sufficient provisions, the strengthening of governance structures, the solutions to the challenges associated with digitalisation, and the efforts made to ensure compliance with climate-related supervisory requirements.

Participation in decision-making at the ECB's SSM

The Latvijas Banka representative on the ECB's Supervisory Board participated in the SSM's decision-making process for significant credit institutions under the direct supervision of the SSM and for the methodology governing the supervision of euro area credit institutions.

The ECB's SSM adopted 2403 supervisory decisions in 2023. Like in previous years, about half of those decisions were approved at the meetings of the ECB's Supervisory Board, while the other half were taken by written procedure.

The bulk of those decisions were the 48.4% that related to the fit and proper assessments, the 9.6% on own funds, the 7.9% on national powers, 7.7% on internal models, 4.7% on the SREP, and 4.7% on reporting.

Supervision over cooperative credit unions

The supervision of cooperative credit unions in 2023 was carried out by monitoring their performance results using analysis of their financial statements, with a particular focus on checking whether the loan loss provisions set aside by the cooperative credit unions are sufficient to cover possible losses, and by carrying out on-site inspections. Latvijas Banka's auditors carried out three on-site inspections during the reporting year to assess the financial standing, management performance, asset quality, income and expenditure composition of the cooperative credit unions, and also their regulatory compliance.

The licence of one union was withdrawn at its own decision within the framework of supervision of cooperative credit unions.

Insurance supervision

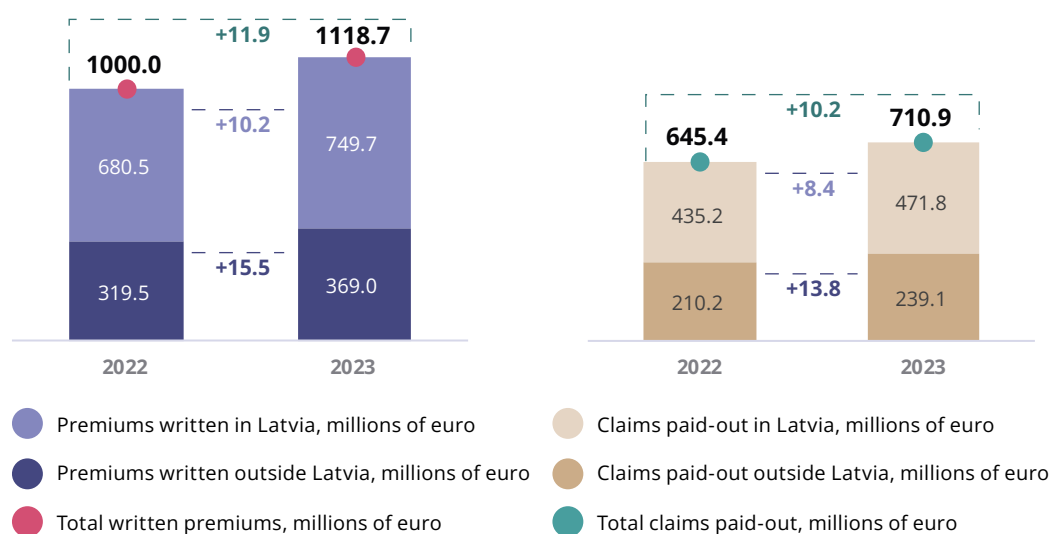
Insurance premiums and claims continued to increase in the insurance market

There were 17 insurers in Latvia at the end of 2023, as there were two life insurance companies and four non-life insurance companies, and 11 branches of insurers from other European Union countries, of which four were branches of life insurers and seven were branches of non-life insurers. The register of insurance and reinsurance brokers maintained by Latvijas Banka contained entries on 81 insurance and reinsurance brokers, which is five more than at the end of 2022.

Premiums written in Latvia's insurance sector increased by 10.2% in 2023, while the claims paid out grew by 8.4%. As high inflation gradually abated in 2023, its effect on insurance services also diminished, and so the rate of growth for insurance premiums and claims was lower in 2023 than in 2022, when the premiums written increased by 15.9% and claims grew by as much as 23%.

The global growth of the insurance sector is confirmed by developments in insurance premiums written abroad by the six insurance undertakings registered in Latvia. Their premiums written in Lithuania, Estonia, Poland, France and Italy increased by 15.5% and their claims paid out by 13.8% in 2023.

Chart 18. Gross premiums written and claims paid-out by insurers (amount; millions of euro; annual growth; %)



The high inflation of the past two years pushed up both the prices of insurance products and the claims paid out. Inflation had a direct effect on the size of insurance claims, fuelled by rising construction costs, and higher prices for spare parts and repairs of vehicles, and for healthcare and medical services. That was taken into account when insurance products were priced, and in most cases the prices to be paid by customers increased. The most significant rises in insurance premiums in 2023 were of 21.1% for health insurance and 19.4% for land vehicle insurance.

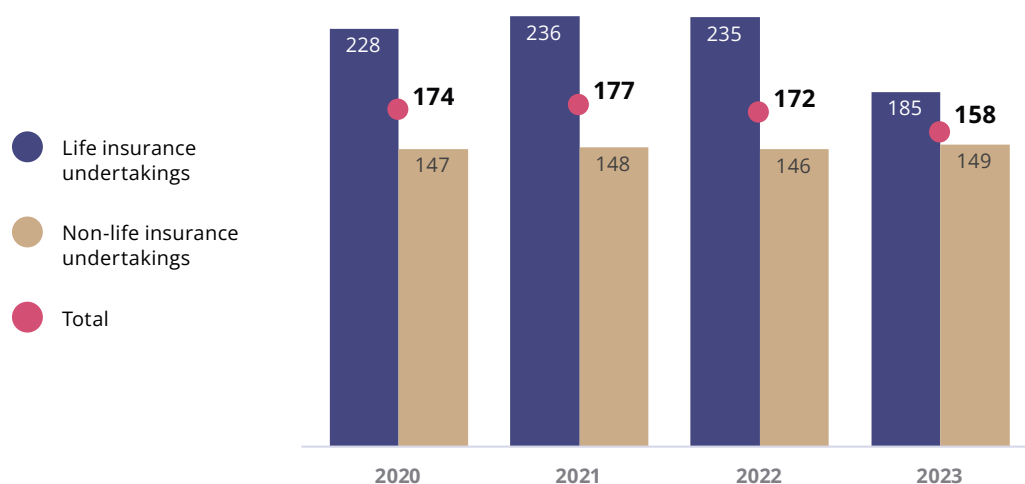
The biggest increases in claims paid out were of 43.7% for property insurance and 14.6% for health insurance. Property insurance claims increased under the influence of inflation in 2023, but also because a larger number of claims were made as climate risks materialised as floods and storms.

The year 2023 was unfavourable for the life insurance segment as the premiums written in Latvia decreased by 18.9% over the year. The most notable fall in the premiums written was of 38% in annuity insurance, as changes in the conditions for pension disbursement meant fewer people in Latvia chose to transfer the capital accumulated to life insurers and receive their pensions from them after retirement. The impact from the uncertainty caused by the tense geopolitical situation and high inflation on the population's purchasing power meant there was less willingness to build up long-term savings, and so contributions to life insurance with savings decreased.

Inflation also caused a steep increase in interest rates, which made the insurance companies reconsider the composition of their investment portfolios. The financial results of the insurance companies were positive in 2023, and the six insurers between them closed the year with a profit of 44.4 million euro.

The insurance companies registered in Latvia also continued to maintain stable, albeit lower, solvency capital ratios that were higher than the minimum requirement. The ratio was 158% at the end of 2023, while the minimum limit is 100%.

Chart 19. Solvency capital ratios of insurance undertakings (%)



The supervisory focus on market conduct risk has consumer protection at heart

Supervisors are paying ever more attention to consumer protection because of the rapidly changing external environment with high inflation, volatility in financial markets, increasing risks from natural disasters and climate change, and the digitalisation of financial services.

Evija Dundure

Head of the Insurance and Pension Supervision Department



Supervisors are paying ever more attention to consumer protection because of the rapidly changing external environment with high inflation, volatility in financial markets, increasing risks from natural disasters and climate change, and the digitalisation of financial services.

To provide an adequate level of protection to their customers, insurers and insurance distributors must have an [effective product oversight and governance process](#) and must reinforce the trust of their customers by [offering clear and understandable information about the financial products and the service provider](#). Regulatory requirements oblige insurers to develop products that meet the needs of their customers and also to make sure constantly that their products are still appropriate for their target market and suit the needs and demands of their customers. Moreover, customers with different levels of financial literacy should be able to understand the information they get about the insurance services however it is distributed, be that through digital communication or through a consultant.

Insurance products meeting the needs of customers

Special attention within the framework of continued supervision of product oversight and governance was paid in 2023 to the value for money that life insurance with savings offered customers. Latvijas Banka's reviews detected an elevated risk that some unit-linked life insurance products were failing to provide value for money in their net return on investment. This was because of the quite weak performance of the underlying investment funds in the previous period, and the relatively high total cost of the product for the customer.

Latvijas Banka carried out targeted supervisory work at specific insurers, and reminded all insurers about the importance of considering a product's value for money for customers during the process of product design and distribution.

Sufficiency of insurance cover in face of macroeconomic shocks

Given the spike in inflation over the last two years, Latvijas Banka analysed not only how it had impacted the solvency position of insurance companies, but also whether the amounts insured remained consistent with current cost of property restoration. Both the insurers and the insured themselves need to pay close attention to the amount insured that is given in a property insurance contract. The analysis shows that the amount insured in insurance contracts does not always correspond to the estimated cost of restoring the property insured. This creates the risk that if there is an accident, the potential insurance indemnity will not cover the total costs of property restoration.

for the owner. As a result of the supervisory work, all the insurers brought the amounts insured in line with the current costs of restoration, thereby protecting the insured against unforeseen losses. Insurance providers and distributors certainly need to continue to offer appropriate insurance cover and sums, but the customers themselves also need to pay close attention to the terms and conditions of their policies.

Completeness of information provided to customers

As customers are becoming increasingly inclined to buy insurance online, it is important to be sure that the information provided to them in the digital environment is timely and of high quality.

As part of its continued monitoring of the compliance of information disclosures with the regulatory [requirements for insurance brokers](#) that started in 2022, Latvijas Banka inspected the digital distribution sites of insurers, insurance agents and ancillary insurance intermediaries in 2023. The overall conclusion was that the requirements for the disclosure of information to customers were not being fully complied with. Often they were complied with only formally, as the information was difficult to understand, and the information displayed on digital distribution websites was not updated regularly. These shortcomings detected by the inspection have since been eliminated, and the implementation of Latvijas Banka's [recommendations to the insurers](#) can be expected to result in customers understanding better the insurance services they receive.

To provide customers with product information that is easy to read, understandable and comparable across products, insurers must produce a standardised information document for non-life insurance products that lets their customers take informed decisions. Latvijas Banka carried out a thematic review of the regulatory compliance of information documents for travel insurance products by assessing the scope and quality of the information provided to customers and the design of the documents.

The [findings](#) about the improvements that were needed to some aspects were communicated to all the market participants involved.

Dialogue to promote meaningful changes

Latvijas Banka maintained its dialogue with the insurance sector and continued the tradition of organising annual strategy meetings with the management of all the insurers operating in Latvia. During the meetings, the strategic development priorities of the insurers were discussed, the findings from the supervisory work were analysed, and the individual risk scores allocated by Latvijas Banka to each market participant were communicated to the insurance companies and branches of foreign insurers. [The supervisory priorities and the supervisory activities scheduled for 2024](#) were also communicated to the insurers.

Supervision of pension and investment funds

Supervision of the second pillar pension managers

Competing for customers and searching for higher returns

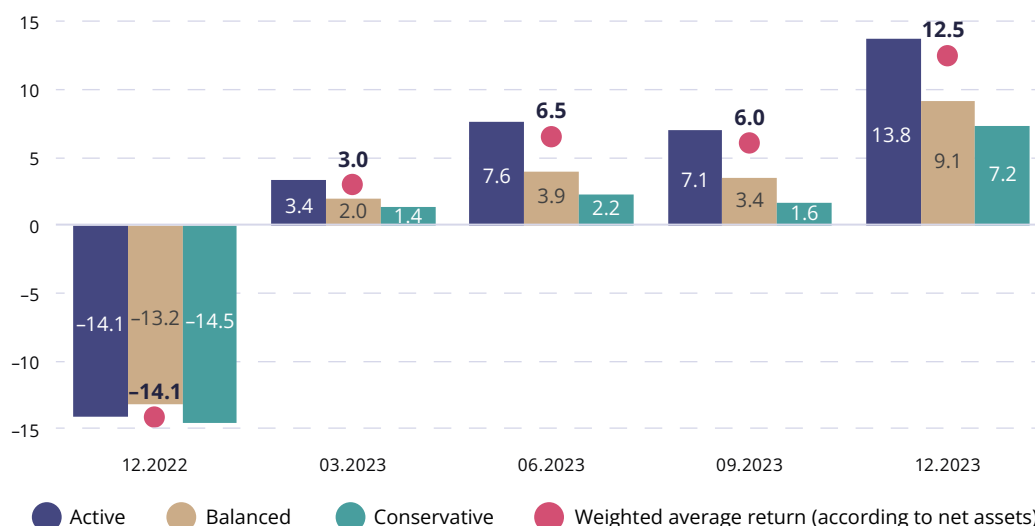
One more asset manager joined the managers of the second pillar state-funded pension scheme assets in Latvia in 2023, and there are currently eight managers. A licence to manage the assets of the state-funded pension scheme was granted to a new market player, VAIRO AS. Meanwhile, Integrum Asset Management IPAS was renamed Signet Pensiju Pārvalde IPAS following a change of ownership.

As at the end of the year there were 33 investment plans with varying degrees of risk on offer to pension savers to manage their second pillar pension capital. Most of the investment plans, almost 70% of them, were active investment plans with higher long-term returns than the balanced and conservative investment plans, allowing their participants to accumulate larger additional pension capital in the long term.

The number of participants in active pension plans is increasing rapidly year by year, and one of the reasons for this is [the changes in regulatory requirements](#) initiated by Latvijas Banka that assign all new participants of the state-funded pension scheme as of 1 January 2023 to active investment plans, where up to 100% of the investments are made in equities. As of 1 January 2026 moreover, all new participants who have not made their own choice will be assigned to one of the investment plans that have demonstrated the highest returns over the past three years, with half of the managers included in the allocation.

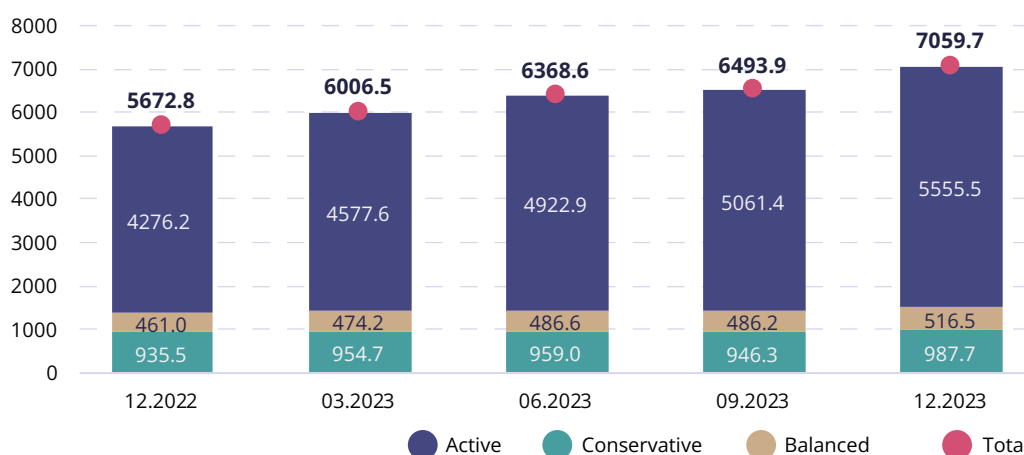
Life-cycle investment plans became increasingly popular in 2023. These plans automatically balance the participant's age against the proportion of equities in the investment portfolio, so that there is a reduction in equities, and consequently in risk, as the participant approaches retirement age.

Chart 20. Return on state-funded pension plans (%)



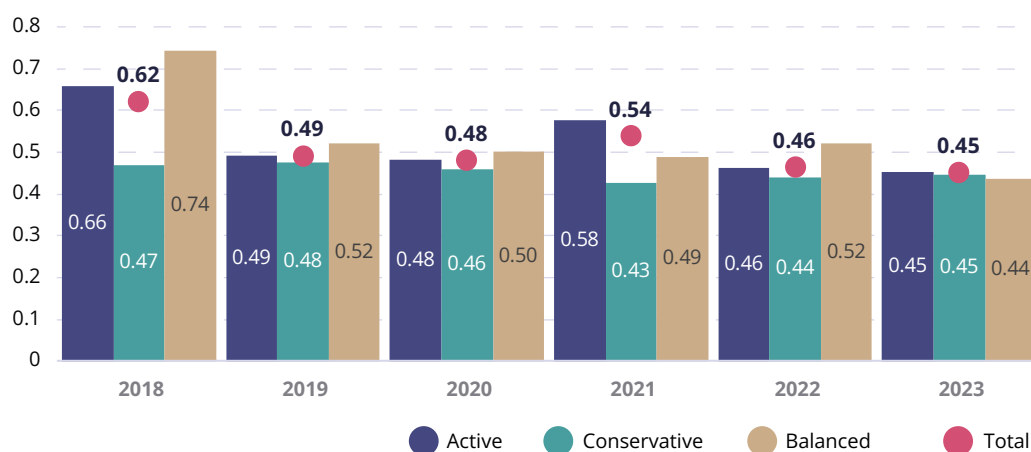
The year 2023 was one of the historically most successful years in the management of second pillar pension assets. It was marked by large returns for all types of investment plan, which helped to reduce significantly the negative effects that the financial market had had on asset values in 2022.

Chart 21. Developments in net assets of the state-funded pension scheme (millions of euro)



The value of assets reached 7.06 billion euro in 2023, which was an increase of 24.5% from 2022. The increase was particularly impressive at 35.9% for the assets accumulated in active pension plans.

Chart 22. Investment plan management expenses (%)



Management fees did not change significantly in 2023. Since [limits on management fees](#) came into force in 2018, the management costs of investment plans as a share of total assets have stabilised, and there is a slight downward trend as asset levels increase.

Larger contributions to second pillar pensions mean a larger pot of accumulated pension capital

Every participant in Latvia's second pillar pension scheme has the right to change their fund manager once a year and to switch between investment plans twice a year. At the end of 2023 however, more than half a million people in Latvia had opted for an investment plan that was inappropriate for their age.

More active involvement of the participants in the state-funded pension scheme in choosing appropriate investment plans could be achieved by managers providing more detailed disclosures and consultations to participants, which would also increase the financial literacy of participants. Latvijas Banka consequently [amended the legislation](#) in 2023, setting managers the obligation to make sure that the investment plans selected by pension scheme participants are suitable for their age and preferences. This represents a fundamental change in the role of managers in engaging with participants. In addition to that, a procedure was established for asset managers to identify the preferences and needs of participants so that they could offer them the most appropriate investment plans. These changes are expected to increase engagement from participants and their understanding of their second pillar pensions, and the investment plans and opportunities that they offer.

Latvijas Banka introduced changes that apply from 1 January 2024 to the requirements for the basic information given to participants in the state-funded pension scheme and for the identification of their needs so that they can have clear information materials where the details of each investment plan are presented in a simple and concise way. This will standardise the information on the main details of investment plans, allowing participants to compare them, assess whether they meet their needs and preferences, and take an informed decision when choosing a suitable plan.

Latvijas Banka reviewed its cooperation with the State Social Insurance Agency in 2023. The aim was to optimise the flows of documents circulating between the two institutions, improve the transparency

of disclosures, and reduce the administrative burden, all of which would ultimately lower fees for customers. The first outcome achieved in 2023 was that the sign-off process for circulated documents was improved and the information exchange procedure in [the Cabinet Regulation](#) on the Operation of the State-Funded Pension Scheme was updated. The result of this cooperation is that participants benefit from clear, transparent and comparable disclosures in the investment plan prospectus, and participants with a higher level of financial literacy are able to use that to decide on the appropriate investment plan.

Challenges in implementation the new procedure

These new regulatory requirements grant the managers of state-funded pensions additional rights when they access participant data, but also impose new obligations on them, as they have to make sure that the investment plans selected are appropriate given the age, needs and preferences of the participant, and must provide consultation about the second pillar pensions and the performance results of their fund. The information published about second pillar pensions also needs to become more comparable, understandable and accessible.

To ensure that these changes are implemented smoothly, Latvijas Banka intends to work closely with the asset managers and the State Social Insurance Agency, overseeing the progress made, providing timely support and advice on implementation, and ensuring clear flows of information between all the parties involved.

Supervision of private pension funds and managers of third pillar pensions

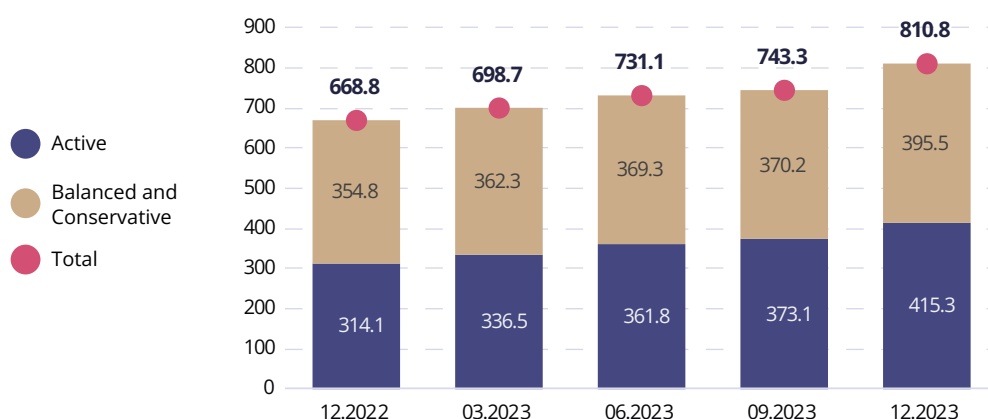
People are increasingly entrusting private pension funds with looking after their retirement savings

There were six open pension funds and one closed pension fund registered in Latvia at the end of 2023 for accumulating third pillar pension savings, between them offering 21 pension plans with various degrees of risk. The number of participants in the pension plans increased by 6.7% over the year to 412 thousand.

The net assets of the pension plans totalled 810.4 million euro at the end of the year. For the first time in their existence, the net assets of the active pension plans exceeded those of the balanced and conservative pension plans, as they increased to 51.2% from 47% in the previous year while the balanced and conservative assets fell to 48.8% from 53%.

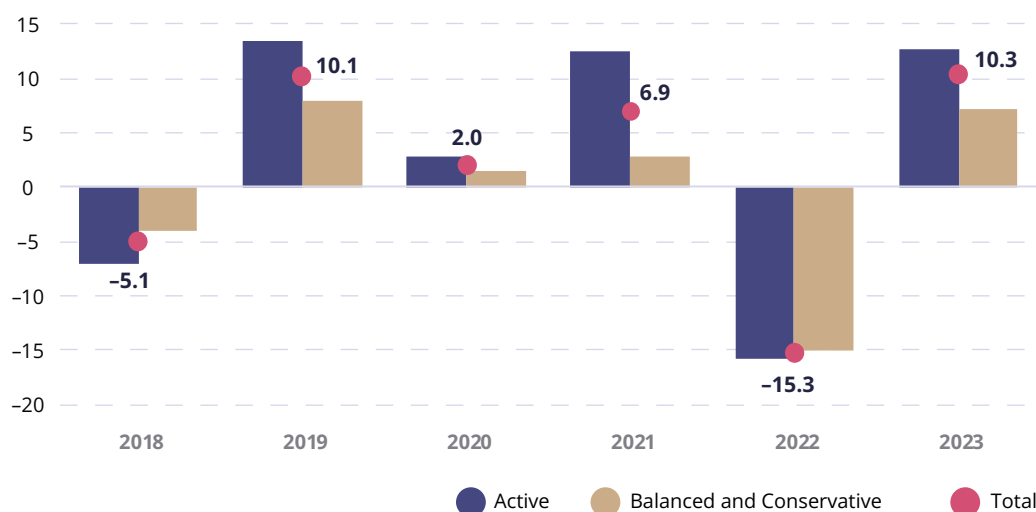
An increasing share of pension plan participants at 61.6% opted for the active investment strategy. This strategy is characterised by higher long-term returns than those of the balanced and conservative pension plans. The number of participants in the active pension plans increased by 12% in the course of the year, whereas the number in the balanced and conservative plans dropped by 2%.

Chart 23. Developments in net assets of the private pension funds (millions of euro)



The value of the total net assets of pension plans grew by 17.5%. This can be explained by the strong performance of the financial markets, which gave the participants in pension plans a weighted average annual return of 10.3%, with the returns on individual pension plans ranging from 7.1% to 17.6%. The highest average return on capital at 12.6% was produced by the pension plans that employ active strategies, followed by the return of balanced plans at 9.1% and that of conservative plans at 7.3%.

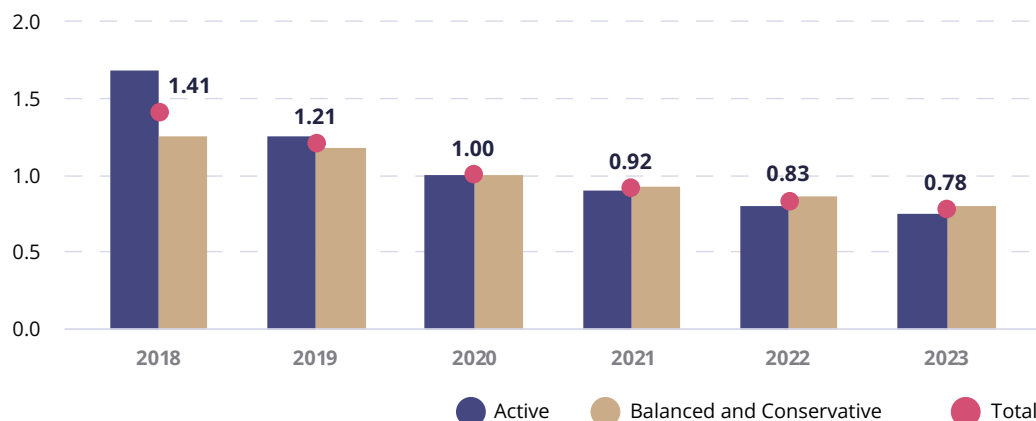
Chart 24. Annual returns of private pension plans (%)



The year 2023 was also remarkable for the contributions of participants, which went above 100 million euro for the second time in the history of private pension plans in Latvia and reached 113.5 million euro.

The overall level of the pension plan management costs, combining administrative expenses and investment management costs to net assets, hit a historical low at 0.78%, down from 0.84% in 2022. The administrative expenses and the costs of investment management have been generally declining since the first quarter of 2019.

Chart 25. Pension plan management expenses in private pension funds (%)



A wider range of products and greater clarity on the expected pension amount

At the start of 2023, a new passively managed pension plan was registered, and since that point, all the open-ended pension funds offer pension plans with a 100% asset investment strategy.

The focus of private pension funds last year was on projections for pension benefits. [Regulations](#) issued under Article 39 of Directive 2016/2341 of the European Parliament and the Council on the introduction of pension benefit projections took effect in Latvia. In implementing the Regulation, private pension funds developed easy-to-use calculators for projected pension benefits or individually tailored statements that are sent each year to the participants in each particular plan to inform them about their projected retirement savings when they reach retirement age.

Latvijas Banka intends to update these regulations to reflect the experience of market participants, the lessons learned and practical recommendations, so that the projections from the private pension funds can be made even more accurate.

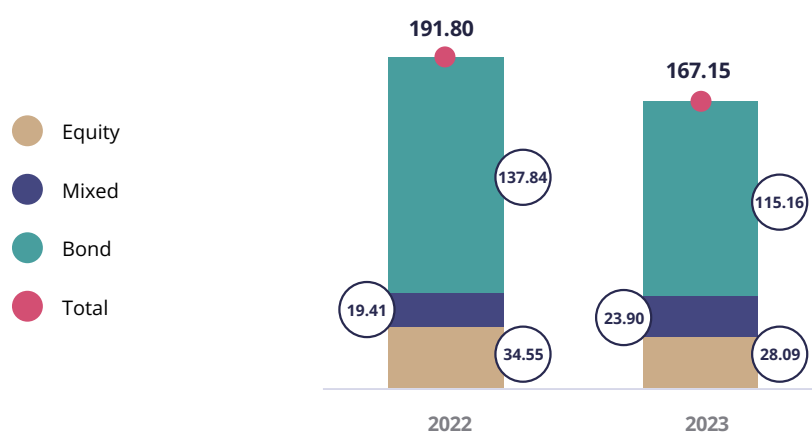
Supervision of investment funds and alternative investment funds

The segment of businesses making collective investments in transferable securities is shrinking in Latvia

There was one fewer investment management company managing businesses that make collective investments in transferable securities, or fund managers, in 2023 than in 2022, and there were three fund managers in Latvia at the end of the year managing 13 funds, which were six bond funds, four mixed funds and three equity funds.

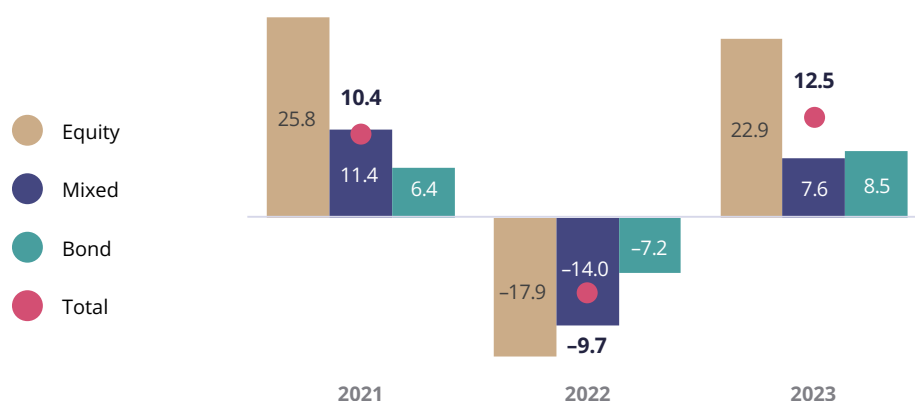
The value of the funds' net assets fell by 13% over the year in 2023 to 167.15 million euro at the end of the year.

Chart 26. Net assets by fund type (millions of euro)



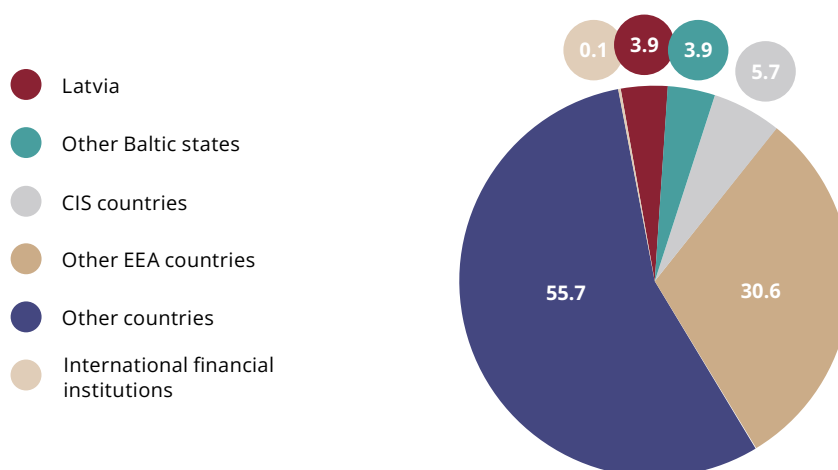
The bulk of the funds at almost 70% were bond funds, which have had lower returns in recent years than mixed funds and equity funds. The performance of the funds was significantly better in 2023 than in the previous year, when all types of fund had negative average returns.

Chart 27. Returns of investment funds (%)



Investments were mostly made in financial instruments issued in the EEA countries and the United States. The investments by funds in financial instruments from issuers incorporated in Latvia was 3.9% of their total assets. Investments in Latvia were primarily in debt securities, and these were 76% of the total value of investment in Latvia.

Chart 28. Geographical distribution of the funds' investments in December 2023 (%)



Challenges faced by the funds registered in Latvia

The biggest challenge faced by the industry in Europe, and consequently also in Latvia, is the tight competition with exchange-traded funds. The general global tendency that has already been observed for several years has been a shift of capital from actively managed funds to passively managed ones, and 2023 was a special year in this respect. [Data from the research company Morningstar](#) show the total assets of passively managed funds of about 13.29 trillion US dollars exceeded the total assets of

actively managed funds of about 13.23 trillion US dollars for the first time in the history of investment funds. The interest in passively managed exchange-traded funds can be explained by their quite simple investment strategies, as they mainly track market indexes, their low management fees, their broad selection of products, and their simplified approach that can easily be understood by the consumer. All these factors will continue to support the performance of exchange-traded funds, while at the same time posing significant challenges to the funds registered in Latvia.

Alternative investment funds and their managers

There were 31 alternative investment fund managers (AIFMs) operating in Latvia in 2023, of which 27 were registered AIFMs and four were licensed AIFMs. Three new AIFMs were registered, while the licences of two licensed AIFMs were withdrawn, and the registration of one registered AIFM was cancelled in 2023. The total number of AIFMs consequently remained unchanged from the previous year.

Although there has not been rapid development in the alternative investment sector, new players have entered the market with more dynamic and forward-looking strategies that enhance economic growth in Latvia, such as investments in houses for rent and solar parks. The dominant strategy of the funds is to invest in private equity, which accounts for about 70% of the total assets of the alternative investment funds.

The role of the supervisor in ensuring financial stability

Within its work of monitoring financial stability and stress resilience, Latvijas Banka carried out various supervisory activities in 2023 that were adjusted to the intensity of supervision in each segment supervised, the shortcomings detected by previous inspections, and the principle of proportionality:

- on-site inspections were carried out in 2023 at individual investment managers, covering SIGNET ASSET MANAGEMENT LATVIA IPS and the investment management company SEB Investment Management, and at the private pension fund AS SEB atklātais pensiju fonds and the alternative investment fund manager SIA SG Capital Partners AIFP;
- a survey of greenwashing risk management was run in AIFMs and investment management companies that manage investment in transferable securities, to see how ready the risk management systems of those market participants are to comply with the new sustainability requirements;
- thematic inspections of all supervised segments were held, with an operational compliance inspection of the core functions and an inspection of compliance with the requirements for sustainability disclosures;
- aspects of risk management, fee calculation procedures and the consistency between strategic planning and operations were also examined and assessed in addition to that, as part of the annual strategy review of Latvijas Banka.

The broad range of supervisory activities undertaken gave an in-depth insight into different operational dimensions of the market participants' business models, while also assessing how various risks impact them. This let Latvijas Banka identify several examples of good practice and potential for improving the operation of individual market participants. Latvijas Banka will continue to follow up on closing the gaps identified in 2024.

Latvijas Banka ran risk assessments at the level of individual market participants and at the sectoral level to maintain the individual supervisory approach to market participants that takes their individual features into account while also gaining a horizontal view of the performance of the whole segment and the impact of the risks from it on the Latvian financial market. The overall operational risk score is different for each manager, but the impact of the risks assessed on the financial market as a whole is

medium-low, which can be explained by the long experience of the fund managers and their relatively good skills in asset management.

The individual risk scores were communicated and explained to each market participant during individual meetings, while the sectoral risk scores were communicated at the annual meetings with the managers of market participants that are organised at the market segment level to maintain an active dialogue with the market participants supervised. During those meetings, the supervisory conclusions were also shared with the participants, and particularly important operational aspects for each market segment were highlighted.

Supervision of payment institutions and electronic money institutions

There were ten payment service providers, which covers both electronic money institutions and payment institutions, operating in Latvia at the end of 2023.

The total value of payments to payment institutions increased by 2.5% from 2022, while the average amount of each payment increased by 2.2% from 2022, but the value of payments to electronic money institutions was down by 36.9% and the average payment amount by 43.3% from 2022. Liabilities to customers, including balances on customer accounts, increased by 1.5% at payment institutions and by 10.8% at electronic money institutions over 2022.

Chart 29. Payments to electronic money institutions and payment institutions (millions of euro)

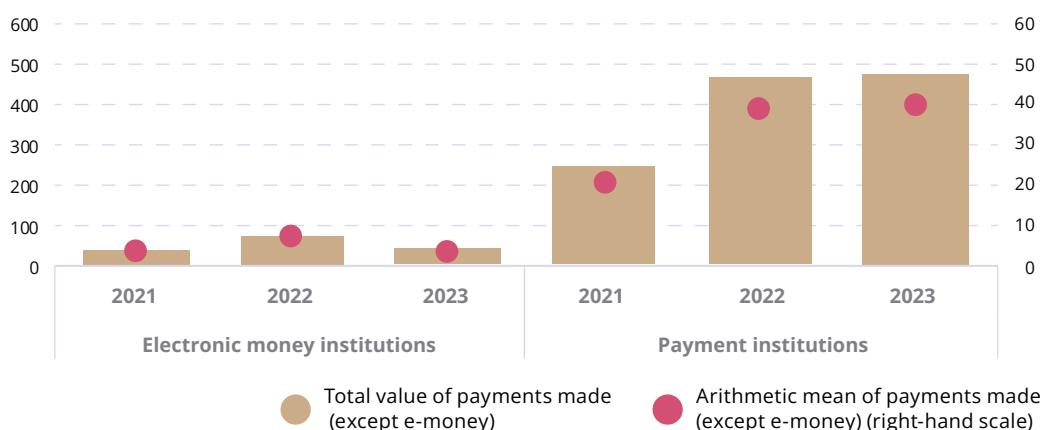


Chart 30. E-money circulation in electronic money institutions (millions of euro)

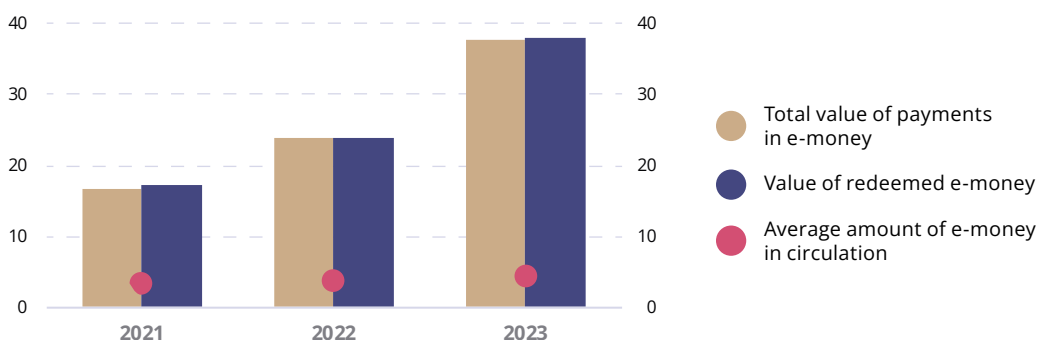


Chart 31. Liquid assets and current liabilities of electronic money institutions and payment institutions (millions of euro)

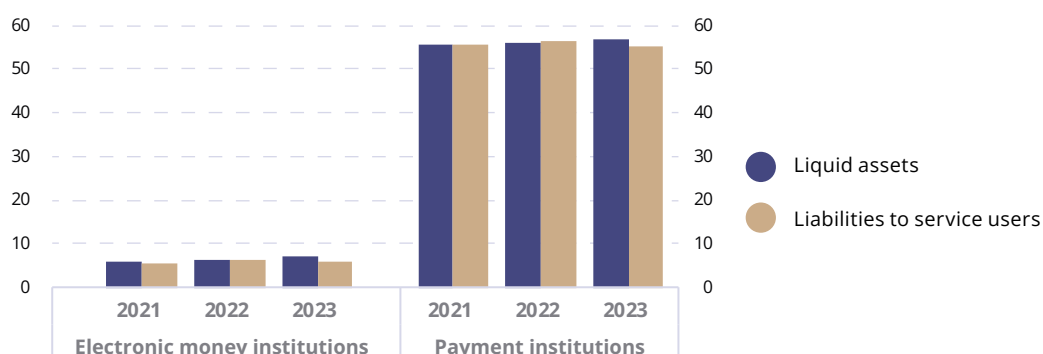
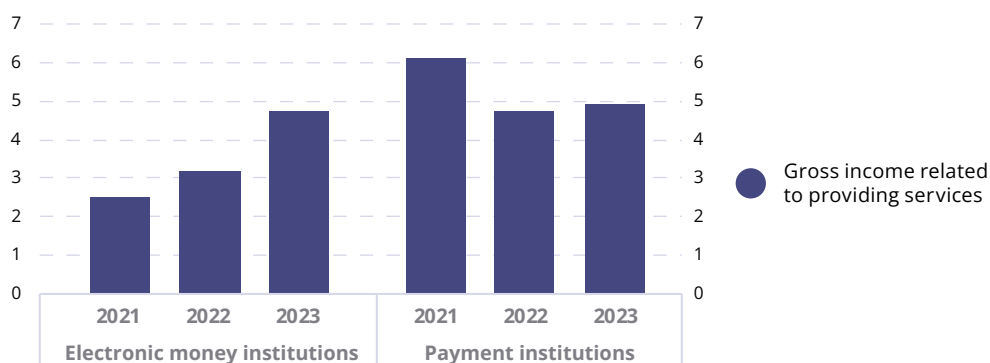


Chart 32. Income from services of electronic money institutions and payment institutions (millions of euro)



The total value of payments made with e-money grew by a significant 57% over 2022, while the total value of e-money redeemed increased by 59.1%.

The income of payment institutions edged up slightly, gaining 3.8% over 2022, while the income of electronic money institutions from the provision of services increased by a more substantial 48.1%.

A risk assessment is carried out each year in payment services as part of the supervisory process. The level of risks at Latvia's payment institutions and electronic money institutions is viewed as ranging from low to medium-high. The market participants covered by supervision in 2023 provided safe services to their customers. One full on-site inspection of the operation of a market participant was held during the year, which did not cover AML/CFTP, and off-site supervisory work was carried out at all participants to suit their risk assessments. Strategy meetings were also held with market participants on business development plans, compliance issues, internal control systems and governance. The supervisor paid particular attention in 2023 to the protection of customer funds by assessing accounting and management methodologies, data quality, business continuity risk management and other points.

The fallout from the Covid-19 pandemic has been absorbed in payment services, and the market participants have turned to working on improving their operational efficiency in response to rising inflation and costs. Significant challenges are posed by the management of ICT security and cybersecurity risks and by ensuring business continuity.

Supervision of crowdfunding service providers

Two authorisations to provide crowdfunding services had been granted in Latvia by the end of 2023, one of them to a service provider that had previously operated under the arrangement of the transitional period that expired on 10 November 2023.

Regular meetings on business development issues, and the main challenges, risks and opportunities are held with the crowdfunding service providers. The discussions in 2023 identified that the public could be interested in using the services of crowdfunding service providers to raise funding and make investments, but at the same time, investors remain quite cautious, which is typical in the startup phase of any new segment. The interests of the project owners and investors as stakeholders are continuously being analysed in consequence to ensure that the services offered evolve accordingly.

At the same time, supervisory work was also carried out to check compliance with the regulatory requirements for disclosures and the organisation of payment flows related to the provision of services.

Supervision of companies trading foreign exchange

There were 15 foreign exchange trading companies operating in Latvia at the end of 2023. One new authorisation was granted during the year, and one authorisation was withdrawn at the application of the company itself. Four new trading venues were registered for companies trading foreign exchange.

Strategy meetings on business development issues and the main challenges and risks were held during the year with the companies trading foreign exchange. They highlighted the willingness of the companies to improve the range of services provided by considering the option of offering automated solutions. Latvijas Banka gave appropriate consultation individually and together with other public institutions.

Given the geopolitical situation and the amendments to the Immigration Law, the amount of US dollars sold was 48% higher in 2023 than in 2022. This came from sales of real estate by Russian and Belarusian nationals and their conversion of euro cash into US dollars when they left Latvia. The amount of Russian roubles sold was 18% higher than in 2022, and roubles purchased was 21% higher.

One of the challenges faced by Latvia and the rest of Europe is trading in Scandinavian currencies. Correspondent banks either limit the amounts they accept or refuse to accept those currencies at all because it is difficult to gain sufficient assurance that the AML/CFTP requirements are being adequately met, making it difficult for foreign exchange trading companies to trade in those currencies. Within the framework of supervision, the balances of those currencies held by Latvian companies trading foreign exchange were identified and communicated to the central banks of the countries concerned. The companies trading foreign exchange were invited to assess the risks associated with exchanging cash in those currencies and holding cash in them, and to adjust their holdings to reflect their ability to manage the risks associated with trading those currencies.

Additionally, a survey was conducted and discussions were held on the access to banking services of companies trading foreign currency. Latvijas Banka used the survey results to develop an action plan to promote access to banking services for companies trading foreign currency. The most important task is to develop a new methodology for risk analysis and present a sectoral risk assessment to credit institutions each year. Joint discussions with industry representatives and individual meetings with market participants will also be held to discuss their areas of operation, business models, challenges to the community and the sector, and opportunities for development.

Supervision of investment service providers

At the end of the reporting year, authorisation to provide investment services in Latvia had been granted to nine investment firms licensed in Latvia, nine credit institutions registered in Latvia and one branch of a credit institution from an EU Member State, and also to seven investment management companies registered in Latvia. In accordance with the principle of freedom to provide services, more than 600 investment service providers from EEA countries also had the right to provide investment services.

One new licence was granted to an investment firm in 2023. Latvijas Banka also continued to engage actively with the investment platforms licensed as investment firms and subject to a transition period by following up on the implementation of the measures planned for the transition period.

Supervision of investment services was focused on the following issues in 2023:

- development of the SREP methodology and conducting the SREP at one investment firm;
- in-depth inspection of three individual market participants, which were two investment firms and one credit institution;
- a horizontal review of the operational integration of customers' sustainability preferences at investment service providers;
- integration of the sustainability risks of investment firms into the risk management framework and questions about sustainability disclosures;
- participation in the ESMA's common supervisory action on marketing communications and advertising;
- evaluation of the reports submitted by market participants and data quality control;
- addressing complaints about investment service providers.

Supervision of the trading venues for financial instruments and the Central Securities Depository

The focus in supervision in 2023 of the stock exchange run by the regulated market operator Nasdaq Riga and the multilateral trading system or alternative market First North Latvia was on:

- on-site operational inspection of the stock exchange;
- pre-trade and post-trade disclosures;
- cooperation in the context of new issuers entering the market and issuers leaving the market;
- the means to ensure adequate trading in financial instruments;
- supervision of trading in financial instruments;
- the operational adequacy of information technology systems and the prevention of incidents;
- assessment of the compliance of the regulations and decisions of the stock exchange.

In 2023, supervision of the Central Securities Depository Nasdaq CSD SE focused on:

- the annual Review and Evaluation in accordance with Article 22 of Regulation (EU) No 909/2014 of the European Parliament and of the Council of 23 July 2014, covering financial stability, business risk, capital requirements, operational risk, business continuity risk, legal risk, evaluation of the operation of the securities settlement system, the functioning of links, incident management, cyber resilience, recovery plans, internal control systems, governance, the availability of the core CSD services, outsourcing, disclosures, external audit assessments, and default procedures for CSD participants. No recommendations were issued to the depository following the assessment;

- regular off-site supervisory activities, covering evaluation of the statements, reports and other information submitted, and meetings with the staff of Nasdaq CSD SE;
- cooperation within the Nasdaq CSD SE supervisory college between the supervisory authorities and the central banks of Lithuania, Estonia and Iceland, and Latvijas Banka. Two meetings of the supervisory college were held in 2023.

Supervision of issuers

The focus in supervision of issuers in 2023 was on:

- the timely disclosure of regulated information;
- observation of the placement process for initial public offerings;
- a horizontal review of the lists of managers and people closely associated with them;
- a horizontal review of the conduct of shareholders' meetings;
- an in-depth inspection of annual statements and interim reports;
- disclosure of corporate governance notifications and remuneration reports, and non-financial disclosures;
- assessment of the compliance of prospectuses for public offerings;
- webinars and presentations on the application of regulatory requirements;
- sustainability issues.

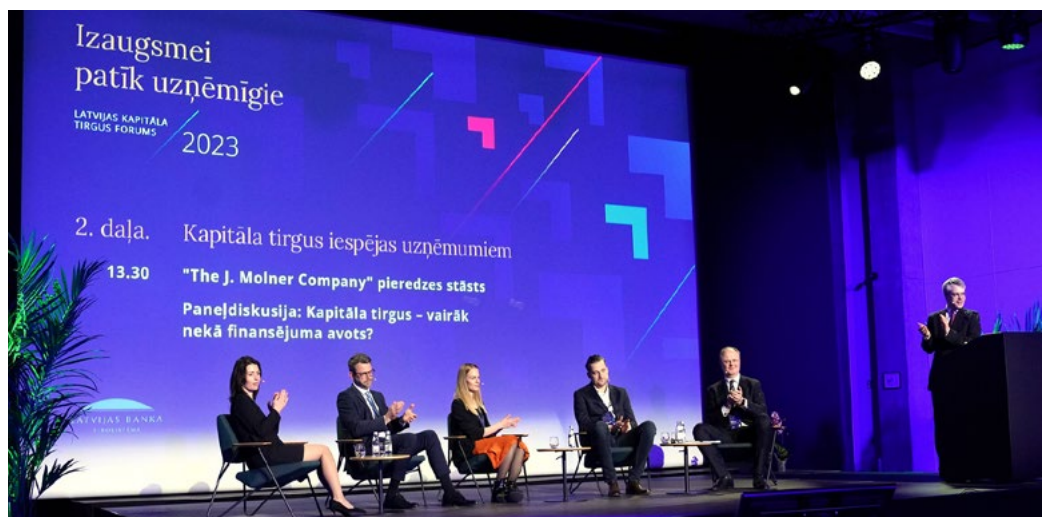
No administrative processes were initiated against issuers within the framework of supervision in 2023. In one of the administrative cases initiated in 2022 for a failure to disclose information to the supervisory authority, specifically the failure of a timely disclosure of the interim report and resolutions passed by the shareholders' meeting, the Supervision Committee of Latvijas Banka imposed a fine of 10.7 thousand euro on the issuer.

Development of the capital market

The capital market is essential for the healthy development of a country's economy, as it provides the infrastructure that businesses and the government need to raise capital, allocate resources efficiently, manage risks and ensure economic growth. Latvijas Banka focuses on growth in the market.

Latvijas Banka passed several measures in 2023 to support the development of the market.

Latvijas Banka organised the Latvian Capital Market Forum 2023 on 8 February 2023, bringing together experts and opinion leaders to discuss opportunities for private investors and businesses in the Latvian and Baltic capital markets, and opportunities for development at the European level. The Forum was well-attended and received positive feedback.



Latvian Capital Market Forum 2023 "Growth Loves Those Who Dare"

A significant move for the development of the Latvian capital market was the Securities Sandbox, which is a unique support mechanism developed jointly by Latvijas Banka and its partners that lets a potential issuer receive an initial assessment from Latvia's most knowledgeable capital market experts and recommendations for the improvements needed before it enters the Latvian capital market.

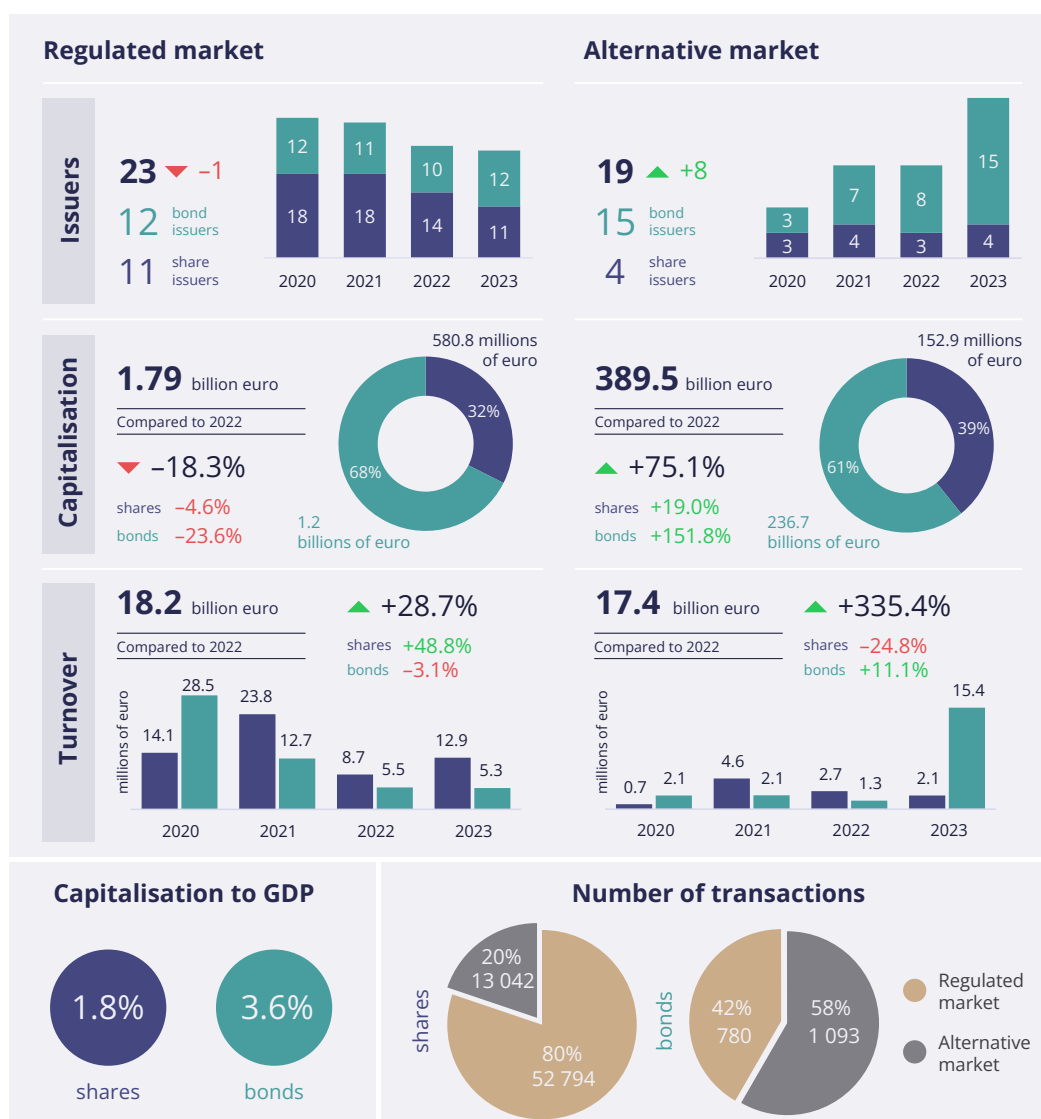
The support mechanism may be used by private companies and by companies based on public and local government capital. Both companies that intend to issue shares and those that intend to raise funding by issuing bonds may apply for advice. In 2023, four companies participated in the Securities Sandbox that was set up in 2022, and seven companies have by now participated in it since its inception.

In 2020, the FCMC in consultation with participants in the Latvian capital market and other stakeholders developed a ten-step programme for development of the capital market in 2021–2023. The programme was highly rated by the market participants, and in 2023 it was in the final stage of its implementation. Development of new measures and the approval of a new programme are scheduled for 2024.

Active cooperation between the Baltic States continued during the reporting year and has resulted in the content and format of the offering document being aligned across all three Baltic States.

A number of educational events were also organised for market participants on the latest regulatory issues.

Latvian capital market indicators 2023



Source: <https://nasdaqbaltic.com/lv>.

Supervision of trading in financial instruments and investor activities

Supervision of trading in financial instruments and investor activities in 2023 focused on:

- supervision of trading in financial instruments;
- a review of reports on suspicious transactions and orders submitted by market participants;
- in-depth inspections of suspicious transactions such as market manipulation or insider dealing;
- cooperation and information exchange with the supervisory authorities of other countries;
- timely and correct submission of investor notifications.

No administrative sanctions for market manipulation or insider dealing were imposed on trading venues within the framework of supervision of markets in financial instruments in 2023. The file of one case of market manipulation that was inspected was handed to the police so they could open criminal proceedings. In some cases, Latvijas Banka carried out in-depth inspections and sent letters to investors outlining the regulatory requirements that prohibit market manipulation, so that the investors would discontinue or abstain from behaviour that could mislead other investors as to the price, demand and supply of shares.

In one case, Latvijas Banka started administrative proceedings for a failure to provide a timely manager's notification in accordance with the requirements of Regulation No. 596/2014 of the European Parliament and of the Council. The administrative proceedings were closed without any sanction being applied to the person in question.

Supervision of sustainable finance

Latvijas Banka carries out financial supervision over sustainable finance in accordance with the requirements of the legislation and supervisory expectations, based on the [roadmap for a sustainable financial sector in Latvia](#).

The annual surveys of financial market participants continued in 2023 to collect information on their self-assessment of compliance and to evaluate the progress achieved in various aspects of sustainability, including the management of sustainability risks and assessment of risk significance, and the incorporation of sustainability issues in the development strategies of the institutions supervised.

Latvijas Banka conducted a thematic inspection on compliance with the requirements for sustainability disclosures in most segments of the financial market, covering insurance companies and branches of insurance companies, investment management companies, alternative investment funds, and private pension funds. This provided insights into the overall understanding of the sustainability requirements and the scope of disclosures, and assessed the presence of possible greenwashing risks. The progress achieved by the various market participants is uneven overall, but some examples of good practice could still be identified. Many areas are not fully compliant with the supervisor's expectations yet, but the overall understanding of sustainability issues and the related risks has improved. Latvijas Banka has communicated the main conclusions of the assessment to the financial market participants, and it will continue to provide support in implementing the supervisory expectations set out for the different steps on the roadmap.

The understanding of sustainable finance and its role in implementing the EU Green Deal is evolving gradually but the regulatory framework is expanding very rapidly, and so it is very important to ensure that financial market participants are constantly improving their skills and are able to comply with the requirements. To this end, Latvijas Banka maintained a dialogue on sustainability with the financial sector by launching a series of Sustainability Breakfast events on 9 March 2023 and inviting

representatives of various financial market segments, cooperation partners and public administration representatives to attend them. The objectives of the series are:

- to discuss practical issues related to sustainability;
- to promote the exchange of views, knowledge and experience;
- to promote the skills of the financial market participants and give stakeholders a better understanding of sustainable finance.

Four events were organised in 2023, covering both general issues like the supervisory priorities of Latvijas Banka for sustainability and the public perception of sustainability, alongside specific subjects that are of importance to market participants like the incorporation of aspects of sustainable finance in development strategies, disclosures, responses to the sustainability preferences of customers in consultations, and management of sustainability risks. Given the high rate of response from the stakeholders, the Sustainability Breakfast series will be continued in 2024.

To promote the development of internal capacity and ability in sustainability risk management in the financial sector, Latvijas Banka and the central banks and financial supervisory authorities of several other EU Member States joined the flagship project ESG risk management framework for the financial sector of the European Commission's DG REFORM financed from the Technical Support Instrument (TSI). Experience and knowledge will be shared within the project, and internal tools will be developed for sustainability regulation, extraction and processing of sustainability data, sustainability risk identification and management, and the prevention of greenwashing. The project is scheduled to be completed in 2026.

Supervision of information and communication technology and security risk management

To ensure that financial institutions and their customers are protected against cyber threats and to improve the resilience of financial services, Latvijas Banka continued its work to strengthen the ICT risk management of financial sector participants, with the main priorities being to improve the quality and efficiency of how ICT security, business continuity and third-party service providers risks are monitored.

The banking sector continued to face ICT security challenges in 2023. The frequency of cyber attacks increased, outsourcing arrangements were used and changed increasingly, and new providers of outsourced services were chosen. The participants continued to implement new technological business processes to improve their financial services, thereby increasing their reliance on ICT solutions.

Latvijas Banka carried out nine inspections of market participants in 2023:

- three full on-site inspections;
- one targeted on-site inspection;
- five targeted off-site inspections in banks and financial institutions looking at ICT and security risks.

The inspections paid particular attention to changes in critical systems, management of operational risks and business continuity, and safeguarding of the three lines of defence against ICT security risks. Regular monitoring of risks including geopolitical risks was carried out in addition to inspections of financial institutions for risk-based ICT supervision. From September to December 2023, experts from Latvijas Banka participated in the on-site inspection of a significant credit institution organised by the ECB. This inspection involved all three Baltic States.

Various security risks were assessed within the supervisory work on risks at investment firms, together with the risks associated with the accessibility of ICT, changes in outsourcing arrangements,

and data integrity. The focus was on ICT governance, ICT organisation, risk management, and operational activities, with a view to gaining assurance that the sector is capable of ensuring the required data protection and regulatory compliance.

Meanwhile, the supervisory activities for payment institutions and electronic money institutions were focused on the ICT areas of governance and strategy, organisation and outsourcing management, risk and security management, continuity management, and internal audit.

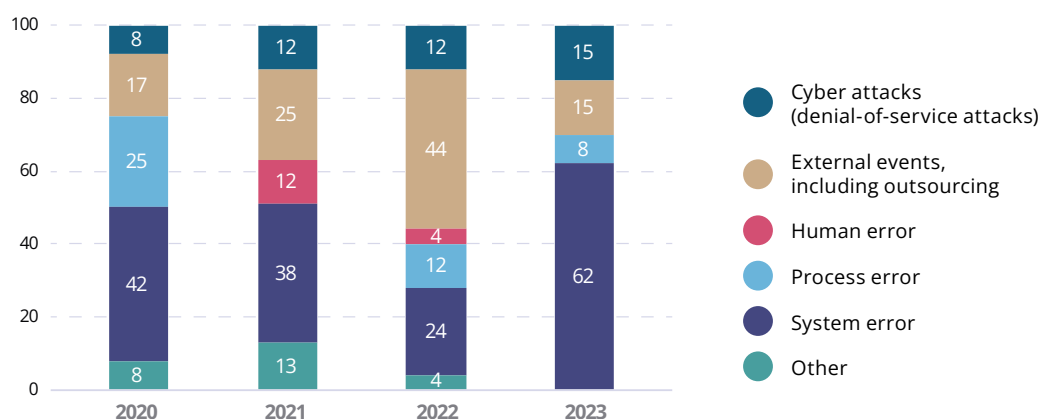
An ICT security risks assessment was also carried out in 2023 for Latvia's insurance sector, focusing on outsourcing management, data integrity and quality risks, security governance risks, change risks, and accessibility and continuity risks.

Data security is essential for insurance companies. They need to make sure that customer data and financial data are secure and reliable. These data can be highly sensitive, and loss or leakage of them may have serious consequences. Data encryption, access control, back-ups and other security measures are therefore extremely important.

To strengthen the management of the ICT security risks, Latvijas Banka prepared recommendations for managing ICT security risk for medium-sized and small financial institutions in 2023. This is a practical guide for financial institutions to assist them in managing ICT risks and improving their internal control systems. The recommendations have been supplemented with practical examples and guidance on issues where a common understanding among market participants and compliance with the requirements are important.

Latvijas Banka carried out a horizontal review of incident management in payment institutions, electronic money institutions and investment firms in 2023.

Chart 33. Main reasons behind significant incidents in payment services of Latvia's financial sector (%)



The number of significant incidents decreased overall in 2023, though wide-scale cyber attacks on Latvia continued. The reasons for the incidents were mainly related to operational risks that arose as a result of an error or third-party influence.

Market participants need to continue to develop and improve their operational risk management to enable more effective monitoring of risk levels and timely review of existing controls. When security incidents happen, market participants with more mature incident management capabilities are able to detect incidents earlier and take the preventive and containment measures required. Market participants that are able to maintain a higher level of cyber resilience are more successful at taking

appropriate defensive action in the event of an attack. This helps to reduce the impact of any potential incident.

Although the number of cases of financial fraud prevented exceeds that of the cases of fraud committed, the amounts of money defrauded from the population are increasing. Latvijas Banka carried out a thematic inspection in 2023 to find out how able the largest commercial banks are to identify and prevent fraud, and prepared recommendations for the banks on ways to reduce financial fraud.

The development of level 2 regulation under the Digital Operational Resilience Act (DORA) and the planning for implementation of it continued in 2023 in cooperation with other EU supervisors. Latvijas Banka organised consultation meetings with finance and insurance industry associations in 2023 to explain the new regulatory requirements and the level 2 regulatory technical standards that will apply from 2025.

As of 17 January 2025, Latvijas Banka will have new functions as the supervising authority for the ICT processes of financial market participants under the DORA, and the scope of the market participants supervised will also change. The DORA gives the supervisor a new mandate and tools for ensuring effective supervision. Latvijas Banka experts participated in the working group organised by the Ministry of Finance to make recommendations for the legal changes needed for the DORA to be implemented.

Supervision of ML/FTP risk and sanctions risk

The goal of supervising ML/FTP risk and sanctions risk is to ensure that the financial sector has adequate and effective control mechanisms in place to prevent the sector being used for money laundering and sanctions violations. The supervision is also important as it means that financial institutions are able to interact with other financial institutions around the world, the costs of international payments can be reduced and the speed of payment execution can be increased. If financial institutions were unable to demonstrate that they have effective control systems, other financial institutions would refuse to cooperate with them as they would be unwilling to expose themselves to the risk of being involved in money laundering and violation of sanctions.



Kristaps Markovskis
Head of the Anti-money Laundering Department

The goal of supervising ML/FTP risk and sanctions risk is to ensure that the financial sector has adequate and effective control mechanisms in place to prevent the sector being used for money laundering and sanctions violations. The supervision is also important as it means that financial institutions are able to interact with other financial institutions around the world, the costs of international payments can be reduced and the speed of payment execution can be increased. If financial institutions were unable to demonstrate that they have effective control systems, other financial institutions would refuse to cooperate with them as they would be unwilling to expose themselves to the risk of being involved in money laundering and violation of sanctions.

The most significant risks in 2023 were associated with circumvention of the EU sanctions against Russia and Belarus, both through the use of complex ownership structures to hide the controlling interest of sanctioned individuals and the use of countries bordering Russia for exports or imports of sanctioned goods. The total value of the frozen assets of people subject to sanctions or companies under their control was 75 million euro at the end of 2023. The assets of six natural persons and 35 legal entities owned or controlled by people under sanctions were frozen.

The broad scope and complexity of the EU sanctions imposed on Russia and Belarus led Latvijas Banka to provide various types of clarification about how the requirements should be interpreted and applied and to work closely with other national supervisors. To make sure that the requirements were applied in a harmonised way across the Baltic States, Latvijas Banka established and chaired a working group for both supervisory authorities and financial intelligence services.

Latvijas Banka also made improvements to its supervisory tools and methodologies in 2023 to make supervision more effective and more efficient in its use of resources. An ICT tool was developed for example that automatically aggregates and groups the data submitted by credit institutions, thereby significantly reducing the resources required for data processing and allowing staff resources to be primarily focused on data assessment and risk identification. The inspection process was also improved to strengthen the application of a risk-based approach in on-site inspections of financial institutions.

Inspections and the results of them

Inspection results in ML/FTP risk management in 2023 reveal that financial institutions have continued to enhance their internal control systems, including those for sanctions risk management and transactions monitoring. The most common shortcomings identified during the AML/CFTP inspections came from failures to adjust internal control systems to the institution-specific risks inherent in the business. Latvijas Banka carried out nine on-site inspections, one targeted off-site inspection and two horizontal reviews in 2023, covering a total of 39 financial institutions.

Latvijas Banka imposed fines for violations of the AML/CFTP rules on two credit institutions in 2023 for a total amount of 2.26 million euro, and also imposed the legal obligation to address the gaps identified and improve the internal control systems. The gaps that triggered the application of financial sanctions were shortcomings in the risk management processes and insufficient risk-based due diligence of high-risk customers and monitoring of their transactions. Both credit institutions acknowledged the gaps identified in their internal control systems, and administrative agreements were signed in both cases, imposing a legal obligation on the credit institutions to strengthen their internal control frameworks and ensure compliance with the AML/CFTP legal provisions. Latvijas Banka continues to monitor the implementation of the plans to address the gaps identified.

Latvijas Banka carried out two horizontal reviews in 2023 in all the credit institutions and the largest non-bank financial institutions. These were:

- **a horizontal review of ML/FTP risk assessments.** Overall, the credit institutions have significantly improved their risk assessment methodologies, they have a good understanding of how to identify and assess money laundering risks, and they conduct and update risk assessments on a regular basis. Institutions need to continue to improve their processes for identifying and assessing the financing of terrorism and proliferation and sanctions risks, particularly sectoral sanctions risks, and must pay attention to the procedure for evaluating the effectiveness of their ML/FTP and sanctions risk management activities;
- **a horizontal review of the effectiveness of sanctions screening in financial institutions.** The main conclusion was that the ICT systems in place are able to identify the subjects of various sanction lists effectively and in a timely manner, even with incomplete data. At the same time, the institutions need to make further improvements to their ICT systems,

particularly to the quality of screening of manipulated data and the efficiency of the system in order to reduce the resources needed for processing false positive alerts; the scope and procedure for testing the ICT systems also need to be enhanced.

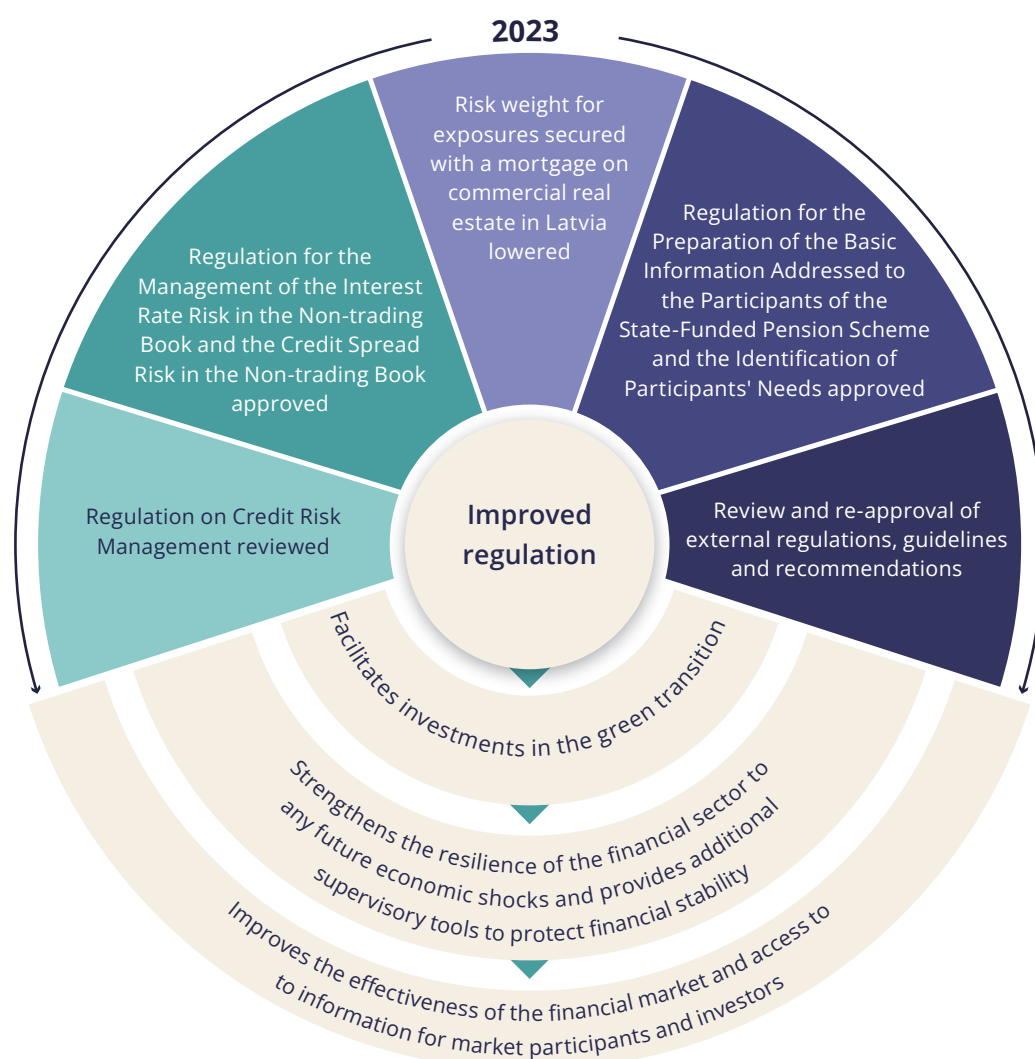
The objective of the horizontal reviews was to identify and compile a list of the good practices of financial institutions and to identify areas for improvement, thereby helping financial institutions to strengthen their internal control systems for managing ML/FTP risk and sanctions risk.

Latvijas Banka not only aligns new products and services, but also reviews and evaluates policies, procedures and risk assessments, which includes making comprehensive evaluations of AML/CFT and sanctions risk, for each new product or service. After examining the procedures, Latvijas Banka makes recommendations for addressing any shortcomings to ensure that the internal control systems operate as effectively as possible well in advance.

Changes in the regulatory framework

Improving the legal framework for financial market participants

Improvements continued to be made to the legal framework governing the operation of financial market participants in 2023, as the requirements laid down by EU directives and the guidelines of the EU institutions were incorporated into it and the application of the directly applicable EU legislation was ensured.



Review and approval of external regulations and guidelines, and recommendations for improved regulation, which:

- strengthens the resilience of the financial sector to any future economic shocks;
- facilitates investment in the green transition;
- provides additional supervisory tools to protect financial stability;
- improves the effectiveness of the financial market and access to information for market participants and investors.

To facilitate sustainable and prudent lending, Latvijas Banka issued a [Regulation on Credit Risk Management](#) to replace the FCMC's Regulation on Credit Risk Management.

The new Regulation:

- includes sustainability issues (see section "[Sustainability](#)");
- takes a more flexible approach to buy-to-let housing loans and other income-generating housing loans to individuals following from the credit risk monitoring of previous years. Previously, there was a loan-to-value (LTV) limit of 70% for such loans, whereas the new Regulation allows duly justified derogations from this limit. The quantitative LTV requirement of 70% for housing loans where the borrower's income from real estate exceeds 20% of their total income has been lifted, and the restriction that the borrower's income from real estate should only be taken into account at 70% has been removed. These restrictions have been replaced with a qualitative requirement to assess the credit risk of such a borrower prudently;
- makes transfers of loan commitments from one credit institution to another easier. The rules have been supplemented by a requirement for a credit institution to set the criteria under which it requires a new collateral assessment from the borrower so that it can properly assess the credit risk associated with the transaction in its internal regulations.

In addition, Latvijas Banka decided on 18 December 2023, within the framework of its regular review of the risk weights applied and following a comprehensive data analysis, to reduce from 100% to 80% the risk weight applied in calculating the capital requirements of credit institutions for credit risk to exposures secured by a mortgage on commercial real estate (CRE) located in Latvia. Credit institutions from Latvia and other EU Member States that use the standardised approach for calculating the capital requirements for such exposures will be able to apply the reduced risk weight as of 30 June 2024.

Latvijas Banka has estimated that the risk weight of 80% is enough in the current circumstances to ensure that credit institutions are sufficiently resilient to the risks associated with such CRE exposures, without creating unjustified obstacles to lending. Given that credit institutions currently do not classify a large part of their CRE exposures as fully secured by a CRE mortgage, which is the criterion for applying the reduced risk weight, the related capital requirements are bound to decrease, with credit institutions granting new eligible loans and reclassifying a part of their existing portfolios. The reduced risk weight will allow a more consistent approach to be taken to calculating credit risk capital requirements across credit institutions that use the standardised approach and those that use the internal ratings based approach.

The ESRB has found the decision to reduce the risk weight to be an appropriate one, describing it in its assessment as an effective and proportionate measure. Latvijas Banka will continue to review the adequacy of the risk weight every year at least, and will recalibrate it again if required.

To improve and expand the requirements and procedures for managing interest rate risk and for assessing and overseeing credit spread risk in credit institutions, and to strengthen the resilience of those institutions to possible future shocks, Latvijas Banka issued [the Regulation for the Management of the Interest Rate Risk in the Non-trading Book and the Credit Spread Risk in the Non-trading Book](#), effective as of 31 December 2023. This Regulation replaces the FCMC's Regulations on the

Management of Interest Rate Risk, Preparation of a Report on the Calculation of Economic Value Depreciation and of a Report on the Term Structure of Interest Rate Risk.

The new Regulation implements the EBA Guidelines by improving the requirements and procedure for managing interest rate risk in the non-trading book in institutions, which includes identifying, assessing, analysing and overseeing the risk, and it lays down the requirements for internal regulatory documents, the system of limits, the set-up of the management information system and information technology systems, risk assessment models, validation of the model applied, and assessment of that model's risks.

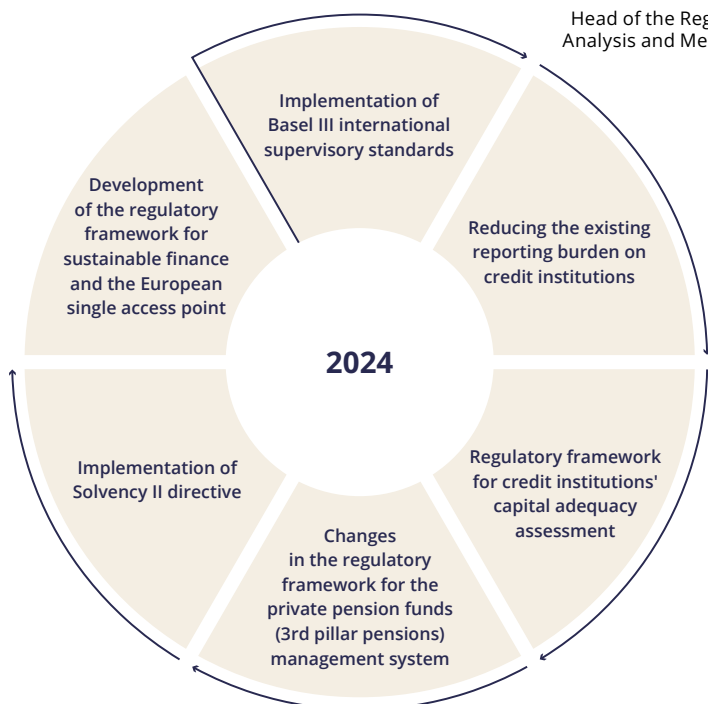
Latvijas Banka approved [the Regulation for the Preparation of the Basic Information Addressed to the Participants of the State-Funded Pension Scheme and the Identification of Participants' Needs](#), which lays down the requirements for the format and contents of the basic information about state-funded investment plans and the procedure for preparing it, the information to be disclosed to participants, the frequency of those disclosures, and the criteria that the managers of the assets of the state-funded pension scheme must follow to let participants select the most appropriate investment plan for them, and which also requires that an internal control system for disclosures to participants be established. It sets out a new and innovative approach to receiving information from pension managers and for integrating that information into a universal format that is a standardised, simple and user-friendly product in the form of a booklet containing the basic information about the second pillar pension investment plans. The regulation is binding on the asset managers of the state-funded pension scheme, while the users of the booklet are all the 1.3 million or so participants in the second pension pillar, who will be able to gain a better understanding of where and how their personalised pension capital is accumulated, while also engaging in a dialogue with the pension manager to clarify important points jointly.

Latvijas Banka continues to participate in developing the EU's regulatory framework for the financial sector and in ensuring the development of binding regulations for Latvia's financial sector based on the best international practice and development trends in the local market.



Ludmila Vojevoda

Head of the Regulatory Requirements,
Analysis and Methodology Department



Latvijas Banka started the extensive process of reviewing and re-approving the external regulations issued by the FCMC in 2023, updating and improving the regulatory framework of the financial sector at the same time.

The most important upcoming amendments to the regulatory framework for credit institutions are the proposed amendments to Directive 2013/36/ EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC, which must be transposed into the legal acts of the Republic of Latvia within 18 months of the publication date and is scheduled for mid-2024; and to Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential

requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012, which will enter into effect from 2025, as these will complete the implementation of the Basel III international supervisory standards in the EU.

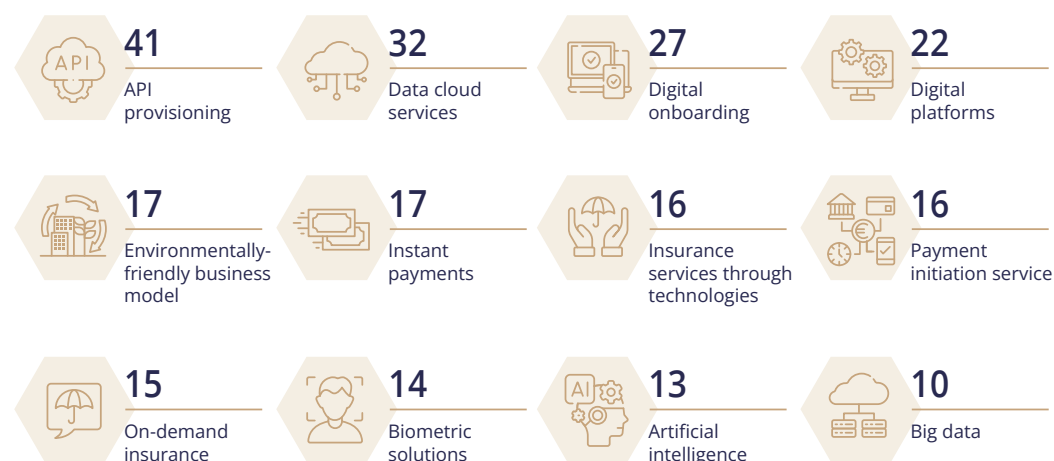
Latvijas Banka evaluated in 2023 whether the existing reporting burden on credit institutions for the purposes of supervision, resolution and statistics could be reduced and discussed this with market participants. Some 114 data queries were assessed and five requirements were cancelled, and further ways of reducing the reporting burden were identified and are scheduled to be implemented in 2024.

Work will also continue in 2024 on developing the regulatory framework for sustainable finance. To promote the development of sustainable financial instruments, the EC published a Recommendation on facilitating finance for the transition to a sustainable economy on 27 June 2023, and on 23 October 2023, it adopted the EU green bond standard regulation, laying down a uniform set of requirements for bond issuers that wish to use the designation "European Green Bond" or "EuGB" for their environmentally sustainable bonds. Latvijas Banka will ensure the application in practice of these regulations.

A business environment that favours innovative and secure financial services

A major share of Latvian financial sector businesses have introduced and are using innovations that improve the customer experience and provide modern and user-friendly services. Businesses are also already employing artificial intelligence solutions, machine learning and big data processing or technologies that could bring significant changes to financial services and the market. Application programming interfaces (API), data cloud services and digital onboarding are the three technologies that are most frequently used by market participants.

Chart 34. Technologies most often used by market participants in 2023 (number of respondents confirming)

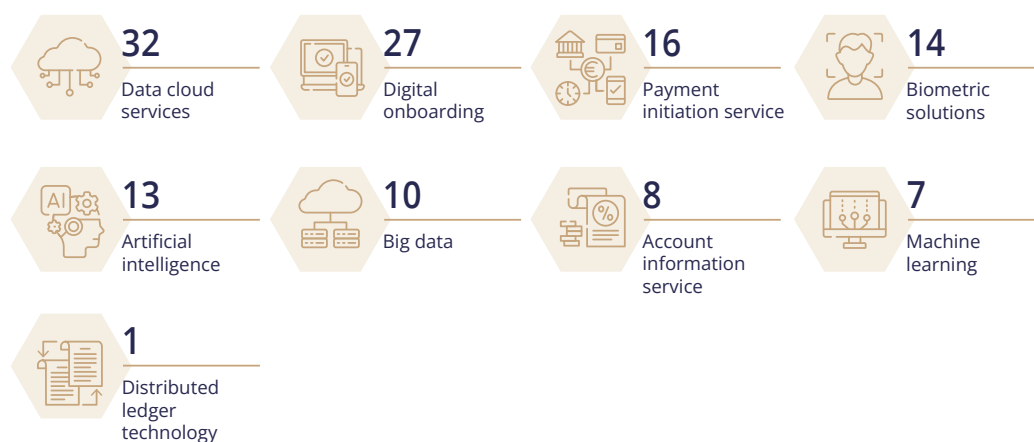


Source: Survey of financial market participants conducted by Latvijas Banka¹.

For the third consecutive year, credit institutions, insurance brokers and insurance corporations have been the market segments that innovate most frequently in their operations. The new and innovative processes used most often are data cloud services, digital onboarding, payment initiation services, biometric solutions, and artificial intelligence. Big data, machine learning and account information services are used less frequently. An innovation that had previously not used by Latvian market participants, the distributed ledger technology (DLT), was mentioned for the first time in 2023. This innovative process is employed by one of the survey participants.

¹ 211 market participants were invited to take part in the survey, with 154 market participants eventually completing the survey. 55 of the respondents confirmed that they were currently using an innovative solution in the provision of financial services, while 34 were planning to start using innovative technologies in the future. 24 businesses had created a team for the development and introduction of innovative solutions. All survey results and the related conclusions are based on the data provided by market participants

Chart 35. Innovative processes used by businesses (number of respondents confirming)



Source: Survey of financial market participants conducted by Latvijas Banka.

The most notable increase from 2022 in the use of any innovation is in the use of artificial intelligence and instant payments. Artificial intelligence is already employed by several insurers, credit institutions and investment firms, and by individual market participants representing such financial market segments as insurance brokers, payment institutions, private pension funds, and crowdfunding service providers.

Artificial intelligence, big data and machine learning tend to be the drivers behind the development of innovative technologies, and they are really able to change the market and the services provided. Not only do artificial intelligence solutions provide the best methods for data processing and enhancing customer experience, they also simplify, accelerate and redefine the traditional processes, making them more efficient. Elsewhere in the world, machine learning is already used in revenue and stock price projections, risk supervision, and management processes.

Latvijas Banka continues to support innovation by providing support tools to the financial sector through the Innovation Hub and the Regulatory Sandbox, which are designed to help in the development of innovative services at inception and to give feedback on compliance risks with the regulatory requirements of the financial sector that are identified during participation in the testing process for the services. Consultation was provided in 52 cases in 2023, and the areas that got the most attention from FinTech companies, and more than 80% of the consultations, were payments, crypto-asset services and crowdfunding.



Latvia's FinTech Forum on 10 October 2023

In 2023, Latvijas Banka was actively involved in implementing the tasks outlined in Latvia's FinTech strategy, as access to services was improved through a dialogue between the supervisory and controlling authority and market participants, and the authority conducted outreach activities on improvements to licensing.

Several initiatives to promote the development of the FinTech environment were also launched in 2023. Latvijas Banka expanded the operational capacity of the Innovation Hub by working with the stakeholders in it, which are the Ministry of Finance, the Fintech Latvia Association, the Investment and Development Agency of Latvia and the Latvian Blockchain Association, and by organising round table discussions and promoting the FinTech sector at more than 15 local and international public events. One of the central events of the Latvian FinTech ecosystem is Latvia's FinTech Forum, which was now organised for the second time by Latvijas Banka jointly with the Investment and Development Agency of Latvia, and which brought together around 300 in-person attendees from Latvia and abroad. The participants were briefed on the implementation of Latvia's FinTech strategy and the progress made in FinTech development, and they received advice from Latvijas Banka and other organisations and learned about the latest trends in FinTech. FinTech Factor, a competition for start-ups, was held for the first time, as the creators of innovative ideas presented their business ideas to the jury and received awards.

Latvijas Banka conducted a survey in 2023 [on cooperation](#) between banks and FinTech companies. The survey identified several potential opportunities for cooperation between the two segments, and defined specific tasks, including some for Latvijas Banka, that could promote awareness and allow various FinTech business models access to routine banking services. Following the survey results, Latvijas Banka organised a dialogue between the participants and committed itself to taking measures to improve cooperation.

The AML/CFTP Manual was supplemented in 2023 with information on the risks associated with payment service providers, virtual assets service providers, and other current FinTech models and their management, so that a common understanding could be built between the banks and the supervisory authority for applying the legislation on preventing financial crimes, and for promoting a risk-based approach.

Latvijas Banka has committed to presenting an annual risk assessment of the non-bank financial sector to credit institutions, which would help those credit institutions strengthen the application of a risk-based approach, partly by building their understanding of the existing and emerging risks that are specific to the non-bank sector. There are several [initiatives underway to foster cooperation and raise capacity in the application of regulatory requirements and in the compliance of innovative services](#) with those requirements.

Marine Krasovska

Head of the Financial Technology Supervision Department



Artificial intelligence, big data and machine learning tend to be the drivers behind the development of innovative technologies, and they are really able to change the market and the services provided. Not only do artificial intelligence solutions provide the best methods for data processing and enhancing customer experience, they also simplify, accelerate and redefine the traditional processes, making them more efficient. Elsewhere in the world, machine learning is already used in revenue and stock price projections, risk supervision, and management processes.

In 2023, Latvijas Banka started the preparations needed for implementing Regulation (EU) 2023/1114 of the European Parliament and of the Council of 31 May 2023 on markets in crypto-assets, and amending Regulations (EU) No 1093/2010 and (EU) No 1095/2010 and Directives 2013/36/EU and (EU) 2019/1937 (MiCA). This will apply from 30 December 2024, with the exception of Titles III and IV, which will apply from 30 June 2024. Latvijas Banka consequently worked hard on drafting the Law on Crypto-Asset Services, and this work will continue in 2024. A working group was set up for that purpose with members from the Latvian Blockchain Association, the Ministry of Finance, the Ministry of Economics, the Ministry of Justice, the Register of Enterprises, the State Revenue Service, the Financial Intelligence Unit, and Latvijas Banka. In addition, a special task force was set up in Latvijas Banka to make the preparations for the implementation of the MiCA regulation. The Law on Crypto-Asset Services is scheduled for adoption in the first half of 2024. It will confer the role of competent authority in this field on Latvijas Banka, which will then have the right to grant authorisation for providing crypto-asset services to crypto-asset service providers.

Development of innovation and supervisory technologies (SupTech) at Latvijas Banka

Supervisory technologies or SupTech is a specialised development area at Latvijas Banka that is intended to provide high-tech supervisory services.

Significant preparations for integrating the supervisory function into Latvijas Banka had already been made in 2022, but 2023 was the year when the integration of technologies and processes was most intensive. The internal migration of various systems was carried out and processes were reviewed and streamlined to maximise the practical benefits from the integration of Latvijas Banka and the FCMC. One of the benefits of this integration was an additional information protection capacity that provides a high level of protection for supervisory information at a time of increasingly high cybersecurity risks.

Following Latvijas Banka's general strategy, the SupTech strategy was reviewed to ensure targeted and well-coordinated development of SupTech. The international aspect is also important, so Latvia does not create any SupTech solutions in isolation, but rather builds on the opportunities provided by the EU's centralised institutions.

Supervisory services were fully integrated into the internal cooperation platform of Latvijas Banka in 2023, while additional functionalities in the supervisory information system were introduced, and the single reporting portal was developed, which will provide smooth access to various analytical resources.

Timely and reliable information is very important in the provision of supervisory services. With both the amount of information and the number of various analytical tools increasing, the risks of data fragmentation have grown. The reporting portal will let the supervisor retrieve the most relevant data and make full use of all the information available to provide more effective and higher-quality supervisory services.

SupTech solutions are also an important part of Latvijas Banka's in-house innovation. Latvijas Banka, like the FCMC before it, introduced an innovation laboratory or iLab during the reporting year. This is an environment for cooperation where innovative ideas can be evaluated and prototypes of them can be built in the shortest possible time and with minimum resources. This allows the practical development of innovations, while also minimising losses if an initiative turns out to be unviable.

The supervisor must handle very large quantities of financial information, but also quite a lot of textual information. In 2023, the iLab started working on automating text processing with a view to reducing the human input into reviewing lengthy textual documents. A study into the practical aspects of artificial intelligence and the prospects for applying it was also conducted.

Integration of the two institutions secured these benefits, but it also entailed, and will continue to entail, various challenges in the provision of better services to Latvijas Banka's customers that will need to be addressed in the near term. The potential development of artificial intelligence solutions for supervision and the benefits of this are currently still hard to evaluate. These issues will definitely remain on the SupTech development agenda in 2024 and beyond. The subject requires a high degree of practical involvement, and target and result orientation, though this new area of technology is one that is developing very quickly and is therefore quite unpredictable.

The resolution mechanism

The Single Resolution Mechanism (SRM) has been in place since 2015. Latvijas Banka, as the resolution authority in Latvia, is a member of the SRM, a position filled until 2023 by the FCMC, and together with the Single Resolution Board (SRB) and the other national resolution authorities of the EU it is constantly working to improve and strengthen the SRM. Resolution covers credit institutions and investment firms that are subject to the requirements of the Law on the Recovery and Resolution of Credit Institutions and Investment Firms. The prudential regulation and supervision of those institutions is designed to minimise the damage that could be caused by liquidity and solvency crises. At the same time however, it has to be remembered that credit institutions and investment firms are private companies, and that although they are subject to tight regulation, and regulation is vital, they may still have problems and fail. The objective of the resolution authorities is to safeguard financial stability by minimising disruptions to the economy and protecting taxpayers from losses when the failure of a market participant becomes inevitable.

Resolution covers credit institutions and investment firms that are subject to the requirements of the Law on the Recovery and Resolution of Credit Institutions and Investment Firms. The prudential regulation and supervision of those institutions is designed to minimise the potential damage from liquidity and solvency crises. The objective of the resolution authorities is to safeguard financial stability by minimising disruptions to the economy and protecting taxpayers from loss when the failure of a market participant becomes inevitable.

Jeļena Ļebedeva

Head of the Resolution and Protection Schemes Department



Resolution is a proactive function. Clear processes for resolving credit institutions and investment firms have been developed over the years, and the main focus is currently on strengthening crisis preparedness, which means providing Latvijas Banka as the resolution authority with all the tools it needs to respond to any potential crisis, to implement the resolution scheme, and to manage any restructuring, recapitalisation or transfer strategy that is required for a market participant.

The functions of the resolution authority for credit institutions that are subject to direct supervision by the ECB within the framework of the SSM and cross-border credit institution groups are discharged by the SRB, but Latvijas Banka's representatives participate in the resolution processes implemented by the SRB and in preparing the SRB's decisions, including those on setting the minimum requirement for own funds and eligible liabilities. Three Latvian credit institutions and one branch of a credit institution from another Member State, accounting for 83% of the total assets of credit institutions, were under the direct responsibility of the SRB in 2023. Latvijas Banka as the national resolution authority is responsible for the resolution function for the remaining six credit institutions and two investment firms.

In 2023, the priorities in resolution were:

- to continue the operationalisation of the resolution mechanism. Building on the experience of previous years, Latvijas Banka integrated and updated several operational regulation processes for resolution in 2023, particularly those concerning the planning of resolution and setting the minimum requirement for own funds and eligible liabilities, and it participated in several dry-run exercises to enhance the resolution process that were organised by the SRB, and in the EC's structural support project 23EE09 *Technical support for national handbook for Estonia, Lithuania and Latvia*. Within the framework of this project, the operationalisation process for the application of resolution tools will be developed and organised, which includes drafting of the working documents like decisions, draft contracts, procedures, and methodologies that are required for the resolution tools to be ready to be applied by the end of 2024. This project is an important step in strengthening the capacity of the resolution process and ensuring it can be implemented effectively if needed.
- to ensure resolution plans are kept up to date and to approve decisions on the minimum requirements for own funds and eligible liabilities. Resolution plans are updated at least once a year to account for any changes in the market and in the credit institutions and investment firms themselves, with a view to ensuring crisis readiness and enhancing the institutions' resolvability.

Eight resolution plans were updated in 2023 in line with the business models and risks of the credit institutions, including five resolution plans of credit institutions under Latvijas Banka's direct responsibility; the resolution plan of one credit institution was not reviewed, because that institution was subject to simplified requirements under which resolution plans may be reviewed every two years. Staff from Latvijas Banka also participated in the updating processes for resolution plans organised by the SRB for the three credit institutions under the direct responsibility of the SRB.

The success of the resolution of a failing institution depends largely on whether the institution has sufficient minimum own funds and eligible liabilities to allow it to absorb losses or recapitalise in a crisis. The minimum requirements for own funds and eligible liabilities were reviewed and reset in 2023 for all the credit institutions in Latvia. The minimum requirements for own funds and eligible liabilities for the six credit institutions under the direct responsibility of Latvijas Banka were set in accordance with the strategies outlined in their business plans, and decisions on implementing the minimum requirements for own funds and eligible liabilities set by the SRB were passed for the three institutions under the SRB's direct remit;

- to ensure timely contributions to the Single Resolution Fund (SRF).

In close cooperation with the national resolution authorities including Latvijas Banka, the SRB is responsible for calculating the annual ex ante contribution payable to the SRF by each institution under the provisions of the SRB Regulation, and for managing and using the SRF. The contributions of Latvia's credit institutions to the SRF made in accordance with the SRB's calculations amounted to 3.6 million euro in 2023, and they total 54.9 million euro since 2015.

The objective of the SRF is to provide funding that can be called upon in a crisis to resolve a credit institution. The SRF was built up from contributions made by credit institutions in Member States including those in Latvia, with a view to gradually reaching its target level of at least 1% of the amount of the deposits covered at the credit institutions of all the participating Member States, and as at 31 December 2023, this target level had been reached. This is a major accomplishment of the SRM, and it provides a substantial fund that can be drawn on in a crisis. It also means that no contributions will be made by credit institutions in 2024 unless the fund is called upon to support a resolution during the year.



Compensation schemes

The compensation schemes in Latvia are:

- The Deposit Guarantee Fund (DGF);
- The Fund for the Protection of the Insured (FPI);
- The Financial Instrument Market Customers (Investors) Protection Scheme.

Deposit Guarantee Fund Members of the DGF make quarterly contributions to the DGF of 0.05% of the average balance of the deposits covered in the previous quarter, multiplied by the adjustment coefficient calculated using a fixed formula. The DGF evaluates the performance indicators of its members and calculates the adjustment coefficients for the contributions to the DGF. The average adjustment coefficient for Latvia's credit institutions was 116% in 2023, and 126% in 2022, and it was 90.62% for cooperative credit institutions and 92.24% in 2022.

Deposit-takers made contributions of 21.5 million euro to the DGF in 2023.

Following the integration of Latvijas Banka and the FCMC, Latvijas Banka focused on the access of depositors to the deposit guarantee scheme, and successfully improved the process for disbursing the guaranteed compensation by developing a new information technology solution that uses a remote, user-friendly and accessible procedure for disbursing the guaranteed compensation to depositors that was first used when the guaranteed compensation was paid out to the depositors of Baltic International Bank SE.

During the year, Latvijas Banka ensured the disbursement of the guaranteed compensation to the depositors of AS Latvijas Krājbanka, ABLV Bank AS, and AS PNB Banka, which were all in liquidation; the liquidated LABA Kooperatīvā Krājaizdevu sabiedrība; and the insolvent Baltic International Bank SE. The amounts compensated were those stipulated in the Deposit Guarantee Law:

- 99 thousand euro to the depositors of LAS Latvijas Krājbanka;
- 2191 thousand euro to the depositors of LAS ABLV Bank;
- 1435 thousand euro to the depositors of LAS PNB Banka;
- 33 116 thousand euro to the depositors of the insolvent Baltic International Bank SE;
- 25 thousand euro to the depositors of the liquidated LABA KKS.

Disbursement of the guaranteed compensation to the depositors of LAS TRASTA KOMERCBANKA is being made by the administrator from the bank's own resources.

Depositors have five years as of the day when the deposits became unavailable to apply for the guaranteed compensation, and that period lapsed on 4 March 2021 for LAS TRASTA KOMERCBANKA

and on 23 February 2023 for LAS ABLV Bank, while it will expire on 12 June 2024 for LAS Latvijas Krājbanka and 31 December 2029 for underage depositors, and on 15 August 2024 for LAS PNB Banka. Disbursements of the guaranteed compensation to the depositors in the insolvent Baltic International Bank SE will continue until 12 December 2027, and to the depositors in the liquidated LABA KKS until 14 July 2025.

Section 19(7) of the Deposit Guarantee Law states that if a sworn bailiff or tax administration has not subjected the financial means of a depositor to enforcement within five years from the day when the deposits become unavailable, the restrictions imposed by the sworn bailiff or tax administration on the disbursement of the guaranteed compensation expire; this date will be 3 March 2026 for LAS TRASTA KOMERCBANKA, and 23 February 2028 for LAS ABLV Bank. If the disbursement of the guaranteed compensation has been deferred under Section 27(1) of the Deposit Guarantee Law though, the depositors will be able to receive the compensation after the circumstances that caused the disbursement to be deferred have ceased to exist.

Latvijas Banka was responsible for the accumulation and management of the DGF in 2023, and its balance at the end of the year was 229.9 million euro. The basic principle in managing the DGF assets is to ensure a high level of liquidity. In 2023, the DGF assets were invested in short-term, liquid, fixed-income, investment-grade, euro area government securities with a maturity of up to 12 months. The annual return on investment was 2.72%.

Regular stress-testing of the DGF is carried out under the provisions of the Deposit Guarantee Law. In 2023, the lists of the recipients of guaranteed compensation of all the credit institutions and cooperative credit unions were inspected. Their ability to prepare a list of depositors and submit the required information to Latvijas Banka in the format specified and within the deadlines was tested. Following the stress test results, Latvijas Banka provided explanations where necessary on how the information requested should be prepared, and after the test the bank sent letters to the market participants requesting improvements to their internal control systems.

Fund for the Protection of the Insured The assets of the FPI consist of the contributions from insurance companies of 0.1% of the total gross insurance premiums received from natural persons for the classes of insurance specified by law. Since its inception, guaranteed compensation of 12.3 thousand euro has been disbursed from the FPI. Since the accumulated holdings of the FPI exceeded the amount stipulated in Section 288 of the Insurance and Reinsurance Law at the end of 2015, contributions to the FPI have been suspended since 2016. At the end of 2023, there were 19.8 million euro in the FPI. The FPI assets were also invested in short-term, liquid, fixed-income, investment-grade, euro area government securities with a maturity of up to 12 months, and the annual return on investment was 2.84% in 2023.

Protection of the customers of the financial instrument market (investors) The investor protection scheme is based on the Investor Protection Law. Compensation for each investor is limited to 20,000 euro and disbursements of compensation are ensured by Latvijas Banka. The Investor Protection Law does not provide for the accumulation of any funds for disbursing compensation, but the resources can if necessary be provided by the system participants or legal entities that have been authorised to provide investment services. The Investor Protection Law was improved in 2023 when the principles of the investor protection scheme were updated. The amendments updated the provisions of the Law to take account of current developments in the investment market and the opportunities for practical application of the protection scheme. The procedure for organising and implementing the investor protection scheme has been adjusted, the requirements for the provision, processing and storage of the information required to organise the disbursement of compensation have been supplemented, and the procedures for communicating to the investor the conditions they must fulfil in order to receive compensation for the investment have been made, while the size of the compensation, the procedure for disbursement and the time frame for it have been further elaborated.



Investment management

Latvijas Banka manages its gold and its financial investments in accordance with the investment management guidelines set by the Council of Latvijas Banka, observing the principles of prudent management. Investments are managed in a such way as to ensure the long-term effects of:

- capital preservation;
- liquidity;
- income generation.

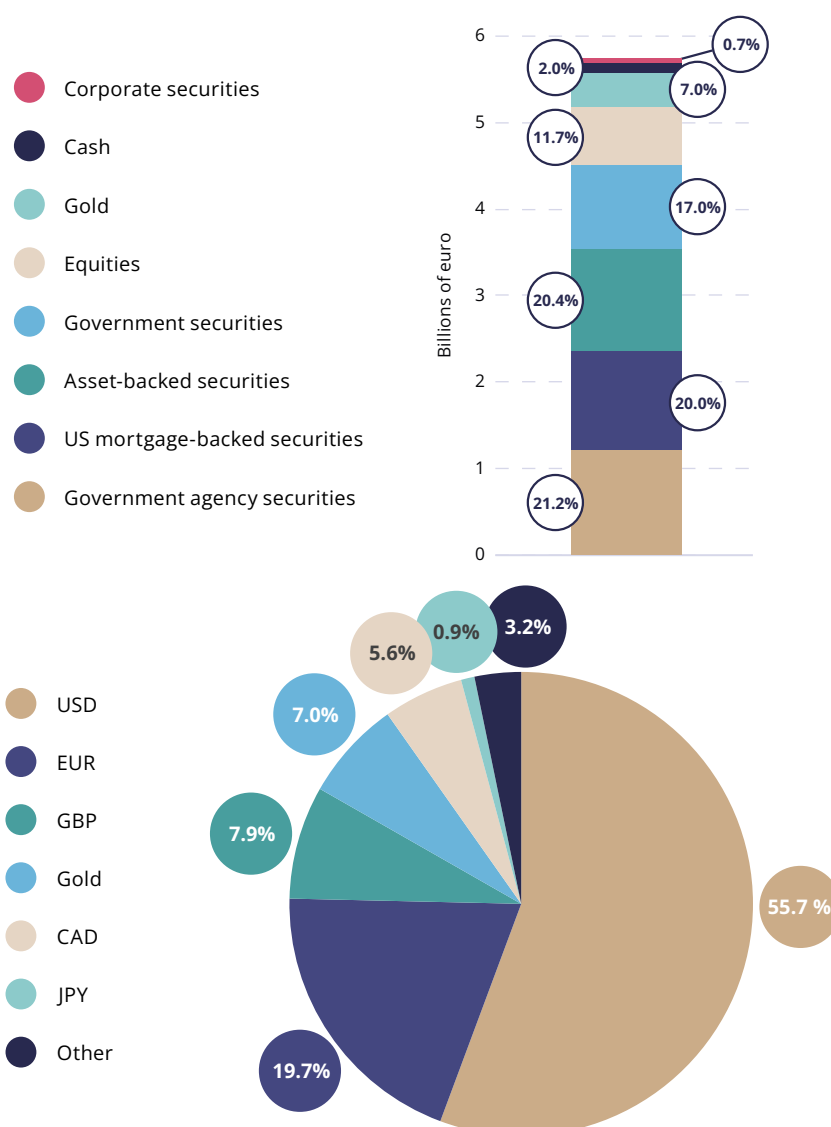
Investment management is based on the principles of sustainability and the Agreement on Net Financial Assets of the Eurosystem central banks.

Investment composition

Diversification is one of the primary strategies used in investment management. Latvijas Banka mostly invests its financial assets in:

- debt securities issued by the governments of the US and European countries, their agencies or international institutions;
- asset-backed securities;
- securities in the emerging markets government securities index;
- securities in the global investment grade fixed income securities index;
- equities issued by companies in developed and emerging markets equity indexes;
- high-quality debt securities issued by corporate issuers.

The total value of Latvijas Banka investment portfolios at the end of 2023 was 5.73 billion euro, which was 0.28 billion euro more than at the end of 2022.

Chart 36. Investment composition, 31 December 2023

Source: Latvijas Banka.

Investment management framework

Latvijas Banka manages its investments in-house and also uses external managers. Investments are made in three main asset classes of fixed income securities, equities and gold.

Investment in fixed income securities

The bulk of investment in fixed income securities is managed in-house. The benchmark of the 1–10 year fixed income securities portfolio managed in-house consists of the weighted index of 1–3 year US and Canadian government securities, and 1–10 year euro area and UK government securities. The benchmark is composed of assets denominated in:

- US dollars – 55%;
- euro – 21%;
- British pounds sterling – 14%;
- Canadian dollars – 10%.

Investments in investment-grade fixed-income government securities market countries are made through exchange-traded funds (ETFs).

Latvijas Banka also uses the services of seven external managers to manage investments in fixed-income securities. They manage a part of Latvijas Banka's financial assets in accordance with the guidelines set by the Council of Latvijas Banka.

- Six managers manage the portfolios of US mortgage-backed fixed income securities;
- One manager manages the portfolio of investment-grade global fixed-income securities.

The currency risk is hedged against the euro for all investments in fixed income securities except for the investment-grade global fixed income securities portfolio.

Investment in equities

Investment in equities mostly comprises the portfolio of equities from advanced markets, which is managed by an external manager. This portfolio is managed under [the sustainability strategy](#) of Latvijas Banka and its targets are:

- to support the achievement of carbon neutrality by 2050 at the latest;
- to adjust the portfolio to the provisions of the Paris Agreement;
- to avoid environmental pollution, conserve biodiversity, and consider environmental, social and governance factors (ESGs) (see [Climate-related disclosures of Latvijas Banka's non-monetary policy portfolios](#)).

Investment in emerging market equities is managed against the corresponding equity index and is made through ETFs.

Investment in gold

Latvijas Banka's gold is stored at the Bank of England.

Under the Statute of the ESCB and of the ECB, Latvijas Banka has transferred a small share of its financial assets to the ECB to be managed as part of the ECB's foreign reserves. The ECB's reserves are managed by the national central banks of the Eurosystem, where each bank is allocated a share of financial assets to manage in accordance with their capital key at the ECB.¹ Latvijas Banka manages its share in Japanese yen together with Oesterreichische Nationalbank. Under the Statute of the ESCB and of the ECB, 1.1 tonnes of Latvijas Banka's gold have been included in the ECB reserves.

Risk management

Risk management is an integral part of investment management. Risk management means developing risk scenarios, assessing the potential returns on financial assets and the risks to them, and modelling the optimal asset allocation. Whether the investment portfolio complies with the guidelines and the risks are distributed in accordance with investment decisions is monitored and controlled on a daily basis.

Interest rate risk is one of the most significant risk factors affecting Latvijas Banka's investments. Particular attention is paid in managing investments to the yields of two, five and ten-year government bonds and their risk premiums.

¹ The ECB's capital consists of the contributions by all national central banks (NCB) of the EU Member States. The NCBs' shares in this capital are calculated using a key which reflects the respective country's share in the total population and gross domestic product of the EU.

2023 in review

Surging interest rates had a strongly negative effect on the short-term value of fixed income portfolios in 2022; nevertheless, higher interest rates and lower equity market values created a positive outlook for better investment performance in the long term.

Although interest rates were at a high level in 2023, they were also very volatile and the level of volatility in them was historically high. This significantly affected the volatility of the whole investment portfolio throughout the year.

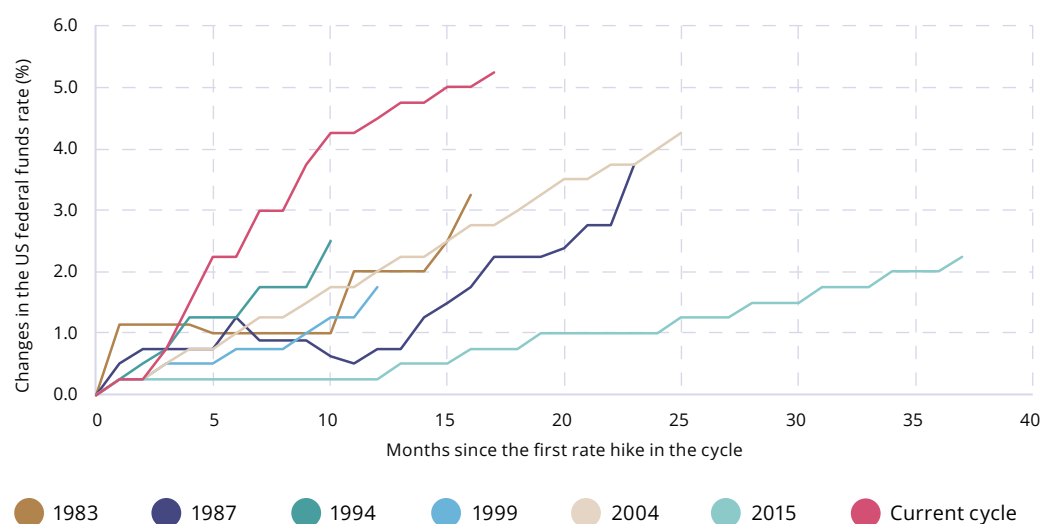
Chart 37. US Bond Market Option Volatility Estimate (MOVE) index over 10 years (index points)



Sources: Bloomberg Finance LP, Latvijas Banka.

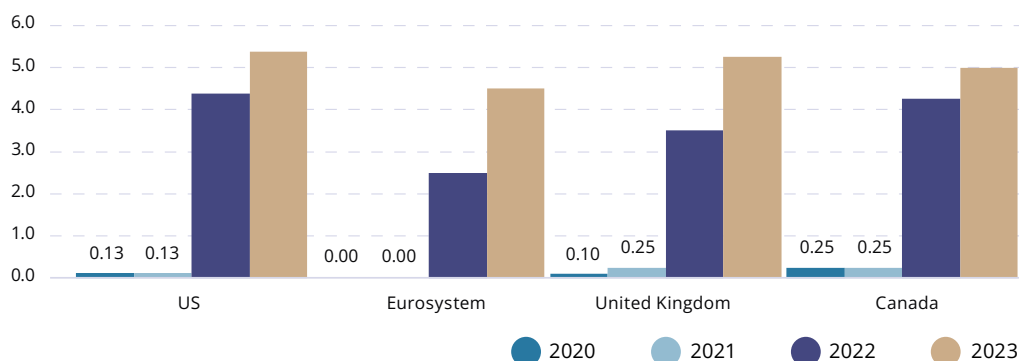
The US Federal Reserve System continued to raise the federal funds rate, with the total uninterrupted increase in the rate since 2022 reaching 525 basis points.

Chart 38. The US federal funds target interest rate hiking cycles



Sources: Bloomberg Finance LP, Latvijas Banka.

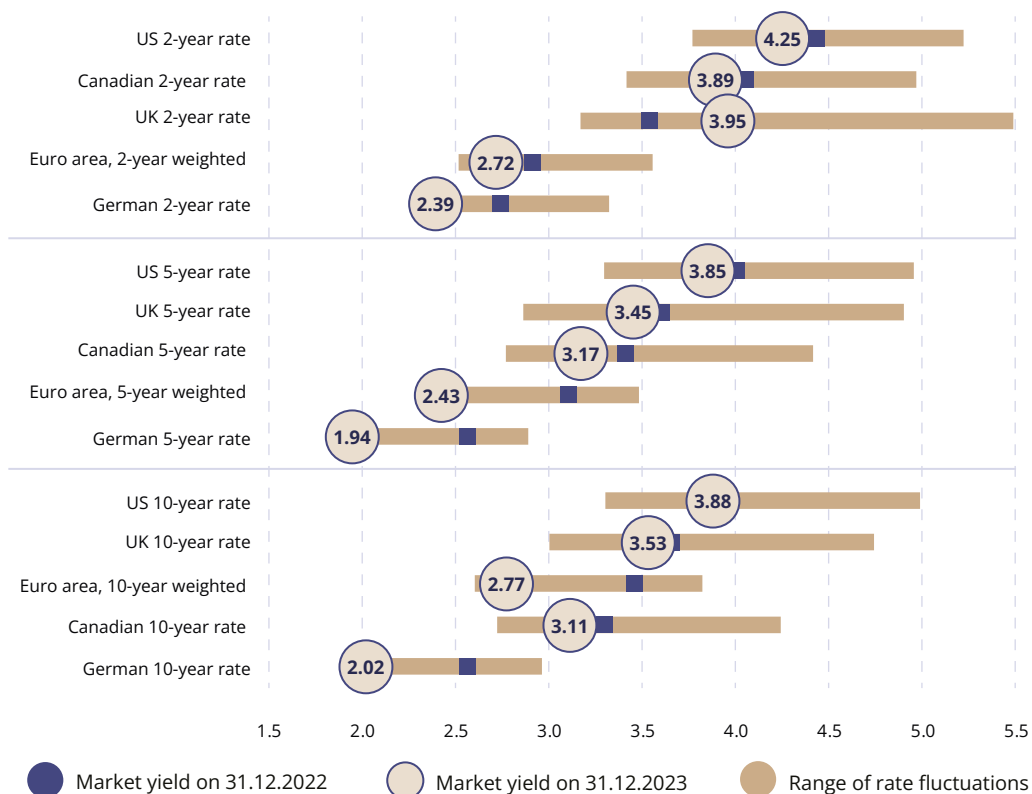
Other central banks also continued to raise their policy rates over the first three quarters of 2023, with the overall increases during the current tightening cycle that started in 2022 ranging from 450 basis points to 515.

Chart 39. Development of central bank policy rates (yields; %)

Sources: Bloomberg Finance LP, Latvijas Banka.

The dynamics of inflation and the decisions of central bank monetary policy, together with the expectations of financial markets, were the main reason why interest rates were so volatile, and they combined to push interest rates upwards from the middle of the second quarter to the end of the third quarter. The rhetoric from central banks changed in the fourth quarter, and this contributed to a fall in interest rates, which had a positive effect on both the fixed income and equity portfolios. Chart 40 shows that:

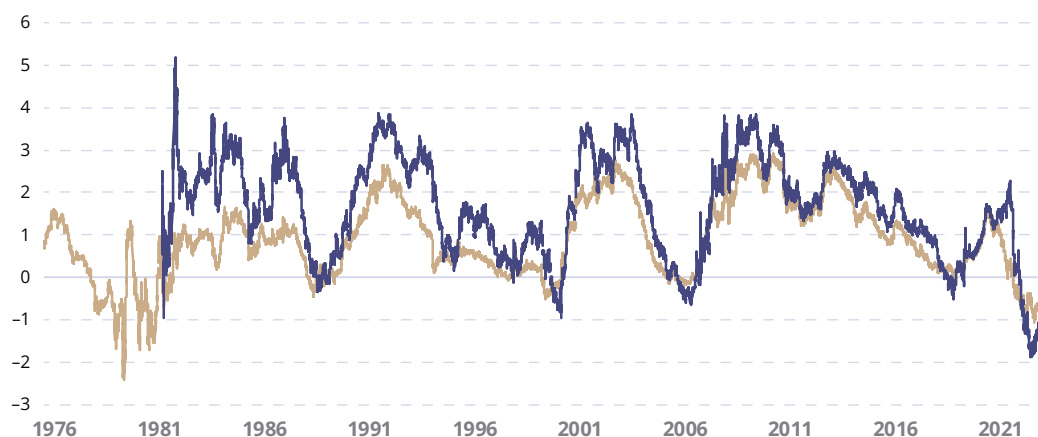
- volatility was lowest for the euro area securities and highest for the UK securities;
- the rates in all the markets and market segments covered by the Chart had fallen markedly by the end of the year from their peaks observed during the year;
- the rates were lower at the end of the year than at the beginning of it, except the yield on the 10-year US Treasury notes, which ended the year 1 basis point higher.

Chart 40. Range of government securities yields in 2023 (yields; %)

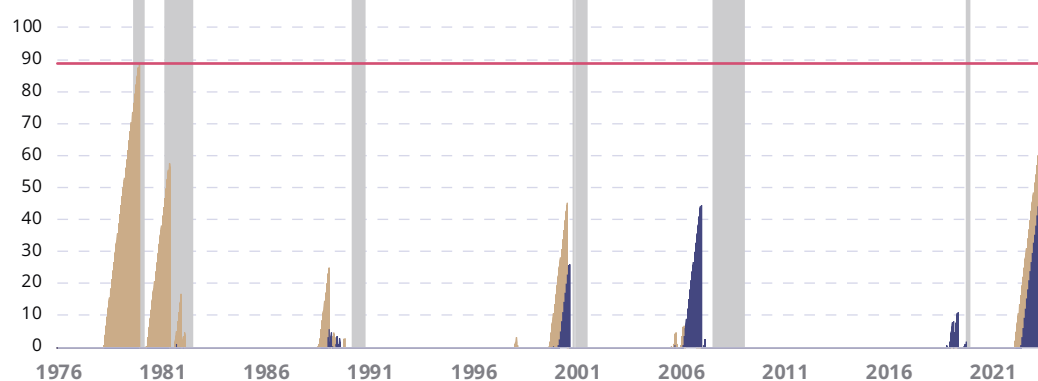
Sources: Bloomberg Finance LP, Latvijas Banka.

Although the restrictive monetary policy of central banks kept short-term interest rates at high levels, the market expectations of weaker economic growth and future rate cuts by central banks maintained the inverted yield curves at historically low levels, with longer-term yields remaining lower than short-term yields throughout the year.

Chart 41. US Treasuries yield curve dynamics (%)



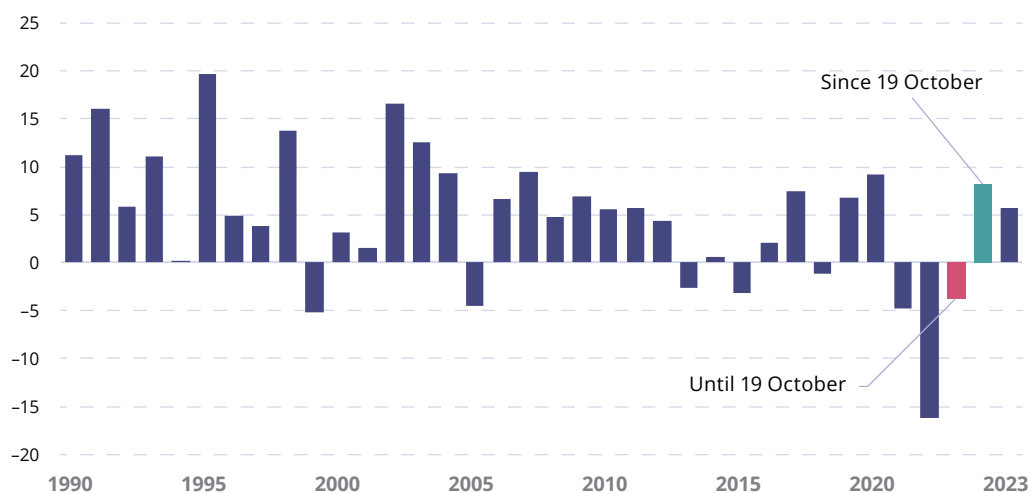
Periods of a negative US Treasury yield curve (duration in weeks)



- Spread between 10-year and 2-year US Treasury yields
- Spread between 10-year and 3-month US Treasury yields
- US recession
- Previous maximum period of a negative spread between 10-year and 2-year yields

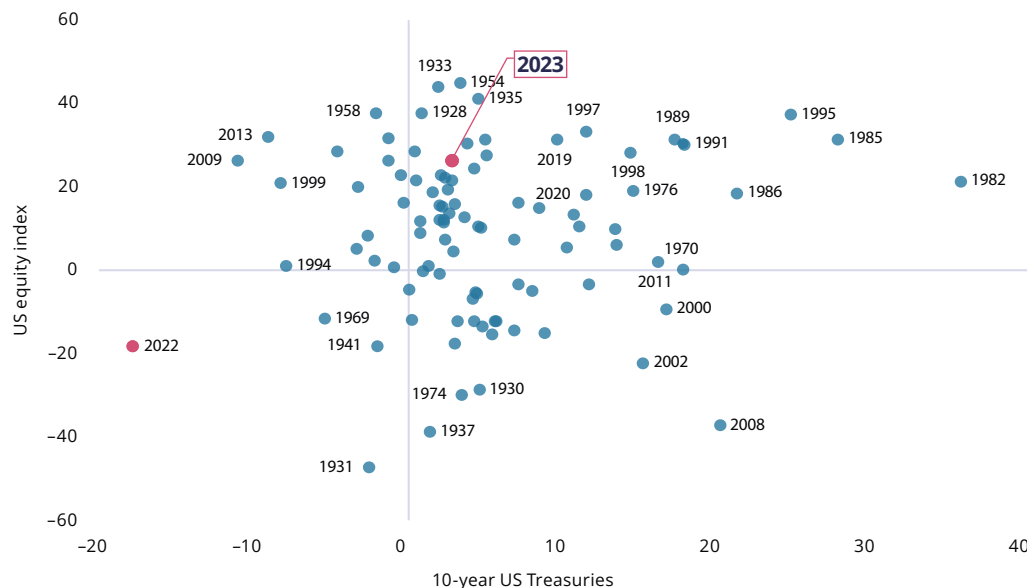
Sources: Federal Reserve Bank of St. Louis, Latvijas Banka.

Following two years of negative returns, with particularly negative returns in 2022, it looked like the overall performance of global fixed income securities would also be negative in 2023, with the annual return bottoming out at -3.8% on 19 October. However, the significant reduction in yields in the fourth quarter, when the global fixed income index showed the fastest two-month rally ever seen, resulted in returns climbing by 8.2% from the lowest point of the year to the end of the year, and thus the total result for the year was 5.7%.

Chart 42. Bloomberg Global Aggregate index annual returns (%)

Sources: Bloomberg Finance LP, Latvijas Banka.

The year 2023 was much more successful than 2022, when investors had no real opportunities to earn profits because of the negative performance of both fixed income securities and equities. Fixed income securities delivered moderate returns in 2023, while the returns on equities were at historical highs.

Chart 43. Annual real returns of the S&P 500 index and 10-year US Treasuries since 1928 (%)

Sources: Bloomberg Finance LP, ICE Data Services, Latvijas Banka.

Payment and settlement systems

Instant payments

The instant payment service of Latvijas Banka's [EKS](#) allows banks to offer [instant payments](#) to their customers to transfer money from an account at one bank to an account at another bank within a matter of seconds on any day and at any time of the day and for the same fee as other credit transfers of the Single Euro Payment Area (SEPA).

At the end of 2023, instant payments were offered in Latvia by Latvijas Banka and seven credit institutions – AS Citadele banka, AS SEB banka, Swedbank AS, Signet Bank AS, BluOr Bank AS, AS Reģionālā investīciju banka and AS LPB Bank – which meant that instant payments were available to more than 90% of the population of Latvia.

The volume and value of instant payments processed through the instant payment service was 1.4 times larger than in the previous year, and a total of 52.9 million instant payments with a value of 22.4 billion euro were processed, with up to 280 thousand instant payments processed on some days. The availability of the instant payment service was higher than 99.9%.

Proxy Registry "Instant Links"

Latvijas Banka also runs the operation of the ["Instant Links" Proxy Registry](#), which lets the customers of several Latvian and Estonian credit institutions make instant payments and other payments even more simply by just indicating the payee's mobile phone number in the payment order.

By the end of 2023, 819 thousand instant links had been registered with the "Instant Links" Proxy Registry, which has availability of over 99.9%, and this is 13% more than at the end of the previous year. The register processed 19.1 million requests in 2023, and 59% of instant links were registered for customers of Latvian banks and 41% for those of Estonian banks.

Digital euro project

Latvijas Banka continues to take an active part in the digital euro project that is being run by the ECB in cooperation with the national central banks of the euro area. The main objective of the digital euro project in 2023 was to finalise the investigation phase by November 2023. Latvijas Banka participated actively in this investigation phase by evaluating whether the design of the digital euro is aligned with Latvia's needs, and by representing Latvia's national interests. This work included participating in the secretariat of the High Level Task Force on Central Bank Digital Currencies (HLTF-CBDC) and preparing the documentation needed.

In 2023, Latvijas Banka enhanced inter-institutional cooperation by providing support and consultation to the Ministry of Finance in its work on the proposed regulatory framework that was published by the EC on 28 June 2023.

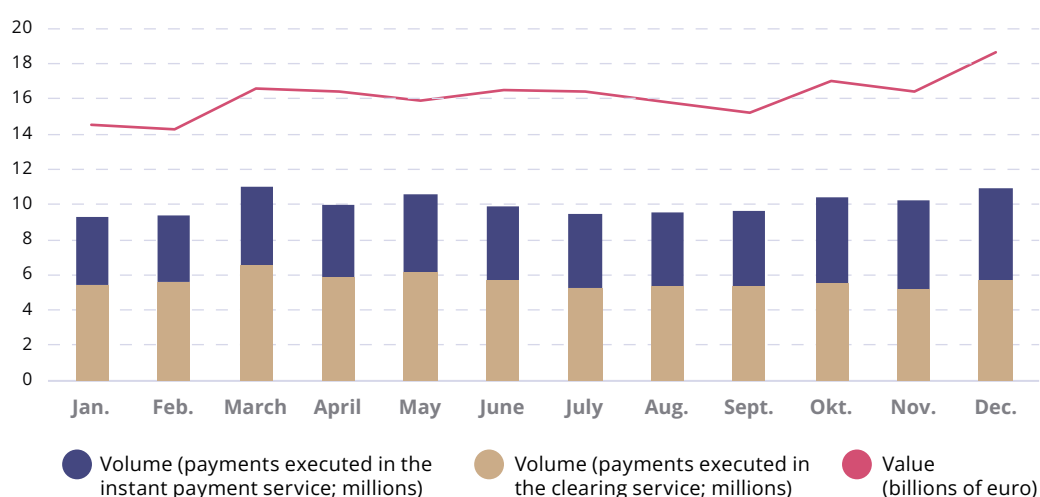
Given the growing public interest in the digital euro project, Latvijas Banka focused on raising public awareness. This work involved producing publications and analytical articles, while ensuring transparency for the project and debunking myths about it. Experts from Latvijas Banka also gave several interviews and offered commentaries to the media to inform the public about the [digital euro](#) project.

Operation of the EKS

The EKS, which was developed and is maintained by Latvijas Banka, continued to provide settlements of customer payments in euro from an account at one bank to an account at another bank for participants in the Latvian payment market through the instant payment service and the clearing service across the SEPA.

The direct participants in the EKS were eight credit institutions, the Treasury and Latvijas Banka. The instant payment service was used by six of the eight credit institutions in 2023, as well as by the Treasury and Latvijas Banka.

Chart 44. Volume and value of payments processed in the EKS

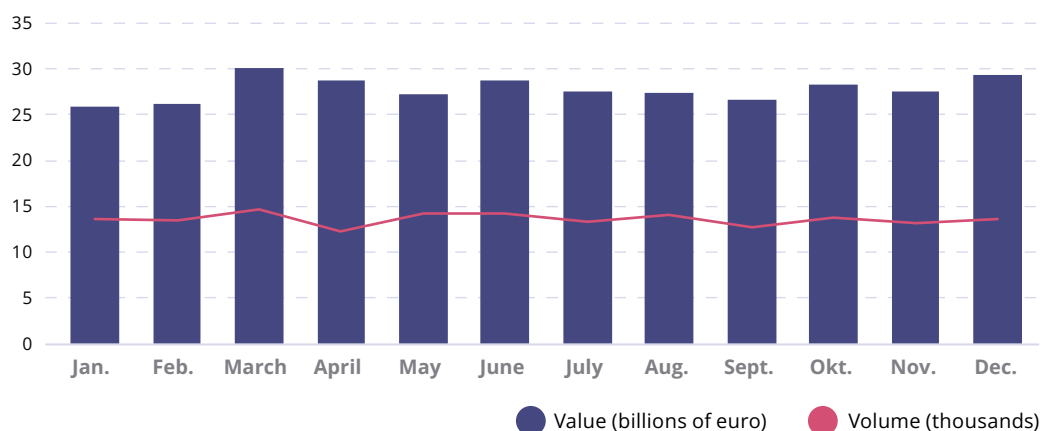


In 2023, 120.4 million SEPA credit transfers totalling 193.7 billion euro were executed in the EKS through the instant payment service and the clearing service combined. The volume of payments executed in the EKS increased by 6.1% over the year and the value by 2.9%.

Operation of TARGET-Latvija

On 20 March 2023, Latvijas Banka along with the other central banks of the Eurosystem finalised the consolidation project for TARGET2 and TARGET2-Securities. A new and innovative TARGET system was established as a result, with its T2 service replacing TARGET2, which had been operational since 2007.

In 2023, Latvijas Banka continued to oversee the operation of TARGET-Latvija, which is a component system of TARGET, the third largest payment system in the world.

Chart 45. Volume and value of payments made in TARGET-Latvija

The availability of the new TARGET, including that of TARGET-Latvija, was 100% in 2023. The system processed an average of 641 payments per day with a value of 1.3 billion euro. While the overall volume of payments declined by 27.54% year on year, primarily because two credit institutions left the system at the end of 2022, the total value of payments fell by a mere 0.52%.

Latvijas Banka also provided payment services in euro to institutions that have settlement accounts at Latvijas Banka, but that were not direct participants of Latvijas Banka's payment system TARGET-Latvija, these being the Treasury and various Latvian, foreign and international financial institutions. The payments by such institutions executed by Latvijas Banka totalled 722 million euro in 2023.

Oversight of the payment system

Latvijas Banka performed day-to-day oversight of the EKS, analysing the system's technical and operational functions, compiling statistical data on it, and making sure that the interbank payment environment in Latvia is secure and efficient.

When overseeing the development of the payment instruments used in Latvia, Latvijas Banka regularly compiled and [analysed](#) data on a semi-annual basis on the payments made by customers of Latvia's payment service providers.

Latvijas Banka participated in projects for drafting the regulatory framework for instant payments and reviewing payment services directives. This involvement included providing support to the Ministry of Finance in formulating Latvia's positions and offering opinions on matters concerning the operation and regulation of payment systems.

Oversight of financial instrument settlement systems

Latvijas Banka worked with Eesti Pank, Lietuvos bankas and the central bank of Iceland in monitoring the implementation of the recommendations and observations outlined in the cyber resilience assessment CROE (Cyber Resilience Oversight Expectations) for the Nasdaq CSD SE depository in 2022. After reviewing the information and evidence provided by the depository, the overseers determined that the depository had implemented a substantial portion of the recommendations and observations by the end of 2023. This effort enhanced its cyber resilience in the areas identified for improvement, and the assessment found that the depository continues to ensure compliance with the CROE standards.

Representing the Eurosystem as the central bank of issue, Latvijas Banka conducted an annual assessment of the compliance of the operations of Nasdaq CSD SE with the requirements of the Eurosystem, gaining assurance that the depository complies with all requirements.

Latvijas Banka offered opinions and commentaries on the amendments to the regulatory framework for settlement and clearing systems in the Central Securities Depositories Regulation (CSDR Refit) and Central Counterparties Regulation (EMIR Refit), partly in order to facilitate effective cooperation between institutions within the supervisory colleges of depositories and to give depositories access to supplementary banking-type services.

Latvijas Banka was involved in the work of Nasdaq CSD SE supervisory college by giving its perspective as an overseer to foster consensus within the college. This included addressing matters surrounding the transfer of existing issuances and settlement efficiency. Latvijas Banka additionally conducted the day-to-day monitoring of the depository, analysing Latvia's securities settlement system from both the technical and operational standpoints.

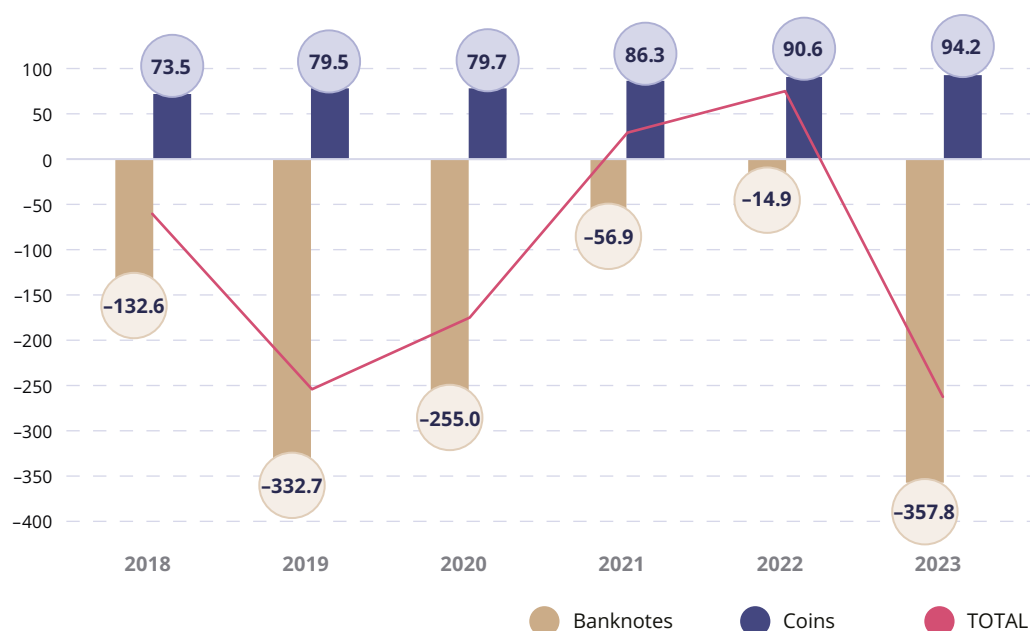
Cash circulation

Securing cash circulation

While non-cash payments are on the rise in Latvia, cash remains a popular choice for purchases. The data from public surveys suggest that the average person makes four payments in cash a week. This makes securing cash circulation one of the most important tasks of Latvijas Banka. Furthermore, cash payments are critical financial services, and the National Security Law stipulates that the availability of them must be ensured in the event of a national security threat.

The net issuance of euro banknotes by Latvijas Banka continued to decline and remained negative in 2023, while the net issuance of euro coins by Latvijas Banka increased. The total net issuance of euro banknotes and coins by Latvijas Banka was consequently -263.6 million euro at the end of 2023.

Chart 46. Net issuance of euro banknotes and coins by Latvijas Banka (millions of euro)



The net issuance of euro banknotes by Latvijas Banka declined by 1.2% in volume in 2023 to 68.9 million banknotes. By the end of 2023, the 50-euro and 20-euro banknotes were the denominations most commonly issued by Latvijas Banka.

The net issuance of euro coins by Latvijas Banka increased meanwhile by 4.8% in volume, reaching 476.1 million coins at the end of December. Of the coins issued by Latvijas Banka, 1 cent and 2 cent coins accounted for the largest numbers of coins in circulation at the end of 2023.

Chart 47. Net issuance of euro banknotes by Latvijas Banka (by nominal value; 2014–2023; volume; millions)

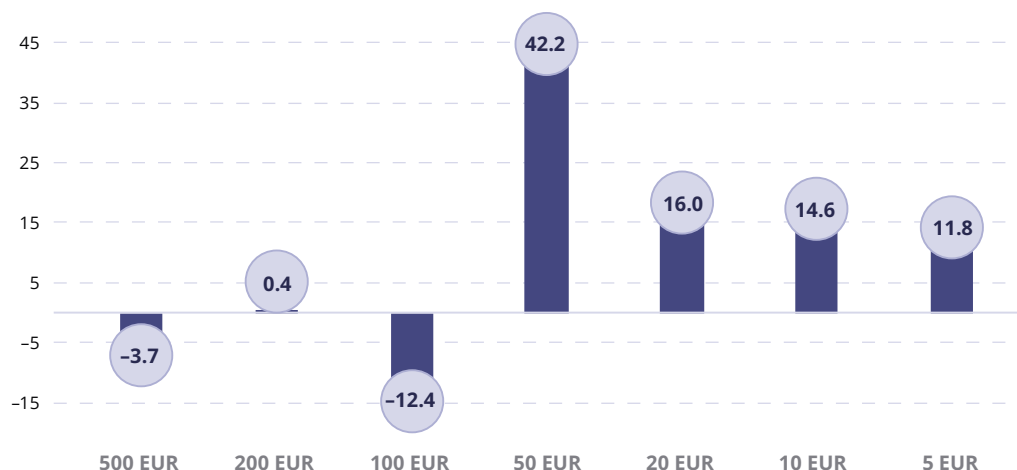
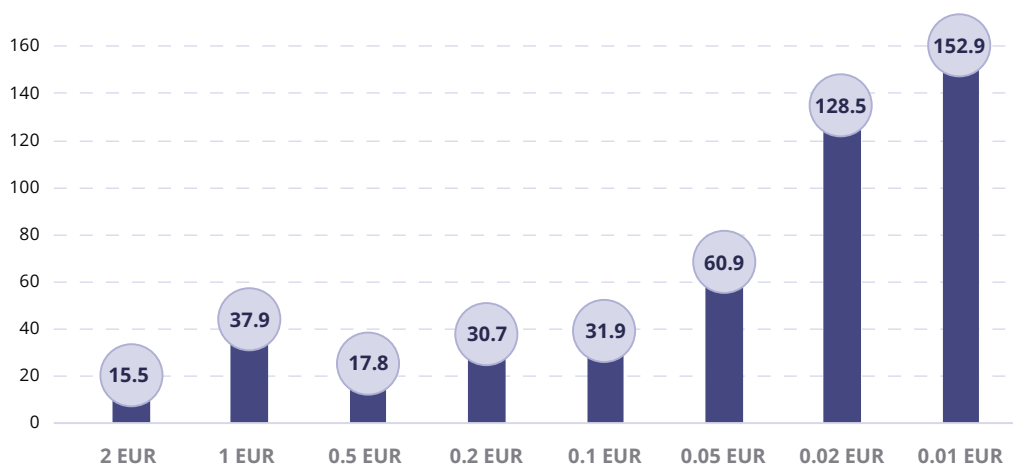


Chart 48. Net issuance of euro coins by Latvijas Banka (by nominal value; 2014–2023; volume; millions)



The cash received from credit institutions was checked for fitness and authenticity by the automated cash processing systems of Latvijas Banka. They processed 141.1 million banknotes in 2023, which was an increase of 11.7% from 2022. Of the banknotes processed, 7.3% or 10.3 million were identified as unfit for circulation and were destroyed.

In 2023, Latvijas Banka continued to register and monitor cash handlers, which are merchants that engage in handling and recirculating euro banknotes and coins. By the end of 2023, 32 cash handlers had been registered in Latvia. Latvijas Banka conducted inspections by assessing how well their operations comply with the requirements in the laws and regulations governing cash handling. Six such inspections were carried out in 2023.

The withdrawal of lats banknotes and coins from circulation continued in 2023. The value of lats banknotes and coins withdrawn from circulation by Latvijas Banka over the year totalled

611.9 thousand lats, with 556.6 thousand lats in banknotes and 55.3 thousand lats in coins. Lats banknotes worth 39.1 million lats and coins worth 43.7 million lats were still in circulation at the end of 2023. At the end of December 2023, the 1.7 million 5 lats and 0.7 million 20 lats banknotes and the 149.3 million 1 santim and 89.4 million 2 santim coins accounted for the majority of the number of banknotes and coins in circulation.

Latvijas Banka, in cooperation with AS Citadele banka, AS SEB banka, Swedbank AS, Luminor Bank AS Latvian branch and the Finance Latvia Association, agreed at the end of 2023 to continue the operation of the Memorandum of Cooperation on Ensuring Access to Cash for Residents of Latvia with slightly revised conditions. The main aim of the Memorandum is to ensure that residents have convenient access to cash across the entire territory of Latvia, and more specifically:

- to maintain the existing network of ATMs with a reduction of no more than 5% in the number of them until 1 January 2025;
- to ensure that 99% of Latvia's population resides within a 20 kilometre straight-line distance from the nearest ATM when the ATM network is created;
- to establish a minimum daily ATM availability of at least 12 hours in alignment with consumer interests.

To ensure the long-term availability of cash in the country, amendments to the Credit Institution Law have been drafted and submitted for further processing to the government and the Saeima. These amendments will clearly outline the responsibilities of banks for the siting and operation of ATMs.

Moreover, Latvijas Banka's regulations were amended to incorporate additional measures for ensuring access to cash in the event of a national threat and maintaining the stability of the financial system under critical circumstances. In light of this, Latvijas Banka now provides support by facilitating the delivery of banknotes to cash handling companies and by allowing the cash handlers authorised by credit institutions to refill their ATM cassettes at the premises of Latvijas Banka.

The law on rounding the total amount of cash payments has been drafted, and discussions with stakeholders have been initiated about how it could be implemented in Latvia for purchases made in cash.

The installation of coin deposit machines at the Riga Branch of Latvijas Banka has made it more convenient and more efficient for the public to exchange small-denomination coins. The public and companies deposited a total of 13 million coins into the cash deposit machines in 2023.

Execution of the functions of the National Analysis Centre and the Coin National Analysis Centre

Number and types of counterfeits

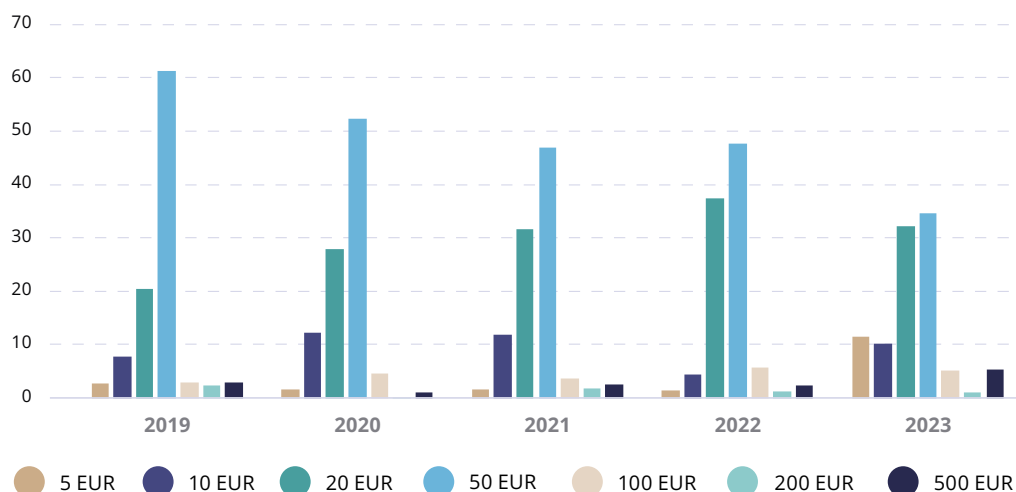
Latvijas Banka serves as the national authority tasked with protecting the euro against counterfeiting, and carrying out the functions of detecting and analysing counterfeit banknotes and coins. To help run these functions, the National Analysis Centre and the Coin National Analysis Centre have been established within the Cash Department of Latvijas Banka.

The main task of the National Analysis Centre is to identify, analyse, record and store all the counterfeit banknotes submitted to Latvijas Banka, thus ensuring that the required measures are implemented and reinforcing coordinated anti-counterfeiting efforts in the EU.

In 2023, Latvijas Banka identified 660 counterfeit euro banknotes and 593 counterfeit euro coins in circulation. The number of counterfeit banknotes increased by 14% year on year, while the number of counterfeit coins rose by 30% over the same period.

The 50-euro and 20-euro banknotes remain the denominations counterfeited most. Counterfeits of them account for over 65% of all the counterfeit euro banknotes in circulation.

Chart 49. Euro banknote counterfeits identified by Latvijas Banka (2019–2023)

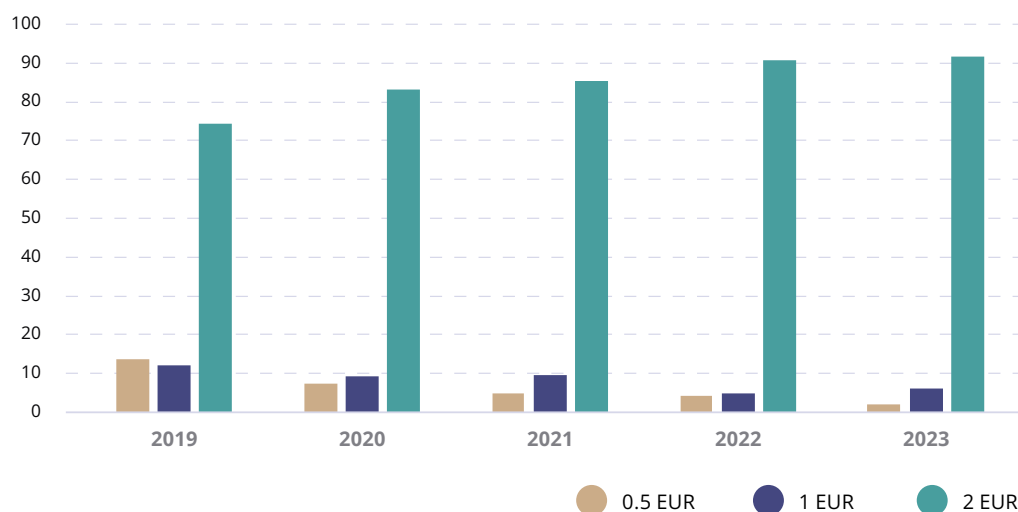


Number of euro banknote counterfeits identified by Latvijas Banka by nominal value

Year	5 €	10 €	20 €	50 €	100 €	200 €	500 €	Total
2019	23	67	178	534	25	20	25	872
2020	13	103	234	437	39	1	9	836
2021	9	71	188	279	22	11	15	595
2022	8	25	217	276	33	7	14	580
2023	76	67	212	229	34	7	35	660
Total	129	333	1029	1755	153	46	98	3543

The majority of counterfeit euro coins identified were two-euro coins. Counterfeit two-euro coins exceeded 90% of all the counterfeit coins identified in 2023.

Chart 50. Euro coin counterfeits identified by Latvijas Banka (2019–2023)



Number of euro coin counterfeits identified by Latvijas Banka by nominal value

Year	50 cents	1 €	2 €	Total
2019	49	43	266	358
2020	17	21	187	225
2021	10	20	176	206
2022	20	22	415	457
2023	13	36	544	593
Total	109	142	1588	1839

Although the number of counterfeits identified in circulation grew by 21% over the year, the overall extent of counterfeits in circulation in Latvia remains consistently at a low level.

Almost all current counterfeit euro banknotes can be easily detected. The counterfeit banknotes identified often exhibit noticeable irregularities in their size, colour shade or image elements. Careful examination of the security features of the banknotes is therefore the best way for people to protect themselves from counterfeits and avoid losses from accepting counterfeit banknotes. So it is important for everyone who uses cash in their daily transactions to be familiar with the features and the design of banknotes and coins and their anti-counterfeiting elements.

Euro commemorative and collector coins issued by Latvijas Banka in 2023

Latvijas Banka issued six collector coins in 2023. They were "Stardust", issued on 11 May 2023; "Song Thrills", issued on 30 June 2023; "100 Years of Basketball in Latvia", issued on 31 October 2023; "The Golden Horses", issued on 15 November 2023; "Fan of Light Rays", issued on 29 November 2023; and "Riga Fashion", issued on 13 December 2023. There was also a two-euro commemorative coin "Sunflower for Ukraine" dedicated to Ukraine's fight for freedom that was issued into circulation from 30 May 2023 in rolls and gift packaging.

Latvijas Banka transferred a donation of 164 684.52 euro to the Ministry of Social Policy of Ukraine in support of Ukraine from the proceeds of the sales of the collector coin "For the Freedom of Ukraine" issued in December 2022 and the 2 euro commemorative coin "Sunflower for Ukraine" issued in May 2023. Mārtiņš Kazāks, Governor of Latvijas Banka, and Jānis Blūms, Head of the Cash Department of Latvijas Banka, symbolically presented the donation to Anatolii Kutsevol, Ambassador of Ukraine to Latvia. During the meeting, the representatives of Latvijas Banka assured the ambassador that Latvijas Banka would continue to support Ukraine and its people in its fight for freedom.



"Stardust"

Weight: 22.00 g; diameter: 35.00 mm
 Metal: silver of fineness .999° with gilding; quality: proof
 Maximum mintage: 4000. Struck in 2023 by
 UAB Lietuvos monetų kalykla (Lithuania)
 Graphic design: Līga Kitchen
 Plaster model: Līgita Franckeviča



"Song Thrills"

Weight: 29.00 g; triangular (52.0 mm × 25.0 mm)
 Metal: silver of fineness .999° with UV print; quality: proof
 Maximum mintage: 4000. Struck in 2023 by
 Regia Autonoma Monetaria Statului (Romania)
 Graphic design: Anna Līva Traumane and Harijs Vucens



"100 years of basketball in Latvia"

Weight: 22.00 g; diameter: 35.00 mm

Metal: silver of fineness .999° with gilding; quality: proof

Maximum mintage: 3000. Struck in 2023 by Istituto

Poligrafico e Zecca dello Stato S.p.A. (Italy)

Graphic design: Paulis Liepa



"The Golden Horses"

Weight: 1.24 g; diameter: 13.92 mm

Metal: gold of fineness 999.9°; quality: proof

Maximum mintage: 2500. Struck in 2023 by

UAB Lietuvos monetų kalykla (Lithuania)

Graphic design: Ivars Heinrihsons

Plaster model: Jānis Strupulis



"Fan of Light Rays"

Weight: 15.00 g; irregular (41 mm x 24 mm)

Metal: silver of fineness .999°; quality: proof

Maximum mintage: 3000. Struck in 2023 by

Koninklijke Nederlandse Munt (the Netherlands)

Graphic design: Ivars Drulle

Plaster model: Līgita Franckeviča



"Riga Fashion"

Weight: 22.00 g; diameter: 35.00 mm

Metal: silver of fineness .999°; colour print on the obverse and reverse; quality: proof

Maximum mintage: 3000. Struck in 2023 by

Istituto Poligrafico e Zecca dello Stato S.p.A. (Italy)

Graphic design: Alīna Grīnpauka

Latvijas Banka invites various Latvian artists to participate in coin design competitions and every coin is therefore a unique work of art.

The themes of the coins are chosen to promote Latvian cultural values and to highlight current topics in society.

Nearly 10 thousand people answered the annual public survey held on the Delfi.lv website, and they voted for the collector coin "Vilhelms Purvītis" as Latvia's Coin of the Year 2022.





Data management, statistics and the Credit Register

Latvijas Banka collects and compiles a wide range of statistical information in pursuit of its tasks. Latvijas Banka uses statistical information for performing financial and macroeconomic analyses, assessing financial stability, supervising financial market participants, and raising public awareness of developments in the financial sector and the economy. The ECB also uses statistical information produced by Latvijas Banka to compile the Eurosystem's monetary statistics and other euro area statistical data, and for other tasks.

Data management

In 2023, the foundations were laid for innovative and modern data management at Latvijas Banka. An assessment of data maturity has been launched, the centralised collection of data has been encouraged, and centralised tools are being phased in to replace some tools with narrower uses.



Aiga Ose
Head of the Data and
Statistics Department

In order to ensure decision making is data driven, it is essential to collect high-quality data of known origin from reliable data sources at the time required and in the manner and amount required, to use appropriate data processing tools, to create an environment that supports modern technologies, and to involve experts with knowledge and experience, and with skills in data processing technologies. By strengthening data management, we also support data-driven decision making.

Latvijas Banka's statistical programmes

To provide transparent information on the activities planned in statistics, [Latvijas Banka publishes its annual statistical programme and a medium-term statistical work](#) programme for three years. Most of the tasks planned that were contained in the statistical programme were successfully fulfilled in 2023, with the exception of three tasks, which were postponed to 2024 for objective reasons. Two of these tasks are ESCB-level tasks of fact-finding and surveying costs for changes in the statistical requirements for insurance companies, and implementation of the new statistical requirements in investment fund statistics, and the third is the national task of expanding the publication of statistics on foreign exchange transactions. Some tasks in supervisory statistics will no longer be classified as tasks relating to statistics.

Development of statistical regulatory framework

The ESCB's complementary cost-benefit assessment on the Integrated Reporting Framework was carried out in the second quarter of 2023, and it also involved Latvian credit institutions, credit unions and other deposit-taking corporations. By total assets, 99% of Latvia's respondents participated in the survey.

The results of the complementary cost-benefit assessment have been summarised at the ESCB level and were published on the ECB's website on 3 April 2024, covering the topics of:

- expansion of the scope of future regulation to cover the country-specific requirements;
- additional functions for optimising the analytical value of the Integrated Reporting Framework;
- operational aspects of reporting and closer alignment of the Integrated Reporting Framework with the supervisory financial reporting (FINREP) requirements set by the EBA at an individual level.

To ease the statistical reporting burden on selected groups of reporting agents given their significance in their segment of the economy, the [Regulation of Latvijas Banka](#) governing the compilation and submission of statistical data on the financial position (1-FP) was amended. These changes reduce significantly the range of statistical data that needs to be submitted by financial corporations that are not supervised by Latvijas Banka and whose economic activity is other than lending.

Development of new experimental statistics

Latvijas Banka participated in the compilation of the [Distributional Wealth Accounts produced by the ECB](#) and in the preparation of their publication. These accounts provide information on the distribution of household wealth and are consistent with the information on the total wealth of the household sector provided in the National Accounts. They also reflect the link between the data from the Household Finance and Consumption Survey and data from the financial and non-financial accounts.

Launch of a new wave of the Household Finance and Consumption Survey

Latvijas Banka launched the 2023–2025 Household Finance and Consumption Survey. This is now [the fourth survey of its kind](#) in Latvia, and in accordance with the ECB requirements, it is run every three years to obtain data on the real and financial assets, liabilities, income and consumption of households. In cooperation with the CSB, a sample of respondents was selected for the survey by using the panel approach, as this provides more complete information on changes in the financial

situation and consumption of households over the longer term. In the panel approach, the sample includes the households that participated in the previous survey. The sampled households were interviewed in autumn 2023.

Improvement of the used data sources

The use of a new data source – [the statistical data on the financial position of financial vehicle corporations](#) – was launched in 2023 in order to:

- prepare statistics on financial vehicle corporations, the balance of payments, the international investment position, the external debt and the financial accounts;
- identify and assess the risks posed to Latvia's financial system by securitisation activities;
- analyse dynamic changes in the economy.

Publication of statistical information

Latvijas Banka continued to provide a wide range of data users with statistical information, both by transmitting statistical data to direct data users on a regular basis and by publishing statistical data in its regular [publications](#) and on its [website](#), including the statistical [database INTS](#). The statistical data produced by Latvijas Banka were also published in ECB publications and the Statistical Data Warehouse, and in IMF publications and within the framework of the IMF Special Data Dissemination Standard Plus (SDDS Plus). Latvijas Banka continued to perform the tasks of the coordinating institution in Latvia within the framework of the SDDS Plus.

The range of interest rate statistics, which covers monetary financial institutions and is published in Latvijas Banka's statistical [database INTS](#), was expanded in 2023, with additional data on the interest rates on various types of loans and deposits by sector without any indication of their maturity.

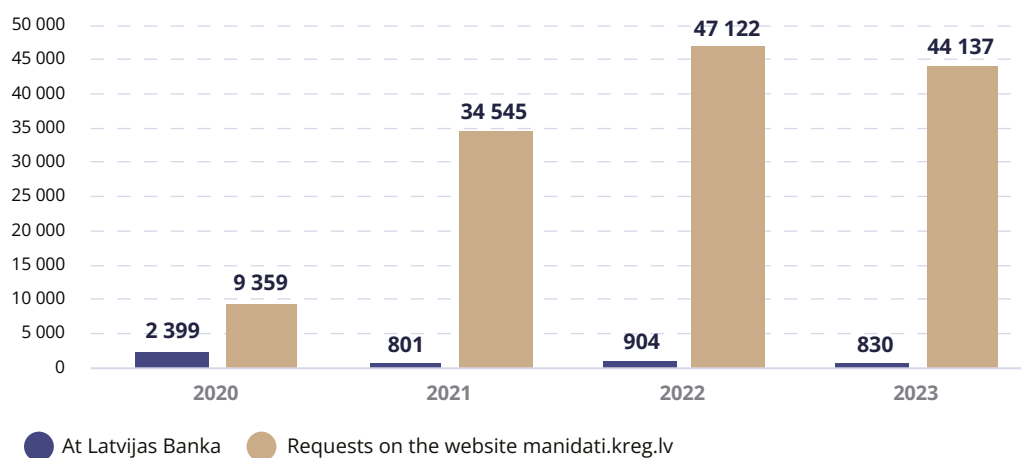
[Financial soundness indicators](#) for non-financial corporations and the expanded banking sector started to be provided, ensuring that an expanded range of indicators on the banking sector was published.

Credit Register

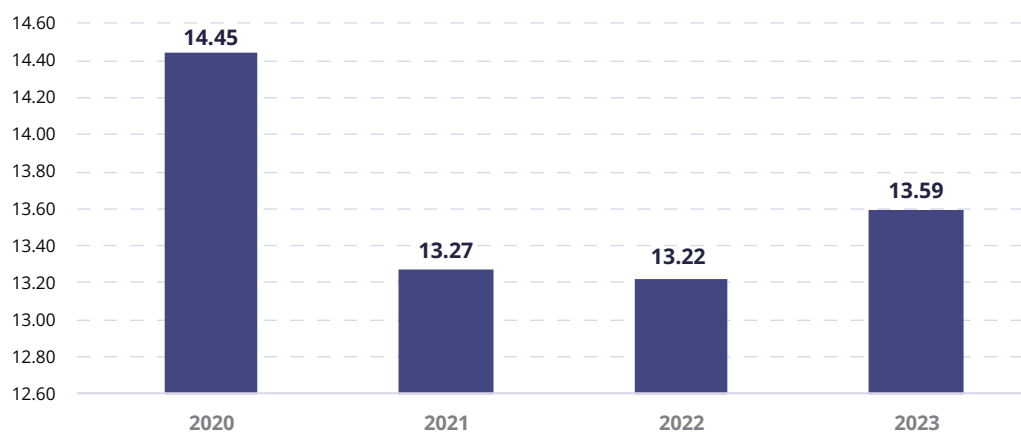
Latvijas Banka ensures the operation of the Credit Register, accumulating data on the loans and guarantees provided to natural and legal persons. The Credit Register provides the information needed for Latvijas Banka to perform its tasks, and gives public institutions an additional way to receive the information that they need for their legally mandated tasks.

At the end of 2023, the [Credit Register](#) held data on 4.7 million obligations, covering outstanding obligations and those that have been fulfilled and are used for the purpose of assessing creditworthiness. These data covered 1.2 million borrowers and guarantors for borrowers from 81 market [participants](#), and the actual outstanding amount of the obligations totalled 21.8 billion euro and the off-balance sheet amount of the obligations totalled 4.7 billion euro. The Credit Register data on loans granted to legal persons are also provided to the ECB within the framework of the [AnaCredit](#) statistics.

Latvijas Banka allows anybody to get a copy of the information held on them in the Credit Register, including on the electronic service website <https://manidati.kreg.lv>, free of charge. The number of requests serviced on this website reached 44 thousand.

Chart 51. Dynamics of the requests received by the Credit Register (number)

In 2023, Credit Register participants submitted 13.6 million requests to the Credit Register to use data from the Credit Register for assessing the creditworthiness of current or potential borrowers and guarantors for borrowers.

Chart 52. Dynamics of the requests made by participants (number; millions)

So that it could conduct additional analysis on the contribution of financial system participants to sustainability, Latvijas Banka expanded the linking of data in the Credit Register with data from other data sources (see the section "[Sustainability](#)").

Advice on matters that Latvijas Banka has responsibility for

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 on aspects of economic policy that are associated with Latvia's participation in the euro area, and on other issues related to the work of Latvijas Banka.

In 2023, officials and staff of Latvijas Banka held regular meetings with members of the Saeima and the government of the Republic of Latvia, for which they 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 to give opinions on financial and economic development.

After analysing the prospects for economic growth in Latvia, Latvijas Banka advised the Saeima and the government on the development of Latvia's economy and other issues in it, such as matters related to taxes, social security, education policy, the second pillar of the pension system, and the pension basis model, and issues relating to Riga's competitiveness and human capital development.

Latvijas Banka also continued to analyse the role of Latvia's financial sector in the economy by continuing an in-depth discussion with financial sector participants and policy makers on lending trends, the factors underlying them, and future developments in Latvia, and by providing an opinion on the proposal to support households against rising interest rates. Latvijas Banka conducted a study of the causes of low customer mobility in Latvia in switching mortgage providers, and developed proposals for how to facilitate mortgage financing, which included drawing up proposals for amendments to regulations in cooperation with other responsible institutions.

Employees of Latvijas Banka participated in various working groups and professional organisations, sharing their experience and providing them with advice and support, including on

- economic forecasts;
- government expenditure and the programming and uptake of EU funds;
- the development of the financial sector, including segments of it like FinTech companies, credit unions, pension funds, crowdfunding service providers, or the capital market, and financial services;
- financial literacy and reducing financial fraud;
- critical financial services;
- the prevention of ML/FTP;
- the availability of cash.

Experts from Latvijas Banka also made proposals and provided support in the process of drafting legal acts and amendments to them that regulate these areas.

Employees of Latvijas Banka continued to participate in their capacity as experts in the Working Group for the Preparation of the Notification of the General Government Budget Deficit and Debt chaired by the CSB, compiling the notification data for the general government budget deficit and debt for 2022 and dealing with the methodological issues related to the compilation of these data.

Experts from Latvijas Banka provided support to the government to enable Latvia to take an active part in the EU and the OECD, and ensured the exchange of information with international rating agencies.

Latvijas Banka organised various training sessions in 2023 for representatives of government authorities and the private sector.

- To improve the knowledge of judges about the nature of financial law and to deepen their understanding of the meaning and application of financial law, a series of seminars for judges who examine cases related to financial activities was organised in cooperation with the Latvian Judicial Training Centre.
 - To facilitate the availability of financial services for the defence sector, training sessions on the standards for preventing ML/FTP and the requirements for providing financial services were organised for businesses in the defence sector and credit institutions.
 - Training and consultations on the basic operating principles of the financial sector and the requirements for internal control systems were held for the Department of Combating Economic Crime and other public institutions.
 - Topical issues in the supervision of the application of sanctions were explained to members of the Latvian Chamber of Commerce and Industry, and the changes and trends in cross-border payments were also explained in the context of sanctions requirements.
-

Cooperation with international organisations and foreign central banks

Latvijas Banka represents the Republic of Latvia in a number of international financial institutions and works with foreign central banks. Latvijas Banka also participates in the operations of other international financial and credit organisations where this is consistent with its objectives and tasks.



Latvijas Banka continued to represent Latvia's interests at the meetings of the IMF Board of Governors, and participated in coordinating operational issues.

- In 2023, the IMF focused particularly on enhancing the resilience of Member States to help them cope with past and potential future shocks like the Covid-19 pandemic, Russia's full-scale invasion of Ukraine, and climate change and resulting natural disasters, and their effects.
- The priorities of the IMF were related to developments in the global economy and the financial system, notably the need to reduce high inflation, maintain financial stability, restore fiscal buffers and debt sustainability, and protect free trade.
- The Member States of the IMF reached an agreement in 2023 on a proportional increase in quotas that will restore the primary role of quotas in the IMF's available resources and maintain the IMF's lending capacity. The IMF provided financial assistance of 84.6 billion US dollars in 2023 to 33 countries around the world

Latvia's interests in the IMF are represented through the Nordic-Baltic Constituency, which consists of Denmark, Estonia, Finland, Iceland, Latvia, Lithuania, Norway and Sweden. One Executive Director represented this constituency on the IMF Executive Board with a total of 3.3% of the votes in 2023. In January 2023, Vitas Vasiļauskas from Lithuania was appointed as the Executive Director of the Nordic-Baltic Constituency, representing the Baltic States. Since January 2023 the central banks of the Baltic States have accordingly been coordinating the cooperation between the central banks and Ministries of Finance of all the Nordic and Baltic countries on IMF issues, and drafting joint positions on items to be considered by the IMF Executive Board.

In 2023, Latvijas Banka continued to coordinate the cooperation of the Latvian institutions with the IMF within the framework of its surveillance mandate or the Article IV Consultation. The annual IMF report on Latvia containing policy recommendations was published in September. The involvement of institutions was also coordinated in the IMF's regional project for the Nordic and Baltic countries *Financial Flows Analysis, AML/CFT Supervision, and Financial Stability*. The results of the report were published in September.

Latvijas Banka continued its membership of the Bank for International Settlements (BIS) in 2023. Latvijas Banka actively participated in the work of the BIS Innovation Network, and in the work of the Eurosystem Innovation Forum (Innov8), where an expert from Latvijas Banka worked on two research projects on the use of artificial intelligence.

Latvijas Banka also continued to work with, exchange information with, and represent Latvia's interests in:

- the European Forum of Deposit Insurers;
- the Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism (MONEYVAL);
- the Group of Banking Supervisors from Central and Eastern European Countries;
- the OECD;
- the International Organization of Securities Commissions (IOSCO);
- the International Association of Insurance Supervisors (IAIS).

At the end of the year, Latvijas Banka submitted a membership application to become a permanent member of the International Organisation of Pension Supervisors (IOPS), and it was admitted to this organisation by the Executive Committee of the IOPS on 13 February 2024.

In addition to working in various EU and international institutions and organisations, Latvijas Banka also cooperated with the supervisory authorities, protection systems or guarantee funds, and resolution authorities of other countries under bilateral cooperation and information exchange agreements. Cooperation with supervisory and resolution colleges also played an important role in exchanges of experience and information.

As is traditional, Latvijas Banka continued to maintain particularly close cooperation with the institutions of other countries within the framework of cooperation between the Nordic and Baltic countries, including the Macroprudential Forum of the Nordic and Baltic countries and its committees and working groups, and also did preparatory work to take over the presidency of this forum in 2024.

Latvijas Banka also continued active daily cooperation within the Baltic region, where similar challenges are often faced in the areas central banks are responsible for, and worked with colleagues from the central banks of Lithuania and Estonia by exchanging experience in issues concerning the availability of critical financial services and in cash processing, and by familiarising colleagues with the regulatory framework for a simplified mortgage refinancing process that was adopted in Latvia.

Experts from Latvijas Banka shared their experience in issues concerning the prevention of ML/FTP and the supervision of the application of sanctions with colleagues from the Netherlands, Czechia,

Ireland, France, Spain, Belgium, Germany and other EU Member States in 2023 within the framework of various EU projects.

In its bilateral cooperation, Latvijas Banka provided support to:

- Ukraine, advising its central bank on information security and cybersecurity issues;
- Moldova, providing training on measures related to preventing ML/FTP in the process of customer due diligence and transaction monitoring;
- Bulgaria, sharing its experience in developing, implementing and coordinating the National Strategy for Financial Literacy;
- Croatia, exchanging experience in issues concerning the supervision of the prevention of ML/FTP, the macroprudential decision-making process, and the processes related to the provision of cash.

Latvijas Banka in the Eurosystem and the institutions of the European Union

Latvijas Banka as a member of the ESCB and the Eurosystem complies in its activities with the legislation of the Republic of Latvia and the EU, including the ECB legal acts, in accordance with the Treaty on the Functioning of the European Union and the Statute of the ESCB and of the ECB.

In 2023, the Governor of Latvijas Banka participated in the work of the Governing Council and the General Council of the ECB, and was involved in setting the monetary policy of the Eurosystem and in making decisions about the tasks of the Eurosystem and the ESCB.

The Deputy Governor of Latvijas Banka participated in the work of the Supervisory Board of the ECB, ensuring that ECB tasks relating to the supervision of credit institutions were executed, and preparing the draft decisions to be submitted to the Governing Council of the ECB under the non-objection procedure. Representatives of Latvijas Banka also participated in the committees and working groups of the Eurosystem and the ESCB, addressing issues of monetary policy, market operations, financial stability, financial sector supervision, payment systems, euro cash and the digital euro, statistics, international relations, communications, sustainability, climate and innovative technologies, and more.

In 2023, Latvijas Banka participated in the work of the ESRB, which took decisions on issues related to EU macroprudential policy, and in the work of the ESRB's committees and working groups.

Continuing its membership in the ESRB, Latvijas Banka integrated the financial sector supervisory functions in 2023 and also became a member of other authorities that form the European System of Financial Supervision¹, representing Latvia and making decisions in the Boards of Supervisors of the EBA, the ESMA and the EIOPA, and actively participating in the work of the committees and working groups of these authorities.

Latvijas Banka as the national resolution authority is a member of the Single Resolution Mechanism. The Member of the Council of Latvijas Banka who chairs the Resolution Committee of Latvijas Banka is a member of the SRB in its plenary session and participates in the SRB's plenary session meetings.

¹ The European System of Financial Supervision is the framework for financial supervision in the EU that has been in operation since 2011. The system consists of three European supervisory authorities (EBA, ESMA, EIOPA), the ESRB, the Joint Committee of the European Supervisory Authorities and the national supervisory authorities of the EU Member States.



Visit of the representatives of the ECB and the Single Resolution Board at Latvijas Banka.

Representatives of Latvijas Banka also participated actively in the work of the committees and working groups of the EU Council, the EC and Eurostat, addressing issues related to financial sector regulation, euro coins, economic forecasting, statistics and other issues, and they provided support to the government in developing the national position on EU regulation.

During the reporting period, active work was under way on the EU legislative proposals published in previous years and on new initiatives published in 2023, including on:

- a set of legal acts concerning anti-money laundering;
- the proposals for strengthening the banking union through the capital requirements regulation for credit institutions and the resolution and crisis management framework, and promoting the further development of the Capital Markets Union through the regulatory framework for financial instruments and fund markets, and central securities depositories, and access to capital for small and medium-sized enterprises from listing their stocks on the stock exchange;
- proposals on the single currency, the euro, with proposals for establishing a legal framework for instant payments and the digital euro, and payment services;
- proposals concerning sustainability and consumer rights protection, and other areas.

When participating in the meetings of the Economic and Financial Committee and its sub-committees, representatives of Latvijas Banka regularly helped prepare decisions concerning the economic development and financial stability of the EU and the development of EU economic policy strategy and the coordination of international relations issues, with a particular focus on assessing the economic consequences and the financial stability risks in the EU resulting from Russia's full-scale invasion of Ukraine, and helped assess the EC's legislative proposals for financial services.

Financial Statements of Latvijas Banka for the Year Ended 31 December 2023

Contents

Balance Sheet	111
Profit and Loss Statement	112
Statement of Total Recognised Gains and Losses	114
Notes to the Financial Statements	115

Abbreviations

BIS	Bank for International Settlements
ECB	European Central Bank
ESCB	European System of Central Banks
EU	European Union
FCMC	Financial and Capital Market Commission
IMF	International Monetary Fund
NCB	national central bank
OTC	over-the-counter
PEPP	Pandemic Emergency Purchase Programme
PSPP	Public Sector Asset Purchase Programme
SDR	Special Drawing Rights
TLTRO	targeted longer-term refinancing operations
UK	United Kingdom
US	United States of America

BALANCE SHEET

(at the end of the year; in thousands of euro)			
	Note ¹	2023	2022
ASSETS			
Gold and gold receivables	6	399 378	364 821
Claims on non-euro area residents denominated in foreign currency	7	4 049 526	3 788 044
Receivables from the International Monetary Fund		534 839	549 961
Balances with banks and security investments, external loans and other external assets		3 514 687	3 238 083
Claims on euro area residents denominated in foreign currency	8	595 802	522 039
Claims on non-euro area residents denominated in euro	9	168 476	156 383
Lending to euro area credit institutions related to monetary policy operations denominated in euro	10	92 900	522 900
Longer-term refinancing operations		92 900	522 900
Other claims on euro area credit institutions denominated in euro	11	133	6 304
Securities of euro area residents denominated in euro	12	13 550 657	14 081 606
Securities held for monetary policy purposes		12 586 724	13 134 812
Other securities		963 933	946 794
Intra-Eurosystem claims	13	6 412 443	5 926 959
Participating interest in the European Central Bank		118 849	118 849
Claims equivalent to the transfer of foreign reserves		157 202	157 202
Other claims within the Eurosystem		6 136 392	5 650 908
Other assets	14	295 505	381 638
TOTAL ASSETS		25 564 820	25 750 694

¹ The accompanying Notes set out on pages 115 to 156 are an integral part of these financial statements.

<i>(continued)</i>	<i>(at the end of the year; in thousands of euro)</i>		
	Note	2023	2022
LIABILITIES			
Banknotes in circulation	15	5 571 492	5 635 738
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	16	7 073 547	5 217 165
Current accounts (covering the minimum reserve system)		205 834	343 816
Deposit facility		6 867 713	4 873 349
Other liabilities to euro area credit institutions denominated in euro	17	314 720	320 273
Liabilities to other euro area residents denominated in euro	18	2 218 786	2 517 104
General government		1 131 021	1 157 761
Other liabilities		1 087 765	1 359 343
Liabilities to non-euro area residents denominated in euro	19	184 075	171 688
Liabilities to euro area residents denominated in foreign currency	20	1 262 758	706 038
Liabilities to non-euro area residents denominated in foreign currency	21	457 718	34 701
Intra-Eurosystem liabilities	13	7 569 389	10 376 364
Liabilities related to TARGET and correspondent accounts (net)		7 569 389	10 370 127
Other liabilities within the Eurosystem		–	6 237
Other liabilities	22	182 217	184 740
Capital and reserves	23	730 118	586 883
TOTAL LIABILITIES		25 564 820	25 750 694

The financial statements set out on pages 110 to 156 were authorised by the Council of Latvijas Banka on 8 March 2024.

Governor of Latvijas Banka

Mārtiņš Kazāks

EXPLANATION REGARDING TRANSLATION

This is a translation of the financial statements from the original, which was prepared in Latvian, and all due care has been taken to ensure that it is an accurate representation. However, the original language version of the financial statements takes precedence.

PROFIT AND LOSS STATEMENT

(in thousands of euro)

	Note	2023	2022
Net interest income	33	-229 006	47 021
Interest income		503 974	211 229
Interest expense		-732 980	-164 208
Net result of financial operations, recognition of revaluation result in the profit and loss statement and financial risk provisions		-10 948	-21 337
Realised gains arising from financial operations	34	9 000	39 732
Recognition of revaluation result on financial assets and positions in the profit and loss statement	23, 35	-34 999	-341 715
Provisions for market risk and credit risk	36	15 051	280 646
Net expense from fees and commissions		-3 912	-4 441
Fees and commissions income		1 037	1 011
Fees and commissions expense		-4 949	-5 452
Income from equity securities and participating interest	37	12 222	14 755
Net result of pooling of monetary income	38	206 554	-6 237
Other operating income	39	19 561	5 766
NET INCOME		-5 529	35 527
Remuneration	40	-24 728	-16 502
Social security costs and solidarity tax	40	-5 540	-3 653
Banknote and coin acquisition costs	41	-2 338	-2 618
Depreciation of fixed assets and amortisation of intangible assets	14	-3 660	-3 641
Other operating expenses	42	-11 965	-9 113
PROFIT/LOSS(-) FOR THE YEAR		-53 760	0

STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

(in thousands of euro)			
	Note	2023	2022
Profit/loss(–) for the year		–53 760	0
Revaluation	23	164 173	–450 273
Realisation of the accumulated revaluation result	23	–2 177	–198 579
Recognition of revaluation result on financial assets and positions in the profit and loss statement	23, 35	34 999	341 715
Total changes in the revaluation account	23	196 995	–307 137
TOTAL		143 235	–307 137

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, in accordance with the Treaty on the Functioning of the European Union the primary objective of Latvijas Banka is to maintain price stability. Without prejudice to the primary objective, Latvijas Banka shall support the general economic policies of the European Union and also contribute to the overall stability of Latvia's financial system.

Latvijas Banka shall participate in the performance of the tasks of the European System of Central Banks and perform other tasks which are not in contradiction with the objectives of Latvijas Banka specified in Section 4 of the Law on Latvijas Banka and the performance of the tasks of the European System of Central Banks, including:

- a) participate in the definition of the monetary policy and implement it;
- b) perform macroeconomic analysis and research;
- c) determine and implement the macroprudential policy;
- d) regulate and supervise the operation of the financial market and its participants;
- e) perform the tasks of a resolution authority;
- f) ensure the operation of the Deposit Guarantee Fund, the operation of the Fund for the Protection of the Insured, the operation of the National Resolution Fund, and the disbursement of compensations to investors;
- g) manage foreign reserves and other assets;
- h) promote smooth operation of the payment and financial instrument settlement systems, including ensure efficient and safe operation and development of the payment system of Latvijas Banka;
- i) store the Treasury funds, including in foreign currency;
- j) issue euro banknotes and coins and also promote their availability in Latvia;
- k) register and control legal entities which carry out the handling of euro banknotes and coins and putting back thereof into circulation;
- l) perform the functions of the National Analysis Centre and the Coin National Analysis Centre;
- m) ensure statistical information, inter alia, assist the European Central Bank in production of statistical information necessary for the performance of the tasks of the European System of Central Banks;
- n) maintain the Credit Register;
- o) consult the *Saeima* and the Cabinet on monetary policy issues and other issues related to the performance of the tasks of Latvijas Banka, including on issues of economic and fiscal policy which affect the effectiveness of monetary policy implementation;
- p) promote financial literacy of and acquisition of economic knowledge by the public.

On 1 January 2023, the new Law on Latvijas Banka, adopted on 23 September 2021, entered into force and provides for the FCMC's incorporation in Latvijas Banka. Accordingly, Latvijas Banka has the tasks referred to in points (c), (d), (e), and (f).

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's activities are overseen 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. In addition, the financial market participants supervised by Latvijas Banka shall, in accordance with the laws governing the activities of the relevant financial market participants, make payments to Latvijas Banka to cover the expenses of supervisory functions, i.e. expenses of Latvijas Banka directly or indirectly related to the regulation and supervision of the activities of the financial market and its participants, the application of resolution and the provision of compensation payment systems (hereinafter – supervision function expenses).

The Head Office of Latvijas Banka is situated at K. Valdemāra iela 2A, Riga. Latvijas Banka manages the storage and processing of cash through its branch at Bezdēlīgu iela 3, Riga.

2. PRINCIPAL ACCOUNTING POLICIES

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 the Council of Latvijas Banka, and the requirements of the Law on Latvijas Banka governing financial reporting.

2.2 Basis of measurement

Gold, participating interest in the BIS, and securities are measured at fair value, except held-to-maturity debt securities and securities held for monetary policy purposes that are measured at amortised cost. Securities held to maturity are securities with fixed or determinable payments and fixed maturity which Latvijas Banka intends to hold to maturity. The participating interest in the ECB is measured according to the procedure referred to in Note 13.1.

Derivatives are accounted for at fair value, except forward exchange rate contracts and currency swap arrangements that are measured according to the principles described in Notes 2.4 and 2.10.

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

Euro banknotes and coins issued are recorded at nominal value on the balance sheet. The lats banknotes and coins issued by Latvijas Banka which have not yet been exchanged for the euro banknotes and coins are recognised on the balance sheet as liabilities, considering the exchange probability of such lats banknotes and coins within 20 years from the euro changeover. Euro collector coins, lats gold circulation coins and lats collector coins are not recognised on the balance sheet (see also Notes 22.1 and 45).

Fixed assets and intangible assets are reported on the balance sheet at cost less the accumulated depreciation and amortisation.

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 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. 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.

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. Forward exchange rate contracts, currency swap arrangements, and spot exchange rate contracts are included in the net position of the respective currency on the transaction day at the spot rate of the transaction and are recorded on the balance sheet in euro at the exchange rate of the respective currency prevailing at the end of the reporting period. The principles 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 2023 and the year ended 31 December 2022 are as follows:

	(at the end of the year)		
	2023	2022	Changes (%)
US dollar (USD)	1.1050	1.0666	3.6
Japanese yen (JPY)	156.33	140.66	11.1
Canadian dollar (CAD)	1.4642	1.4440	1.4
British pound sterling (GBP)	0.86905	0.88693	-2.0
Gold (XAU)	1867.828	1706.075	9.5

2.5 Reverse and other collateralised transactions

Securities that are pledged for the benefit of Latvijas Banka or purchased under reverse transactions are not reported on Latvijas Banka's balance sheet. Securities that are lent, pledged for the benefit of a counterparty or sold under reverse transactions are reported on Latvijas Banka's balance sheet along with other securities that are not pledged in such transactions. Any cash paid or received in reverse or collateralised transactions is reported on Latvijas Banka's balance sheet as loans or deposits respectively.

2.6 Fixed and intangible assets

Fixed and intangible assets are long-term assets with the useful life of over one year. The capitalisation limit of fixed and intangible assets in 2023 and 2022 was 1000 euro, except for the costs related to real estate improvements and replacement of fixed asset parts for which the Council of Latvijas Banka has set a higher capitalisation limit depending on their significance.

Depreciation and amortisation are recognised using the straight-line method over the estimated useful life of the fixed or intangible asset. Buildings and structures are accounted for by separate components, with individual useful life set for each such component.

In 2023, the useful lives set for fixed and intangible assets were not changed. In 2023 and 2022, the useful lives set were as follows:

	(years)	
	2023	2022
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
Intangible assets	1–10	1–10

2.7 Use of estimates and assumptions

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 2.2), the useful life of fixed assets and intangible assets (see Note 2.6), impairment of assets (see Note 2.8), the exchange probability of those lats banknotes and coins that have not been yet exchanged for euro banknotes and coins (see Note 2.2), the repurchasing probability of collector coins (see Note 45), provisions for market risk and credit risk (see Note 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).

2.8 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, e.g. a significant deterioration of the credit quality or event of default. 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).

2.9 Recognition of gains and losses on financial instruments, foreign currency and gold positions

Gains and losses on financial instruments, foreign currency and gold positions 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;

(f) 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;

(g) 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;

(h) when recognising income from equity securities, the income recognition principles 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.

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

2.10 Interest income and expense

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

Interest on securities also includes premium and discount, which are amortised over the remaining life of the respective securities using the straight-line method.

The spot and forward currency exchange 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.

2.11 Other expenses and income

Banknote and coin acquisition costs are charged to the profit and loss statement at the time of banknote and coin acquisition.

Proceeds from sales of collector coins are recognised in the profit and loss statement when incurred.

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 2023, Latvijas Banka's assets decreased by 185.9 million euro to 25.6 billion euro.

Foreign currency claims on non-euro area residents increased by 261.5 million euro as a result of income received and revaluation.

The balance sheet item "Securities held for monetary policy purposes" decreased by 548.1 million euro due to redemption of securities under the PSPP and PEPP. At the end of 2023, Latvijas Banka held securities purchased for monetary policy purposes amounting to 12.6 billion euro, of which Latvian government securities – 4.0 billion euro.

The amount of loans granted to credit institutions by Latvijas Banka as a result of longer-term refinancing operations decreased by 430.0 million euro as a result of their repayment (see also Note 10.2).

Other claims related to other operational requirements within the Eurosystem grew by 485.5 million euro, mostly due to a rise in claims on banknote allocation in the Eurosystem (see also Note 13.4) and an increase in claims to the ECB associated with the net result of pooling of monetary income.

Banknotes in circulation decreased by 64.2 million euro, in line with the fall in the overall amount of banknotes in circulation of the euro area NCBs.

The increase of 556.7 million euro under the balance sheet item "Liabilities to euro area residents denominated in foreign currency", as well as the increase of 423.0 million euro under the balance sheet item "Liabilities to non-euro area residents denominated in foreign currency" are mostly related to the increase in repurchase agreements and gold swaps arrangements.

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 1856.4 million euro.

As a result of cross-border payments, liabilities to the ECB for the settlement result in TARGET, reported under the balance sheet item "Intra-Eurosystem liabilities", decreased by 2800.7 million euro.

The capital and reserves of Latvijas Banka increased by 143.2 million euro due to net increase in the financial instruments revaluation account balance (197.0 million euro) and the operating result of the reporting year (loss of 53.8 million euro).

3.2 Financial performance

Taking into account global geopolitical and economic developments, which led the ECB to significantly increase interest rates with the aim of curbing inflation in the euro area, Latvijas Banka closed the year 2023 with a negative financial result – losses of 53.8 million euro – reflected in the profit and loss statement (Latvijas Banka recorded a neutral financial result of 0 euro in 2022). Meanwhile, the total financial result of its activities reached 143.2 million euro, increasing Latvijas Banka's capital and reserves to 730.1 million euro at the end of the year. The total gains of capital and reserves were mainly driven by the rise in the market value of financial investments by 197.0 million euro (in 2022, the market value of financial investments decreased by 307.1 million euro), which is reported in capital and reserves as a revaluation reserve and is not included in the profit and loss statement of the reporting year.

In 2023, Latvijas Banka's financial performance was adversely affected by the Eurosystem's monetary policy operations decisions related to curbing inflation. The ECB raised the interest rate on the main refinancing operations by 450 basis points over a year and a half from 0% in July 2022 to 2.5% and 4.5% at the end of 2022 and 2023 respectively, the deposit facility rate (from –0.5% in July 2022 to 2% and 4% at the end of 2022 and 2023 respectively), and the marginal lending facility rate (from 0.25% in July 2022 to 2.75% and 4.75% at the end of 2022 and 2023 respectively). As interest rates increased, expenditure by the central banks of the Eurosystem, including Latvijas Banka, on monetary policy operations and deposits by the government and other institutions increased significantly. Since the beginning of 2022, there was uncertainty and the global economy was particularly negatively affected by the war waged by Russia against Ukraine. With the supply chain bottlenecks intensifying and energy and food prices rising at the same time, inflation hit record highs. To curb inflation, central banks began to sharply raise base interest rates in 2022 and continued to do so in 2023.

Net interest expenses in 2023 were 229.0 million euro (net interest income in 2022 was 47.0 million euro). This was driven by higher interest expenses (EUR 733.0 million (in 2022 – EUR 164.2 million)) than interest income (EUR 504.0 million (in 2022 – EUR 211.2 million)) due to higher interest income on securities, higher interest income on intra-Eurosystem claims, but also higher interest expense on deposits of Latvian credit institutions, reaching 173.9 million euro (18.1 million euro in 2022), higher interest expense on Latvian government deposits, reaching 45.3 million euro (interest income 1.6 million euro in 2022), and higher interest expense on intra-Eurosystem liabilities as a result of rising interest rates.

The realised gains on financial operations amounted to 9.0 million euro (39.7 million euro in 2022), which was positively affected by the result of the realised gains from the disposal of debt securities, but recognition of the negative revaluation result on financial assets and positions in the profit and loss statement stood at 35.0 million euro (341.7 million euro in 2022), and this was mainly due to the significantly smaller decrease in debt securities market value driven by the stabilisation of the rise in interest rates.

Latvijas Banka used the established provisions for financial risks amounting to 15.1 million euro (in 2022, the respective provisions were used in the amount of 280.6 million euro).

Income from equity securities and participating interest amounted to 12.2 million euro (14.8 million euro in 2022).

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. Latvijas Banka's net result of pooling of monetary income increased and stood at 206.6 million euro in 2023 (it was negative in 2023 – –6.2 million euro), as the ECB's interest rate hikes led to a significant increase in interest expenditure included in the reallocation of monetary income in 2023.

Other operating income stood at 19.6 million euro (5.8 million euro in 2022). The increase in income was mainly due to payments of 13.9 million euro from the financial market participants supervised by Latvijas Banka, as since 1 January 2023 when the FCMC was incorporated in Latvijas Banka, those financial market participants make payments to cover supervision function expenses.

The bank's operating expenses amounted to 48.2 million euro (35.5 million euro in 2022). The increase in expenses is mainly related to supervision function expenses since the FCMC was incorporated in Latvijas Banka as of 1 January 2023.

Losses or low profit ratios are expected to persist for many central banks for several years. In the future, Latvijas Banka's financial performance will also be mostly 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.

4. FINANCIAL INVESTMENT POLICY

Investments are managed in compliance with the basic principles set by the Council of Latvijas Banka – preserving the value of investments, ensuring their liquidity and earning income within the framework of acceptable risk in the medium term. In addition the sustainability principle is respected 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. Latvijas Banka's investments include the portfolios of 1–10 year fixed income securities, mortgage-backed securities, developed markets equity securities, long-term fixed income securities, global fixed income securities, emerging markets equity securities, emerging markets fixed income securities, Latvian government securities, and gold. The developed markets equity securities portfolio, the mortgage-backed securities portfolios and the global fixed income securities portfolio 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 portfolio, mortgage-backed securities portfolios, the portfolio of borrowed funds, the developed markets equity securities portfolio, the global fixed income securities portfolio, the emerging markets equity securities portfolio and emerging markets fixed income securities portfolio.

The breakdown of investments by type of investment portfolio at the end of 2023 and 2022 was as follows:

	Book value (in thousands of euro)		Proportion (%)	
	2023	2022	2023	2022
1–10 year fixed income securities portfolio	2 920 052	2 790 364	46.8	46.8
Mortgage-backed securities portfolios	1 064 521	1 052 437	17.0	17.7
Developed markets equity securities portfolio	607 748	509 656	9.8	8.5
The portfolio of borrowed funds	539 561	551 032	8.7	9.2
Gold portfolio	399 378	364 821	6.4	6.1
Emerging markets fixed income securities portfolio	293 431	301 579	4.7	5.0
Long-term fixed income securities portfolio	168 394	168 320	2.7	2.8
Global fixed income securities portfolio	140 426	138 623	2.3	2.3
Emerging markets equity securities portfolio	60 792	59 002	1.0	1.0
Latvian government securities portfolio	36 424	36 416	0.6	0.6
Total	6 230 727	5 972 250	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 developed markets equity securities portfolio benchmark is the equity securities index comprised of issuers from developed countries.

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

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

The emerging markets fixed income securities portfolio benchmark is the public sector issuer index of emerging market countries with an investment grade rating by international credit rating agencies.

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 global fixed income securities portfolio benchmark is a global fixed income securities index that meets investment grade determined by international credit rating agencies.

The emerging markets equity securities portfolio benchmark is the equity securities index comprised of issuers from emerging market countries.

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 is the euro (limiting the currency risk) for Latvijas Banka's investment portfolios that include the 1–10 year fixed income securities portfolio, the mortgage-backed securities portfolios, the long-term fixed income securities portfolio, the emerging markets fixed income securities portfolio, and the Latvian government securities portfolio. 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 identical or similar 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 2023 and 2022, Latvijas Banka's assets carried at fair value were generally valued on the basis of a quoted market price in active markets.

At the end of 2023 and 2022, 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 2023 and 2022, 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 2023						
Gold	399 378	399 378	–	–	399 378	–
Securities in investment portfolios	5 166 827	4 439 729	723 120	–	5 162 849	–3 978
Forward exchange rate contracts	31 752	–	31 296	–	31 296	–456
Securities held for monetary policy purposes	12 671 386	11 026 232	–	–	11 026 232	–1 645 154
Participating interest in the Bank for International Settlements	37 863	–	–	37 863	37 863	–
Total	18 307 206	15 865 339	754 416	37 863	16 657 618	–1 649 588
As at 31 December 2022						
Gold	364 821	364 821	–	–	364 821	–
Securities in investment portfolios	4 815 309	4 165 042	638 344	–	4 803 386	–11 923
Forward exchange rate contracts	171 694	–	170 486	–	170 486	–1 208
Securities held for monetary policy purposes	13 212 490	10 985 608	–	–	10 985 608	–2 226 882
Participating interest in the Bank for International Settlements	37 119	–	–	37 119	37 119	–
Total	18 601 433	15 515 471	808 830	37 119	16 361 420	–2 240 013

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 2021	213 836	344 166
During 2022		
Net change resulting from gold swaps arrangements	x	20 655
As at 31 December 2022	213 836	364 821
During 2023		
Increase in gold market value	x	34 589
Net change as a result of gold swaps arrangements	-17	-32
As at 31 December 2023	213 819	399 378

The revaluation result of gold is recognised under the balance sheet item "Capital and reserves" as the revaluation result (see also Note 23).

To limit the gold maintenance costs and ensure return on gold investments, gold may be involved in gold swaps arrangements (at the end of 2023, gold in the amount of 186 783 thousand euro was involved in gold swaps arrangements; at the end of 2022 Latvijas Banka had not concluded gold swaps arrangements (see also Notes 20, 21 and 43)). Gold swaps arrangements are treated as repurchase agreements.

At the end of 2023 and 2022, 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 a promissory note 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 2023, the receivables from the IMF in SDR as recorded on Latvijas Banka's balance sheet were equivalent to 534 839 thousand euro (549 961 thousand euro at the end of 2022), whereas the liabilities to the IMF were made up of funds at the disposal of the IMF in the amount of 1405 thousand euro (1449 thousand euro at the end of 2022) held on its Accounts No. 1 and No. 2 (see also Note 19).

At the end of 2023 and 2022, Latvia's net receivables from the IMF were as follows:

	(in thousands of euro)		(in thousands of SDR)	
	2023	2022	2023	2022
Latvia's quota in the International Monetary Fund	403 977	415 940	332 300	332 300
International Monetary Fund holdings in euro	-377 157	-394 586	-310 239	-315 239
Promissory note of the Latvian government	-375 752	-393 137	-309 083	-314 082
Account No. 1	-1 010	-1 040	-831	-831
Account No. 2	-395	-409	-325	-326
Reserve position in the International Monetary Fund	27 215	21 763	22 386	17 387
incl. financing of the Financial Transaction Plan	26 745	21 279	22 000	17 000
SDR	534 839	549 961	439 943	439 372
General allocation	-501 468	-516 316	-412 493	-412 493
Special allocation	-32 610	-33 576	-26 824	-26 824
Latvia's net receivables from the International Monetary Fund	27 976	21 832	23 012	17 442

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. In 2022, considering Latvia's economic development and following the policies and procedures of membership of the IMF, Latvia was included in the IMF's Financial Transaction Plan. The countries included in the plan participate in the financing of the IMF's lending operations, not exceeding the amount of the national quota, receiving interest payments in return. At the end of 2023, the financing of the Financial Transaction Plan amounted to 22 million SDR (at the end of 2022 – 17 million SDR).

7.2 Balances with credit institutions and security investments, external loans and other external assets

	(in thousands of euro)	
	2023	2022
Securities	3 425 188	3 182 643
Demand deposits	89 499	44 939
Reverse repurchase agreements	–	10 407
Foreign currency in cash	–	94
Total	3 514 687	3 238 083

8. CLAIMS ON EURO AREA RESIDENTS DENOMINATED IN FOREIGN CURRENCY

	(in thousands of euro)	
	2023	2022
Securities	595 515	521 132
Demand deposits	287	907
Total	595 802	522 039

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

	(in thousands of euro)	
	2023	2022
Securities	160 464	148 569
Demand deposits	8 012	7 814
Total	168 476	156 383

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

At the end of 2023, the total amount of Eurosystem loans in monetary policy operations reached 410 290 million euro (1 324 347 million euro at the end of 2022), including 92.9 million euro (522.9 million euro at the end of 2022) 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. 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 2023 and 2022, 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 maturity of three 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 had a four-year maturity, with a possibility of early repayment after two years. In 2021, the operations were discontinued. Additionally, 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 and since September 2021 – after one year. In 2020, the Governing Council of the ECB added three further operations to this series, which were 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%. In addition, on 27 October 2022, the Governing Council of the ECB decided that, from 23 November 2022 until the maturity date or early repayment date of each respective outstanding TLTRO III operation, the interest rate on TLTRO III operations will be indexed to the average applicable key ECB interest rates over this period. On the same date, the Governing Council of the ECB decided to introduce three additional voluntary early repayment dates to provide TLTRO III participants with additional opportunities to partly, or fully, repay their respective TLTRO III borrowings before their maturity. The Governing Council of the ECB launched four additional pandemic emergency longer-term refinancing operations (PELTROs) in 2021 (three matured in the course of 2022 and one – in January 2023). 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 2023, Latvijas Banka received 430 000 thousand euro as repayment of loans granted to credit institutions. At the end of 2023, the balance of the TLTROs conducted by Latvijas Banka stood at 92 000 thousand euro (at the end of 2022, the balance was 522 900 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 (133 thousand euro at the end of 2023; 6304 thousand euro at the end of 2022).

12. SECURITIES OF EURO AREA RESIDENTS DENOMINATED IN EURO

At the end of 2023, the amount of securities held by the Eurosystem for monetary policy purposes totalled 4 694 345 million euro (4 937 179 million euro at the end of 2022). Of them, Latvijas Banka held 12 587 million euro (13 135 million euro at the end of 2022). 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 2023, the amount of government securities purchased by the euro area NCBs under the PSPP totalled 1923 billion euro (2067 billion euro at the end of 2022); of them, Latvijas Banka held Latvian government securities in the amount of 2635 million euro (2758 million euro at the end of 2022). At the end of 2023, the amount of government securities purchased by the euro area NCBs under the PEPP totalled 1297 billion euro (1318 billion euro at the end of 2022); of them, the amount of Latvian government securities held by Latvijas Banka was 1414 million euro (1450 million euro at the end of 2022).

Until the end of February 2023, the Eurosystem continued reinvesting, in full, the principal payments from maturing securities purchased under the asset purchase programme (APP). Subsequently, the APP portfolio declined at a gradual pace. Until the end of June 2023, the decline amounted to 15 billion euro per month on average as the Eurosystem did not reinvest all of the principal payments from maturing securities. In June 2023, the Governing Council decided to discontinue the reinvestments under the APP as of July 2023. 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, whereby net asset purchases continued until March 2022. The Governing Council of the ECB intends to continue reinvesting, in full, the principal payments from maturing securities purchased under this programme during the first half of 2024.

	(in thousands of euro)	
	2023	2022
Securities held for monetary policy purposes	12 586 724	13 134 812
Latvian government securities	4 048 732	4 207 501
PSPP government securities	2 634 861	2 757 748
PEPP government securities	1 413 871	1 449 753
Debt securities issued by international institutions	8 537 992	8 927 311
PSPP debt securities issued by international institutions	6 523 191	7 034 553
PEPP debt securities issued by international institutions	2 014 801	1 892 758
Other securities	963 933	946 794
Securities not held to maturity	795 539	778 474
Securities held to maturity	168 394	168 320
Total	13 550 657	14 081 606

13. INTRA-EUROSYSTEM CLAIMS/LIABILITIES (–)

		(in thousands of euro)	
	Note	2023	2022
Participating interest in the European Central Bank	13.1	118 849	118 849
Claims in respect of foreign reserves transferred to the European Central Bank	13.2	157 202	157 202
Claims related to the allocation of banknotes in the Eurosystem	13.4	5 929 327	5 650 608
Claims related to other operational requirements within the Eurosystem	13.5	207 065	300
Total intra-Eurosystem claims		6 412 443	5 926 959
Liabilities related to TARGET and national central bank correspondent accounts (net)	13.3	–7 569 389	–10 370 127
Other liabilities within the Eurosystem	13.5	–	–6 237
Total intra-Eurosystem liabilities		–7 569 389	–10 376 364
Intra-Eurosystem net liabilities		–1 156 946	–4 449 405

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. The ECB's capital subscription key was last adjusted in 2023 considering up-to-date information on the population of NCB countries and the share of gross domestic product in the EU. The adjusted ECB capital keys will enter into force on 1 January 2024, and the ECB's capital key will remain unchanged for Latvia. The ECB capital key for Latvijas Banka is 0.3169%, which corresponds 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.

At the end of 2023, Latvijas Banka's participating interest in the ECB consisted of the paid-up shares in the amount of 34 304 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 total subscribed capital of the ECB remained unchanged in 2023. The accession of Hrvatska narodna banka to the Eurosystem on 1 January 2023 did not change the amount of the ECB's total subscribed capital, but generated an increase in the ECB's total paid-up capital of 68 714 thousand euro.

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)	
	2023	2022
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	34 304
The paid-up share of Latvijas Banka in the European Central Bank's capital	34 304	34 304
The percentage share of Latvijas Banka in the European Central Bank's capital (capital key; %)	0.3169	0.3169

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 is fixed in proportion to the capital key weighting of each euro area NCB in the ECB's capital. In exchange for the foreign reserves transferred to the ECB, Latvijas Banka received a euro-denominated claim on the ECB in proportion to the value of the respective claims of other euro area NCBs. At the end of 2023 and of 2022, this claim amounted to 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 TARGET and national central bank correspondent accounts (net)

TARGET is a real-time gross settlement system for large value payments in euro. Claims and liabilities related to TARGET 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 TARGET accounts held by NCBs. The net positions for the bilateral balances of claims and liabilities 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 TARGET settlements.

In 2023, the liabilities related to TARGET and national central bank correspondent accounts (net) decreased as a result of the lower 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 Eurosystem

In view of the fact that euro banknotes are issued by all euro area NCBs and the ECB, they report a definite share of the total amount of euro banknotes issued by the Eurosystem on their balance sheets. 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 Eurosystem

Claims/liabilities related to other operational requirements within the Eurosystem comprise claims for the ECB's interim profit distribution and other claims on and liabilities to the ECB associated with the net result of pooling of monetary income and Latvijas Banka's correspondent account.

Monetary income to be pooled by Latvijas Banka and to be received in 2023 was positive and this resulted in claims on the ECB associated with the net result of pooling of monetary income, standing at 206 554 thousand euro at the end of 2023 (6237 thousand euro liability at the end of 2022; see also Note 38).

Claims for the ECB's interim profit distribution are set as per Latvijas Banka's percentage share in the ECB's capital (0 euro at the end of 2023 and 2022; see also Note 37).

14. OTHER ASSETS

(in thousands of euro)

	Note	2023	2022
Accrued interest on securities held for monetary policy purposes		84 662	77 678
Accrued interest on claims against the ECB		72 419	26 528
OTC financial derivative contracts and spot exchange rate contracts	24	41 242	189 050
Participating interest in the Bank for International Settlements	14.2	37 863	37 119
Fixed assets	14.1	26 910	28 852
Accrued interest on other securities		20 539	17 234
Claims for payments of supervised financial market participants		3 206	–
Intangible assets	14.1	3 179	2 941
Accrued interest on longer-term refinancing operations		2 521	–
Prepaid expenses		2 296	1 610
Other		668	626
Total		295 505	381 638

14.1 Fixed assets and intangible assets

(in thousands of euro)

	Buildings, improve- ment of territory, and land	Furniture and office equipment	Computer and telecom- munication equipment	Cash processing and storage equipment	Other fixed assets	Total fixed assets	Intangible assets
As at 31 December 2021							
Cost	58 817	6 055	4 980	5 293	8 137	83 282	9 135
Accumulated depreciation/amortisation	-34 449	-4 510	-4 233	-2 813	-6 452	-52 457	-7 096
Net book value	24 368	1 545	747	2 480	1 685	30 825	2 039
During 2022							
Additions	411	31	406	113	229	1 190	1 383
Change in classification	–	–	9	–	-9	–	–
Disposals and write-offs	–	-27	-468	-1	-702	-1 198	-208
Net change in cost	411	4	-53	112	-482	-8	1 175
Depreciation/amortisation charge	-1 884	-223	-378	-281	-397	-3 163	-478
Accumulated depreciation/amortisation on disposals and write-offs	–	27	468	1	702	1 198	205
Net change in accumulated depreciation/amortisation	-1 884	-196	90	-280	305	-1 965	-273
As at 31 December 2022							
Cost	59 228	6 059	4 927	5 405	7 655	83 274	10 310
Accumulated depreciation/amortisation	-36 333	-4 706	-4 143	-3 093	-6 147	-54 422	-7 369
Net book value	22 895	1 353	784	2 312	1 508	28 852	2 941
During 2023							
Additions	701	6	393	123	60	1 283	658
Assets acquired from the FCMC at original cost	–	252	563	–	6	821	1 012
Disposals and write-offs	-16	-110	-248	-32	-859	-1 265	–
Net change in cost	685	148	708	91	-793	839	1 670
Depreciation/amortisation charge	-1 777	-217	-499	-271	-307	-3 071	-589
Accumulated depreciation/amortisation of assets acquired from the FCMC	–	-176	-379	–	-3	-558	-843
Accumulated depreciation/amortisation on disposals and write-offs	16	105	248	32	447	848	–
Net change in accumulated depreciation/amortisation	-1 761	-288	-630	-239	137	-2 781	-1 432
As at 31 December 2023							
Cost	59 913	6 207	5 635	5 496	6 862	84 113	11 980
Accumulated depreciation/amortisation	-38 094	-4 994	-4 773	-3 332	-6 010	-57 203	-8 801
Net book value	21 819	1 213	862	2 164	852	26 910	3 179

At the end of 2023, Latvijas Banka's contractual commitments related to acquisition of fixed assets were 40 thousand euro (480 thousand euro at the end of 2022).

14.2 Participating interest in the Bank for International Settlements

At the end of 2023 and 2022, 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 45). At the end of 2023 and 2022, the BIS shareholding is reported on 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. Pursuant to the Statutes of the BIS, only central banks can be shareholders in the BIS. At the end of 2023, the estimated fair value of BIS shares owned by Latvijas Banka was 37 863 thousand euro (37 119 thousand euro at the end of 2022).

15. BANKNOTES IN CIRCULATION

	(in thousands of euro)	
	2023	2022
Euro banknotes	5 571 492	5 635 738
Net issuance of euro banknotes by Latvijas Banka	-357 835	-14 870
Adjustment for banknote allocation in the Eurosystem	5 929 327	5 650 608
Total	5 571 492	5 635 738

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".

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 2023 increased, amplifying 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 357 835 thousand euro. As a result, an increase in the adjustment for banknote allocation in the Eurosystem was reported on the balance sheet of Latvijas Banka. At the end of 2023, the total amount of euro banknotes in circulation in the Eurosystem decreased to 1567 billion euro (1572 billion euro at the end of 2022).

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. Banks' minimum reserve balances were remunerated at the latest available interest rate used by the Eurosystem in its tenders for main refinancing operations until 20 December 2022, and at the ECB's deposit facility rate between 21 December 2022 and 19 September 2023. On 27 July 2023, the Governing Council decided that, starting from 20 September 2023, these balances will be remunerated at a zero percent rate.

At the end of 2023, the balance on the current accounts with Latvijas Banka was 205 834 thousand euro (343 816 thousand euro at the end of 2022), including the minimum reserves in the amount of 205 944 thousand euro (200 197 thousand euro at the end of 2022). The average minimum reserves during the reserve maintenance period at the end of 2023 stood at 205 944 thousand euro (200 197 thousand euro at the end of 2022).

16.2 Deposit facility

Deposit facility is a standing facility of the Eurosystem used by credit institutions to place their overnight deposits at a pre-specified rate. At the end of 2023, the balance of deposit facility accounts was 6 867 713 thousand euro (4 873 349 thousand euro at the end of 2022).

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

	(in thousands of euro)	
	2023	2022
Liabilities for repurchase agreements	232 672	210 805
Collateral received for the use of the instant payment service	73 795	51 401
Liabilities for collateral for forward exchange rate contracts	8 253	58 067
Total	314 720	320 273

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.

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

Liabilities to other financial institutions mostly comprise funds received from European Commission and under repurchase agreements.

	(in thousands of euro)	
	2023	2022
European Commission	102 303	112 249
Other financial institutions	80 367	57 990
International Monetary Fund	1 405	1 449
Total	184 075	171 688

20. LIABILITIES TO EURO AREA RESIDENTS DENOMINATED IN FOREIGN CURRENCY

	(in thousands of euro)	
	2023	2022
Liabilities for repurchase agreements	685 785	155 006
Demand deposits of the Latvian government	539 561	551 032
Liabilities for gold swap arrangements	37 412	–
Total	1 262 758	706 038

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

	(in thousands of euro)	
	2023	2022
Liabilities for repurchase agreements	295 782	–
Liabilities for gold swap arrangements	146 661	–
Liabilities for collateral for financial derivative instruments	15 275	34 512
Demand deposits	–	189
Total	457 718	34 701

22. OTHER LIABILITIES

		(in thousands of euro)	
	Note	2023	2022
Euro coins in circulation	22.1	94 242	90 555
Accrued expense and similar liabilities		57 246	41 694
Lats banknotes in circulation	22.1	10 684	14 746
Lats coins in circulation	22.1	1 437	1 920
OTC financial derivative contracts and spot exchange rate contracts	24	8 302	18 419
Provisions for supervision function expenses		5 359	—
Tax liabilities		1 091	129
Provisions for market risk and credit risk	36	166	15 051
Other		3 690	2 226
Total		182 217	184 740

22.1 Banknotes and coins in circulation

Euro coins in circulation include the euro coins issued by Latvijas Banka in circulation, except collector coins. The extent of liabilities regarding the lats banknotes and coins in circulation has been estimated, considering the probability of exchanging the lats banknotes and coins in a period of 20 years following the euro changeover in 2014 (see also Note 2.2).

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 7282 thousand euro at the end of 2023 (7187 thousand euro at the end of 2022). The above coins in circulation have not been reported under the balance sheet item "Other liabilities" (see also Note 45).

Issued lats banknotes and coins with a low probability of exchange in the amount of 105 753 thousand euro (lats banknotes in the amount of 44 945 thousand euro and lats coins in the amount of 60 808 thousand euro at the end of 2023; 102 080 thousand euro at the end of 2022, including lats banknotes in the amount of 41 675 thousand euro and lats coins in the amount of 60 405 thousand euro at the end of 2022) have not been reported as a liability on the balance sheet at the end of 2023 (see also Note 45). 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.

23. CAPITAL AND RESERVES

(in thousands of euro)

	Nominal capital	Reserve capital	Revaluation account	Profit/loss(–) for the year	Capital and reserves
As at 31 December 2021	100 000	256 873	530 874	20 908	908 655
During 2022					
Net result of revaluation, realisation, and revaluation result recognition in the profit and loss statement	x	x	–307 137	x	–307 137
Profit appropriated to the State budget	x	x	x	–14 635	–14 635
Profit transferred to the reserve capital	x	6 273	x	–6 273	–
Profit/loss(–) for the year	x	x	x	–	–
As at 31 December 2022	100 000	263 146	223 737	–	586 883
During 2023					
Net result of revaluation, realisation, and revaluation result recognition in the profit and loss statement	x	x	196 995	x	196 995
Profit/loss(–) for the year	x	x	x	–53 760	–53 760
As at 31 December 2023	100 000	263 146	420 732	–53 760	730 118

The capital and reserves of Latvijas Banka comprise the nominal capital, reserve capital and the revaluation account, as well as the undistributed profit/loss 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 stipulates that Latvijas Banka shall transfer to the state basic budget the part of the profit earned in the reporting year, which is calculated by multiplying the profit earned in the reporting year, which has remained after covering the losses accumulated in the previous years (if any), by the enterprise income tax rate specified in the Enterprise Income Tax Law, and shall make a payment for the usage of the state capital in the amount of 50% of the profit earned in the reporting year, remaining after covering losses (if any) accumulated in the previous years. 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 2023 and 2022, the corporate income tax rate was 20%. In 2023, the financial result of Latvijas Banka's activities was negative, showing a loss of 53 760 thousand euro therefore Latvijas Banka will not make transfers to the State budget in 2024 (also in 2023, Latvijas Banka did not make such a transfer, as it ended 2022 with a neutral operating financial result of 0 euro). 14 636 thousand euro of Latvijas Banka's profit for 2021 was transferred to the State budget in 2022.

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 part of the losses for the covering of which there is not enough reserve capital has to be covered from the profit of subsequent periods of Latvijas Banka. Thus, in accordance with the Law on Latvijas Banka, the losses referred to will be covered from the reserve capital, in which 263 146 thousand euro has been accumulated from Latvijas Banka's profit for previous years.

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 only the realised gains are recognised in the profit and loss statement, while unrealised gains are recorded under the balance sheet item "Capital and reserves" as the revaluation reserve, thus facilitating preservation of capital in the circumstances of adverse changes in prices of financial instruments and gold.

In 2023 and 2022, the changes in the revaluation account were as follows:

(in thousands of euro)					
	2023	Recognition in profit and loss statement	Revaluation	Realisation	2022
Revaluation reserve for participating interest	35 354	–	744	–	34 610
Result on revaluation of foreign currencies and gold	203 540	12 097	14 465	–474	177 452
Result on revaluation of securities	181 838	22 902	148 964	–1 703	11 675
Total	420 732	34 999	164 173	–2 177	223 737
	2022	Recognition in profit and loss statement	Revaluation	Realisation	2021
Revaluation reserve for participating interest	34 610	–	–190	–	34 800
Result on revaluation of foreign currencies and gold	177 452	5 184	7 962	–175	164 481
Result on revaluation of securities	11 675	336 531	–458 045	–198 404	331 593
Total	223 737	341 715	–450 273	–198 579	530 874

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 2023 and 2022, the contract or notional amounts and book value of the above transactions were as follows:

(in thousands of euro)						
	Contract or notional amount		Book value			
	2023	2022	Assets		Liabilities	
	2023	2022	2023	2022	2023	2022
OTC financial derivative and spot exchange rate contracts						
Forward exchange rate contracts and currency swap arrangements	2 866 469	3 662 071	35 141	186 562	3 494	15 052
Spot exchange rate contracts	518 097	345 480	161	184	56	–
Forward transactions in securities	1 161 323	1 817 672	5 940	2 304	4 752	3 367
Interest rate swap arrangements	60 814	52 685	–	–	–	–
Total	x	x	41 242	189 050	8 302	18 419
Derivative OTC gold swap arrangements	184 072	–	186 783	–	184 815	–
Traded financial derivative contracts						
Interest rate future contracts	2 161 597	1 655 421	x	x	x	x

The book value of the OTC financial derivative contracts and spot exchange rate contracts is reported under the balance sheet item "Other assets" or "Other liabilities" (see also Notes 14 and 22). Since settlement is made for the daily changes in the fair value of traded financial derivative contracts, the changes are reported as demand deposits under the respective balance sheet asset item.

To limit the gold maintenance costs and increase return on financial investments, Latvijas Banka engages in gold swap arrangements (see also Notes 6, 20, 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 makes it possible 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, as well as the compliance with sustainability principles.

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 established by the Council of Latvijas Banka, duly notifies the Council of Latvijas Banka in accordance with the procedure adopted by the Council 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 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 Council 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. As a result of the implementation of monetary policy, the interest rate risk arises due to imbalances in the assets and liabilities associated with monetary policy operations that are subject to changes in interest rates. This risk is related to monetary policy decisions resulting from the implementation of the Eurosystem's core tasks therefore Latvijas Banka cannot limit this risk.

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 portfolio of borrowed funds where the currency structure is built considering the currency of the respective liabilities, the global fixed income securities portfolio whose currency structure is formed by the benchmark portfolio structure, as well as the gold portfolio and the equity securities portfolios 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 portfolio, the global fixed income securities portfolio, mortgage-backed securities portfolios, and the developed markets equity securities portfolio (see Note 4) is managed by determining the tracking error limit. The tracking error in 2023 and 2022 is disclosed in Note 28.

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.

Equity securities portfolios are exposed to the market price risk (a risk that the value of an investment could decrease due to price changes). As the equity securities portfolios are highly diversified, they are mainly exposed to a systematic stock volatility risk.

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 2023 and 2022) 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) and the Credit Support Annexes thereto. 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 the Securities Industry and Financial Markets Association (SIFMA) and the International Capital Market Association (ICMA), whereas the external managers of mortgage-backed securities portfolios enter into Treasury Market Practices Group (TMPG) Master Securities Forward Transaction Agreements with their counterparties. 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 2023 and 2022, 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 credit risk (as at the end of 2023 and 2022) is disclosed in Notes 30–32.

25.1.3 Liquidity risk

Liquidity risk is associated with a failure to dispose 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 2023 and 2022 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, as well as 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 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 ensuring the effectiveness of this management model. Operational risk management is coordinated by the Operational Risk Committee of Latvijas Banka.

Compliance risks are managed to ensure the compliance of Latvijas Banka's operation and its employees and their conduct, when exercising their official and professional duties, 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 other events, 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 the 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 provides 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.

In 2023, the main focus of operational risk management was on the operational risk management framework, taking into account trends in the field of risk management, accumulated experience, as well as changes in the external and internal environment. Operational risks were appropriately managed in 2023, and the risk mitigation measures limited those risks to acceptable levels.

26. CURRENCY STRUCTURE

	(in thousands of euro)						
	EUR	USD	CAD	GBP	Gold	Other	Total
As at 31 December 2023							
Total assets	20 719 133	3 420 583	320 350	489 372	399 378	216 004	25 564 820
Total liabilities	24 047 535	999 314	237 149	234 636	–	46 186	25 564 820
Net position on balance sheet	–3 328 402	2 421 269	83 201	254 736	399 378	169 818	0
Net position on financial instruments' off-balance sheet accounts	2 309 803	–1 941 064	–59 140	–227 547	–	–49 112	32 940
Net position on balance sheet and off-balance sheet accounts	–1 018 599	480 205	24 061	27 189	399 378	120 706	32 940
Net position on balance sheet and off-balance sheet accounts to total assets (%)	–4.1	1.9	0.1	0.1	1.6	0.5	0.1
As at 31 December 2022							
Total assets	21 226 504	3 231 603	287 411	404 647	364 821	235 708	25 750 694
Total liabilities	24 927 618	291 007	383	195 901	–	335 785	25 750 694
Net position on balance sheet	–3 701 114	2 940 596	287 028	208 746	364 821	–100 077	0
Net position on financial instruments' off-balance sheet accounts	3 190 118	–2 556 638	–263 906	–184 474	–	–14 469	170 631
Net position on balance sheet and off-balance sheet accounts	–510 996	383 958	23 122	24 272	364 821	–114 546	170 631
Net position on balance sheet and off-balance sheet accounts to total assets (%)	–2.0	1.5	0.1	0.1	1.4	–0.4	0.7

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 rate 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 2023							
Gold and gold receivables	–	–	–	–	–	399 378	399 378
Claims on non-euro area residents denominated in foreign currency	626 918	1	815 198	–	2 074 911	532 498	4 049 526
Claims on euro area residents denominated in foreign currency	288 914	–	181 984	1	109 822	15 081	595 802
Claims on non-euro area residents denominated in euro	7 940	–	40 371	–	118 329	1 836	168 476
Lending to euro area credit institutions related to monetary policy operations denominated in euro	–	–	92 900	–	–	–	92 900
Other claims on euro area credit institutions denominated in euro	133	–	–	–	–	–	133
Securities of euro area residents denominated in euro	60 792	–	337 461	–	13 152 404	–	13 550 657
Intra-Eurosystem claims	6 318 491	–	–	–	–	93 952	6 412 443
Other assets	–	–	10 905	–	96 294	188 306	295 505
Total assets	7 303 188	1	1 478 819	1	15 551 760	1 231 051	25 564 820
Banknotes in circulation	–	–	–	–	–	5 571 492	5 571 492
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	7 073 547	–	–	–	–	–	7 073 547
Other liabilities to euro area credit institutions denominated in euro	314 720	–	–	–	–	–	314 720
Liabilities to other euro area residents denominated in euro	2 216 025	–	–	–	–	2 761	2 218 786
Liabilities to non-euro area residents denominated in euro	75 019	–	–	–	–	109 056	184 075
Liabilities to euro area residents denominated in foreign currency	727 037	–	–	–	–	535 721	1 262 758
Liabilities to non-euro area residents denominated in foreign currency	457 718	–	–	–	–	–	457 718
Intra-Eurosystem liabilities	7 569 389	–	–	–	–	–	7 569 389
Other liabilities	8 139	–	–	–	–	174 078	182 217
Capital and reserves	–	–	–	–	–	730 118	730 118
Total liabilities	18 441 594	–	–	–	–	7 123 226	25 564 820
Net position on the balance sheet	–11 138 406	1	1 478 819	1	15 551 760	–5 892 175	–
Assets on financial instruments' off-balance sheet accounts	944 076	299	3 822 360	173 254	1 763 974	–	6 703 963
Liabilities on financial instruments' off-balance sheet accounts	5 727 551	285	59 151	13 927	870 109	–	6 671 023
Net position on balance sheet and off-balance sheet accounts	–15 921 881	15	5 242 028	159 328	16 445 625	–5 892 175	32 940

(continued)

(in thousands of euro)

141

	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 2022							
Gold and gold receivables	–	–	–	–	–	364 821	364 821
Claims on non-euro area residents denominated in foreign currency	602 235	45 962	180 991	420 060	2 084 836	453 960	3 788 044
Claims on euro area residents denominated in foreign currency	907	–	36 764	94 536	100 909	288 923	522 039
Claims on non-euro area residents denominated in euro	7 568	–	895	1 319	146 355	246	156 383
Lending to euro area credit institutions related to monetary policy operations denominated in euro	–	–	522 900	–	–	–	522 900
Other claims on euro area credit institutions denominated in euro	6 304	–	–	–	–	–	6 304
Securities of euro area residents denominated in euro	–	–	288 279	373 686	13 419 641	–	14 081 606
Intra-Eurosystem claims	5 808 110	–	–	–	–	118 849	5 926 959
Other assets	2	–	1 054	3 333	90 082	287 167	381 638
Total assets	6 425 126	45 962	1 030 883	892 934	15 841 823	1 513 966	25 750 694
Banknotes in circulation	–	–	–	–	–	5 635 738	5 635 738
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	4 982 193	–	–	–	–	234 972	5 217 165
Other liabilities to euro area credit institutions denominated in euro	320 273	–	–	–	–	–	320 273
Liabilities to other euro area residents denominated in euro	2 517 104	–	–	–	–	–	2 517 104
Liabilities to non-euro area residents denominated in euro	59 440	–	–	–	–	112 248	171 688
Liabilities to euro area residents denominated in foreign currency	155 539	–	–	–	–	550 499	706 038
Liabilities to non-euro area residents denominated in foreign currency	34 701	–	–	–	–	–	34 701
Intra-Eurosystem liabilities	10 376 364	–	–	–	–	–	10 376 364
Other liabilities	886	–	–	–	–	183 854	184 740
Capital and reserves	–	–	–	–	–	586 883	586 883
Total liabilities	18 446 500	–	–	–	–	7 304 194	25 750 694
Net position on the balance sheet	–12 021 374	45 962	1 030 883	892 934	15 841 823	–5 790 228	–
Assets on financial instruments' off-balance sheet accounts	765 385	5 752	3 410 527	123 289	2 007 300	–	6 312 253
Liabilities on financial instruments' off-balance sheet accounts	5 387 367	5 738	100 506	127 407	520 604	–	6 141 622
Net position on balance sheet and off-balance sheet accounts	–16 643 356	45 976	4 340 904	888 816	17 328 519	–5 790 228	170 631

28. TRACKING ERROR

The exposure to aggregate market risk and credit risk of investments, included in the 1–10 year government fixed income securities portfolio, mortgage-backed securities portfolios, the global fixed income securities portfolio, and the developed markets 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 2023 and 2022, the actual (ex-post) tracking error was as follows:

	(basis points)	
	2023	2022
1–10 year fixed income securities portfolio	34	83
Mortgage-backed securities portfolios	80	98
Developed markets equity securities portfolio	100	26
Global fixed income securities portfolio	67	108

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 2023						
1–10 year fixed income securities portfolio	2 920 052	99	151	–	–	–
Mortgage-backed securities portfolios	1 064 521	–	189	61	–	–
Global fixed income securities portfolio	140 426	5	196	46	3	–
During 2022						
1–10 year fixed income securities portfolios	2 790 364	126	126	–	–	–
Mortgage-backed securities portfolios	1 052 437	–	206	46	–	–
Global fixed income securities portfolio	138 623	70	134	5	–	–

The expected (ex-ante) tracking error of the developed markets equity securities portfolio at the end of months was on average 87 basis points and did not exceed 96 basis points during the year and the compliance with this limit is monitored by the respective external manager.

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 2023				
Assets				
Gold and gold receivables	399 378	–	–	399 378
Claims on non-euro area residents denominated in foreign currency	4 049 526	–	–	4 049 526
Claims on euro area residents denominated in foreign currency	595 802	–	–	595 802
Claims on non-euro area residents denominated in euro	168 476	–	–	168 476
Lending to euro area credit institutions related to monetary policy operations denominated in euro	–	92 900	–	92 900
Other claims on euro area credit institutions denominated in euro	133	–	–	133
Securities of euro area residents denominated in euro	13 382 263	168 394	–	13 550 657
Intra-Eurosystem claims	207 065	–	6 205 378	6 412 443
Other assets	224 589	2 521	68 395	295 505
Total assets	19 027 232	263 815	6 273 773	25 564 820
Liabilities				
Banknotes in circulation	–	–	5 571 492	5 571 492
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	7 073 547	–	–	7 073 547
Other liabilities to euro area credit institutions denominated in euro	314 720	–	–	314 720
Liabilities to other euro area residents denominated in euro	2 218 786	–	–	2 218 786
Liabilities to non-euro area residents denominated in euro	184 075	–	–	184 075
Liabilities to euro area residents denominated in foreign currency	1 262 758	–	–	1 262 758
Liabilities to non-euro area residents denominated in foreign currency	457 718	–	–	457 718
Intra-Eurosystem liabilities	7 569 389	–	–	7 569 389
Other liabilities	74 250	–	107 967	182 217
Total liabilities	19 155 243	–	5 679 459	24 834 702
Net position	–128 011	263 815	594 314	x

<i>(continued)</i>		(in thousands of euro)		
	Up to 3 months	Over 3 months	No fixed maturity	Total
As at 31 December 2022				
Assets				
Gold and gold receivables	364 821	–	–	364 821
Claims on non-euro area residents denominated in foreign currency	3 788 044	–	–	3 788 044
Claims on euro area residents denominated in foreign currency	522 039	–	–	522 039
Claims on non-euro area residents denominated in euro	156 383	–	–	156 383
Lending to euro area credit institutions related to monetary policy operations denominated in euro	–	522 900	–	522 900
Other claims on euro area credit institutions denominated in euro	6 304	–	–	6 304
Securities of euro area residents denominated in euro	13 913 286	168 320	–	14 081 606
Intra-Eurosystem claims	300	–	5 926 659	5 926 959
Other assets	310 494	–	71 144	381 638
Total assets	19 061 671	691 220	5 997 803	25 750 694
Liabilities				
Banknotes in circulation	–	–	5 635 738	5 635 738
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	5 217 165	–	–	5 217 165
Other liabilities to euro area credit institutions denominated in euro	320 273	–	–	320 273
Liabilities to other euro area residents denominated in euro	2 517 104	–	–	2 517 104
Liabilities to non-euro area residents denominated in euro	171 688	–	–	171 688
Liabilities to euro area residents denominated in foreign currency	706 038	–	–	706 038
Liabilities to non-euro area residents denominated in foreign currency	34 701	–	–	34 701
Intra-Eurosystem liabilities	10 376 364	–	–	10 376 364
Other liabilities	77 502	–	107 238	184 740
Total liabilities	19 420 835	–	5 742 976	25 163 811
Net position	–359 164	691 220	254 827	x

30. SECTORAL STRUCTURE OF ASSETS

145

	Amount (in thousands of euro)		Proportion (%)	
	2023	2022	2023	2022
Investment operations	6 239 029	5 990 669	24.4	23.3
Central governments and other governmental institutions	2 147 163	2 084 543	8.5	8.1
Other financial institutions	1 999 679	1 820 689	7.8	7.1
Central banks and credit institutions	724 600	803 443	2.8	3.1
International institutions	695 165	684 134	2.7	2.7
Non-financial corporations	533 841	424 373	2.1	1.6
Local governments	138 581	173 487	0.5	0.7
Monetary policy operations	12 764 286	13 735 390	49.9	53.3
International institutions	8 587 294	8 977 665	33.6	34.9
Central governments and other governmental institutions	4 084 092	4 234 825	15.9	16.4
Credit institutions	92 900	522 900	0.4	2.0
Other operations	6 561 505	6 024 635	25.7	23.4
Intra-Eurosystem claims	6 412 443	5 926 959	25.1	23.0
International institutions	37 863	37 119	0.1	0.1
Unclassified assets	111 199	60 557	0.5	0.3
Total	25 564 820	25 750 694	100.0	100.0

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

	Amount (in thousands of euro)		Proportion (%)	
	2023	2022	2023	2022
Investment operations	6 239 029	5 990 669	24.4	23.3
US	2 029 422	1 651 157	8.0	6.3
Euro area countries	1 584 857	1 638 969	6.2	6.4
UK	892 969	892 279	3.5	3.5
International institutions	695 165	684 134	2.7	2.7
Canada	549 374	546 800	2.1	2.1
Japan	123 380	145 185	0.5	0.6
Other EU countries	123 630	143 159	0.5	0.6
Other countries	240 232	288 986	0.9	1.1
Monetary policy operations	12 764 286	13 735 390	49.9	53.3
International institutions	8 587 294	8 977 665	33.6	34.9
Euro area countries	4 176 992	4 757 725	16.3	18.4
Other operations	6 561 505	6 024 635	25.7	23.4
Intra-Eurosystem claims	6 412 443	5 926 959	25.1	23.0
International institutions	37 863	37 119	0.1	0.1
Unclassified assets	111 199	60 557	0.5	0.3
Total	25 564 820	25 750 694	100.0	100.0

32. ASSETS BY CREDIT RATING ASSIGNED TO THE COUNTERPARTY

147

	Amount (in thousands of euro)		Proportion (%)	
	2023	2022	2023	2022
Investment operations	6 239 029	5 990 669	24.4	23.3
AAA	2 377 089	3 280 166	9.2	12.8
AA	2 396 518	1 178 470	9.4	4.6
A	243 697	413 085	1.0	1.6
BBB	554 875	552 610	2.2	2.1
Assets without counterparty credit rating	61 271	60 000	0.2	0.2
Assets not exposed to credit risk	605 579	506 338	2.4	2.0
Monetary policy operations	12 764 286	13 735 390	49.9	53.3
AAA	7 791 077	8 052 698	30.4	31.3
AA	796 217	924 967	3.1	3.6
A	4 084 092	4 234 825	16.0	16.4
Assets without counterparty credit rating	92 900	522 900	0.4	2.0
Other operations	6 561 505	6 024 635	25.7	23.4
Intra-Eurosystem claims	6 412 443	5 926 959	25.1	23.0
Unclassified assets	116 453	65 883	0.5	0.3
Assets not exposed to credit risk	32 609	31 793	0.1	0.1
Total	25 564 820	25 750 694	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 developed markets equity securities portfolio, participating interest in the BIS, fixed assets and intangible assets.

33. NET INTEREST INCOME

	(in thousands of euro)	
	2023	2022
Interest income	503 974	211 229
Interest on investments	184 035	92 817
Interest on customer deposits	–	11 912
Interest on monetary policy operations	92 937	72 795
Interest on intra-Eurosystem claims	227 002	33 705
Interest expense	–732 980	–164 208
Interest on investments	–115 948	–63 098
Interest on customer deposits	–80 181	–9 997
Interest on monetary policy operations	–181 827	–31 374
Interest on intra-Eurosystem liabilities	–355 024	–59 739
Net interest income	–229 006	47 021

Interest income on investments was mainly derived from interest on debt securities, and its growth by 88 429 thousand euro in 2023 (14 558 thousand euro in 2022) was driven by higher average securities yields. Interest expense on investments largely consisted of interest on repurchase transactions and interest on OTC forward exchange rate contracts and its increase was driven by a repurchase transactions carried out to reduce hedging costs and financing costs of investment operations.

Interest income and interest expense on customer deposits was shaped by interest on deposits from the government and other financial institutions. As the ECB raised interest rates, in 2023 Latvijas Banka's expenditure on government and other financial institution deposits increased sharply, interest expense on Latvian government deposits reaching 45 253 thousand euro. 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). Pursuant to this Guideline, Latvijas Banka applies the following interest rates to Treasury current account balances: for the account balances in euro – euro short-term interest rate €STR (at the end of 2023 it was 3.882%), minus 20 basis points; current account balances in foreign currencies, with the exception of SDR, are subject to conditions comparable to those applied to euro account balances. At the end of 2022, Latvijas Banka applied the following interest rates to Treasury current account balances: to the Treasury's deposits in euro up to 200 million euro Latvijas Banka applied the euro short-term interest rate €STR (it was 1.89% at the end of 2022). Regarding the total amount of the Treasury's settlement account balances in euro and foreign currencies exceeding 200 million euro, Latvijas Banka applied the ECB's deposit facility rate or the euro short-term interest rate €STR, whichever was lower (on 31 December 2022 the ECB's deposit facility rate was 2.0%).

Interest income on monetary policy operations in 2023 primarily consisted of interest on PSPP and PEPP securities. Interest expense on monetary policy operations consisted mainly of interest on deposit facility transactions and negative interest on PSPP and PEPP securities. As the ECB raised the interest rate on the deposit facility (from –0.5% in July 2022 to 2% and 4% at the end of 2022 and 2023 respectively), Latvijas Banka's expenditure on deposits of Latvian credit institutions increased sharply in 2023, reaching 173 852 thousand euro.

Interest income from and interest expense on the intra-Eurosystem claims and liabilities are remunerated by applying the ECB's main refinancing operations interest rate and include income from foreign reserves transferred to the ECB and claims related to the allocation of banknotes in the Eurosystem, as well as expense on liabilities related to TARGET settlements. As the ECB raised the interest rate on its main refinancing operations from 0% in July 2022 to 2.5% and 4.5% at the end of 2022 and 2023, respectively, Latvijas Banka's interest income and expenditure on intra-Eurosystem claims and liabilities increased sharply in 2023, which also led to an increase in the amount of interest expense included in the reallocation of monetary income.

34. REALISED GAINS/LOSSES ARISING FROM FINANCIAL OPERATIONS

	(in thousands of euro)	
	2023	2022
Securities	19 019	32 332
Derivative financial instruments	-8 136	-29 394
Foreign exchange transactions	-1 883	36 794
Total	9 000	39 732

In 2023, the realised gains on foreign exchange transactions were 38 677 thousand euro less than in 2022, because greater realised profit on the developed markets equity securities portfolio in 2022 had a negative comparative effect.

The result of the disposal of securities decreased by 13 313 thousand euro in comparison with 2022. The greater realised gains from the developed markets equity securities portfolio in 2022 had a negative comparative effect. Smaller fluctuations in the market value of debt securities as a result of the stabilisation of market yield increases had a positive impact.

The result of derivative financial instruments increased by 21 258 thousand euro in comparison with 2022. This was mainly on account of the result of interest rate future contracts due to the stabilisation of market yield increases.

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

	(in thousands of euro)	
	2023	2022
Securities	-22 901	-336 530
Foreign currency positions	-12 098	-5 185
Total	-34 999	-341 715

The revaluation result of several debt securities, equity securities, and foreign currency positions at the end of 2023 and 2022 was negative and has been recognised in the profit and loss statement. The positive result on the revaluation of debt securities, equity securities, and foreign currency positions has been reported under the balance sheet item "Capital and reserves" as the revaluation result of securities and foreign currency positions respectively (see also Note 23).

The decrease in the negative revaluation result of securities is related to the stabilisation of market yield increases, as opposed to the sharp rise in 2022.

36. PROVISIONS FOR MARKET RISK AND CREDIT RISK

On the basis of reasonable risk estimates and in accordance with the legal framework for accounting and financial reporting in the ESCB, the Council of Latvijas Banka 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 as well as on the use of these provisions should the above risks materialise.

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 2023, the level of financial risks did not change fundamentally and was estimated at 998.6 million euro (993.4 million euro in 2022).

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)	
	2023	2022
Level of financial risks	998 600	993 400
Provisions for the market risk and credit risk	166	15 051
Provisions for the market risk and credit risk against the level of financial risks (%)	0	2

In 2023, due to the Eurosystem's monetary policy decisions related to curbing inflation, Latvijas Banka's interest expenditure on monetary operations increased sharply. Therefore, the total financial result included in the profit and loss statement before provisions for financial risks was negative (see also Note 35). Therefore, the Council of Latvijas Banka decided to use the remaining provisions for financial risks in 2023, reducing them by a total of 15 051 thousand euro (in 2022, the respective provisions were reduced by 280 646 thousand euro). In addition, provisions were made for credit risk of the Eurosystem's monetary policy operations in the amount of 166 thousand euro (Latvijas Banka had no such provisions at the end of 2022).

37. INCOME FROM EQUITY SECURITIES AND PARTICIPATING INTEREST

Income from equity securities comprises dividends of the equity securities portfolio in the amount of 11 849 thousand euro (14 218 thousand euro in 2022).

Income from participating interest comprises dividends received from the participating interest in the BIS totalling 373 thousand euro (374 thousand euro in 2022; see also Note 14.2) and income from the participating interest in the ECB. The ECB did not distribute profits for 2023 and 2022, but in 2022 the remainder of the ECB's annual profit for the previous year in the amount of 163 thousand euro was paid.

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.

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).

38. NET RESULT OF POOLING OF MONETARY INCOME

Pursuant to the Statute of the ESCB and of the ECB, Eurosystem NCBs gain income from the implementation of the single monetary policy of the Eurosystem. Total monetary income of Eurosystem NCBs equals the income on assets arising from the issue of euro banknotes and receiving deposits from credit institutions. The income is pooled and reallocated to euro area NCBs in proportion to their shares in the capital of the ECB, resulting in a net pooling of monetary income for each Eurosystem NCB, which includes monetary income paid and monetary income received.

The net result of pooling of monetary income is determined by the difference in yields on securities purchased for monetary policy purposes between the Eurosystem NCBs, as well as by the difference between the proportion of the earmarked assets and liability base items of individual Eurosystem NCBs in the respective Eurosystem's total items of the earmarked asset and liability base compared to the percentage share of that NCB in the ECB's capital.

The 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 received comprises Latvijas Banka's share in the Eurosystem's total monetary income set on the basis of Latvijas Banka's share in the ECB's capital. The increase in the net result of pooling of monetary income was driven by higher monetary income pooled and received, resulting from the increase in ECB interest rates. The total monetary income of the Eurosystem NCBs and the distribution of the net result of pooling of monetary income by Latvijas Banka in 2023 and 2022 were as follows.

(in thousands of euro)				
	Total monetary income of the Eurosystem NCBs	Monetary income of the Latvijas Banka		
		Monetary income pooled	Monetary income received	Net result of pooling of monetary income
In 2023				
Lending to euro area credit institutions related to monetary policy operations denominated in euro	26 854 254	-6 889	103 797	96 908
Securities held for monetary policy purposes subject to risk sharing	8 483 280	-51 442	32 790	-18 652
Securities held for monetary policy purposes not subject to risk sharing	127 854 247	-159 073	494 182	335 109
Claims in respect of foreign reserves transferred to the European Central Bank	1 334 524	-5 158	5 158	-
Claims and liabilities related to the allocation of euro banknotes within the Eurosystem	-4 816 858	-221 818	-18 618	-240 436
Excess of the liability base over earmarked assets	-2 722 452	-33 773	-10 523	-44 296
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	-130 387 326	172 352	-503 973	-331 621
Claims and liabilities related to TARGET correspondent accounts	14 159 899	355 055	54 731	409 786
Other	-62 563	-	-244	-244
Total	40 697 005	49 254	157 300	206 554
In 2022				
Lending to euro area credit institutions related to monetary policy operations denominated in euro	-10 533 334	2 850	-41 043	-38 193
Securities held for monetary policy purposes subject to risk sharing	5 924 132	-34 998	23 083	-11 915
Securities held for monetary policy purposes not subject to risk sharing	19 907 123	-24 419	77 568	53 149
Claims in respect of foreign reserves transferred to the European Central Bank	201 229	- 784	784	-
Claims and liabilities related to the allocation of euro banknotes within the Eurosystem	-735 700	-32 921	-2 867	-35 788
Excess of the liability base over earmarked assets	-3 185 995	-8 935	-12 414	-21 349
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	-6 526 743	5 256	-25 431	-20 175
Claims and liabilities related to TARGET correspondent accounts	2 085 344	59 739	8 126	67 865
Other	43 346	-	169	169
Total	7 179 402	-34 212	27 975	-6 237

In the calculation of monetary income pooled, securities held for monetary policy purposes for which risks are not shared, generate income at the ECB's main refinancing operations rate, so that the amount of monetary income pooled differs from that recognised in net interest income (see Note 33).

39. OTHER OPERATING INCOME

		(in thousands of euro)	
	Note	2023	2022
Income from payments by supervised financial market participants	39.1.	13 939	–
Revaluation of liabilities for the issued lats banknotes and coins	39.2.	3 674	4 100
Income from sale of numismatic products		1 382	1 014
Other		566	652
Total		19 561	5 766

39.1 Income from payments by supervised financial market participants

	(in thousands of euro)	
	2023	2022
Income related to the supervision of monetary financial institutions	8 658	–
Income related to insurance supervision	1 888	–
Income related to the supervision of the market financial instruments and pension funds	1 301	–
Other payments of market participants	238	–
Provisions used for supervisory function expenses	1 854	–
Total	13 939	–

Provisions used for supervisory function expenses amounting to 1854 thousand euro consisted of the excess of supervisory function expenses in 2023 over income from payments of supervised financial market participants in the reporting year. Supervisory function expenses for the current reporting period amounted to 12 904 thousand euro and income from payments of supervised financial market participants – to 12 085 thousand euro. The total supervisory function expenses in 2023 increased due to provisions for lease obligations of 1035 thousand euro for former FCMC office premises at Kungu iela 1, Riga (see also Note 45).

39.2 Revaluation of liabilities for the issued lats banknotes and coins

The issued lats banknotes and coins with a low exchange probability are not reported on the balance sheet pursuant to the "Financial Accounting Policy of Latvijas Banka" (see also Note 2.2). In 2023, with the exchange of the lats banknotes and coins decelerating, the valuation of liabilities for the issued lats banknotes and coins decreased (see also Note 22.1) and the corresponding income was recognised.

40. REMUNERATION, SOCIAL SECURITY COSTS, AND SOLIDARITY TAX

	(in thousands of euro)	
	2023	2022
Remuneration		
Remuneration of the members of the Council	–838	–592
Remuneration of other personnel	–23 890	–15 910
Total remuneration	–24 728	–16 502
Social security costs and solidarity tax	–5 540	–3 653
Total remuneration, social security costs, and solidarity tax	–30 268	–20 155

At the end of 2023, the number of employees was 531 (376 at the end of 2022), representing 519 full-time equivalents in 2023 (374 in 2022). The increase in the number of employees is related to the FCMC incorporation in Latvijas Banka on 1 January 2023, which also determined a corresponding increase in remuneration expenses in 2023.

Following the FCMC incorporation in Latvijas Banka, its Council consists of seven Council members. In 2022, before the FCMC was incorporated to Latvijas Banka, its Council consisted of six Council members, while the FCMC's Board consisted of three Board members.

41. BANKNOTE AND COIN ACQUISITION COSTS

	(in thousands of euro)	
	2023	2022
Acquisition of banknotes	-1 056	-1 688
Acquisition of collector coins	-933	-739
Acquisition of circulation coins	-349	-191
Total	-2 338	-2 618

42. OTHER OPERATING EXPENSES

	(in thousands of euro)	
	2023	2022
Maintenance and operation of information systems	-4 866	-4 588
Payments to the EU and international organizations	-1 130	-92
Security services	-715	-269
Municipal services	-601	-1 158
Business travel	-544	-288
Maintenance of buildings, territory and equipment	-434	-508
Public education and information	-423	-623
Personnel training	-303	-203
Telecommunication services and system maintenance	-262	-209
Event services	-262	-132
Acquisition of low value office supplies	-225	-261
Tax on real estate	-172	-172
Risk insurance	-96	-92
Other	-1 932	-518
Total	-11 965	-9 113

Payments to the EU and international organizations mainly include supervision-related membership fees to the European Banking Authority, European Insurance and Occupational Pensions Authority, European Securities and Markets Authority. Other operating expenses increased mainly due to accrued expenses for rental obligations relating to the premises at Kungu iela 1 in the amount of 1035 thousand euro and remuneration totalling 51 thousand euro paid to SIA ERNST & YOUNG BALTIC for the audit of 2023 financial statements of Latvijas Banka (33 thousand euro in 2022).

OTHER NOTES

43. PLEDGED ASSETS

Debt securities, other financial instruments and gold purchased by Latvijas Banka with the total market value of 1 451 160 thousand euro as at the end of 2023 (364 618 thousand euro at the end of 2022) have been pledged to provide repurchase agreement deals, collateral for gold swap arrangements, forward exchange rate contracts, interest rate and currency future contracts. At the end of 2023, the pledged assets mostly consisted of securities

pledged under repurchase agreements in the amount of 1 264 263 thousand euro (358 360 thousand euro at the end of 2022).

44. 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.

In order to promote liquidity in the securities market, Latvijas Banka, together with other euro area NCBs, lends securities purchased under the PSPP and the PEPP, and Latvijas Banka does so within the framework of the automated securities lending programme.

At the end of 2023, the fair value of the securities lent, determined using quoted prices in an active market, was 942 261 thousand euro (1 571 469 thousand euro at the end of 2022); inter alia, the fair value of securities purchased and lent under the PSPP and PEPP stood at 934 498 thousand euro at the end of 2023 (1 473 321 thousand euro at the end of 2022).

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.

45. 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 2023, the uncalled portion of the BIS shareholding was 4012 thousand SDR (4877 thousand euro; 4012 thousand SDR (5022 thousand euro) at the end of 2022; see also Note 14.2).

At the end of 2023, Latvijas Banka had issued euro collector coins, lats collector coins and precious metal circulation coins in the nominal value of 7282 thousand euro (7187 thousand euro at the end of 2022). 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, since the value of the precious metal contained in them exceeds their nominal value.

At the end of 2023, Latvijas Banka had issued lats banknotes and coins with the face value of 117 875 thousand euro (118 746 thousand euro at the end of 2022), reported on the balance sheet in the amount of 12 122 thousand euro (16 666 thousand euro at the end of 2022). Pursuant to the Law on the Procedure for Introduction of 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 105 753 thousand euro (102 080 thousand euro at the end of 2022) at face value is low.

At the end of 2023, Latvijas Banka had six administrative legal proceedings related to the regulation and supervision of the financial market and its participants. These legal proceedings have been initiated in accordance with the administrative procedure for the annulment of the decisions of Latvijas Banka, but according to the assessment by Latvijas Banka's management, no losses will be incurred as a result of the aforementioned legal proceedings therefore provisions have not been created.

The FCMC leased the premises at Kungu iela 1, Riga, to ensure its operation. With the FCMC's incorporation in Latvijas Banka, the aforementioned premises have not been used since 1 January 2023, and the lessor has been informed about the termination of the lease agreement. In accordance with the amendments to the lease agreement for the premises concluded in 2018, the legal basis for termination of the contract cannot be interpreted unambiguously in the particular circumstances and create a risk that, due to the termination of this agreement, Latvijas Banka may be obliged to cover the expenses attributable to rental of the aforementioned premises rent, management of the building and utilities, and the payment of the real estate tax until 31 December 2026. Latvijas Banka does not consider that there is a legal basis for these liabilities to exceed the provisions created.

46. IMPACT OF THE FCMC INCORPORATION ON OPENING BALANCES OF BALANCE SHEET ITEMS

On 1 January 2023, the new Law on Latvijas Banka, adopted on 23 September 2021, entered into force and provides for incorporation of the FCMC's in Latvijas Banka. In accordance with the transitional provisions of the aforementioned Law, Latvijas Banka is the successor of the FCMC's property, financial resources, rights and liabilities. Thus, as of 1 January 2023, the assets and liabilities reflected on the FCMC's balance sheet as at 31 December 2022 are included on Latvijas Banka's balance sheet. As of 1 January 2023, Latvijas Banka also manages the Deposit Guarantee Fund, the Fund for the Protection of the Insured and the National Resolution Fund.

Since the assets of the aforementioned funds each constitute a distinct set of assets and are managed separately, the respective assets and liabilities are not shown on Latvijas Banka's balance sheet.

The impact of the FCMC's incorporation in Latvijas Banka on the opening balances of Latvijas Banka's balance sheet items as at 1 January 2023 was as follows.

	(in thousands of euro)		
	As at 31 December 2022	Impact of incorporation of the FCMC	As at 1 January 2023
Gold and gold receivables	364 821		364 821
Claims on non-euro area residents denominated in foreign currency	3 788 044		3 788 044
Claims on euro area residents denominated in foreign currency	522 039		522 039
Claims on non-euro area residents denominated in euro	156 383		156 383
Lending to euro area credit institutions related to monetary policy operations denominated in euro	522 900		522 900
Other claims on euro area credit institutions denominated in euro	6 304	5	6 309
Securities of euro area residents denominated in euro	14 081 606		14 081 606
Intra-Eurosystem claims	5 926 959		5 926 959
Other assets	381 638	3 557	385 195
Total assets	25 750 694	3 562	25 754 256
Banknotes in circulation	5 635 738		5 635 738
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	5 217 165		5 217 165
Other liabilities to euro area credit institutions denominated in euro	320 273		320 273
Liabilities to other euro area residents denominated in euro	2 517 104	-6 138	2 510 966
Liabilities to non-euro area residents denominated in euro	171 688		171 688
Liabilities to euro area residents denominated in foreign currency	706 038		706 038
Liabilities to non-euro area residents denominated in foreign currency	34 701		34 701
Intra-Eurosystem liabilities	10 376 364		10 376 364
Other liabilities	184 740	9 700	194 440
Capital and reserves	586 883		586 883
Total liabilities	25 750 694	3 562	25 754 256

The growth in other assets includes acquired fixed assets and intangible assets, the residual value of which amounted to 431 thousand euro, and other claims totalling 3126 thousand euro taken over by Latvijas Banka. The above claims mainly consisted of requirements for payments by market participants for the fourth quarter of 2022.

The reduction in liabilities in euro to other residents of euro area countries includes the FCMC's demand deposit with Latvijas Banka amounting to 6138 thousand euro.

The increase in other liabilities mainly includes the FCMC's own funds or net assets totalling 7213 thousand euro taken over by Latvijas Banka, which, in accordance with the transitional provisions of the Law on Latvijas

Banka, are intended to further reduce the aforementioned payments of market participants to cover supervision function expenses.

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.

Independent Auditors' Report

Translation from Latvian

08.03.2024

To the Council of Latvijas Banka

Opinion

We have audited the accompanying financial statements of Latvijas Banka (the Bank) set out on pages 3 to 45, which comprise the balance sheet as at 31 December 2023 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 2023, 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 Council and Those Charged with Governance for the Financial Statements

The Council 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 Council of the Bank is responsible for such internal control as the Council 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 Council 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 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 Council of the Bank.
- Conclude on the appropriateness of Council'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

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

Rīgā 2023. gada 8. martā

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

Appendix 1. Month-End Balance Sheets of Latvijas Banka for 2023

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

	01	02	03	04	05	06	07	08	09	10	11	12
ASSETS	25 728 234	25 756 393	25 769 693	25 431 054	25 551 151	25 328 381	25 406 277	25 506 606	25 564 081	25 344 132	25 467 044	25 564 820
Gold and gold receivables	376 765	364 291	389 369	386 000	392 624	374 922	379 815	382 704	377 383	401 978	399 131	399 378
Claims on non-euro area residents denominated in foreign currency	3 957 698	3 894 757	3 843 201	3 884 633	4 005 013	3 967 874	3 973 241	3 991 821	3 959 672	3 898 000	3 943 406	4 049 526
Receivables from the International Monetary Fund	546 798	550 205	543 745	539 043	546 494	538 318	535 284	538 133	545 477	543 454	536 995	534 839
Balances with credit institutions and security investments, external loans and other external assets	3 410 900	3 344 552	3 299 456	3 345 590	3 458 519	3 429 556	3 437 957	3 453 688	3 414 195	3 354 546	3 406 411	3 514 687
Claims on euro area residents denominated in foreign currency	526 199	616 587	584 505	582 025	586 571	579 539	584 013	586 023	619 050	578 440	586 218	595 802
Claims on non-euro area residents denominated in euro	155 895	168 853	160 831	156 487	165 830	150 672	152 388	156 651	166 357	153 421	160 492	168 476
Lending to euro area credit institutions related to monetary policy operations denominated in euro	422 900	342 900	342 900	343 900	342 900	92 900	92 900	92 900	92 900	92 900	92 900	92 900
Main refinancing operations	-	-	-	1 000	-	-	-	-	-	-	-	-
Longer-term refinancing operations	422 900	342 900	342 900	342 900	342 900	92 900	92 900	92 900	92 900	92 900	92 900	92 900
Fine-tuning reverse operations	-	-	-	-	-	-	-	-	-	-	-	-
Structural reverse operations	-	-	-	-	-	-	-	-	-	-	-	-
Marginal lending facility	-	-	-	-	-	-	-	-	-	-	-	-
Credits related to margin calls	-	-	-	-	-	-	-	-	-	-	-	-
Other claims on euro area credit institutions denominated in euro	1 480	29 876	16	4 048	21 130	4 569	510	9 021	16 881	1 084	1 850	133
Securities of euro area residents denominated in euro	14 147 770	14 225 126	14 247 674	13 918 325	13 811 943	13 840 841	13 871 479	13 869 897	13 876 916	13 753 565	13 709 924	13 550 657
Securities held for monetary policy purposes	13 210 127	13 269 799	13 304 297	12 979 960	12 869 183	12 904 343	12 927 655	12 932 870	12 945 880	12 814 301	12 763 552	12 586 724
Other securities	937 643	955 327	943 377	938 365	942 760	936 498	943 824	937 027	931 036	939 264	946 372	963 933
Intra-Eurosystem claims	5 888 311	5 894 658	5 900 755	5 898 663	5 958 579	5 980 470	6 024 763	6 070 004	6 069 666	6 094 712	6 123 008	6 412 443
Participating interest in the European Central Bank	118 849	118 849	118 849	118 849	118 849	118 849	118 849	118 849	118 849	118 849	118 849	118 849
Claims equivalent to the transfer of foreign reserves to the European Central Bank	157 202	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 TARGET2 and national central bank correspondent accounts (net)	-	-	-	-	-	-	-	-	-	-	-	-
Claims related to other operational requirements within the Eurosystem	5 612 260	5 618 607	5 624 704	5 622 612	5 682 528	5 704 419	5 748 712	5 793 953	5 793 615	5 818 661	5 846 957	6 136 392
Pending settlements	-	-	-	-	-	-	-	-	-	-	-	-
Other assets	251 216	219 345	300 442	256 973	266 561	336 594	327 168	347 585	385 256	370 032	450 115	295 505

	01	02	03	04	05	06	07	08	09	10	11	12
LIABILITIES	25 728 234	25 756 393	25 769 693	25 431 054	25 551 151	25 328 381	25 406 277	25 506 606	25 564 081	25 344 132	25 467 044	25 564 820
Banknotes in circulation	5 533 315	5 519 258	5 531 093	5 555 982	5 558 022	5 565 232	5 576 473	5 552 618	5 535 142	5 520 503	5 505 109	5 571 492
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	4 732 951	4 720 730	4 828 086	5 140 310	5 117 089	5 142 963	5 226 832	5 358 508	5 293 026	5 404 463	5 883 838	7 073 547
Current accounts (covering the minimum reserve system)	307 906	296 179	228 219	215 253	226 853	241 780	175 578	157 331	191 497	254 093	231 705	205 834
Deposit facility	4 425 045	4 424 551	4 599 867	4 925 057	4 890 236	4 901 183	5 051 254	5 201 177	5 101 529	5 150 370	5 652 133	6 867 713
Time deposits	-	-	-	-	-	-	-	-	-	-	-	-
Fine-tuning reverse operations	-	-	-	-	-	-	-	-	-	-	-	-
Deposits related to margin calls	-	-	-	-	-	-	-	-	-	-	-	-
Other liabilities to euro area credit institutions denominated in euro	369 158	431 903	440 981	434 513	426 190	437 794	428 121	390 683	388 936	407 871	400 529	314 720
Liabilities to other euro area residents denominated in euro	3 288 229	3 330 624	3 521 517	2 480 115	2 395 624	1 906 867	3 173 155	2 322 501	2 893 951	2 818 272	3 062 914	2 218 786
General government	2 129 453	2 170 675	2 364 869	1 352 823	1 266 469	772 040	2 065 859	1 211 899	1 778 614	1 720 366	1 955 670	1 131 021
Other liabilities	1 158 776	1 159 949	1 156 648	1 127 292	1 129 155	1 134 827	1 107 296	1 110 602	1 115 337	1 097 906	1 107 244	1 087 765
Liabilities to non-euro area residents denominated in euro	111 955	74 717	102 237	113 700	111 438	98 221	131 566	129 890	160 799	164 844	150 607	184 075
Liabilities to euro area residents denominated in foreign currency	1 139 841	1 215 264	1 369 478	1 326 174	1 352 262	1 330 240	1 352 100	1 364 399	1 312 284	1 295 325	1 358 099	1 262 758
Liabilities to non-euro area residents denominated in foreign currency	81 135	237 820	345 097	341 889	349 745	302 352	353 953	352 042	324 078	478 273	509 876	457 718
Intra-Eurosystem liabilities	9 586 944	9 403 298	8 766 083	9 183 990	9 352 278	9 738 901	8 342 507	9 227 930	8 916 152	8 574 324	7 791 311	7 569 389
Liabilities related to TARGET and national central bank correspondent accounts (net)	9 586 944	9 403 298	8 766 083	9 183 990	9 352 278	9 738 901	8 342 507	9 227 930	8 916 152	8 574 324	7 791 311	7 569 389
Liabilities related to other operational requirements within the Eurosystem	-	-	-	-	-	-	-	-	-	-	-	-
Pending settlements	-	-	-	-	-	-	-	-	-	-	-	-
Other liabilities	193 417	224 295	192 406	191 512	246 313	199 559	200 156	219 168	238 978	207 755	205 228	182 217
Capital and reserves	691 289	598 484	672 715	662 869	642 190	606 252	621 414	588 867	500 735	472 502	599 533	730 118

Appendix 2. Balance Sheets of Latvijas Banka for the Years 2019–2023

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

	2019	2020	2021	2022	2023
ASSETS	18 745 509	23 045 742	25 074 429	25 750 694	25 564 820
Gold and gold receivables	289 043	330 139	344 166	364 821	399 378
Claims on non-euro area residents denominated in foreign currency	3 688 972	3 970 780	4 495 181	3 788 044	4 049 526
Receivables from the International Monetary Fund	149 082	142 411	542 959	549 961	534 839
Balances with credit institutions and security investments, external loans and other external assets	3 539 890	3 828 369	3 952 222	3 238 083	3 514 687
Claims on euro area residents denominated in foreign currency	460 415	333 706	528 428	522 039	595 802
Claims on non-euro area residents denominated in euro	90 139	119 143	174 081	156 383	168 476
Lending to euro area credit institutions related to monetary policy operations denominated in euro	12 250	1 260 000	616 600	522 900	92 900
Main refinancing operations	–	–	–	–	–
Longer-term refinancing operations	12 250	1 260 000	616 600	522 900	92 900
Fine-tuning reverse operations	–	–	–	–	–
Structural reverse operations	–	–	–	–	–
Marginal lending facility	–	–	–	–	–
Credits related to margin calls	–	–	–	–	–
Other claims on euro area credit institutions denominated in euro	8	120	4 255	6 304	133
Securities of euro area residents denominated in euro	8 721 137	11 129 440	12 839 996	14 081 606	13 550 657
Securities held for monetary policy purposes	7 636 472	10 008 456	11 690 783	13 134 812	12 586 724
Other securities	1 084 665	1 120 984	1 149 213	946 794	963 933
Intra-Eurosystem claims	5 277 483	5 673 974	5 868 008	5 926 959	6 412 443
Participating interest in the European Central Bank	114 108	114 095	116 472	118 849	118 849
Claims equivalent to the transfer of foreign reserves to the European Central Bank	158 264	157 202	157 202	157 202	157 202
Claims related to TARGET and national central bank correspondent accounts (net)	–	–	–	–	–
Claims related to other operational requirements within the Eurosystem	5 005 111	5 402 677	5 594 334	5 650 908	6 136 392
Pending settlements	–	–	–	–	–
Other assets	206 062	228 440	203 714	381 638	295 505

	2019	2020	2021	2022	2023
LIABILITIES	18 745 509	23 045 742	25 074 429	25 750 694	25 564 820
Banknotes in circulation	4 666 799	5 142 726	5 536 624	5 635 738	5 571 492
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	5 660 676	6 053 812	6 406 673	5 217 165	7 073 547
Current accounts (covering the minimum reserve system)	5 660 676	6 053 812	6 406 673	343 816	205 834
Deposit facility	-	-	-	4 873 349	6 867 713
Time deposits	-	-	-	-	-
Fine-tuning reverse operations	-	-	-	-	-
Deposits related to margin calls	-	-	-	-	-
Other liabilities to euro area credit institutions denominated in euro	11 871	577 746	649 746	320 273	314 720
Liabilities to other euro area residents denominated in euro	1 506 709	3 012 014	3 438 792	2 517 104	2 218 786
General government	442 044	1 588 192	1 803 339	1 157 761	1 131 021
Other liabilities	1 064 665	1 423 822	1 635 453	1 359 343	1 087 765
Liabilities to non-euro area residents denominated in euro	307 239	238 737	57 955	171 688	184 075
Liabilities to euro area residents denominated in foreign currency	153 351	615 986	1 594 262	706 038	1 262 758
Liabilities to non-euro area residents denominated in foreign currency	1 642 368	1 364 010	688 359	34 701	457 718
Intra-Eurosystem liabilities	3 833 540	4 837 613	5 356 980	10 376 364	7 569 389
Liabilities related to TARGET and national central bank correspondent accounts (net)	3 826 452	4 809 553	5 322 638	10 370 127	7 569 389
Liabilities related to other operational requirements within the Eurosystem	7 088	28 060	34 342	6 237	-
Pending settlements	-	-	-	-	-
Other liabilities	329 326	409 700	436 383	184 740	182 217
Capital and reserves	633 630	793 398	908 655	586 883	730 118

Appendix 3. Profit and Loss Statements of Latvijas Banka for the Years 2019–2023

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

	2019	2020	2021	2022	2023
Net interest income	95 946	139 537	123 981	47 021	-229 006
Interest income	198 804	190 313	165 248	211 229	503 974
Interest expense	-102 858	-50 776	-41 267	-164 208	-732 980
Net result of financial operations, recognition of revaluation result in profit and loss statement and financial risk provisions	-37 821	-68 947	-50 235	-21 337	-10 948
Realised gains arising from financial operations	46 253	44 471	357	39 732	9 000
Recognition of revaluation result on financial assets and positions in profit and loss statement	-3 856	-35 237	-36 618	-341 715	-34 999
Provisions for market risk and credit risk	-80 218	-78 181	-13 974	280 646	15 051
Net expense from fees and commissions	-3 607	-3 394	-3 951	-4 441	-3 912
Fees and commissions income	811	949	981	1 011	1 037
Fees and commissions expense	-4 418	-4 343	-4 932	-5 452	-4 949
Income from participating interest	14 884	18 605	14 575	14 755	12 222
Net result of pooling of monetary income	-6 801	-27 701	-34 342	-6 237	206 554
Other operating income	1 300	1 268	3 591	5 766	19 561
NET INCOME	63 901	59 368	53 619	35 527	-5 529
Remuneration	-17 660	-16 867	-16 403	-16 502	-24 728
Social security costs and solidarity tax	-3 941	-3 764	-3 582	-3 653	-5 540
Banknote and coin acquisition costs	-1 791	-1 546	-1 831	-2 618	-2 338
Depreciation of fixed assets and amortisation of intangible assets	-4 129	-3 851	-3 802	-3 641	-3 660
Other operating expenses	-9 225	-6 694	-7 093	-9 113	-11 965
PROFIT OF THE REPORTING YEAR	27 155	26 646	20 908	0	-53 760
Profit transferrable to the reserve capital	8 146	7 994	6 272	0	0
Profit transferrable to the state budget	19 009	18 652	14 636	0	0

Appendix 4. Latvijas Banka's Publications and Major Publications by the Experts of Latvijas Banka in 2023

Working papers

BENĶOVSKIS, Konstantīns, FADEJEVA, Ludmila, PLUTA, Anna, ZASOVA, Anna. Keeping the best of two worlds: Linking CGE and microsimulation models for policy analysis. Riga: Latvijas Banka, Working Paper No 1, 2023, 33 p. Available: https://datnes.latvijasbanka.lv/papers/WP_1-2023.pdf.

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BENĶOVSKIS, Konstantīns, TKAČEVŠ, Oļegs, VILERTS, Kārlis. Did Job Retention Schemes Save Jobs during the Covid-19 Pandemic? Firm-level Evidence from Latvia. Riga: Latvijas Banka, Working Paper No 3, 2023, 37 p. Available: https://datnes.latvijasbanka.lv/papers/WP_3-2023.pdf

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ZLOBINS, Andrejs. Is There a Portfolio Rebalancing Channel of QE in Latvia? Riga: Latvijas Banka, Working Paper No 5, 2023, 31 p. Available: https://datnes.latvijasbanka.lv/papers/WP_5-2023.pdf.

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ALVES, Jose, AFONSO, Antonio, MATVEJEVS, Oļegs, TKAČEVŠ, Oļegs. Fiscal Sustainability and the Role of Inflation. Riga: Latvijas Banka, Working Paper No 8, 2023, 29 p. Available: https://datnes.latvijasbanka.lv/papers/WP_8-2023.pdf.

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Appendix 5. Glossary

AnaCredit (analytical credit datasets): a common Eurosystem's granular analytical credit and credit risk database containing 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.

Clearing: the process of transmitting, processing and reconciling payment documents or securities transfer orders prior to settlement, resulting in the 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 transactions 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.

Credit union: a co-operative society that has a variable number of members and capital and that provides financial services to its members in accordance with the Law on Credit Unions.

Deposit facility: a standing facility of the Eurosystem which credit institutions registered in Latvia and branches in Latvia of credit institutions registered in other countries may use to make overnight deposits with Latvijas Banka at a pre-specified interest rate.

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

Deposit-taking corporations – monetary financial institutions, except money market funds and the central bank, i.e. credit institutions (except credit institutions other than monetary financial institutions), credit unions and other financial institutions whose business is to receive deposits or close substitutes for deposits from customers other than monetary financial institutions, and, for their own account, to grant loans and invest in securities, as well as electronic money institutions whose core business is to issue electronic money.

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. Direct investment data are compiled both on an asset/liability basis (balance of payments and the international investment position data) and according to the directional principle – direct investment in Latvia and direct investment abroad.

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 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.

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 2023, the euro area comprised Austria, Belgium, Croatia, Cyprus, Estonia, Finland, France, Germany, Greece, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Portugal, Slovakia, Slovenia and Spain.

European Banking Authority (EBA): an EU body with legal personality which forms part of the European System of Financial Supervision and works to ensure effective and consistent prudential regulation and supervision across the EU 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 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, and 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 literacy: a combination of understanding financial matters, knowledge, skills, attitudes and behaviours needed to make sound financial decisions and ultimately achieve the well-being of individuals.

Financial resilience: an individual's ability to withstand, in financial terms, unexpected life events affecting income and/or assets, such as job loss, health issues, accidents, etc.

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

Financial sustainability: an individual's ability to ensure development and the planned long-term growth, while concurrently upholding the present quality of life. Financial sustainability empowers an individual to achieve financial security both in the present and in the future.

Financial vehicle corporation: an institutional unit other than an MFI that has been set up for the purpose of carrying out one or more securitisations. Latvijas Banka establishes, maintains and regularly updates the List of Financial Vehicle Corporations in the Statistics section of Latvijas Banka's website www.bank.lv.

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.

FINREP: supervisory financial reporting in compliance with Commission Implementing Regulation (EU) 2021/451 of 17 December 2020 laying down implementing technical standards for the application of Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to supervisory reporting of institutions and repealing Implementing Regulation (EU) No 680/2014 (Text with EEA relevance).

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.

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 a group of natural persons in the capacity of a consumer and a producer of goods and a provider of non-financial services exclusively for their own final use, as well as a sole proprietor that is an economic unit established by a natural person or a group of natural persons, provided this natural person or group of natural persons is liable to settle the obligations of the economic unit with their entire property, and that organises accounting 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 weekends and holidays.

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 and ensuring optimal data availability on the level of both granular and aggregated data. IReF

envisages collection of data from credit institutions' information systems and reporting of data in accordance with an integrated reporting dictionary and standard for data exchange.

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 deposit facility, the main refinancing operations and the marginal lending facility set by the Governing Council of the ECB.

Longer-term refinancing operation (LTRO): a regular open market operation of the Eurosystem, executed through reverse transactions with the aim of providing credit institutions with additional longer-term financing.

Main refinancing operation (MRO): 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.

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 financial institution (MFI): a central bank, credit institution (except for a non-MFI 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. MFIs in Latvia include Latvijas Banka, credit institutions registered in Latvia (except for non-MFI credit institutions), credit unions, electronic money institutions that have commenced the issue of electronic money, money market funds managed by investment management companies registered in an EEA country, as well as branches of MFIs of other countries in Latvia. Latvijas Banka establishes, maintains and regularly updates the List of Monetary Financial Institutions of Latvia in 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 2023, there were 46 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 ECB's 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.

Network for Greening the Financial System (NGFS): a group of central banks and supervisors committed to sharing best practices, contributing to the development of the climate and environment risk management in the financial sector and to mobilise finance to support the transition toward a sustainable economy.

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, provided this natural person or group of natural persons is liable for settling the obligations of the economic unit with its entire property, and whose accounting is organised in accordance with the double-entry system, as well as head offices, whose subsidiaries or their largest part are non-financial corporations.

Non-MFI credit institution: a credit institution that does not take deposits or other repayable funds from the public and does not grant credits for its own account, i.e. its business activities are not the activities referred to in Article 4(1)(1)(a) of Regulation (EU) No 575/2013.

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 stimulating policies that improve the economic and social well-being of persons.

Pandemic emergency asset 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 also stated that, in the pursuit of price stability, it aims to maintain inflation rates at 2% in the medium term.

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.

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 is 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.

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

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.

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 payment system developed within the framework of TARGET2 and TARGET2-Securities consolidation project and whose T2 service replaced TARGET2 on 20 March 2023. TARGET is a multiplicity of the TARGET component systems of all central banks. TARGET 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. TARGET operation is ensured by Latvijas Banka in conjunction with the national central banks of the ESCB participating in TARGET.

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.

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

Abbreviations

AML/CFT	anti-money laundering and countering the financing of terrorism
AML/CFTP	anti-money laundering and countering the financing of terrorism and proliferation
AS	joint stock company
BBM	borrower-based measure
CSB	Central Statistical Bureau of Latvia
EBA	European Banking Authority
EC	European Commission
ECB	European Central Bank
EEA	European Economic Area
EIB	European Investment Bank
EIOPA	European Insurance and Occupational Pensions Authority
ESCB	European System of Central Banks
ESMA	European Securities and Markets Authority
ESRB	European Systemic Risk Board
EU	European Union
FCMC	Financial and Capital Market Commission
FinTech	financial technologies
GDP	gross domestic product
ICT	information and communication technologies
IMF	International Monetary Fund
ML/FTP	money laundering and the financing of terrorism and proliferation
OECD	Organisation for Economic Co-operation and Development
SREP	supervisory review and evaluation process
SSM	single supervisory mechanism
UK	United Kingdom
US	United States of America