

# **LATVIJAS BANKA**

FINANCIAL STATEMENTS OF LATVIJAS BANKA  
FOR THE YEAR ENDED 31 DECEMBER 2021

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## 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
SDR	Special Drawing Rights
UK	United Kingdom
US	United States of America
PEPP	Pandemic Emergency Purchase Programme
PSPP	public sector asset purchase programme
TLTRO	targeted longer-term refinancing operations

## BALANCE SHEET

		(at the end of the year; in thousands of euro)	
	Note <sup>1</sup>	<b>2021</b>	2020
<b>ASSETS</b>			
Gold and gold receivables	6	<b>344 166</b>	330 139
Claims on non-euro area residents denominated in foreign currency	7	<b>4 495 181</b>	3 970 780
Receivables from the International Monetary Fund		542 959	142 411
Balances with banks and security investments, external loans and other external assets		3 952 222	3 828 369
Claims on euro area residents denominated in foreign currency	8	<b>528 428</b>	333 706
Claims on non-euro area residents denominated in euro	9	<b>174 081</b>	119 143
Lending to euro area credit institutions related to monetary policy operations denominated in euro	10	<b>616 600</b>	1 260 000
Longer-term refinancing operations		616 600	1 260 000
Other claims on euro area credit institutions denominated in euro	11	<b>4 255</b>	120
Securities of euro area residents denominated in euro	12	<b>12 839 996</b>	11 129 440
Securities held for monetary policy purposes		11 690 783	10 008 456
Other securities		1 149 213	1 120 984
Intra-Eurosystem claims	13	<b>5 868 008</b>	5 673 974
Participating interest in the European Central Bank		116 472	114 095
Claims equivalent to the transfer of foreign reserves		157 202	157 202
Other claims within the Eurosystem		5 594 334	5 402 677
Other assets	14	<b>203 714</b>	228 440
<b>TOTAL ASSETS</b>		<b>25 074 429</b>	23 045 742

<sup>1</sup> The accompanying Notes set out on pages 7 to 43 are an integral part of these financial statements.

<i>(continued)</i>	(at the end of the year; in thousands of euro)		
	Note	<b>2021</b>	2020
<b>LIABILITIES</b>			
Banknotes in circulation	15	<b>5 536 624</b>	5 142 726
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	16	<b>6 406 673</b>	6 053 812
Current accounts (covering the minimum reserve system)		6 406 673	6 053 812
Other liabilities to euro area credit institutions denominated in euro	0	<b>649 746</b>	577 746
Liabilities to other euro area residents denominated in euro	18	<b>3 438 792</b>	3 012 014
General government		1 803 339	1 588 192
Other liabilities		1 635 453	1 423 822
Liabilities to non-euro area residents denominated in euro	19	<b>57 955</b>	238 737
Liabilities to euro area residents denominated in foreign currency	20	<b>1 594 262</b>	615 986
Liabilities to non-euro area residents denominated in foreign currency	21	<b>688 359</b>	1 364 010
Intra-Eurosystem liabilities	13	<b>5 356 980</b>	4 837 613
Liabilities related to TARGET2 and correspondent accounts (net)		5 322 638	4 809 553
Other liabilities within the Eurosystem		34 342	28 060
Other liabilities	22	<b>436 383</b>	409 700
Capital and reserves	23	<b>908 655</b>	793 398
<b>TOTAL LIABILITIES</b>		<b>25 074 429</b>	23 045 742

## PROFIT AND LOSS STATEMENT

(in thousands of euro)

	Note	2021	2020
Net interest income	33	<b>123 981</b>	139 537
Interest income		165 248	190 313
Interest expense		-41 267	-50 776
Net result of financial operations, recognition of revaluation result in profit and loss statement and financial risk provisions		<b>-50 235</b>	-68 947
Realised gains arising from financial operations	34	357	44 471
Recognition of revaluation result on financial assets and positions in profit and loss statement	23, 35	-36 618	-35 237
Provisions for market risk and credit risk	36	-13 974	-78 181
Net expense from fees and commissions		<b>-3 951</b>	-3 394
Fees and commissions income		981	949
Fees and commissions expense		-4 932	-4 343
Income from equity securities and participating interest	37	<b>14 575</b>	18 605
Net result of pooling of monetary income	38	<b>-34 342</b>	-27 701
Other operating income	39	<b>3 591</b>	1 268
<b>NET INCOME</b>		<b>53 619</b>	59 368
Remuneration	40	<b>-16 403</b>	-16 867
Social security costs and solidarity tax	40	<b>-3 582</b>	-3 764
Banknote and coin acquisition costs	41	<b>-1 831</b>	-1 546
Depreciation of fixed assets and amortisation of intangible assets	14	<b>-3 802</b>	-3 851
Other operating expenses	42	<b>-7 093</b>	-6 694
<b>PROFIT FOR THE YEAR</b>		<b>20 908</b>	26 646

## STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES

		(in thousands of euro)	
	Note	2021	2020
Profit for the year		<b>20 908</b>	26 646
Revaluation	23	<b>119 670</b>	140 950
Realisation of the accumulated revaluation result	23	<b>-43 287</b>	-24 056
Recognition of revaluation result on financial assets and positions in profit and loss statement	23, 35	<b>36 618</b>	35 237
Total changes in the revaluation account	23	<b>113 001</b>	152 131
<b>TOTAL</b>		<b>133 909</b>	178 777

The financial statements set out on pages 3 to 43 were authorised by the Council of Latvijas Banka on 10 March 2022.

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.*

## NOTES TO THE FINANCIAL STATEMENTS

### 1. PRINCIPAL ACTIVITIES

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

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

- participate in the formulation and implementation of the Eurosystem's monetary policy;
- manage foreign reserves and other financial investments;
- ensure cash currency circulation in Latvia and contribute to ensuring cash currency circulation in the euro area;
- participate in promoting the smooth functioning of payment systems;
- compile and publish statistical information in order to ensure the performance of the tasks of Latvijas Banka;
- cooperate with the ECB, the central banks of other EU Member States and other countries as well as other financial institutions;
- promote the stability of Latvia's financial system at the macro level;
- operate as the financial agent of the Latvian government and provide financial services to other market participants;
- act as an advisor to the Saeima (Parliament) and Cabinet of Ministers of the Republic of Latvia on monetary policy issues and other issues related to the implementation of Latvijas Banka's tasks;
- maintain and develop the Credit Register;
- issue licences to legal persons listed in the Register of Enterprises of the Republic of Latvia, except credit institutions, for the purchase and sale of foreign currency as a commercial activity;
- perform the function of the National Analysis Centre and the Coin National Analysis Centre, ensuring efficient analysis of currency counterfeits.

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

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

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

In line with amendments to the Law on Latvijas Banka, Latvijas Banka introduced a single-tier top management model, discontinuing the operation of the Board of Latvijas Banka and reassigning its tasks to the Council of Latvijas Banka, committees and departments. Ensuring more effective management, as of 1 June 2021, all significant decisions on behalf of Latvijas Banka, within the scope of their respective competencies, are made by the Council of Latvijas Banka and the Governor of Latvijas Banka.

### 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 Latvijas Banka's Council, 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 Note 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 Note 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 price of gold is set on the basis of the quoted gold market price in US dollars and the exchange rate of the US dollar against the euro published by the ECB. The exchange rate of the SDR is set on the basis of the weights of currencies in the SDR basket published by the IMF and the exchange rates of the respective currencies published by the ECB.

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

Transactions in foreign currencies are included in the calculation of net foreign currency position of the respective currency. 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 2021 and the year ended 31 December 2020 are as follows:

	(at the end of the year)		
	2021	2020	Changes (%)
US dollar (USD)	<b>1.1326</b>	1.1234	-7.7
Japanese yen (JPY)	<b>130.38</b>	121.94	3.1
Canadian dollar (CAD)	<b>1.4393</b>	1.4598	-7.9
British pound sterling (GBP)	<b>0.84028</b>	0.85080	-6.5
Gold (XAU)	<b>1609.483</b>	1354.104	4.2

### 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 was 1000 euro in 2021 (150 euro in 2020), 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 2021, the useful lives set for fixed and intangible assets were not changed. In 2021 and 2020, the useful lives set were as follows:

	(years)	
	2021	2020
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. 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 2021, Latvijas Banka's assets grew by 2028.7 million euro.

In 2021, the balance sheet item "Securities held for monetary policy purposes" increased by 1682.3 million euro due to asset purchases made by Latvijas Banka under the PEPP and PSPP.

In 2021, the amount of loans granted to credit institutions by Latvijas Banka as a result of longer-term refinancing operations decreased by 643.4 million euro (see also Note 10.2).

Other claims related to other operational requirements within the Eurosystem grew by 191.7 million euro, mostly due to a rise in claims on banknote allocation in the Eurosystem (see also Note 13.4).

In 2021, banknotes in circulation increased by 393.9 million euro, in line with the pickup in the overall amount of banknotes in circulation of the euro area NCBs.

The increases of 978.3 million euro under balance sheet item "Liabilities to euro area residents denominated in foreign currency" respectively, as well as a decrease of 675.7 million euro under the balance sheet item "Liabilities to non-euro area residents denominated in foreign currency" are mostly related to repurchase agreements and gold swaps arrangements to reduce the costs for hedging currency risks and increase return on financial investments.

At the end of 2021, 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 352.9 million euro. As a result of cross-border payments, liabilities to the ECB for the settlement result in TARGET2, reported under the balance sheet item "Intra-Eurosystem liabilities", increased by 513.1 million euro.

The capital and reserves of Latvijas Banka increased by 115.3 million euro due to net changes in the "Revaluation account" balance (113.0 million euro) and the profits earned in 2021 (20.9 million euro), while the share of profits earned in 2020 and remitted to the state budget revenue (18.7 million euro) had a decreasing effect.

### **3.2 Financial performance**

In 2021, Latvijas Banka's profit amounted to 20.9 million euro (26.6 million euro in 2020).

Net interest income in 2021 decreased by 15.6 million euro as compared to 2020 and reached the amount of 124.0 million euro. This mainly resulted from a 25.1 million euro decrease in interest income and a 9.5 million euro decrease in interest expense on account of lower average yields on securities and costs of hedging currency risks and larger interest expense on monetary policy operations on account of increased volume of monetary policy operations and larger interest payments.

The realised gains on financial operations amounted to 0.4 million euro (44.5 million euro in 2020), while the recognition of the negative revaluation result on financial assets and positions in the profit and loss statement

increased to stand at 36.6 million euro (35.2 million euro in 2020), mostly on account of decreasing market value of debt securities due to rising yields.

In 2021, additional provisions in the amount of 14.0 million euro were established for market risk and credit risk (78.2 million in 2020).

Income from equity securities and participating interest amounted to 14.6 million euro (18.6 million euro in 2020), the decrease resulting from lower income from participating interest in the ECB.

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 was negative (34.3 million euro; 27.7 million euro in 2020).

Other operating income stood at 3.6 million euro (1.3 million euro in 2020). Income increased primarily on account of a revaluation of liabilities for the issued lats banknotes and coins.

The total recognised financial result, including changes in the "Revaluation account" balance, decreased by 44.9 million euro in comparison with 2020 and reached 133.9 million euro on account of a decrease of 40.5 million euro in the positive result of revaluation and a 1.4 million euro rise in the negative result on revaluation of financial assets and positions in the profit and loss statement, while the profit for the reporting year was 5.7 million euro lower than in 2020.

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

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

#### **4. FINANCIAL INVESTMENT POLICY**

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

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

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

The parameters for a benchmark reflecting the acceptable level of financial risks and expected return are set out for the 1–10 year fixed income securities portfolios, mortgage-backed securities portfolios, the portfolio of borrowed funds, the developed markets equity 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 2021 and 2020 was as follows:

	Book value (in thousands of euro)		Proportion (%)	
	2021	2020	2021	2020
1–10 year fixed income securities portfolios	<b>3 209 547</b>	3 445 980	<b>47.9</b>	58.2
Mortgage-backed securities portfolios	<b>1 186 537</b>	1 211 775	<b>17.7</b>	20.5
Developed markets equity securities portfolio	<b>793 702</b>	573 316	<b>11.8</b>	9.7
The portfolio of borrowed funds	<b>544 413</b>	143 350	<b>8.1</b>	2.4
Gold portfolio	<b>344 166</b>	330 139	<b>5.1</b>	5.6
Emerging markets fixed income securities portfolio	<b>325 212</b>	–	<b>4.9</b>	–
Long-term fixed income securities portfolio	<b>168 246</b>	168 173	<b>2.5</b>	2.8
Emerging markets equity securities portfolio	<b>94 391</b>	–	<b>1.4</b>	–
Latvian government securities portfolio	<b>39 167</b>	47 025	<b>0.6</b>	0.8
<b>Total</b>	<b>6 705 381</b>	5 919 758	<b>100.0</b>	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.

In 2021, Latvijas Banka established an emerging markets fixed income securities portfolio. 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.

In 2021, Latvijas Banka established an emerging markets equity securities portfolio. 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 of Latvijas Banka's investment portfolios is the euro, except for the portfolio of borrowed funds, the equity securities portfolio, developed markets equity securities portfolio, emerging markets equity securities portfolio and the gold portfolio, thus limiting the currency risk. For the portfolio of borrowed funds, the benchmark currency structure is formed considering the currency of the respective liabilities.

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

## BALANCE SHEET NOTES

### 5. FAIR VALUE MEASUREMENT

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

– quoted market price. The fair value is determined using quoted prices for identical financial instruments in active markets;

– observable data. The fair value is determined using quoted prices for similar financial instruments in active markets, quoted prices for 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 2021 and 2020, 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 2021 and 2020, 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 2021 and 2020, 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		
<b>As at 31 December 2020</b>						
Gold	330 139	330 139	–	–	330 139	–
Securities in investment portfolios	5 362 253	4 842 019	541 405	–	5 383 424	21 171
Forward exchange rate contracts	25 613	–	25 063	–	25 063	–550
Interest rate swap arrangements	1	1	–	–	1	–
Securities held for monetary policy purposes	10 082 251	10 897 433	–	–	10 897 433	815 182
Participating interest in the Bank for International Settlements	35 960	–	–	35 960	35 960	–
<b>Total</b>	<b>15 836 217</b>	<b>16 069 592</b>	<b>566 468</b>	<b>35 960</b>	<b>16 672 020</b>	<b>835 803</b>
<b>As at 31 December 2021</b>						
Gold	344 166	344 166	–	–	344 166	–
Securities in investment portfolios	5 741 342	5 014 198	741 456	–	5 755 654	14 312
Forward exchange rate contracts	–5 850	–	–6 314	–	–6 314	–464
Interest rate swap arrangements	1	1	–	–	1	–
Securities held for monetary policy purposes	11 761 724	12 096 792	–	–	12 096 792	335 068
Participating interest in the Bank for International Settlements	37 309	–	–	37 309	37 309	–
<b>Total</b>	<b>17 878 692</b>	<b>17 455 157</b>	<b>735 142</b>	<b>37 309</b>	<b>18 227 608</b>	<b>348 916</b>

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 2019	213 457	289 043
<b>During 2020</b>		
Increase in gold market value	x	40 511
Net change resulting from gold swaps arrangements	379	585
As at 31 December 2020	213 836	330 139
<b>During 2021</b>		
Increase in gold market value	x	14 027
<b>As at 31 December 2021</b>	<b>213 836</b>	<b>344 166</b>

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

To limit the gold maintenance costs and ensure return on gold investments, at the end of 2021, all gold in the amount of 344 166 thousand euro (330 139 thousand euro at the end of 2020) had been involved in gold swaps arrangements (see also Notes 21 and 43). Gold swap arrangements are treated as repurchase agreements.

At the end of 2021 and 2020, 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 2021, the receivables from the IMF in SDR as recorded on Latvijas Banka's balance sheet were equivalent to 542 959 thousand euro (142 411 thousand euro at the end of 2020), whereas the liabilities to the IMF are made up of funds at the disposal of the IMF in the amount of 1436 thousand euro (983 thousand euro at the end of 2020) held on its Accounts No. 1 and No. 2 (see also Note 19). In 2021, the IMF member countries were granted a general SDR allocation of 456 billion SDR to boost global liquidity, of which Latvia received 318 million SDR.

At the end of 2021 and 2020, Latvia's net receivables from the IMF were as follows:

	(in thousands of euro)		(in thousands of SDR)	
	2021	2020	2021	2020
Latvia's quota in the International Monetary Fund	<b>410 690</b>	391 649	<b>332 300</b>	332 300
International Monetary Fund holdings in euro	<b>-410 621</b>	-391 588	<b>-332 244</b>	-332 249
Promissory note of the Latvian government	-409 185	-390 605	-331 082	-331 414
Account No. 1	-1 027	-979	-831	-831
Account No. 2	-409	-4	-331	-4
Reserve position in the International Monetary Fund	<b>478</b>	65	<b>387</b>	55
SDR	<b>542 959</b>	142 411	<b>439 323</b>	120 830
General allocation	<b>-509 799</b>	-110 786	<b>-412 493</b>	-93 998
Special allocation	<b>-33 152</b>	-31 615	<b>-26 824</b>	-26 824
Latvia's net receivables from the International Monetary Fund	<b>486</b>	75	<b>393</b>	63

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

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

	(in thousands of euro)	
	2021	2020
Securities	<b>3 881 610</b>	3 783 432
Demand deposits	<b>70 594</b>	44 920
Foreign currency in cash	<b>18</b>	17
Total	<b>3 952 222</b>	3 828 369

## 8. CLAIMS ON EURO AREA RESIDENTS DENOMINATED IN FOREIGN CURRENCY

	(in thousands of euro)	
	2021	2020
Securities	<b>527 531</b>	332 969
Demand deposits	<b>897</b>	737
Total	<b>528 428</b>	333 706

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

	(in thousands of euro)	
	2021	2020
Securities	<b>167 048</b>	105 509
Demand deposits	<b>7 033</b>	13 634
Total	<b>174 081</b>	119 143

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

At the end of 2021, the total amount of Eurosystem loans in monetary policy operations reached 2 201 882 million euro (1 793 194 million euro at the end of 2020), including 616.6 million euro (1260 million euro at the end of 2020) 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 2021 and 2020, Latvijas Banka had granted no loans in main refinancing operations.

### **10.2 Longer-term refinancing operations**

Longer-term refinancing operations are open market operations, executed through reverse transactions with the aim to provide credit institutions with additional longer-term refinancing. Such operations are conducted through monthly standard tenders with maturities between 3 and 48 months. In addition, following the decision of the Governing Council of the ECB, TLTROs were launched in 2014. They are liquidity providing reverse operations providing longer-term liquidity to credit institutions on attractive terms, so that they can continue easing the terms and conditions of lending to the private sector and to encourage their lending to the real economy. In 2016, the Governing Council of the ECB introduced a new series of four targeted longer-term refinancing operations (TLTRO II). These operations 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%. Additionally, in April 2020, the Governing Council of the ECB decided to conduct a new series of seven additional longer-term refinancing operations (maturing at the third quarter of 2021) called pandemic emergency longer-term refinancing operations (PELTROs). These operations provide further liquidity support after the expiry of the bridge longer-term refinancing operations (LTROs) that have been conducted since March 2020. In 2021, Latvijas Banka granted loans in the amount of 101 600 thousand euro to Latvian credit institutions at TLTRO III auctions and received 745 000 thousand euro as repayment of loans granted to credit institutions. At the end of 2021, the balance of the TLTROs conducted by Latvijas Banka stood at 616 600 thousand euro; these operations will mature in 2023 and 2024 (at the end of 2020, the balance was 1 260 000 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 (4255 thousand euro at the end of 2021; 120 thousand euro at the end of 2020).

## **12. SECURITIES OF EURO AREA RESIDENTS DENOMINATED IN EURO**

At the end of 2021, the amount of securities held by the Eurosystem for monetary policy purposes totalled 4 713 403.5 million euro (3 694 641.8 million euro at the end of 2020). Of them, Latvijas Banka held 11 691.7 million euro (10 008.5 million euro at the end of 2020). 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 2021, the amount of government securities purchased by the euro area NCBs under the PSPP totalled 1989 billion euro (1872 billion euro at the end of 2020); of them, Latvijas Banka held Latvian government securities in the amount of 2307 million euro (1848 million euro at the end of 2020). At the end of 2020, the amount of government securities purchased by the euro area NCBs under the PEPP totalled 1244 billion euro (586 billion euro at the end of 2020); of them, the amount of Latvian government securities held by Latvijas Banka was 1242 million euro.



In 2021, the Eurosystem's purchases of securities under the APP continued at a monthly net pace of 20 billion euro. The Governing Council of the ECB expects them to run for as long as necessary to reinforce the accommodative impact of its monetary policy rates, and to end shortly before the ECB starts raising the key ECB interest rates. In response to the COVID-19 pandemic and the related potential risks to the monetary policy transmission mechanism and the euro area economic outlook, in March 2020, the Governing Council of the ECB launched a new asset purchase programme, the PEPP, whereby net asset purchases will be continued until March 2022 or until the crisis caused by the COVID-19 pandemic is over.

	(in thousands of euro)	
	Book value	
	<b>2021</b>	2020
Securities held for monetary policy purposes	<b>11 690 783</b>	10 008 456
Latvian government securities	3 548 199	2 596 791
PSPP government securities	2 306 559	1 848 233
PEPP government securities	1 241 640	748 558
Debt securities issued by international institutions	8 142 584	7 411 665
PSPP debt securities issued by international institutions	6 564 407	6 469 341
PEPP debt securities issued by international institutions	1 578 177	942 324
Other securities	<b>1 149 213</b>	1 120 984
Securities not held to maturity	980 967	952 811
Securities held to maturity	168 246	168 173
<b>Total</b>	<b>12 839 996</b>	11 129 440

### 13. INTRA-EUROSISTEM CLAIMS/LIABILITIES (-)

	Note	(in thousands of euro)	
		<b>2021</b>	2020
Participating interest in the European Central Bank	13.1	<b>116 472</b>	114 095
Claims in respect of foreign reserves transferred to the European Central Bank	13.2	<b>157 202</b>	157 202
Claims related to the allocation of banknotes in the Eurosystem	13.4	<b>5 593 565</b>	5 397 767
Claims related to other operational requirements within the Eurosystem	13.5	<b>769</b>	4 910
<b>Total intra-Eurosystem claims</b>		<b>5 868 008</b>	5 673 974
Liabilities related to TARGET2 and national central bank correspondent accounts (net)	13.3	<b>-5 322 638</b>	-4 809 553
Other liabilities within the Eurosystem	13.5	<b>-34 342</b>	-28 060
<b>Total intra-Eurosystem liabilities</b>		<b>-5 356 980</b>	-4 837 613
<b>Intra-Eurosystem claims</b>		<b>511 028</b>	836 361

#### 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 2020 because of the departure of the United Kingdom from the European Union and the subsequent withdrawal of the Bank of England from the ESCB. The Bank of England's

share in the ECB's subscribed capital (14.3374%) was reallocated among other NCBs; hence the capital key of Latvijas Banka increased from 0.2731% to 0.3169%, equivalent to 34 304 thousand euro.

The Statute of the ESCB and of the ECB stipulates that a euro area NCB shall pay up its subscribed share in the ECB's capital in full, as well as contribute to the ECB's reserve capital, to those provisions equivalent to reserves and to the revaluation account for financial instruments in proportion to its share in the ECB's capital. Following the withdrawal of the Bank of England from the ESCB, the ECB's total paid-up capital increased by 1221 million euro, as the subscriptions of the euro area NCB's (subscribed capital paid up in full) in the ECB's subscribed capital grew and the subscriptions of non-euro area NCB's (pay up 3.75% of their subscriptions) in the ECB's subscribed capital decreased accordingly. The Governing Council of the ECB decided that the euro area NCB's were to pay up their subscriptions fully; therefore, their subscribed capital would increase in two instalments, at the end of 2021 and 2022 respectively.

In 2021, Latvijas Banka made the first of two payments in the amount of 2377 thousand euro. At the end of 2021, Latvijas Banka's participating interest in the ECB consisted of the paid-up shares in the amount of 31 927 thousand euro in the ECB's capital, transfers to the financial instrument revaluation account amounted to 42 752 thousand euro and the difference between the market value of the foreign reserves transferred to the ECB and the value of the corresponding euro-denominated claim amounted to 41 793 thousand euro (see also Note 13.2).

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

	(in thousands of euro)	
	2021	2020
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	<b>31 927</b>	29 550
The percentage share of Latvijas Banka in the European Central Bank's capital (capital key; %)	<b>0.3169</b>	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 2021 and of 2020, 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 TARGET2 and national central bank correspondent accounts (net)**

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

In 2021, the liabilities related to TARGET2 and national central bank correspondent accounts (net) increased as a result of the cross-border payments effected by credit institutions and Latvijas Banka.

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

### **13.4 Claims related to the allocation of banknotes within the 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.

Monetary income to be pooled by Latvijas Banka in 2021 was higher than monetary income to be received. This resulted in a liability to the ECB associated with the net result of pooling of monetary income, standing at 34 342 thousand euro at the end of 2021 (28 060 thousand euro claim at the end of 2020; see also Notes 38).

Claims for the ECB's interim profit distribution in the amount of 584 thousand euro are set as per Latvijas Banka's percentage share in the ECB's capital (4910 thousand euro at the end of 2020; see also Note 37).

## 14. OTHER ASSETS

		(in thousands of euro)	
	Note	2021	2020
Accrued interest on securities held for monetary policy purposes		70 941	73 795
Participating interest in the Bank for International Settlements	14.2	37 309	35 960
Claims on collateral for the use of the instant payment service	0	37 022	26 306
Fixed assets	14.1	30 825	33 590
Accrued interest on other securities		15 111	18 196
OTC financial derivative contracts and spot exchange rate contracts	24	7 203	34 169
Intangible assets	14.1	2 039	2 160
Other accrued income		1 634	2 660
Prepaid expenses		1 070	1 030
Other		560	574
<b>Total</b>		<b>203 714</b>	<b>228 440</b>

## 14.1 Fixed assets and intangible assets

(in thousands of euro)

	Buildings, improvement of territory, and land	Furniture and office equipment	Computer and telecom- munication equipment	Cash processing and storage equipment	Other fixed assets	Total fixed assets	Intangible assets
<b>As at 31 December 2019</b>							
Cost	58 298	6 231	4 767	5 333	9 830	84 459	8 110
Accumulated depreciation/amortisation	-30 581	-4 246	-3 778	-3 031	-7 504	-49 140	-5 847
Net book value	27 717	1 985	989	2 302	2 326	35 319	2 263
<b>During 2020</b>							
Additions	346	48	430	673	165	1 662	457
Change in classification	-1	-6	6	-	-24	-25	25
Disposals and write-offs	-	-146	-154	-86	-1 483	-1 869	-
Net change in cost	345	-104	282	587	-1 342	-232	482
Depreciation/amortisation charge	-1 917	-252	-444	-251	-427	-3 291	-560
Change in classification	1	6	-6	-	24	25	-25
Accumulated depreciation/amortisation on disposals and write-offs	-	144	153	86	1 386	1 769	-
Net change in accumulated depreciation/amortisation	-1 916	-102	-297	-165	983	-1 497	-585
<b>As at 31 December 2020</b>							
Cost	58 643	6 127	5 049	5 920	8 488	84 227	8 592
Accumulated depreciation/amortisation	-32 497	-4 348	-4 075	-3 196	-6 521	-50 637	-6 432
Net book value	26 146	1 779	974	2 724	1 967	33 590	2 160
<b>During 2021</b>							
Additions	174	-	171	38	215	598	432
Change in classification	-	-	-	-	-145	-145	145
Disposals and write-offs	-	-72	-240	-665	-421	-1 398	-34
Net change in cost	174	-72	-69	-627	-351	-945	543
Depreciation/amortisation charge	-1 952	-234	-398	-279	-420	-3 283	-519
Change in classification	-	-	-	-	145	145	-145
Accumulated depreciation/amortisation on disposals and write-offs	-	72	240	662	344	1 318	-
Net change in accumulated depreciation/amortisation	-1 952	-162	-158	383	69	-1 820	-664
<b>As at 31 December 2021</b>							
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
<b>Net book value</b>	<b>24 368</b>	<b>1 545</b>	<b>747</b>	<b>2 480</b>	<b>1 685</b>	<b>30 825</b>	<b>2 039</b>

At the end of 2021, Latvijas Banka's contractual commitments related to acquisition of fixed assets were 128 thousand euro (24 thousand euro at the end of 2020).

#### 14.2 Participating interest in the Bank for International Settlements

At the end of 2021 and 2020, 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 2021 and 2020, the BIS shareholding is reported in Latvijas Banka's balance sheet at fair value. The shares in the BIS are not traded in the public securities market. In the opinion of Latvijas Banka, the most appropriate method for establishing the fair value of the BIS shares is the use of 70% of the BIS net asset value based on the latest published financial statements of the BIS. Pursuant to the Statutes of the BIS, only central banks can be shareholders in the BIS. At the end of 2021, the estimated fair value of BIS shares was 37 309 thousand euro (35 960 thousand euro at the end of 2020).

#### 15. BANKNOTES IN CIRCULATION

	(in thousands of euro)	
	2021	2020
Euro banknotes	5 536 624	5 142 726
Net issuance of euro banknotes by Latvijas Banka	-56 941	-255 041
Adjustment for banknote allocation in the Eurosystem	5 593 565	5 397 767
Total	5 536 624	5 142 726

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 2021 decreased, reducing the difference between the amount of banknotes deposited with Latvijas Banka and the amount of banknotes withdrawn from Latvijas Banka; consequently, the negative net issuance of euro banknotes by Latvijas Banka reached 56 941 thousand euro. At the end of 2021, the total amount of euro banknotes in circulation in the Eurosystem grew to 1544 billion euro (1435 billion euro at the end of 2020); as a result, an increase in the adjustment for banknote allocation in the Eurosystem was reported on the balance sheet of Latvijas Banka.

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

##### 16.1 Current accounts (covering the minimum reserve system)

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

At the end of 2021, the balance on the current accounts with Latvijas Banka was 6 406 673 thousand euro (6 053 812 thousand euro at the end of 2020), including the minimum reserves in the amount of 183 129 thousand euro (168 154 thousand euro at the end of 2020).

##### 16.2 Deposit facility

Deposit facility is a standing facility of the Eurosystem used by credit institutions to place their overnight deposits at a pre-specified rate. No such deposits were placed with Latvijas Banka at the end of 2021 and 2020.

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

(in thousands of euro)

	<b>2021</b>	2020
Liabilities for repurchase agreements	<b>612 898</b>	551 537
Collateral received for the use of the instant payment service	<b>36 848</b>	26 209
Total	<b>649 746</b>	577 746

**18. LIABILITIES TO OTHER EURO AREA RESIDENTS DENOMINATED IN EURO**

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

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

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

(in thousands of euro)

	<b>2021</b>	2020
Other financial institutions	<b>56 509</b>	237 745
International Monetary Fund	<b>1 436</b>	983
European Commission	<b>10</b>	9
Total	<b>57 955</b>	238 737

**20. LIABILITIES TO EURO AREA RESIDENTS DENOMINATED IN FOREIGN CURRENCY**

(in thousands of euro)

	<b>2021</b>	2020
Liabilities for repurchase agreements	<b>1 049 849</b>	472 636
Demand deposits of the Latvian government	<b>544 413</b>	143 350
Total	<b>1 594 262</b>	615 986

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

(in thousands of euro)

	<b>2021</b>	2020
Liabilities for repurchase agreements	<b>347 148</b>	1 042 015
Liabilities for gold swap arrangements	<b>341 211</b>	321 995
Total	<b>688 359</b>	1 364 010

## 22. OTHER LIABILITIES

		(in thousands of euro)	
	Note	2021	2020
Provisions for market risk and credit risk	36	<b>295 697</b>	281 723
Euro coins in circulation	22.1	<b>86 274</b>	79 690
Lats banknotes in circulation	22.1	<b>19 264</b>	22 584
Accrued expense and similar liabilities		<b>15 353</b>	13 637
OTC financial derivative contracts and spot exchange rate contracts	24	<b>12 257</b>	7 479
Lats coins in circulation	22.1	<b>2 631</b>	2 750
Tax liabilities		<b>703</b>	19
Other		<b>4 204</b>	1 818
Total		<b>436 383</b>	409 700

### 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 (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 7096 thousand euro at the end of 2021 (7034 thousand euro at the end of 2020). The above coins in circulation have not been reported under the balance sheet item "Other liabilities" (see also Notes 45).

Issued lats banknotes and coins with a low probability of exchange in the amount of 97 980 thousand euro (lats banknotes in the amount of 38 189 thousand euro and lats coins in the amount of 59 791 thousand euro at the end of 2021; 95 600 thousand euro at the end of 2020, including lats banknotes in the amount of 35 791 thousand euro and lats coins in the amount of 59 808 thousand euro) have not been reported as a liability on the balance sheet at the end of 2021 (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 for the year	Capital and reserves
As at 31 December 2019	100 000	240 733	265 742	27 155	633 630
<b>During 2020</b>					
Net result of revaluation, realisation, and revaluation result recognition in profit and loss statement	x	x	152 131	x	152 131
Profit appropriated to the state budget	x	x	x	-19 009	-19 009
Profit transferred to the reserve capital	x	8 146	x	-8 146	-
Profit for the year	x	x	x	26 646	26 646
As at 31 December 2020	100 000	248 879	417 873	26 646	793 398
<b>During 2021</b>					
Net result of revaluation, realisation, and revaluation result recognition in profit and loss statement	x	x	113 001	x	113 001
Profit appropriated to the state budget	x	x	x	-18 652	-18 652
Profit transferred to the reserve capital	x	7 994	x	-7 994	-
Profit for the year	x	x	x	20 908	20 908
<b>As at 31 December 2021</b>	<b>100 000</b>	<b>256 873</b>	<b>530 874</b>	<b>20 908</b>	<b>908 655</b>

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

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

The nominal capital of Latvijas Banka has historically been comprised of the state-allotted resources, transfers from the reserve capital and Latvijas Banka's profit allocations.

The Law on Latvijas Banka establishes that a part of Latvijas Banka's profit for the reporting year, calculated by applying the same percentage as the corporate income tax rate set by the Law on Corporate Income Tax, together with a payment in the amount of 50% of the profit for the reporting year for the usage of state capital shall be transferred to the state budget. Furthermore, the Council of Latvijas Banka, upon approving the annual report, may make a decision on reducing the percentage share of the payment for the usage of state capital, where it is necessary for increasing the reserve capital of Latvijas Banka in relation to the financial risks Latvijas Banka is exposed to when executing its tasks. At the end of 2021 and 2020, the corporate income tax rate was 20%. Therefore, unless the Council of Latvijas Banka decides otherwise, 70% of Latvijas Banka's profit for 2021 or 14 636 thousand euro will be transferred to the state budget in 2022 (18 652 thousand euro were transferred in 2021 and 19 009 thousand euro in 2020).

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

The revaluation account comprises the positive result on revaluation of the financial instruments and gold. The accounting policy, harmonised with the principal accounting policies established by the ECB's legal framework for accounting and financial reporting and described in Note 2 stipulates that 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 2021 and 2020, the changes in the revaluation account were as follows:

(in thousands of euro)

	2021	Recognition in profit and loss statement	Revaluation	Realisation	2020
Revaluation reserve for participating interest	<b>34 800</b>	–	1 349	–	33 451
Result on revaluation of foreign currencies and gold	<b>164 481</b>	935	31 864	–1	131 683
Result on revaluation of interest rate swap arrangements	–	21	–21	–	–
Result on revaluation of securities	<b>331 593</b>	35 662	86 478	–43 286	252 739
<b>Total</b>	<b>530 874</b>	36 618	119 670	–43 287	417 873

  

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

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 2021 and 2020, 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			
			Assets		Liabilities	
	2021	2020	2021	2020	2021	2020
OTC financial derivative and spot exchange rate contracts						
Forward exchange rate contracts and currency swap arrangements	2 477 704	2 487 071	4 091	31 971	11 604	5 004
Spot exchange rate contracts	403 020	409 272	1 663	–	–	1 354
Forward transactions in securities	1 817 672	1 186 202	1 448	2 197	618	812
Interest rate swap arrangements	37 696	24 366	1	1	35	309
<b>Total</b>	<b>x</b>	<b>x</b>	<b>7 203</b>	<b>34 169</b>	<b>12 257</b>	<b>7 479</b>
Derivative OTC gold swap arrangements	341 211	321 995	344 166	330 139	339 203	322 104
Traded financial derivative contracts						
Interest rate future contracts	869 374	912 276	x	x	x	x
Currency future contracts	–	100 000	x	x	x	x

The book value of the OTC financial derivative contracts and spot exchange rate contracts is reported under the balance sheet items "Other assets" or "Other liabilities" (see also Notes 14 and 22). Since a 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 and 21).

## MAJOR RISKS AND PRINCIPLES FOR THEIR MANAGEMENT

### 25. RISK MANAGEMENT

Financial and operational risks are the main risks associated with the activities of Latvijas Banka. Latvijas Banka's risk management is organised and implemented according to the Risk Management Policy of Latvijas Banka approved by the Council of Latvijas Banka.

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

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

#### 25.1 Financial risks

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

Latvijas Banka manages financial risks related to its investments in line with the Procedure adopted by the Council of Latvijas Banka; the basic principles of the investment policy are described in Note 4. Investments are

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

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 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 portfolios, 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 2021 and 2020 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 2021 and 2020) is disclosed in Notes 26–28.

#### **25.1.2 Credit risk**

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

Latvijas Banka manages exposure to credit risk related to investments made in foreign financial instruments by establishing limits on investments of different credit quality. Credit quality is evaluated on the basis of ratings assigned by the international credit rating agencies Fitch Ratings, Moody's Investors Service, Standard & Poor's, and DBRS. Limits are also set on the maximum investment in financial instruments of the same class and counterparty as well as in financial instruments of one issuer. Forward transactions in mortgage-backed securities are partly secured with short-term financial instruments. To hedge the credit risk associated with OTC derivative counterparties, Latvijas Banka and the respective counterparties enter into Master Agreements of International

Swaps and Derivatives Association, Inc. (ISDA Master Agreement) with Credit Support Annex. To hedge the credit risk associated with the counterparties of repurchase agreements and reverse repurchase agreements, Latvijas Banka and the respective counterparties enter into Global Master Repurchase Agreements of Securities Industry and Financial Markets Association (SIFMA) and International Capital Market Association (ICMA), whereas the external managers of mortgage-backed securities portfolios enter with their counterparties into Treasury Market Practices Group (TMPG) Master Securities Forward Transaction Agreements. In order to monitor Latvijas Banka's credit risk exposure associated with its investments, the Risk Management Division of the Market Operations Department monitors the compliance with the Procedure adopted by the Council of Latvijas Banka.

In 2021 and 2020, 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 2021 and 2020) is disclosed in Notes 30–32.

### **25.1.3 Liquidity risk**

Liquidity risk is associated with a failure to dispose of investments in a short time and at a competitive market price. Since Latvia joined the euro area, the need for liquidity and the risk associated with a failure to meet liabilities in a timely manner have considerably decreased. In compliance with its investment strategy, Latvijas Banka manages liquidity risk by investing a certain amount of its investments in liquid debt securities issued by international institutions, foreign governments and the corporate sector, in short-term deposits with foreign financial institutions and in other financial instruments. The liquidity structure of Latvijas Banka's assets and liabilities as at the end of 2021 and 2020 is disclosed in Note 29.

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

### **25.2 Operational risks**

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

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

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

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

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

Risks related to physical security, inter alia, risks associated with fire safety and civil protection are managed to mitigate a potential negative impact on the physical security of persons, the premises of Latvijas Banka, the transportation of its valuables and 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 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.

Within the framework of operational risk mitigation measures, Latvijas Banka is insured against potential impact of certain types of operational risks.

In 2021, the main focus of operational risk management was on managing risks related to the COVID-19 pandemic, remote working, changes in the physical security framework, as well as the risks associated with the merger with the FCMC as of 1 January 2023. Operational risks were appropriately managed in 2021, and the risk mitigation measures limit those risks to acceptable levels.

## 26. CURRENCY STRUCTURE

	(in thousands of euro)						
	EUR	USD	CAD	GBP	Gold	Other	Total
<b>As at 31 December 2021</b>							
Total assets	19 865 163	3 795 589	359 253	439 453	344 166	270 805	25 074 429
Total liabilities	22 989 156	1 487 248	302 731	207 936	–	87 358	25 074 429
Net position on balance sheet	–3 123 993	2 308 341	56 522	231 517	344 166	183 447	–
Net position on financial instruments' off-balance sheet accounts	2 018 068	–1 759 042	–29 245	–199 913	–	–34 922	–5 054
<b>Net position on balance sheet and off-balance sheet accounts</b>	<b>–1 105 925</b>	<b>549 299</b>	<b>27 277</b>	<b>31 604</b>	<b>344 166</b>	<b>148 525</b>	<b>–5 054</b>
<b>Net position on balance sheet and off-balance sheet accounts to total assets (%)</b>	<b>–4.4</b>	<b>2.2</b>	<b>0.1</b>	<b>0.1</b>	<b>1.4</b>	<b>0.6</b>	<b>0</b>
<b>As at 31 December 2020</b>							
Total assets	18 443 448	3 400 387	367 842	348 093	330 139	155 833	23 045 742
Total liabilities	21 108 390	1 445 139	337 486	127 662	–	27 065	23 045 742
Net position on balance sheet	–2 664 942	1 955 248	30 356	220 431	330 139	128 768	–
Net position on financial instruments' off-balance sheet accounts	1 842 451	–1 575 561	–10 287	–195 983	–	–33 930	26 690
<b>Net position on balance sheet and off-balance sheet accounts</b>	<b>–822 491</b>	<b>379 687</b>	<b>20 069</b>	<b>24 448</b>	<b>330 139</b>	<b>94 838</b>	<b>26 690</b>
<b>Net position on balance sheet and off-balance sheet accounts to total assets (%)</b>	<b>–3.5</b>	<b>1.6</b>	<b>0.1</b>	<b>0.1</b>	<b>1.4</b>	<b>0.4</b>	<b>0.1</b>

## 27. REPRICING MATURITY

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

	(in thousands of euro)						
	Up to 3 months	3–12 months	1–3 years	3–5 years	Over 5 years	Non-interest bearing items	Total
<b>As at 31 December 2021</b>							
Gold and gold receivables	–	–	–	–	–	344 166	344 166
Claims on non-euro area residents denominated in foreign currency	14 124	272 185	99 584	462 493	2 327 595	1 319 200	4 495 181
Claims on euro area residents denominated in foreign currency	–	–	17 775	87 739	83 817	339 097	528 428
Claims on non-euro area residents denominated in euro	1 230	–	–	1 623	164 471	6 757	174 081
Lending to euro area credit institutions related to monetary policy operations denominated in euro	–	–	616 600	–	–	–	616 600
Other claims on euro area credit institutions denominated in euro	4 138	–	–	–	–	117	4 255
Securities of euro area residents denominated in euro	–	–	261 894	180 054	12 398 048	–	12 839 996
Intra-Eurosystem claims	5 750 951	–	–	–	–	117 057	5 868 008
Other assets	5	34	426	2 650	82 203	118 396	203 714
<b>Total assets</b>	<b>5 770 448</b>	<b>272 219</b>	<b>996 279</b>	<b>734 559</b>	<b>15 056 134</b>	<b>2 244 790</b>	<b>25 074 429</b>
Banknotes in circulation	–	–	–	–	–	5 536 624	5 536 624
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	6 406 673	–	–	–	–	–	6 406 673
Other liabilities to euro area credit institutions denominated in euro	649 746	–	–	–	–	–	649 746
Liabilities to other euro area residents denominated in euro	3 438 792	–	–	–	–	–	3 438 792
Liabilities to non-euro area residents denominated in euro	56 519	–	–	–	–	1 436	57 955
Liabilities to euro area residents denominated in foreign currency	1 594 262	–	–	–	–	–	1 594 262
Liabilities to non-euro area residents denominated in foreign currency	688 359	–	–	–	–	–	688 359
Intra-Eurosystem liabilities	5 322 638	–	–	–	–	34 342	5 356 980
Other liabilities	24 198	–	–	–	–	412 185	436 383
Capital and reserves	–	–	–	–	–	908 655	908 655
<b>Total liabilities</b>	<b>18 181 187</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>–</b>	<b>6 893 242</b>	<b>25 074 429</b>
Net position on balance sheet	–12 410 739	272 219	996 279	734 559	15 056 134	–4 648 452	–
Assets on financial instruments' off-balance sheet accounts	4 423 728	33 551	180 823	42 681	886 285	–	5 567 068
Liabilities on financial instruments' off-balance sheet accounts	4 031 948	–	146 151	133 672	1 260 351	–	5 572 122
<b>Net position on balance sheet and off-balance sheet accounts</b>	<b>–12 018 959</b>	<b>305 770</b>	<b>1 030 951</b>	<b>643 568</b>	<b>14 682 068</b>	<b>–4 648 452</b>	<b>–5 054</b>

*(continued)*

(in thousands of euro)

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

## 28. TRACKING ERROR

The exposure to aggregate market risk and credit risk of investments, included in the 1–10 year government fixed income securities portfolios, mortgage-backed securities portfolios and the 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 2021 and 2020, the actual (ex-post) tracking error was as follows:

	(basis points)	
	2021	2020
1–10 year fixed income securities portfolios	34	89
Mortgage-backed securities portfolios	102	159
Developed markets equity securities portfolio	14	17

The expected (ex-ante) tracking error of the developed markets equity securities portfolio does not exceed 30 basis points during the year and the compliance with this limit is monitored by the respective external manager. The expected (ex-ante) tracking error in the 1–10 year government fixed income securities portfolios and mortgage-backed securities portfolios lay within the following basis point intervals during the year:

	Book value (at the end of the year; in thousands of euro)	Expected tracking error (number of business days)				
		10–39	40–69	70–99	100–139	140–179
<b>During 2021</b>						
1–10 year fixed income securities portfolios	3 209 547	107	145	–	–	–
Mortgage-backed securities portfolios	1 186 537	–	143	106	3	–
<b>During 2020</b>						
1–10 year fixed income securities portfolios	3 445 980	51	106	45	23	26
Mortgage-backed securities portfolios	1 211 775	49	8	146	48	–



## 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	<b>Total</b>
<b>As at 31 December 2021</b>				
<b>Assets</b>				
Gold and gold receivables	344 166	–	–	<b>344 166</b>
Claims on non-euro area residents denominated in foreign currency	4 495 181	–	–	<b>4 495 181</b>
Claims on euro area residents denominated in foreign currency	528 428	–	–	<b>528 428</b>
Claims on non-euro area residents denominated in euro	174 081	–	–	<b>174 081</b>
Lending to euro area credit institutions related to monetary policy operations denominated in euro	–	616 600	–	<b>616 600</b>
Other claims on euro area credit institutions denominated in euro	4 255	–	–	<b>4 255</b>
Securities of euro area residents denominated in euro	12 671 750	168 246	–	<b>12 839 996</b>
Intra-Eurosystem claims	769	–	5 867 239	<b>5 868 008</b>
Other assets	131 911	–	71 803	<b>203 714</b>
<b>Total assets</b>	<b>18 350 541</b>	<b>784 846</b>	<b>5 939 042</b>	<b>25 074 429</b>
<b>Liabilities</b>				
Banknotes in circulation	–	–	5 536 624	<b>5 536 624</b>
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	6 406 673	–	–	<b>6 406 673</b>
Other liabilities to euro area credit institutions denominated in euro	649 746	–	–	<b>649 746</b>
Liabilities to other euro area residents denominated in euro	3 438 792	–	–	<b>3 438 792</b>
Liabilities to non-euro area residents denominated in euro	57 955	–	–	<b>57 955</b>
Liabilities to euro area residents denominated in foreign currency	1 594 262	–	–	<b>1 594 262</b>
Liabilities to non-euro area residents denominated in foreign currency	688 359	–	–	<b>688 359</b>
Intra-Eurosystem liabilities	5 356 980	–	–	<b>5 356 980</b>
Other liabilities	328 191	–	108 192	<b>436 383</b>
<b>Total liabilities</b>	<b>18 520 958</b>	<b>–</b>	<b>5 644 816</b>	<b>24 165 774</b>
<b>Net position</b>	<b>–170 417</b>	<b>784 846</b>	<b>294 226</b>	<b>x</b>

*(continued)*

(in thousands of euro)

	Up to 3 months	Over 3 months	No fixed maturity	Total
As at 31 December 2020				
<b>Assets</b>				
Gold and gold receivables	330 139	–	–	330 139
Claims on non-euro area residents denominated in foreign currency	3 970 780	–	–	3 970 780
Claims on euro area residents denominated in foreign currency	333 706	–	–	333 706
Claims on non-euro area residents denominated in euro	119 143	–	–	119 143
Lending to euro area credit institutions related to monetary policy operations denominated in euro	–	1 260 000	–	1 260 000
Other claims on euro area credit institutions denominated in euro	120	–	–	120
Securities of euro area residents denominated in euro	10 961 267	168 173	–	11 129 440
Intra-Eurosystem claims	4 910	–	5 669 064	5 673 974
Other assets	155 126	–	73 314	228 440
<b>Total assets</b>	<b>15 875 191</b>	<b>1 428 173</b>	<b>5 742 378</b>	<b>23 045 742</b>
<b>Liabilities</b>				
Banknotes in circulation	–	–	5 142 726	5 142 726
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	6 053 812	–	–	6 053 812
Other liabilities to euro area credit institutions denominated in euro	577 746	–	–	577 746
Liabilities to other euro area residents denominated in euro	3 012 014	–	–	3 012 014
Liabilities to non-euro area residents denominated in euro	238 737	–	–	238 737
Liabilities to euro area residents denominated in foreign currency	615 986	–	–	615 986
Liabilities to non-euro area residents denominated in foreign currency	1 364 010	–	–	1 364 010
Intra-Eurosystem liabilities	4 837 613	–	–	4 837 613
Other liabilities	304 655	–	105 045	409 700
<b>Total liabilities</b>	<b>17 004 573</b>	<b>–</b>	<b>5 247 771</b>	<b>22 252 344</b>
<b>Net position</b>	<b>–1 129 382</b>	<b>1 428 173</b>	<b>494 607</b>	<b>x</b>

### 30. SECTORAL STRUCTURE OF ASSETS

	Amount (in thousands of euro)		Proportion (%)	
	2021	2020	2021	2020
Investment operations	<b>6 717 638</b>	5 927 237	<b>26.8</b>	25.7
Central governments and other governmental institutions	2 533 137	2 726 649	10.2	11.7
Other financial institutions	1 861 846	1 474 111	7.4	6.4
Central banks and credit institutions	680 415	710 982	2.7	3.1
Non-financial corporations	695 528	519 143	2.8	2.3
International institutions	713 453	275 804	2.8	1.2
Local governments	233 067	219 950	0.9	1.0
Unclassified assets	192	598	0	0
Monetary policy operations	<b>12 378 324</b>	11 342 251	<b>49.4</b>	49.2
International institutions	8 191 153	7 461 626	32.7	32.4
Central governments and other governmental institutions	3 570 571	2 620 625	14.2	11.3
Credit institutions	616 600	1 260 000	2.5	5.5
Other operations	<b>5 978 467</b>	5 776 254	<b>23.8</b>	25.1
Intra-Eurosystem claims	5 868 008	5 673 974	23.4	24.6
International institutions	74 331	62 266	0.3	0.3
Unclassified assets	36 128	40 014	0.1	0.2
<b>Total</b>	<b>25 074 429</b>	23 045 742	<b>100.0</b>	100.0

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

	Amount (in thousands of euro)		Proportion (%)	
	2021	2020	2021	2020
Investment operations	<b>6 717 638</b>	5 927 237	<b>26.8</b>	25.7
US	2 381 318	2 293 603	9.5	9.9
Euro area countries	1 688 507	1 441 336	6.7	6.2
UK	780 426	707 186	3.1	3.1
Canada	691 395	669 855	2.8	2.9
International institutions	713 453	275 804	2.8	1.2
Other EU countries	68 137	165 045	0.3	0.7
Japan	141 048	152 276	0.6	0.7
Other countries	253 354	222 132	1.0	1.0
Monetary policy operations	<b>12 378 324</b>	11 342 251	<b>49.4</b>	49.2
International institutions	8 191 153	7 461 626	32.7	32.4
Euro area countries	4 187 171	3 880 625	16.7	16.8
Other operations	<b>5 978 467</b>	5 776 254	<b>23.8</b>	25.1
Intra-Eurosystem claims	5 868 008	5 673 974	23.4	24.6
International institutions	74 331	62 266	0.3	0.3
Unclassified assets	36 128	40 014	0.1	0.2
<b>Total</b>	<b>25 074 429</b>	23 045 742	<b>100.0</b>	100.0

### 32. ASSETS BY CREDIT RATING ASSIGNED TO THE COUNTERPARTY

	Amount (in thousands of euro)		Proportion (%)	
	2021	2020	2021	2020
Investment operations	<b>6 717 638</b>	5 927 237	<b>26.8</b>	25.7
AAA	3 592 177	3 203 434	14.4	13.8
AA	1 137 779	1 288 025	4.5	5.6
A	422 964	495 629	1.7	2.2
BBB	668 350	367 665	2.7	1.6
Assets without counterparty credit rating	10 587	1 944	0	0
Assets not exposed to credit risk	885 781	570 540	3.5	2.5
Monetary policy operations	<b>12 378 324</b>	11 342 251	<b>49.4</b>	49.2
AAA	6 024 560	5 983 541	24.1	25.9
AA	2 166 593	1 478 085	8.6	6.4
A	3 570 571	2 620 625	14.2	11.4
Assets without counterparty credit rating	616 600	1 260 000	2.5	5.5
Other operations	<b>5 978 467</b>	5 776 254	<b>23.8</b>	25.1
Intra-Eurosystem claims	5 868 008	5 673 974	23.4	24.6
Unclassified assets	77 595	66 530	0.3	0.3
Assets not exposed to credit risk	32 864	35 750	0.1	0.2
<b>Total</b>	<b>25 074 429</b>	23 045 742	<b>100.0</b>	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.

## PROFIT AND LOSS STATEMENT NOTES

### 33. NET INTEREST INCOME

	(in thousands of euro)	
	2021	2020
Interest income	<b>165 248</b>	190 313
Interest on investments	78 780	105 848
Interest on customer deposits	15 481	16 662
Interest on monetary policy operations	70 987	67 803
Interest expense	<b>-41 267</b>	-50 776
Interest on investments	-21 082	-40 021
Interest on monetary policy operations	-20 185	-10 755
Net interest income	<b>123 981</b>	139 537

Net interest income was mainly derived from debt securities investments in debt securities as well as from interest income on monetary policy operations. In 2021, net interest income decreased by 15 556 thousand euro compared to 2020.

In 2021, interest income on investment declined on account of lower average yields on securities and a reduction of the 1–10 year fixed income securities portfolio. A decrease in interest expense on investment resulted from lower costs of hedging currency risk, as the average money market interest rates in the US dollar, Canadian dollar and British pound sterling were considerably higher in 2021 than in 2020, while the average euro money market rate in 2021 was only slightly higher than in 2020.

In 2021, interest income on deposits received was mostly shaped by negative interest on deposits from the government and other financial institutions. The application of interest on deposits is stipulated in Guideline (EU) 2019/671 of the ECB of 9 April 2019 on domestic asset and liability management operations by the national central banks (recast) (ECB/2019/7). Pursuant to this Guideline, Latvijas Banka applies the euro overnight index average (EONIA) rate (it was negative at the end of both 2021 and 2020 (-0.505% and -0.498% respectively)) to the amount of the Treasury's deposits in euro up to 200 million euro. As regards the total outstanding amount of the Treasury's settlement accounts in euro and foreign currencies exceeding 200 million euro, until 30 September 2019, Latvijas Banka applied the deposit facility rate set by the ECB, whereas from 1 October 2019 – the lower of the following rates: the ECB's deposit facility rate or the euro overnight index average (EONIA) rate (the ECB's deposit facility rate was negative at the end of both 2021 and 2020 at -0.50%).

In 2021, interest income on monetary policy operations grew as a result of increasing the PSPP and PEPP. A rise in interest expense on monetary policy operations in 2020 mostly resulted from granting TLTRO III and higher negative interest under the PSPP and PEPP. Interest income from and interest expense on the intra-Eurosystem claims and liabilities are remunerated by applying the ECB's interest rate on the main refinancing operations and include income from foreign reserves transferred to the ECB and claims on allocation of banknotes in the Eurosystem, as well as expense on liabilities related to TARGET2 settlements. The interest rate on the main refinancing operations set by the ECB was 0% in 2021 and 2020; therefore, Latvijas Banka had neither such interest income nor interest expense.

### 34. REALISED GAINS/LOSSES ARISING FROM FINANCIAL OPERATIONS

	(in thousands of euro)	
	2021	2020
Foreign exchange transactions	10 063	827
Derivative financial instruments	-7 503	11 392
Debt securities	-2 203	32 252
Total	357	44 471

In 2021, the realised gains on foreign exchange transactions were 9236 thousand euro larger than in 2020 and that was positively affected by the appreciation of the US dollar against the euro.

The result on derivative financial instruments showed an improvement of 18 895 thousand euro compared to 2020, mostly on account of the negative result on interest rate future contracts due to rising interest rates in the course of 2021, and on account of the negative result on currency future contracts concluded for the purpose of hedging currency risk exposure, affected by the US dollar appreciation against the euro. The negative result of the currency future contracts concluded for the purpose of hedging currency risk exposure is offset in an equal value by the positive revaluation result of the balance sheet items hedged for foreign currency risk.

The result on the disposal of debt securities decreased by 34 455 thousand euro compared to 2020, mostly due to a decrease in the market value of the securities on account of rising yields.

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

	(in thousands of euro)	
	2021	2020
Securities	-35 662	-6 299
Foreign currency positions	-935	-28 642
Interest rate swap arrangements	-21	-296
Total	-36 618	-35 237

The revaluation result of several debt securities, foreign currency positions, and interest rate swap arrangements at the end of 2021 and 2020 was negative and has been recognised in the profit and loss statement. The positive result on the revaluation of debt securities, equity securities, foreign currency positions, and interest rate swap arrangements has been reported under the balance sheet item "Capital and reserves" as the revaluation reserve of securities, foreign currency, and interest rate swap arrangements respectively (see also Note 23).

The increase in the negative result on debt securities revaluation is related to a rise in market yields.

The decrease in the negative result on the revaluation of foreign currencies is related to appreciation of the US dollar against the euro.

### 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, Latvijas Banka's Council takes decisions on making provisions for market risk (price, interest rate and currency risks) and credit risk associated with Latvijas Banka's investment management and other financial transactions 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 2021, the level of financial risks has been estimated at 1048.4 million euro (771.9 million euro in 2020). In 2021, the level of financial risks rose mainly on account of changes in the placement of investments, i.e. the creation of an emerging markets fixed income securities portfolio and an emerging markets equity securities portfolio along with an increase in the developed markets equity securities portfolio.

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)	
	<b>2021</b>	2020
Level of financial risks	<b>1 048 400</b>	771 900
Provisions for the market risk and credit risk	<b>295 697</b>	281 723
Provisions for the market risk and credit risk against the level of financial risks (%)	<b>28</b>	36

In 2021, due to the above-mentioned risk assessment, the Council of Latvijas Banka decided to increase the provisions for market risk and credit risk related to the financial investments managed by Latvijas Banka by 13 974 thousand euro according to a percentage of the positive total financial performance result included in the profit and loss statement before establishing provisions for financial risks as laid down in the above-mentioned methodology (in 2020, the respective provisions were increased by 78 181 thousand euro). Latvijas Banka had no provisions for credit risk associated with the Eurosystem monetary policy operations at the end of 2021 and at the end of 2020.

### **37. INCOME FROM EQUITY SECURITIES AND PARTICIPATING INTEREST**

Income from equity securities comprises dividends of the equity securities portfolio in the amount of 11 828 thousand euro (8989 thousand euro in 2020). Income grew on account of higher dividends due to an increase in the developed markets equity securities portfolio.

Income from participating interest comprises dividends received from the participating interest in the BIS (670 in 2021, dividends from the participating interest in the BIS were not paid out in 2020; see also Note 14.2) and income from the ECB's interim profit distribution for the reporting year, the remainder of the ECB's annual profit for the previous year in the amount of 2077 thousand euro (9616 thousand euro in 2020).

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**

	(in thousands of euro)	
	<b>2021</b>	2020
Monetary income pooled	<b>-39 502</b>	-44 679
Monetary income received	<b>5 160</b>	16 978
Net result of pooling of monetary income	<b>-34 342</b>	-27 701

Pursuant to the Statute of the ESCB and of the ECB, euro area NCBs gain income from the implementation of the single monetary policy of the Eurosystem. Total monetary income of the Eurosystem equals the income on



assets arising from the issue of euro banknotes and receiving deposits from credit institutions. The income is allocated to euro area NCBs in proportion to their shares in the capital of the ECB.

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. Net result of pooling of monetary income decreased on account of smaller monetary income received, primarily due to the decisions of the Governing Council of the ECB on applying more favourable conditions to TLTRO III.

### 39. OTHER OPERATING INCOME

	(in thousands of euro)	
	2021	2020
Revaluation of liabilities for the issued lats banknotes and coins	2 380	–
Income from sale of numismatic products	627	613
Other	584	655
<b>Total</b>	<b>3 591</b>	<b>1 268</b>

Revaluation of liabilities for the issued lats banknotes and coins resulted in income, as 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 2021, 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).

### 40. REMUNERATION, SOCIAL SECURITY COSTS, AND SOLIDARITY TAX

	(in thousands of euro)	
	2021	2020
Remuneration		
Remuneration for performance of duties of the Council and the Board	–728	–855
Remuneration of other personnel	–15 675	–16 012
<b>Total remuneration</b>	<b>–16 403</b>	<b>–16 867</b>
Social security costs and solidarity tax	–3 582	–3 764
<b>Total remuneration, social security costs, and solidarity tax</b>	<b>–19 985</b>	<b>–20 631</b>

At the end of 2021, the number of employees was 380 (421 at the end of 2020), representing 400 full-time equivalents at the end of 2021 (425 at the end of 2020). The decrease in the number of employees is mostly related to the implementation of cost efficiency improvement measures.

Latvijas Banka introduced a single-tier top management model as of 1 June 2021, and the Board of Latvijas Banka discontinued its operation.

#### 41. BANKNOTE AND COIN ACQUISITION COSTS

	(in thousands of euro)	
	2021	2020
Acquisition of banknotes	-1 363	-1 229
Acquisition of collector coins	-380	-188
Acquisition of circulation coins	-88	-129
Total	-1 831	-1 546

#### 42. OTHER OPERATING EXPENSES

	(in thousands of euro)	
	2021	2020
Maintenance and operation of information systems	-4 116	-4 023
Municipal services	-771	-547
Acquisition of low value office supplies	-360	-94
Maintenance of buildings, territory and equipment	-335	-436
Information and public relations	-289	-231
Tax on real estate	-217	-220
Telecommunication services and system maintenance	-190	-168
Risk insurance	-134	-254
Personnel training	-126	-85
Disposal of material values	-33	-30
Business travel	-26	-66
Transport provision	-12	-30
Event services	-10	-32
Other	-474	-478
Total	-7 093	-6 694

Other operating expenses also comprise remuneration in the amount of 33 thousand euro paid to SIA ERNST & YOUNG BALTIC for the audit of 2021 financial statements of Latvijas Banka (33 thousand euro in 2020 ).

#### OTHER NOTES

##### 43. PLEDGED ASSETS

Debt securities, other financial instruments and gold purchased by Latvijas Banka with the total market value of 2 503 139 thousand euro as at the end of 2021 (2 667 712 thousand euro at the end of 2020) have been pledged to provide repurchase agreement deals, collateral for gold swap arrangements, forward exchange rate contracts, interest rate and currency future contracts, and to ensure the operation of payment systems. At the end of 2021, the pledged assets mostly consisted of securities pledged under repurchase agreements in the amount of 2 135 996 thousand euro (2 309 742 thousand euro at the end of 2020).

##### 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.

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

At the end of 2021, the fair value of the securities lent, determined using quoted prices in an active market, was 27 418 thousand euro (439 thousand euro at the end of 2020); inter alia, the fair value of securities purchased and lent under the PSPP and PEPP stood at 22 650 thousand euro at the end of 2021 (285 thousand euro at the end of 2020).

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 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 make payments into the ECB's reserve capital, provisions equivalent to reserves and the valuation account for financial instruments, in proportion to its share in the ECB's capital. Following the Bank of England's withdrawal from the ESCB, the total amount of the ECB's capital to be paid up increased. The ECB's Governing Council decided that euro area NCBs would pay up in full their increased subscriptions in two instalments: at the end of 2021 and 2022 respectively. In 2022, Latvijas Banka has to make a payment in the amount of 2377 thousand euro (see also Note 13.1).

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 2021, the uncalled portion of the BIS shareholding was 4012 thousand SDR (4958 thousand euro; 4012 thousand SDR (4729 thousand euro) at the end of 2020; see also Note 14.2).

At the end of 2021, Latvijas Banka had issued euro collector coins, lats collector coins and precious metal circulation coins in the nominal value of 7096 thousand euro (7034 thousand euro at the end of 2020). 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.

At the end of 2021, Latvijas Banka had issued lats banknotes and coins with the face value of 119 875 thousand euro (120 934 thousand euro at the end of 2020), reported on the balance sheet in the amount of 21 895 thousand euro (25 334 thousand euro at the end of 2020). Pursuant to the Law on the Procedure for Introducing the Euro, the period for exchanging the lats cash to the euro at Latvijas Banka is unlimited. In the opinion of Latvijas Banka's management, the probability that Latvijas Banka would be required to exchange lats banknotes and coins in the amount of 97 980 thousand euro (95 600 thousand euro at the end of 2020) at face value is low.

The new Law on Latvijas Banka which was adopted on 23 September 2021 and is coming to effect on 1 January 2023 provides for a merger of the FCMC with Latvijas Banka, including the take-over of the FCMC's rights and liabilities.

#### **46. EVENTS AFTER THE REPORTING YEAR**

Geopolitical crisis caused by the war against Ukraine started by Russia in February 2022 has increased the degree of uncertainty and caused significant volatility in the global financial markets, which will continue to affect the financial performance of Latvijas Banka due to its exposure to the interest rate risk and other financial risks. Nevertheless, it has no significant effect on the financial position and the financial performance of Latvijas Banka in 2021.

There have been no other 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.