

THE GOVERNOR'S MESSAGE



2011 was the year of the sovereign debt crisis in the euro area, marked by a reemergence of jittery markets over the summer, that spilled over to the real economy.

After the economic uptick of the first semester, most growth forecasts for the euro area member countries were revised downwards. The Luxembourg economy, which only grew by about 1% in 2011, was no exception.

Since the beginning of 2012, signs have been pointing to economic stabilization and a slow and gradual restoration of market confidence. The measures taken by the authorities at the euro area and domestic levels are starting to bear fruit even though much more needs to be done. In terms of economic governance, twenty-five European countries signed a new fiscal treaty, labeled "Fiscal Compact", on 2 March 2012.

Despite these measures, tensions remain on the sovereign debt markets; the economy and its financing remain affected. Generally, subdued global demand and measures aiming at restoring fiscal balances and competitiveness explain why the growth forecast for the euro area for 2012 remains slightly negative.

Confronted with the crisis, the Eurosystem has strengthened its non-conventional measures.

At the domestic level, in light of its financial stability and liquidity supervision functions, the BCL further developed macro-prudential indicators and carried on research in this area.

The BCL also strengthened its oversight over financial market infrastructures. It participated in the inception of the new central securities depository in Luxembourg, LuxCSD, which will allow market participants to benefit from settling their securities transactions in central bank money, thereby mitigating the risks of settling these transactions with commercial banks. LuxCSD is poised to join TARGET2-Securities, a clearing and settlement platform and landmark project of the Eurosystem that is due to start operations in 2015.

The "BCL Foundation", created in March 2011 and aiming at promoting education and research in activities that pertain to the BCL, chose research on financial stability issues as a priority topic for the period 2011-2012.

At the European level, the BCL participates in the new European System of Financial Supervisors (ESFS). The Governor of the BCL is a voting member of the European Systemic Risk Board (ESRB), which is responsible for macro-prudential surveillance of the financial system in the European Union. Since its first meeting in January 2011, the ESRB has issued three public recommendations, among which the recommendation of 22 December 2011 that provides for European Union Member States to select a domestic institution to be in charge of macro-prudential policies and for the domestic central bank to play a significant role in that policy without putting its independence into jeopardy.

Besides, in line with an agreement signed in 2011, the BCL provided operational assistance to the European Financial Stability Facility (EFSF) following its establishment in Luxembourg.

The BCL became a shareholder of the Bank for International Settlements (BIS), where it participates in different committees and working groups.

The Governor of the BCL was elected as a Co-Chair of the Regional Consultative Group for Europe, which was set up by the Financial Stability Board (FSB). The BCL hosted the inaugural meeting in Luxembourg in December 2011.

The BCL contributes to international institutions that aim at overseeing and supporting the development of Islamic finance.

The year 2012 comes with new challenges for the euro area and the Eurosystem, as well as for Luxembourg and its central bank.

At the European level, the measures adopted to improve economic governance, especially within the euro area, must be implemented without delay. Priority should be given to coordinating economic and fiscal policies of Member States effectively through the European Semester, ensuring the prevention and correction of excessive deficits and monitoring excessive macroeconomic imbalances, in line with the provisions included in the "six-pack". There is also a need to adopt harmonized constraining fiscal rules in accordance with the aforementioned Fiscal Compact.

The strengthening of the resources of the EFSF and the early entry into force of its successor, the European Stability Mechanism (ESM), on 1 July 2012 are welcome.

As regards the Eurosystem, the priority is to phase out gradually the non-conventional measures adopted during the crisis, which are by definition temporary, in order to return to a conventional monetary policy regime. The challenge is to restore confidence on the financial markets and to ensure an optimal transmission of the monetary policy and the financing of the economy.

In Luxembourg, as in other countries, we have to ensure the sustainability of public finances, while restoring competitiveness to boost potential growth that is instrumental in fostering the sustainable development of our country. Substantial structural reforms must be implemented to ensure the future of Luxembourg's economy. These reforms relate, among others, to the financing of the pension system as well as to the labour market, the educational system, the promotion of research and development as well as infrastructure development.

The BCL is determined to pursue its efforts. The Luxembourg central bank supports legislative progress achieved in Luxembourg in the field of new constitutional and legal rules, notably in the fiscal area but also in the setup of resolution mechanisms for financial institutions, which should be funded in order to protect public finances. A change in the organic law of the BCL is vital, in line with the proposals submitted two years ago, to allow the BCL to fulfill its tasks adequately.

The BCL takes particular care in informing the public about its activities. The Annual Report, which the law requires the BCL to present, after approval by its Council, follows a new format. The French version of the 2011 Annual Report was published three months earlier in comparison with the previous editions. The first part of this Report presents the Bank's most important activities. Its second part expounds the BCL's organisational developments and presents its financial accounts. As for the detailed presentation of the economic and financial situation, which was included in the previous Reports, it will henceforth be available in the Bank's other publications, in particular in its regular Bulletins and its Financial Stability Review.

Last, but not least, I would like to express my deep gratitude toward those who, over the years, in the various bodies, services and departments of the Bank, have assisted me, supported me and advised me in my constant efforts to fulfill the legal missions of the BCL and by applying the values expressed in the Bank's Mission Statement.

I share with them the pride to belong to an institution which is solidly anchored at the national, European and international levels.



Yves Mersch