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BANQUE CENTRALE DU LUXEMBOURG
EUROSYSTEM

MISSION STATEMENT OF THE BCL

The Central Bank of Luxembourg (BCL), member of the European System of Central Banks (ESCB), is a public institution created by Luxembourg law. The BCL's independence is based on its organic law and the European Union Treaties.

THE MISSION

The BCL is in charge of managing all the monetary and financial responsibilities granted to it as one of the National Central Banks of the ESCB.

It is also a member of the Eurosystem that gathers the European Central Bank and the National Central Banks that have adopted the euro.

On a national level, the Bank has to carry out the tasks imposed on it by the national laws and conventions.

It is developing the following fields of competence:

- Research and studies and their communication thereof, which aim to prepare, on the one hand, monetary policy decisions and, on the other hand, the development of wider knowledge concerning monetary, financial and economic issues;
- Collection and analysis of statistics in the monetary, financial and balance of payments fields;
- Implementation of monetary policy instruments;
- Organisation and supervision of payment and securities settlement systems;
- Issuance and circulation of banknotes and coins;
- Financial asset management, both on own account and for third parties;
- Participation in the prudential supervision of the financial system and the exercise of the oversight of payment and securities settlement systems, in order to ensure the stability of the financial system in Luxembourg;
- Advisory services to legislative and regulatory authorities in financial and monetary areas.

THE VISION

The BCL intends to become a centre of competence, excellence even, whose performance will generate public confidence in the Central Bank.

Among Luxembourg institutions, the BCL takes every care that it is capable of fulfilling all its national, European and international obligations.

In view of the wide variety of its duties and activities, both in the public sector and in a competitive environment, the BCL must generate an income guaranteeing its institutional, functional and financial independence.

CORPORATE VALUES

Consequently, the values associated with its action are:

- Professionalism, guaranteed by highly specialised employees, high-performance tools and a high-level infrastructure;
- Quality in all its services;
- Stability provided by its long term vision of all its activities;
- Objectivity resulting from the establishment of precise rules that are equally applied;
- Integrity, guaranteed by the transparency of its internal operations and with respect to professional ethics.

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THE GOVERNOR'S MESSAGE[1]

1 Finalised on 30 April 2013.

In 2012, the euro area has continued to be marked by the crisis and the measures aimed at trying to ward it off.

The Governing Council of the European Central Bank (ECB) has acted in a determined way. The lowering of the interest rate of the main refinancing operations to 0.75%, against the backdrop of receding inflation expectations, was followed by the announcement of the introduction of the Outright Monetary Transactions (OMTs) in September. This new non-standard measure aims at restoring the transmission mechanism of monetary policy within the euro area. It allows the Eurosystem to intervene, without limits, in the secondary market for sovereign debt, with a maturity below or equal to three years, in countries which have an adjustment programme with the European Stability Mechanism (ESM). The programmes of the ESM, the successor to the European Financial Stability Facility (EFSF), are designed and monitored with the assistance of the IMF. As with the Securities Markets Programme (SMP), which was terminated with the introduction of the OMTs, additional liquidity funnelled to the markets through OMTs would be sterilised.

In order to continue supplying the euro area money market with liquidity, the Eurosystem completed a second longer term refinancing operation with a maturity of 36 months in February 2012; a first such operation had been completed in December 2011. These two liquidity-providing operations have been very successful, channelling more than € 1000 billion to banks within the euro area. By the same token, the Eurosystem maintained a fixed rate full allotment policy during the whole year of 2012. In order to ensure access to liquidity in foreign currencies, the ECB also extended swap agreements with certain foreign central banks, notably the American Federal Reserve System for liquidity in US dollars. Besides, the Eurosystem adjusted the rules pertaining to collateral which, in conformity with the Treaty, counterparts of the Eurosystem have to deposit in order to obtain the liquidity they need.

The year 2012 has seen important reforms of the European Union's economic and financial governance, especially in the euro area.

Article 136 of the Treaty on the Functioning of the European Union (TFEU) was modified to ensure the operation of the new ESM, of which the Incorporation Treaty became effective in September 2012. Also, the Treaty on Stability, Coordination and Governance in the Economic and Monetary Union (TSCG), also referred to as Fiscal Treaty, was signed on 2 March 2012 and became effective on 1 January 2013; Luxembourg ratified the Treaty only on 27 February 2013. This treaty aims at strengthening fiscal discipline in EU Member States with the introduction of constraining fiscal rules containing an automatic correction mechanism through the inception, in every Member State that is a signatory, of a national institution tasked with monitoring the compliance with such rules and through enhanced monitoring of economic policies. In 2013, based on proposals made by the European Commission, dubbed 'Two Pack', legal acts will complement the fiscal rules already strengthened by the 'Six Pack'.

In addition, the European Council decided, in its meeting of 28 and 29 June 2012, on the creation of a Single Supervisory Mechanism (SSM) for the banks established within the euro area, aiming at consolidating the supervision of those banks under the aegis of the ECB. This mechanism, which is expected to be created in 2013, is destined to be complemented by a single resolution mechanism and a single deposit insurance scheme. Beyond strengthening financial stability, this new structure should also break the vicious feedback loop between banking crises and national public finances. This mechanism will be open to Member States that are outside the euro area. The implementation of new rules on surveillance will inevitably entail a strengthened cooperation between the BCL and the *Commission de Surveillance du Secteur Financier* (CSSF).

While financial markets have stabilised, notably due to the announcement of the introduction of OMTs, the effects of the crisis continue to weigh on the real economy. At the level of the euro area, real GDP contracted by 0.5% in 2012; signs of recovery remain timid. Inflation slightly receded and the unemployment rate exceeded 11.5% at the end of 2012. Although Luxembourg's real GDP did not contract, economic growth has slowed down markedly. According to the national accounts published in early April 2013, real GDP grew by only 0.3% in 2012, well below the growth rate reached in 2011 (1.7%). The domestic inflation rate, measured by the National Index of Consumer Prices (IPCN), reached an annual average of 2.7%, which lies above the Harmonised Index of Consumer Prices (HIPC) for the whole euro area (average inflation rate of 2.5% in 2012). The deficit of the central administration, with 2.6 percent of GDP according to the latest stability programme and revised compared to previous figures, has reached a worrisome level. While the fiscal deficit as defined in the Maastricht Treaty, which includes the central administration but also local administrations and social security, seems to have remained below the 3% mark, it remains, *ceteris paribus*, alarming over the medium to long haul, as this result is due the accumulation of large surpluses by the pension system.

In Luxembourg, as in other Member States of the euro area, priority should be given to the implementation of structural reforms laying the ground for a competitive and productive economy as well as sustainable public finances over the medium term. The ongoing fiscal, financial and economic reforms in the European Union should be implemented in a steadfast way at the national level. In the context of the Fiscal Treaty, it is important to point out the necessity to set up, at the national level, an independent body or a body endowed with an operational independence and acting as a watchdog in order to ensure fiscal rules are being complied with. Also, in the realm of financial sector regulation, the State is called upon to follow up as soon as July 2013 to the recommendation of the European Systemic Risk Board (ESRB) on the macro-prudential mandate of national authorities, notably with the designation of the authority in charge of macro-prudential policies. This new authority must be appointed by the Government with diligence.

The BCL has continued to play an active role in various domestic and international fora dealing with macro-prudential surveillance and financial stability: the ESRB, which has been operating for its second year in 2012, the Bank for International Settlements (BIS), of which the BCL has been a shareholder since 2011 and the Regional Consultative Group for Europe under the Financial Stability Board (FSB), created in 2011.

At the national level, the BCL will further the promotion of research in economics, finance and public finance in view, inter alia, of a better understanding of the mechanisms underpinning the Luxembourg economy. The BCL Foundation, incepted in 2011 to promote research and tertiary education in the areas pertaining to central banking, has granted for the first time in 2012 the award for the best PhD thesis on financial stability.

To fulfil its growing missions, notably of a sovereign character, and to respond to the increasing demands by the Eurosystem, the BCL had to continue increasing its staffing. As of December 2012, 303 staff members were employed by the BCL. Human capital remains the Bank's main asset and the social dialogue has taken a particularly important dimension. The question of the status of BCL staff arises in the context of the reform of the Luxembourg public service, which is in the course of being adopted.

The intensification of the crisis has engendered an intensification of current missions and the emergence of new sovereign missions, notably in the framework of the establishment of a SSM. Hence, the BCL needs to review, concomitantly with a review of its asset and liability management and its yield/risk balance, its capital and income-generating base as it is far too low per se and in comparison to other central banks of the euro area[2].

To conclude, I would like to pay tribute to my predecessor, Yves Mersch, who was appointed as a member of the ECB's Executive Board as of 15 December 2012. I would like to thank him for what he has done for the Bank and wish him best of luck in his new endeavours.

Gaston Reinesch

2 See graphs on page 77 to 78 of the report.