



ANNUAL
REPORT
2 0 1 9



BANQUE CENTRALE DU LUXEMBOURG
EUROSYSTEM



MISSION
STATEMENT
OF THE BCL

The *Banque centrale du Luxembourg* (BCL) is a public institution created by Luxembourg law. The BCL's independence is based on its organic law, the Treaty on the European Union and the Treaty on the Functioning of the European Union. The BCL is a member of the European System of Central Banks (ESCB) composed of the National Central Banks of all 28 EU Member States and the European Central Bank (ECB).

THE MISSION

The Bank is a member of the Eurosystem that consists of the European Central Bank and the National Central Banks of the Member States that have adopted the euro. It takes part in the Single Supervisory Mechanism (SSM). It is in charge of managing the monetary and financial responsibilities granted to it as one of the National Central Banks of the ESCB.

At the national level, the central bank has to carry out the tasks conferred 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;
- 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 ensures 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;
- A good governance, within and through the governing bodies concerned with the use of the highest standards in governance.

TABLE OF CONTENTS

THE GOVERNOR'S MESSAGE	1
1 THE BCL'S ACTIVITIES	6
1.1 Monetary Policy Operations	6
1.1.1 Conventional operations	6
1.1.1.1 Open market operations in 2019	7
1.1.1.1.1 Main refinancing operations	7
1.1.1.1.2 Longer-term refinancing operations (LTROs)	9
1.1.1.1.3 Other operations (fine-tuning and structural operations)	9
1.1.1.2 Standing Facilities in 2019	9
1.1.1.3 Reserve requirements in 2019	10
1.1.2 Non-conventional operations	11
1.1.2.1 Temporary foreign exchange auctions	11
1.1.2.2 Extension of the maturities of operations	12
1.1.2.3 Asset purchase programmes	13
1.1.2.4 Other Asset Purchase Programmes - Completed Programmes	14
1.1.3 Management of collateralisation of Eurosystem credit operations	15
1.2 Foreign exchange reserve management by BCL	16
1.3 Management of the BCL's assets	16
1.3.1 Conceptual Framework	16
1.3.1.1 Investment Policy Objectives	16
1.3.1.2 Sustainable investment policy objectives	17
1.3.1.3 Performance Measurement	17
1.3.2 Institutional Structure	17
1.3.3 Risk Control	18
1.3.4 Structure and Composition of the Portfolios	18
1.4 Banknotes and coins	19
1.4.1 Production of banknotes and coins	20
1.4.2 Circulation of banknotes and coins	20
1.4.2.1 Euro banknotes and coins	20
1.4.2.1.1 Banknotes	20
1.4.2.1.2 Coins	22
1.4.2.2 Luxembourg franc banknotes	23
1.4.3 Sorting of euro banknotes and coins	23
1.4.4 National and international cooperation	24
1.4.5 Issuance of the new "Europa" banknote series	24
1.4.6 Numismatic issues	25
1.5 Statistics	25
1.5.1 New data collections	26
1.5.2 Other statistical developments	26
1.6 Payments and Security Settlement Systems	27
1.6.1 Vision 2020	27
1.6.2 TARGET2-LU	27
1.6.3 Retail payments in Luxembourg	31
1.6.4 Securities settlement systems	35
1.6.5 TARGET2-Securities	38
1.6.6 LuxCSD	38

1.7	Financial stability and prudential supervision	39
1.7.1	Macro-prudential supervision	39
1.7.1.1	Macro-prudential surveillance in Luxembourg	40
1.7.1.2	The European Systemic Risk Board	42
1.7.1.3	The Secretariat of the Systemic Risk Committee	44
1.7.2	Micro-prudential supervision	47
1.7.2.1	Liquidity supervision	47
1.7.2.1.1	Liquidity risk supervision of credit institutions established in Luxembourg in the context of the Single Supervisory Mechanism	47
1.7.2.1.2	Tools for liquidity supervision	48
1.7.2.1.3	National and international cooperation	49
1.7.2.2	Oversight of payment and settlement infrastructures	49
1.8	Regulatory and legislative developments	51
1.8.1	European legislation	51
1.8.1.1	Banking Union	52
1.8.1.1.1	Prudential supervision	52
1.8.1.1.2	Resolution of banks	53
1.8.1.1.3	Deposit Protection	54
1.8.1.2	Economic Governance	55
1.8.1.3	ECB Legal Acts	56
1.8.1.4	Litigation related to the European System of Central Banks and the Single Supervisory Mechanism	59
1.8.2	National legislation	60
1.8.2.1	Enacted Law	60
1.8.2.2	BCL Regulations	62
1.8.2.3	Legal interest rate	62
1.8.2.4	Draft laws	62
1.9	Communication	64
1.9.1	Publications	64
1.9.2	External BCL training	64
1.9.2.1	Cooperation with secondary schools	64
1.9.2.2	Cooperation with schools	65
1.9.2.3	Presentations for groups of visitors	66
1.9.3	The BCL website	66
1.9.4	Video communication	66
1.9.5	The BCL library	67
1.9.6	Press relations	67
1.9.7	Information campaign on the new 100 and 200 euro banknotes from the Europa series	67
1.9.8	Conferences and events	67
1.9.9	Research activities and university cooperation	77
1.10	European activities	78
1.10.1	Activities at the level of the European Central Bank	78
1.10.2	The Economic and Financial Committee	79
1.10.3	Other European committees	80
1.11	National and external activities	81
1.11.1	National Activities	81
1.11.1.1	Relations with the Parliament	81
1.11.1.2	BCL Committee Activities	81
1.11.1.3	Activities of external committees in which the BCL participates	81
1.11.2	International activities	83
1.12	Eurosystem Procurement Coordination Office (EPCO)	85

2	THE BCL AS AN ORGANISATION	90
2.1	Corporate Governance	90
2.1.1	The Council	90
2.1.2	The Governor	91
2.1.3	The Executive Board	91
2.1.4	Organisation chart as at 31 December 2019	92
2.1.5	Internal control and risk management	92
2.1.6	External control	94
2.1.7	Codes of Conduct	94
2.2	Human Resources	95
2.2.1	Evolution of the workforce	95
2.2.2	Human Resources Management	95
2.2.3	BCL Pension Fund	96
2.3	Internal finance and strategy	96
2.3.1	Accounting and reporting	96
2.3.2	Budget	97
2.3.3	Strategic Planning and Management Control	97
2.4	Financial statements	98
2.4.1	Key figures as of year-end (in euro)	98
2.4.2	Report of the Réviseur d'Entreprises agréé	99
2.4.3	Balance sheet as at 31 December 2019	101
2.4.4	Off-balance sheet as at 31 December 2019	102
2.4.5	Profit and loss account for the year ending 31 December 2019	103
2.4.6	Notes to the financial statements as at 31 December 2019	103
3	ANNEXES	130
3.1	ECB legal acts published in 2019	130
3.2	BCL regulations published in 2019	132
3.3	List of BCL circulars published in 2019	132
3.4	List of BCL publications published in 2019	132
3.4.1	BCL bulletins	132
3.4.2	BCL annual report	132
3.4.3	Financial Stability Review	132
3.4.4	BCL working papers	132
3.4.5	BCL brochures	133
3.4.6	Information material about the security features of Euro banknotes and coins	133
3.4.7	Publications and external presentations of BCL staff	134
	3.4.7.1 External publications of the BCL's staff members	134
	3.4.7.2 External presentations	134
3.5	European central bank publications	134
3.6	Monetary, economic and financial statistics published on the website of the BCL	134
3.7	List of abbreviations	137
3.8	Glossary	138

THE GOVERNOR'S MESSAGE



The year 2019 marked the 20th anniversary of the advent of the euro. On 1 January 1999, eleven countries decided to share their monetary sovereignty in order to create a single currency and a single monetary policy. The Economic and Monetary Union, already advocated in the Werner Report, whose 50th anniversary we will celebrate in October 2020, was to become a reality. The tangible expression of this decision came three years later with the introduction of banknotes and coins.

Today, the euro, the second most important currency in the world, is shared by some 340 million citizens in 19 countries. While the single currency has transformed our daily lives and increased the efficiency of the single market, the financial and sovereign debt crisis has exposed the risks of an unfinished institutional architecture. The lessons learned have led to the strengthening of the Economic and Monetary Union, notably through the establishment of a single supervisory mechanism and a new crisis management set-up. While this has significantly strengthened the resilience of the euro area, fur-

ther progress is needed, such as the completion of the Banking Union and the creation of a capital markets union.

At the time of writing, we are facing another crisis, of a global dimension and of a completely different nature, which we need to address in a spirit of solidarity. While the COVID-19 pandemic is first and foremost a human tragedy, it also has major economic consequences.

The sanitary crisis has generated a supply shock, coupled with a demand shock. Entire segments of economic activity have been put on hold, causing an increase in unemployment and plunging many economic agents into precariousness. The intensity of the shock we are facing depends on several variables that are difficult to predict, including the evolution of the virus and the associated periods of lockdown. Moreover, while the economic shock would undoubtedly have been more severe in the absence of the ambitious mitigation measures put in place, their effectiveness can only be measured over time.

Given the high degree of uncertainty surrounding the various scenarios and projections, they should be treated with caution. While the expected size of the negative economic impact can vary greatly depending on the assumptions chosen, it is recognised that the euro area will not escape a recession in 2020. This severe economic impact, coupled with falling energy prices, have also put downward pressure on inflation in the euro area.

The Governing Council of the European Central Bank (ECB) has taken a series of measures to support the euro area economy in this difficult environment. These aim to ensure the smooth transmission of the Eurosystem's monetary policy. By contributing to the easing of financing conditions, these measures support the provision of credit by banks to households and businesses on favourable terms, complementing the fiscal measures already taken or to be taken at national and European levels.

Since the resumption of the Eurosystem's asset purchase programme in November 2019, monthly net purchases have amounted to €20 billion. Because of the COVID-19 crisis, the Governing Council decided to introduce a temporary envelope of €120 billion to make additional asset purchases by the end of the year. The Governing Council plans to use net asset purchases for as long as necessary and to discontinue them shortly before starting to raise the key ECB interest rates.

The Governing Council also decided to create a new temporary programme directly related to the pandemic. This programme, the Pandemic Emergency Purchase Programme (PEPP), announced in March 2020, initially amounted to €750 billion and was increased to €1,350 billion in June. Purchases will be made at least until the end of June 2021 and for as long as necessary until the Governing Council deems that the coronavirus crisis is over. Also, maturing principal payments will be reinvested at least until the end of 2022. Under this programme, the Eurosystem purchases both public and private securities. As with the asset purchase programme, the risks related to the acquisition of private securities are fully shared, while those related to the acquisition of public securities are pooled up to 20%. The risk relating to the acquisition of the remaining 80%, representing purchases on the secondary market of national debt by national central banks, is not shared.

Also in the context of the crisis, the Governing Council launched a series of seven Pandemic Emergency Longer-Term Refinancing Operations (PELTROs). These operations are aimed at supporting liquidity conditions in the euro area financial system and helping to preserve the smooth functioning of money markets. They started in May 2020 and will mature gradually between July 2021 and September 2021.

In order to provide banks with longer-term liquidity, the Governing Council decided to conduct temporary additional longer-term refinancing operations (LTROs). It also decided to apply more favourable conditions to all targeted longer-term refinancing operations launched in September 2019 (TLTRO III) from June 2020 for a one-year period. This liquidity provision aims to stimulate the provision of credit to the real economy by offering participating banks extremely low interest rates, provided that they channel sufficient loans to non-financial corporations and households. If these conditions are met, the banks repay less to the central bank than they borrowed. Housing loans are excluded from this mechanism.

Another important measure has been the easing of the eligibility conditions for collateral. Indeed, the central bank can only grant credit to banks against collateral. If the eligibility conditions are no longer met, for example because of downgrades by rating agencies, the pool of available collateral is reduced, which may constrain banks' ability to borrow from the central bank and, at the same time, their ability to finance the economy. This can be avoided by easing eligibility requirements. By increasing its risk tolerance, the Eurosystem therefore also supports the provision of credit.

Finally, mention should be made of prudential measures. The Single Supervisory Mechanism has taken microprudential measures to facilitate the provision of bank credit to the real economy. The same applies to many national macroprudential authorities, whose measures facilitate the absorption of bank losses.

While monetary and prudential policy measures have contributed significantly to the crisis response, they can only come in support of other ambitious measures. I therefore welcome the European initiatives to address the impact of the pandemic. Concerted national measures aligned with European initiatives are also needed.

In 2019, in addition to the resumption of asset purchases and the launch of the third round of targeted longer-term refinancing operations, the Governing Council decided to lower the rate on the deposit facility from -0.4% to -0.5%. Moreover, it decided to introduce a two-tier reserve remuneration system (tiering). Since 30 October 2019, this mechanism aims to exclude from the application of the deposit facility rate part of the reserves that banks deposit with euro area central banks in excess of their reserve requirements. This exempted part is remunerated at 0%.

The year under review was also marked by the launch on 28 May of the new 100- and 200-euro banknotes of the Europa series. The production of the 500-euro banknote was discontinued in May 2016 and the series is now complete.

Finally, 2019 saw the end of Mario Draghi's term of office as President of the ECB on 31 October. Ms Christine Lagarde, former Managing Director of the International Monetary Fund, replaced him in this position for a term of eight years.

At the national level, the 20th anniversary of the introduction of the euro provided an opportunity for the BCL to organise an open door event in an expanded format. The public was thus able to learn about the Bank's European and national missions and discover the very rich history of Luxembourg's currency thanks to an exceptional exhibition covering the period from the time of John the Blind to the banknotes issued by the Luxembourg Monetary Institute. Banknotes from other countries prior to the advent of the euro were also on display. A workshop on the security features of the euro banknotes was also a great success. The Prime Minister honoured us with his presence to celebrate this symbolic milestone. I would like to thank all those who joined us on that day.

In September, the BCL organised, in co-operation with the Toulouse School of Economics (TSE), a conference on the future of the international monetary system. This highly notable event benefited from the contribution of Jean Tirole and Emmanuel Farhi. It was with great emotion that we learned that Emmanuel Farhi passed away prematurely¹. Considered as one of the most brilliant and influential economists, he was also appreciated for his modesty. Our thoughts go out to his family and loved ones.

This event, which was attended by some 800 people, brought together policy makers from international institutions and leading academics to discuss issues that could shape the evolution of the international monetary system in the years ahead, such as the emergence of crypto-actives and "stable coins". The wealth of the exchanges that have taken place can only encourage us to repeat this experience.

In order to attract promising young talent, the Bank has set up a Graduate programme. The first edition of this programme, which aims to recruit a limited number of candidates per year and train them in the various central banking activities, attracted a large number of applications. We hope to maintain this interest.

Before concluding, on behalf of the governing bodies of the BCL, I would like to thank the staff for their commitment during this sanitary crisis. Their dedication and the smooth transition to home-based work for a large majority of staff ensured the continuity of our operations. In particular, I would also like to express my gratitude to those who faced an exceptional workload due to the preparation and implementation of the monetary policy measures taken by the Governing Council over the past few months.

Finally, on behalf of the governing bodies of the BCL and its staff, I would like to pay a final tribute to His Royal Highness Grand Duke Jean, who passed away on 23 April 2019. His courage, integrity, humanity and unwavering commitment will remain an example to us all.



Gaston Reinesch

1 * Emmanuel Farhi passed away on 23 July 2020.