



MISSION STATEMENT OF THE BCL

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The *Banque centrale du Luxembourg* (BCL) is a public institution created by Luxembourg law. The BCL's independance 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

A WORD FROM THE GOVERNOR		
1	THE BCL'S ACTIVITIES	6
1.1 1.1.1	Monetary Policy OperationsConventional operations1.1.1.1Open market operations in 20201.1.1.2Standing Facilities in 20201.1.1.3Reserve requirements in 2020	6 7 9 10
1.1.2	 Non-conventional operations 1.1.2.1 Temporary foreign exchange auctions 1.1.2.2 Extension of the maturities of operations 1.1.2.3 Asset purchase programmes 1.1.2.4 Other Asset Purchase Programmes - Completed Programmes 	11 11 12 14 14
1.1.3	Collateralisation of Eurosystem credit operations	17
1.2	Foreign exchange reserve management by BCL	16
1.3 1.3.1 1.3.2	Management of the BCL's assets Conceptual Framework 1.3.1.1 Investment Policy Objectives 1.3.1.2 Sustainable investment policy objectives 1.3.1.3 Performance Measurement Institutional Structure	18 18 19 19 20
1.3.3 1.3.4	Risk Control Structure and Composition of the Portfolios	20 20
1.4 1.4.1 1.4.2 1.4.3 1.4.4 1.4.5	Banknotes and coins Production of banknotes and coins Circulation of banknotes and coins 1.4.2.1 Euro banknotes and coins 1.4.2.1.1 Banknotes 1.4.2.1.2 Coins 1.4.2.2 Luxembourg franc banknotes Sorting of euro banknotes and coins National and international cooperation Issuance of the new "Europa" banknote series	22 22 22 22 22 24 25 25 26 26
1.4.6	Numismatic issues	26
1.5	Statistics	27
1.6 1.6.1 1.6.2 1.6.3 1.6.4	Payments and Security Settlement Systems Vision 2020 TARGET2-LU Retail payments in Luxembourg Securities settlement systems 1.6.4.1 TARGET2-Securities 1.6.4.2 LuxCSD	28 28 29 33 37 40 40
1.7 1.7.1	Financial stability and prudential supervisionMacro-prudential supervision1.7.1.1Macro-prudential surveillance in Luxembourg1.7.1.2The European Systemic Risk Board1.7.1.3The Secretariat of the Systemic Risk Committee	41 41 42 45 47

1.7.2	Micro-prudential supervision	49
	1.7.2.1 Liquidity supervision	49
	1.7.2.1.1 Liquidity risk supervision of credit institutions established	
	in Luxembourg in the context of the Single Supervisory Mechanism	50
	1.7.2.1.2 Tools for liquidity supervision	51
	1.7.2.1.3 National and international cooperation	51
	1.7.2.2 Oversight of payment and settlement infrastructures	51
		0
1.8	Regulatory and legislative developments	55
1.8.1	European legislation	55
	1.8.1.1 Banking Union	55
	1.8.1.1.1 Prudential supervision	55
	1.8.1.1.2 The resolution of banks	57
	1.8.1.1.3 Deposit Protection	57
	1.8.1.2 Economic Governance	58
	1.8.1.3 ECB Legal Acts	6
	1.8.1.4 Litigation related to the European System of Central Banks	
	and the Single Supervisory Mechanism	64
1.8.2	National legislation	65
	1.8.2.1 Enacted Law	65
	1.8.2.2 BCL Regulations	66
	1.8.2.3 Legal interest rate	66
	1.8.2.4 Draft laws	67
1.9	Communication	67
1.9.1	Publications	67
1.9.2	External BCL training	67
1.7.2	1.9.2.1 Cooperation with secondary schools	67
	1.9.2.2 Cooperation with schools	67
	1.9.2.3 Presentations for groups of visitors	68
1.9.3	The BCL website	69
1.7.3	Video communication	69
1.7.4	The BCL library	69
1.7.5	Press relations	69
1.7.0	Information campaign on the new 100 and 200 euro banknotes from the Europa series	69
1.7.7	mormation campaign on the new 100 and 200 euro bankhotes nom the Europa series	0.
1.10	European activities	70
1.10.1	Activities at the level of the European Central Bank	70
1.10.2	The Economic and Financial Committee	72
1.10.3	Other European committees	73
1.11	National and external activities	73
1.11.1	National Activities	73
	1.11.1.1 Relations with the Parliament	73
	1.11.1.2 BCL Committee Activities	74
	1.11.1.3 Activities of external committees in which the BCL participates	74
1.11.2	International activities	76
1.12	Eurosystem Procurement Coordination Office (EPCO)	78

2	THE BCL AS AN ORGANISATION	82
2.1	Corporate Governance	82
2.1.1	The Council	82
2.1.2	The Governor	83
2.1.3	The Executive Board	83
2.1.4	Organisation chart as at 31 December 2020	84
2.1.5	Internal control and risk management	85
2.1.6	External control	86
2.1.7	Codes of Conduct	86
2.2	Human Resources	86
2.2.1	Evolution of the workforce	86
2.2.2	Human Resources Management	86
2.2.3	BCL Pension Fund	87
2.3	Internal finance and strategy	87
2.3.1	Accounting and reporting	87
2.3.2	Budget	88
2.3.3	Strategic Planning and Management Control	89
2.4	Financial statements	89
2.4.1	Key figures as of year-end (in euro)	89
2.4.2	Report of the Réviseur d'Entreprises agréé	91
2.4.3	Balance sheet as at 31 December 2020	93
2.4.4	Off-balance sheet as at 31 December 2020	94
2.4.5	Profit and loss account for the year ending 31 December 2020	95
2.4.6	Notes to the financial statements as at 31 December 2020	95
3	ANNEXES	122
3.1	ECB legal acts published in 2020	122
3.2	BCL regulations published in 2020	124
3.3	List of BCL circulars published in 2020	125
3.4	List of BCL publications published in 2020	125
3.4.1	BCL bulletins	125
3.4.2	BCL annual report	125
3.4.3	Financial Stability Review	125
3.4.4	BCL working papers	125
3.4.5	BCL brochures	126
3.4.6	Information material about the security features of Euro banknotes and coins	126
3.4.7	Publications and external presentations of BCL staff	126
	3.4.7.1 External publications of the BCL's staff members	126
	3.4.7.2 External presentations	126
3.5	European central bank publications	127
3.6	Monetary, economic and financial statistics published on the website of the BCL	127
3.7	List of abbreviations	129
3.8	Glossary	130

A WORD FROM THE GOVERNOR



2020 was marked by the most severe recession that Europe has endured since World War II. The consequences of the health crisis were dire, both from a human and economic perspective. Consequently, the euro area economy contracted by almost 7% in 2020 compared to the previous year. Faced with this crisis, ambitious mitigation measures were put in place at European level and by Member States. Without these measures, the impact of the crisis would have been much more severe. According to recent projections by Eurosystem staff, the euro area economy should recover strongly and grow by 4.6% in 2021, owing in particular to our economies gradually coming out of lockdown. Real GDP is expected to grow by 4.7% in 2022 and 2.1% in 2023.

The COVID-19 crisis, an exogenous shock that affected both supply and demand, strongly dampened rises in consumer prices. Thus, annual inflation in the euro area averaged 0.3% in 2020, with prices even falling slightly in the last five months of the year. Eurosystem staff expect inflation to reach 1.9% in 2021. This increase is essentially due to temporary factors. According to these same projections, inflation should fall to 1.5% in 2022 and 1.4% in 2023.

In line with its mandate to ensure price stability, defined as annual consumer price inflation below, but close to 2% over the medium term, the Governing Council of the ECB has taken a number of monetary policy measures aimed at bringing inflation closer to its objective.

Thus, on 12 March 2020, the Governing Council took the decision to temporarily expand the envelope of its asset purchase programme (APP¹) \in 120 billion to purchase additional assets by the end of the same year. Purchases under this programme are carried out at a monthly rate of \in 20 billion and the Governing Council plans to use the net asset purchases under the APP for as long as necessary and to end the programme shortly before it starts raising the key ECB interest rates. In addition, the Governing Council also intends to continue to fully reinvest the principal repayments of maturing securities acquired under the APP. These reinvestments will be made for an extended period beyond the date on which the Governing Council begins to raise key interest rates, and in any case for as long as necessary to maintain favourable liquidity conditions and an ample degree of monetary accommodation.

On 18 March, the Governing Council announced the establishment of a temporary envelope of €750 billion dedicated to the emergency purchasing programme in the face of the pandemic (Pandemic Emergency Purchase Programme, PEPP). This envelope was subsequently increased twice, by €600 billion in June and €500 billion in December, to reach a total envelope of €1,850 billion. This unconventional monetary policy measure, the overall envelope of which will not necessarily be exhausted, aims to counter the significant risks that the pandemic poses to the monetary policy transmission mechanism and the outlook for the euro area. The related purchases will be made at least until the end of March 2022 and for as long as necessary, until such time as the Governing Council judges the coronavirus crisis to be over. Also, principal payments coming due will be reinvested at least until the end of 2023. This programme has undoubtedly helped to alleviate a deeper economic crisis and to avoid negative amplification effects on the financial sector. In view of the importance of the Luxembourg financial centre, its impact has been particularly beneficial for Luxembourg.

On 30 April 2020, the Governing Council decided to establish a series of non-targeted Pandemic Emergency Longer-Term Refinancing Operations (PELTROS). These new operations, initially a series of seven operations, carried out from May 2020 and maturing between July 2021 and September 2021, aim to provide support for liquidity conditions in the euro area financial system and contribute to preserving the smooth functioning of money markets. On 10 December 2020, the Governing Council decided to offer four additional refinancing operations, to be allocated in 2021.

In addition, the Governing Council decided to launch longer-term refinancing operations (Longer-Term Refinancing Operations, LTRO) and has on two occasions eased the financing conditions for the third round of targeted longer-term refinancing operations (Targeted Longer-Term Refinancing Operations III, TLTRO III) in order to encourage banks in the euro area to grant loans to economic agents more particularly affected by the health crisis, in particular small and medium-sized enterprises. Under certain conditions, the interest rate applied by the Eurosystem to participating credit institutions may drop down to -1%.

The Governing Council also considered it necessary to take new measures concerning the guarantees accepted in the framework of monetary policy operations. Firstly, it agreed to broaden the range of eligible assets under the programme to purchase bonds issued by companies (Corporate Sector Purchase Programme, CSPP) non-financial commercial papers, by making all commercial paper of sufficient credit quality eligible for purchase under the CSPP. Subsequently, it took a set of temporary collateral relaxation measures aimed at facilitating the availability of eligible collateral for Eurosystem counterparties participating in liquidity-providing operations.

Finally, the ECB reactivated swap lines and improved existing swap lines with a number of central banks and introduced a new repo facility to provide liquidity in euros to central banks outside the euro area.

During the period under review, the Governing Council did not change the Eurosystem's key rates. Thus, the rate on the main refinancing operations stood at 0%, while the rates on the deposit facility and the marginal credit facility were -0.5% and 0.25% respectively.

At microprudential level, the Single Supervisory Mechanism has also taken steps to support credit flows to the real economy.

At European level, significant budgetary measures, equivalent to more than \pounds 2.3 trillion, have been taken to counter the effects of the crisis. These include the multi-annual budget plan, covering the period 2021-2027 and amounting to \pounds 1,074 billion, which will enable EU Member States to invest in the green and digital transition of their economies, as well as the temporary \pounds 750 billion NextGenerationEU recovery instrument. At the heart of this unprecedented European plan is the Recovery and Resilience Facility; it makes available \pounds 672.5 billion, of which \pounds 312.5 billion is offered in the form of grants. These measures are further supplemented by the EU's \pounds 100 billion SURE² instrument to protect jobs and workers, the European Investment Bank's Guarantee Fund which aims to make available up to \pounds 200 billion in financing for businesses, and the European Stability Mechanism's (ESM) pandemic support instrument, which provides euro area Member States with additional budgetary capacity to cover healthcare costs. Through this instrument, each beneficiary can access precautionary financial assistance of up to 2% of its 2019 gross domestic product, the overall amount accessible under the instrument being limited to \pounds 240 billion. In order to facilitate the budget support of the Member States, the European Commission has decided to activate the general exemption clause of the Stability and Growth Pact, i.e. to freeze the budgetary rules, until the end of 2022.

At Member State level, many initiatives have also helped to support economies, in particular through employment support measures, bank guarantees and moratoria. The same is true for many national macroprudential authorities, whose measures make it easier for banks to absorb any losses.

2020 was also marked by the decision of the Governing Council in January to launch an assessment of the Eurosystem's monetary policy strategy. While this strategy was adopted in 1998 and revised in 2003, the financial crisis and structural changes in the global economy have since pushed the Eurosystem's key interest rates down, forcing it to resort to unconventional monetary policy measures. In addition, major challenges such as climate change and digitisation, to name just two, have also

² Support to mitigate Unemployment Risks in an Emergency.

transformed the environment in which monetary policy is conducted. Against this backdrop, it was deemed necessary to carry out a review, performed in strict compliance with the ECB's mandate to maintain price stability. The scope of this exercise, which is expected to be finalised in July 2021, focuses on the quantitative definition of price stability, the various instruments of monetary policy, economic and monetary analysis and modes of communication. Other considerations relating to financial stability, sustainable development and employment will also be taken into account.

Two important aspects still deserve special mention. Firstly, a roadmap will be drawn up to integrate the evolution of the costs of owner-occupied housing in the European harmonised consumer price index. Secondly, an ambitious action plan will be drawn up integrating climate change considerations into the monetary policy strategy.

The Governing Council has decided to conduct this review in an inclusive manner, taking into account the views of civil society in each of the euro area Member States. As a result, each national central bank in the Eurosystem has launched a consultation exercise with a wide range of stakeholders. The Banque centrale du Luxembourg (BCL) has thus organised several consultations - internally, with civil society, as well as the academic and student community - in order to provide input on the subject. I would like to thank everyone who took part in these sessions.

In addition to these consultations, I had the opportunity to present to the Finance and Budget Committee of the Chamber of Deputies the purpose of this strategic review and the role played by the BCL in this context during an informal session.

During the period under review, the BCL also invested in three important areas: the continued greening of the investment of its own funds, the study of the possible introduction of a digital euro, which would be complementary to the euro banknotes and would also constitute a claim on the central banks of the Eurosystem, as well as the modernisation and further harmonisation of the payment infrastructure at European level.

Our greening strategy now also forms part of a common Eurosystem effort in this field. Indeed, in early February 2021, the latter agreed on a common position on sustainable and responsible investment principles related to climate change for non-policy related own portfolios denominated in euros. This common position encourages in particular the communication of information on risks linked to climate change. The Eurosystem aims to start publishing this information by early 2023.

With regard to the internal governance of the BCL, Mr Pierre Beck, Director of the BCL since 2009, retired on 1 June 2021, i.e. at the end of his second term of office as a member of the Management of the BCL. On behalf of the decision-making bodies and agents of the BCL, I would like to thank him for his invaluable contribution to the development of the BCL and wish him all the best for his well-deserved retirement. By virtue of a Grand-Ducal decree of 23 April 2021, the Council of Government has appointed Mr Nicolas Weber as his successor for a renewable term of six years.

To conclude, on behalf of the Management, I would like to thank all the BCL agents for their commitment and dedication during this health crisis. Their exemplary work has enabled the Bank to ensure the smooth continuity of its operations during these exceptional times.

Gaston Reinesch