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LIETUVOS BANKAS
EUROSISTEMA

2018

Annual Report

The 2018 Annual Report was approved by the Board of the Bank of Lithuania on 14 May 2019.
The cut-off date for the data included in this report was 14 March 2019.

ABBREVIATIONS

AB	public limited liability company	IT	information technology
ABSPP	asset-backed securities purchase programme	KYC	know your customer
API	application programming interface	LTRO	long-term refinancing operation
APP	asset purchase programme	MFI	monetary financial institution
CBPP	covered bond purchase programme	MRO	main refinancing operation
CCyB	countercyclical capital buffer	MTPL	motor third party liability
CIU	collective investment undertaking	O-Slls	other systemically important institutions
CPSS	Committee on Payment and Settlement Systems	P2P	peer-to-peer
CSPP	corporate sector purchase programme	PSPP	public sector purchase programme
ECB	European Central Bank	RE	real estate
EEA	European Economic Area	RegTech	regulatory technology
ERPB	Euro Retail Payments Board	SEPA	Single Euro Payments Area
ESCB	European System of Central Banks	SMP	securities market programme
EU	European Union	T2S	TARGET2-Securities
FinTech	financial technology	TLTRO	targeted longer-term refinancing operation
GDP	gross domestic product	UAB	private limited liability company
HICP	Harmonised Index of Consumer Prices	UK	United Kingdom
IMF	International Monetary Fund	US	United States of America
IOSCO	International Organization of Securities Commissions		

Totals/percentages in some tables and charts may not add up due to rounding ('Total' and 100%).

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Foreword



Under its mandate as the central bank of the Republic of Lithuania, the Bank of Lithuania continued working towards implementing its strategic goals and objectives.

The accommodative monetary policy implemented in 2018 has further contributed to the acceleration of economic growth in the euro area and Lithuania. The latter was mostly stimulated through the tradable sector – stronger demand in the euro area and depreciation of the euro several years prior have opened up more possibilities for the country's exporters.

The Eurosystem maintained a very accommodative monetary policy stance. As a member of the Eurosystem since 2015, the Bank of Lithuania, together with the ECB and the central banks of 18 other euro area countries, has been participating in the formulation and implementation of monetary policy in the euro area.

We have been expanding the scope of our activities, aiming to become a local centre of excellence in economics and finance. By sharing their assessments and recommendations, our experts have been actively contributing to the restructuring of Lithuania's tax and pension systems. The Bank of Lithuania has extended its range of analysis and research directions, developed new analytical tools, and put forward proposals and estimations regarding the potential economic policy response to domestic economic problems. Having drawn the attention to regional developments, we took action to present them to the general public all across Lithuania.

Strong growth of the country's economy reinforced lending activities, therefore, certain measures had to be taken to strengthen the resilience of the domestic financial system. In order to properly prepare for an economic slowdown, the Bank of Lithuania set higher countercyclical capital buffer requirements aimed at ensuring that banks hold a sufficient capital buffer for covering potential losses caused by cyclical systemic risks or an economic downturn.

The banking and credit union sector was stable. Robust lending had a positive impact on banks' profitability – almost two-thirds of their operating income stemmed from the increase in corporate and household loan volumes. The restructured credit union sector recorded gains for the second consecutive year, while the number of sustainable shares continued growing. The landscape of the banking sector has changed – in order to reduce costs, two banks have reorganised into foreign bank branches. Following the assessment and proposal of the Bank of Lithuania, at the end of 2018 the ECB granted the first three specialised bank licences; one of the banks has already commenced its activities and is in operation. We expect that over time new market participants will boost competition and provide consumers with wider choice of financial services.

We have also been encouraging innovation in the field of payments. Participants of CENTROLink – a payment system managed and operated by the Bank of Lithuania – have

introduced the most cutting-edge innovation – instant payments. They allow consumers to initiate payments with just a few clicks on their mobile devices and transfer funds within seconds. In addition, the share of residents who have chosen payment service packages has increased: according to survey results, two-thirds of account holders in Lithuania used payment service packages in 2018, compared to a half in 2017.

Furthermore, we have been creating a business-friendly regulatory environment. Together with other public sector institutions, we have lowered the barriers to market entry and operation therein. The Bank of Lithuania has been providing consultations to potential financial market participants on business opportunities in Lithuania. FinTech companies can now test their innovative financial products in the Bank of Lithuania's regulatory sandbox. As a result, Lithuania has grabbed the attention of world-renowned companies and was ranked first in continental Europe in terms of licensed electronic money institutions in 2018. Yet the doors to the Lithuanian, and, in turn, the EU, market is not open to everyone. The Bank of Lithuania grants licences only to carefully selected companies seeking to enter Lithuania's financial sector. To strengthen its international relations, the Bank of Lithuania signed FinTech cooperation agreements with the Monetary Authority of Singapore, the National Bank of Ukraine and the Astana Financial Services Authority (Kazakhstan).

The Bank of Lithuania has been acknowledged as a pro-active institution in terms of anti-money laundering supervision. The Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism (MONEYVAL) has recognised the effective controls that we introduced in relation to authorisation of financial market participants in order to prevent criminals from managing or acquiring a holding in financial institutions. Cooperation between the Bank of Lithuania and the Financial Crime Investigation Service in inspecting financial market participants and exchanging information did not go unnoticed as well.

We have been also implementing new solutions for financial asset investment. The upgraded strategic asset allocation model aimed at enhancing risk diversification has already proved to be successful. The Bank of Lithuania was the first central bank in the world to implement such an innovative approach that has already garnered significant attention from our colleagues in other central banks. The Bank of Lithuania's 3-year return on financial assets investment was €80.5 million.

We have achieved tangible results in our efforts to raise the quality of economic research and studies in Lithuania. On the initiative of the Center for Excellence in Finance and Economic Research of the Bank of Lithuania (CEFERR), Vilnius University introduced a new bachelor's programme in Quantitative Economics, offering a unique blend of mathematics, statistics, economics and data science, thus providing the youth an opportunity to study contemporary economics in Lithuania. CEFERR has also organised joint PhD courses, various seminars and workshops aimed at increasing the competence of researchers working at Lithuanian universities.

Vitas Vasiliauskas

Chairman of the Board of the Bank of Lithuania

1. To become a centre of excellence in economics and finance



Surveys show that the Bank of Lithuania is the most competent institution in the economic and financial field.



The central bank has set out its constructive position and suggestions on tax and pension reforms as well as the minimum wage threshold.



The Bank of Lithuania organised two conferences on relevant economic and financial issues and co-organised two joint conferences.



Publications: 7 occasional, 8 working and 5 discussion papers, 18 studies in peer-reviewed scientific journals. Economic and financial comments by Bank of Lithuania economists reached a wide audience.



The Bank of Lithuania took part in international programmes and shared its best practices.

the potential economic policy response to domestic economic problems. To present the results of research carried out at the Bank of Lithuania (18 publications in peer-reviewed scientific journals, 7 occasional, 8 working and 5 discussion papers), it organised 25 presentations abroad and 60 presentations for local authorities, organisations and experts (26 of which were open seminars for non-specialists). The Bank of Lithuania organised two conferences on relevant economic and financial issues: an economics conference 'Lithuanian Pension System: How to Ensure Socially Just yet Sustainable Pensions?' and the annual Real Estate Conference. It also took part in arranging two joint conferences: the 7th Annual Lithuanian Conference on Economic Research held in Vilnius and the International Spillovers Conference held in cooperation with the National Bank of Poland in Warsaw. In view of the relevance of issues related to cybersecurity, the Bank of Lithuania took action to analyse cyber threats, dedicating to this topic a chapter in its Financial Stability Review.

The Bank of Lithuania has been actively cooperating with public authorities on relevant issues related to economic and financial policy. In 2018, the Bank of Lithuania took an active role in working groups on tax and pension accumulation reforms, where it provided its position and practical suggestions. Moreover, the central bank submitted its proposals on the minimum wage to Lithuania's Tripartite Council.

The Bank of Lithuania was visible in the Lithuanian media and foreign publications. In 2018, 19% of the content produced by the Bank of Lithuania centred on financial stability and economic issues. Comments by the economists of the Bank of Lithuania were widely published in the media. Furthermore, the Bank of Lithuania was cited in the foreign media, specialised portals (e.g. voxeu.org) and scientific publications.

The central bank continued its involvement in international cooperation initiatives. In addition to providing technical assistance, the Bank of Lithuania has also been participating in the EU Twinning Project. The project aims to enhance the capacity of the National Bank of Belarus to effectively pursue its core responsibilities in several key areas. Two of the Bank of Lithuania staff members coordinate the consortium experts' work in the fields of financial stability and banking supervision, while 12 more experts share their experience with the Belarusian counterparts in such areas as payment systems, banking supervision, financial stability, consumer protection and communication policy.

With the aim of becoming the local centre of excellence in economics and finance, the Bank of Lithuania has been stimulating its research activities and actively communicating with the general public and market participants. In pursuit of its strategic goals, in 2018, the Bank of Lithuania extended its range of analysis and research directions, devoted attention to regional and demographic issues (taking into account their impact on the country's long-term economic outlook), and developed new tools for assessing and analysing

Main goals



2. To become a financial sector partner, promoting innovation and sustainable growth



The Bank of Lithuania reviewed various legislative provisions and made a list of necessary amendments.



The central bank launched a regulatory sandbox.



The Newcomer Programme¹ was used by 131 potential market participants from over 50 countries.



The Bank of Lithuania issued 34 FinTech licences.²



The central bank established a cooperation platform for authorities responsible for risk management.

As a financial conduct authority, the Bank of Lithuania takes active measures to ensure that the road towards innovation and market competition remains open. To this end, it works in several directions.

Strengthening partnership with financial market participants. With its goal to maintain regulatory hygiene, the central bank is gradually abandoning excessive and outdated solutions. The Bank of Lithuania took the initiative to review relevant legislative acts: in collaboration with market participants, it identified provisions to be amended and is dedicated to focusing on the implementation of the necessary changes. It also seeks to ensure that its actions are predictable and communicated to market participants in advance. Therefore, the Bank of Lithuania started announcing its plans for inspections and regulatory amendments as well as organising periodic meetings with market participants. It also took up new ways of fulfilling its supervisory mandate (on-site visits, etc.).

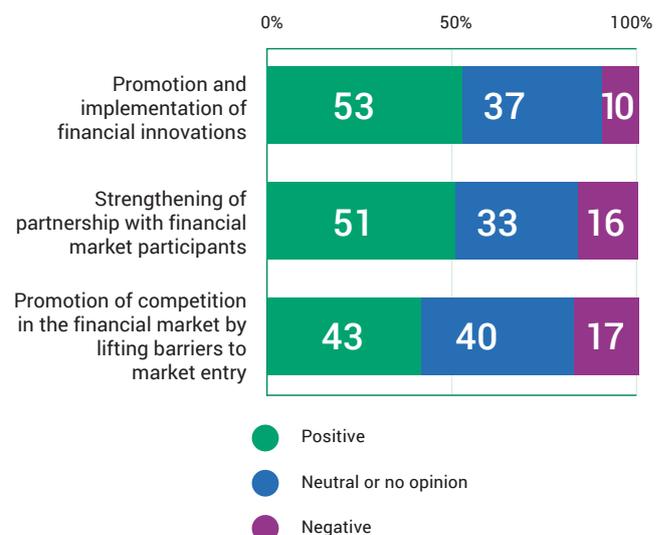
Encouraging competition in the financial market. In a joint effort with other public sector institutions, the Bank of Lithuania has been lowering barriers to market entry and operation therein, at the same time ensuring financial market resilience and its sustainable development. Therefore, the central bank improved remote customer identification processes, introduced the possibility to obtain a specialised bank licence, granted

payment and e-money institutions access to its retail payment system, and allowed potential financial market participants to apply for a licence remotely – all these are just a few examples reaffirming Lithuania’s position as an attractive jurisdiction for foreign capital.

Promoting innovation in the financial market. Seeking to analyse the blockchain potential, the central bank organised a hackathon, whose participants proposed the concept for a digital collector coin (LBCoin) which would be designed using blockchain technology. The Bank of Lithuania has been further working on the LBCoin project and, having launched a pre-commercial procurement, is already halfway through the process of developing an innovation accelerator. It has also created a regulatory sandbox for testing innovative financial products and solutions. Promotion of financial innovation is inseparably linked to public sector authorities and their increasing eagerness to implement new technologies. Therefore, it has also launched the GovTech Forum, which promotes cooperation and exchange of information between Lithuania’s public authorities.

Foreign capital and innovation inevitably entail certain risks (money laundering, terrorist financing, cybersecurity, etc.). The Bank of Lithuania has been taking effective measures to mitigate them: it took action to develop the competences of its supervisory staff, increased internal resources, continued maintaining close cooperation with law enforcement authorities to evaluate the shareholders and management members of licence seekers, as well as established connections with foreign supervisory authorities.

Financial market participants’ assessment of Bank of Lithuania initiatives



¹ A one-stop shop for new market participants interested in obtaining licences in Lithuania.

² 20 e-money institution, 8 payment institution and 3 specialised bank licenses, 3 authorisations for crowdfunding platform operators.

3. To create a competitive and advanced payments market in Lithuania

 The Bank of Lithuania created an infrastructure that will provide more opportunities for the development of innovative payments.

 First payment service providers started offering the instant payment service.

 Cooperation in the Payments Council helps to determine market inefficiencies and ways of improving them.

 The Bank of Lithuania launched an initiative to promote non-cash payments in education institutions.

in Lithuania, optimisation of KYC processes and timely legal recognition of innovative remote identification measures.

The Bank of Lithuania developed and offers to the payments market a solution that ensures easier and faster interbank payments – funds are transferred within seconds, 24 hours a day, 365 days a year, using just the payee's phone number or email address. The system allows the client to link a bank account (IBAN) with a phone number or email address and make interbank payments simply by choosing the recipient from the contact list in their mobile phone. The Bank of Lithuania has already signed agreements on the provision of the service linking a bank account with a phone number with three banks which process half of all payments made in Lithuania. They plan to start providing the service in the second half of 2019. This service developed by the Bank of Lithuania will facilitate faster expansion of the domestic payments system and strengthen the development of mobile instant payments, an alternative to ordinary and cash payments.

The Bank of Lithuania took the initiative to make non-cash payments available in education institutions, thus seeking to increase students' financial literacy and form their non-cash payment habits. Students usually use cash when buying lunch at their school's canteen, which makes it the best place for them to learn about non-cash payment instruments, understand their advantages and familiarise with the necessary safety measures (e.g. not revealing a payment card PIN code to strangers). This would ensure greater security (money would not be lost if, upon losing the payment instrument, the issuing institution were to be notified) and provide more information to parents on how their children are managing their money. The chosen payment instrument could also serve as a way to reduce social exclusion (there would be no way to find out which children receive free meals). Integration of non-cash payment instruments with mobile learning apps would provide students with an opportunity to improve their finance management skills on a daily basis. The central bank's initiative received support from other institutions, such as the Ministry of Finance, Vilnius city municipality, banks and FinTech companies. However, implementation of the initiative on a national scale would require joint efforts from both government institutions and private companies.

The work carried out by the Payments Council in 2018 has shown that cooperation of institutions and associations representing different payment market participants produces new and valuable insights into issues relevant to the market and helps to determine deficiencies of existing processes and practices as well as ways of improving them.

At the end of 2017, the Bank of Lithuania and the Ministry of Finance created an independent forum – the Payments Council – which brought together payment service providers, payment service users, regulators and the academia. In 2018, institutions and associations representing the Payments Council analysed three priority issues: the development of instant payments in Lithuania, optimisation of KYC processes and introduction of new client identification measures. In the course of examining these issues, the Payments Council conducted a market analysis and looked for solutions to eliminate the identified shortcomings. In April 2019, the Payments Council prepared recommendations for relevant institutions regarding their contribution to the development of instant payments

Solution for easier and faster interbank payments



4. To enhance application of financial asset investment strategies

 In 2018, the upgraded strategic asset allocation model aimed at enhancing risk diversification proved to be successful.

 The quantitative investment strategies project reached its final stages.

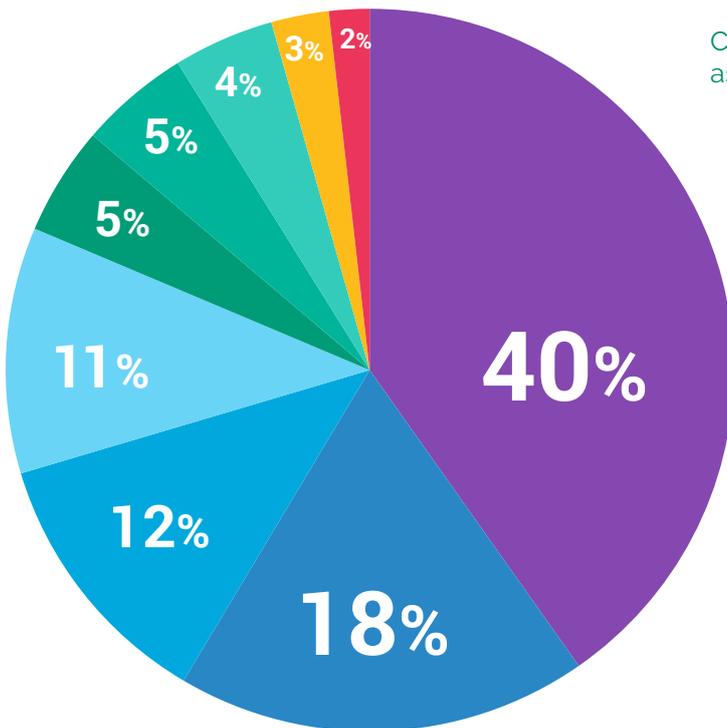
 The Bank of Lithuania has been actively developing a risk management methodology for automated quantitative investment.

 The central bank started a feasibility study, which will allow adopting long-term development strategies for investment-supporting information systems.

Aiming at maximum risk diversification, in 2017 the Bank of Lithuania upgraded its strategic asset allocation, which proved to be successful in 2018, ensuring the stability of the risk parity portfolio. The Bank of Lithuania was the first central bank in the world to implement such an innovative strategic asset allocation model, which has already garnered significant attention from other central banks.

In 2018, the Bank of Lithuania consistently worked on the implementation of the quantitative investment strategies project: it computerised market monitoring, ensured automated trading and trusted carefully selected algorithms with part of investment decision-making. At the same time, the central bank was also actively preparing for quantitative investment risk management.

In terms of managing its financial assets, the central bank launched a feasibility study, which will allow adopting long-term strategies for the development of investment-supporting information systems. In the long run, the chosen alternative must ensure a more rapid development of investment activities.



Composition of the strategic benchmark portfolio as at 31 December 2018

-  Money market instruments
-  US government bonds
-  US corporate bonds
-  European corporate bonds
-  Canada government bonds
-  UK government bonds
-  Inflation-linked bonds
-  Equity
-  China government bonds

5. To be one of the top three most efficient central banks in the Nordic-Baltic region



The Bank of Lithuania continued implementing its infrastructural project aimed at concentrating all activities under one roof.



The central bank implemented a budget planning and control system.



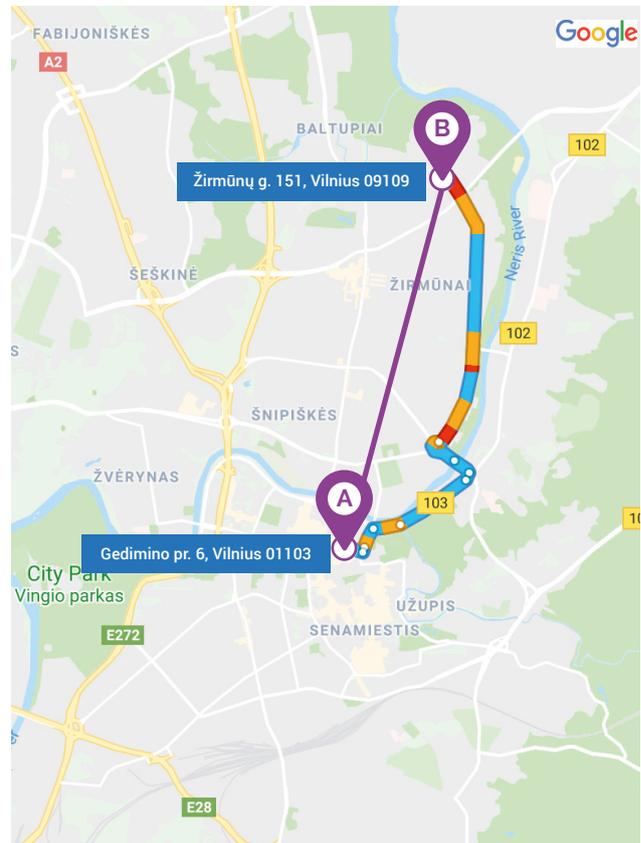
It launched an e-shop for purchasing numismatic items.



The Bank of Lithuania introduced a customer query and incident management system.

The Bank of Lithuania seeks to be a modern and efficient organisation, managing and organising its activities based on best management practices. Pursuing its aim to optimise internal and operational costs, the Bank of Lithuania continued implementing its infrastructural project aimed at concentrating all of the central bank's activities under one roof (Žirmūnų g. 151, Vilnius). The central bank also reviewed its organisational and management strategies related to internal transport services seeking to optimise its transport facilities and cut exploitation costs. The Bank of Lithuania reduced the number of its private vehicles and started renting electric cars. The operating costs of the Bank of Lithuania have been steadily decreasing.

Keeping up to date with the latest technology trends, the Bank of Lithuania has been reviewing its IT infrastructure, looking for standard market solutions and implementing them in practice. In 2018, the Bank of Lithuania acquired new systems, started projects for upgrading the credit register, implemented budget planning and control systems, as well as launched an e-shop for purchasing numismatic items and a customer query and incident management system. Modern information systems allow for more flexibility, acceleration of operating procedures and more efficient service provision.



Managing its internal activities, the Bank of Lithuania has been strengthening its competence in process management. In 2018, the central bank launched pilot projects for implementing LEAN system tools in order to objectively evaluate its performance, assess and effectively address emerging issues, as well as plan and manage business processes in a more efficient manner. The Bank of Lithuania has been also reviewing and improving its project management processes. Taking into account operational risks, it also improved its personnel management systems and strengthened the central bank's employer image by attracting and retaining new talents. One of the achievements that came along with the changed labour relations regulation was the new Bank of Lithuania collective agreement.

Real economy

-  Lithuania's economy grew by 3.4% in 2018.
-  Domestic demand was the main driver of economic growth.
-  Household consumption was mainly underpinned by the rising household disposable income.
-  Investment growth almost reached its five-year peak.
-  Rather robust growth contributed to the widening output gap.

economic growth in 2018 could have been even stronger. As a result, the value added generated in agriculture in the second half of 2018 was almost 15% lower than the year before. The value added in other sectors increased at a rather rapid and steady pace, close to 4%. It should be noted that the relatively fast economic expansion, which has been maintained for some time, leads to a widening positive output gap, which shows the extent to which the current economic development has deviated from its sustainable path. A widening output gap leads to imbalances, which are now mostly noticeable in the labour market.

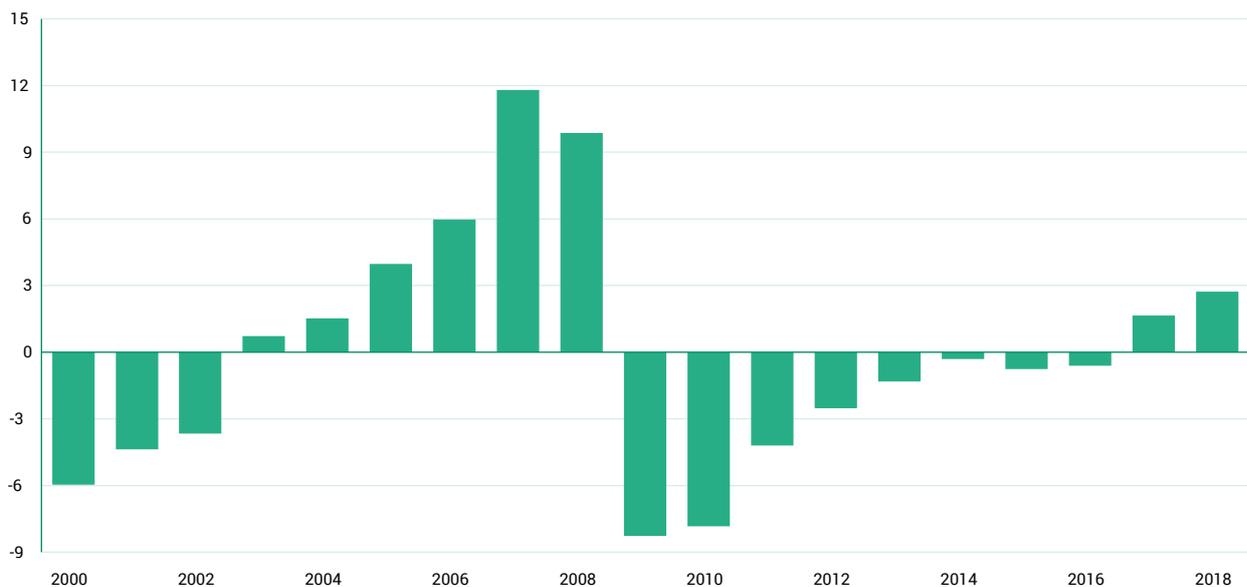
Strong growth was mainly fuelled by domestic demand, particularly household consumption. The main driver of household consumption was the rapid growth in household disposable income, which is likely to have hit its ten-year peak in 2018. Such evolution was largely attributable to labour market tensions and government decisions. According to the Bank of Lithuania estimates, in 2018 these decisions could have increased household disposable income by up to €635 million and added 2.3 percentage points to disposable income growth.

In 2018, investment growth almost reached its five-year peak. This was mainly driven by the upswing in construction of engineering buildings, which to a large extent came from recovering EU capital flows – in 2018, they increased by almost a third. The most prominent engineering construction projects include the cogeneration power plant, the modernisation and expansion of water supply and sewage networks as well as transport infrastructure.

Despite weakening external demand, economic growth in Lithuania remained robust, reaching 3.4% (adjusted for seasonal and workday effects). If not for the poor grain harvest caused by drought, which took out several percentage points,

Output gap

Percentage of GDP



Sources: Statistics Lithuania and Bank of Lithuania calculations.

Price dynamics

 Average annual inflation in Lithuania stood at 2.5% in 2018.

 The average annual change of food prices was roughly 2%.

 Fuel prices accounted for nearly a fifth of average annual inflation in 2018.

 Administered prices increased by 0.9%.

 Service prices continued to grow steadily with their annual change slightly above 4%.

After a rapid rise in domestic consumer prices in 2017, annual headline inflation decreased to 2.5% in 2018. This was attributable to price components that are most closely linked to domestic economic developments (specifically – service prices) and the evolving trends in global commodity, particularly oil, markets.

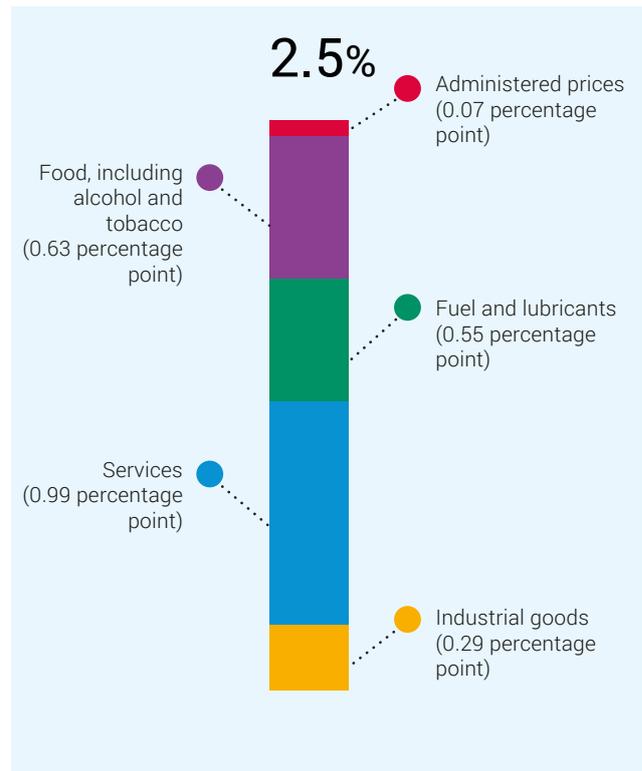
Sharp increases in global oil prices put upward pressure on inflation. In 2018, oil prices reached their four-year peak, reflecting concerns over the potential oil supply disruptions due to tensions between the US and Iran, as well as the political turmoil in such major oil-exporting countries as Venezuela and Libya. However, having reached the highest point in recent years, oil prices dropped sharply at the end of 2018. This was led by escalating market concerns over the global economic outlook and the higher-than-projected oil supply.

Slightly more than half of inflation was attributable to underlying inflation. The latter is underpinned by price components that are most closely linked to domestic economic developments, particularly service prices. In 2018, underlying inflation, which covers prices of industrial goods, went down slightly. This, however, was mainly determined by short-term factors, i.e. prices for passenger transport by air which soared during the summer months of 2017 but, due to the base effect, saw a significant year-on-year drop in the summer of 2018. Excluding the contribution of the already-mentioned prices, underlying inflation remained rather stable, driven by

continued upward pressure of domestic economic factors, for example, robust wage growth, which had been outpacing labour productivity, and rising domestic demand, both of which contributed to the increase in service prices.

Growth in food prices (including alcohol and tobacco) has moderated, reflecting the zero rise in excise duties on alcoholic beverages in 2018, the slightly weaker impact of increased excise duties on tobacco compared to 2017, the decline in global food commodity prices and the considerable drop in farm-gate prices for basic agricultural products. As a result, food prices, including alcohol and tobacco, attributed for a much smaller share of inflation than in 2017.

Contributions to average annual inflation in 2018



Sources: Statistics Lithuania and Bank of Lithuania calculations.

Labour market



Labour market developments are underpinned by labour shortages.



In 2018, the number of arrivals to Lithuania almost equalled that of departures.



Unemployment in Lithuania stood at 6.1%, in the country's largest cities – 3.8%, in the rest of the country – 7.6%.



Wages increased sharply – wage growth reached almost 10%. Wage increases in the public sector accelerated.

also linked to higher immigration. Reaching its highest level since 1990, immigration was boosted by looser Lithuanian immigration policy, which for the past two years resulted in approximately triple the usual number of immigrants from non-EU countries, as well as the increased number of returning emigrants.

Labour shortages have eased due to more favourable migration trends and a more conservative assessment of demand for new workers. Nonetheless, labour shortages still affect a considerable number of companies and are the main driver of rapid wage growth. Such shortages are attributable to the fact that in Lithuania's largest cities the unemployment rate fell to 3.8%. In the rest of the country unemployment is much higher and accounts for 7.6%; still, the number of unemployed persons that have marketable skills could be relatively small.

Government decisions and rather substantial tensions in the labour market led to rapid wage increases. Wages in the private sector increased by 9.4%. Similar growth trends have been observed for the past two years, which means that wage growth acceleration in the sector is losing steam. A significant change in wage dynamics, however, has been observed in the public sector. Having been rising at around 6-7% for a prolonged period of time, public sector wages increased by 10.2% in 2018. This was mainly the result of the decision to substantially raise wages for workers in higher education and healthcare.

The number of arrivals to Lithuania almost equalled that of departures. One of the contributing factors to the broadly balanced migration flows was emigration, which has reached its lowest point since the start of economic recovery. This was mainly attributed to Brexit, which led to a significantly smaller outflow of people to the UK, and improvements in Lithuania's labour market conditions. The balance in migration flows was

Wage dynamics



Monetary policy of the Eurosystem

Decisions



In 2018, the Eurosystem continued to maintain a strong accommodative monetary policy stance to ensure the continued sustained convergence of inflation towards levels below, but close to, 2% over the medium term:

- » In June 2018, the Governing Council announced that it would end net asset purchases and expects the key ECB interest rates to remain at their present levels at least through the summer of 2019.
- » At the end of December 2018, the Eurosystem ended net purchases under the extended APP and continued its reinvestment policy.
- » In March 2019, the Governing Council announced that it expects the key ECB interest rates to remain at their present levels at least through the end of 2019; it also plans to launch TLTRO-III.

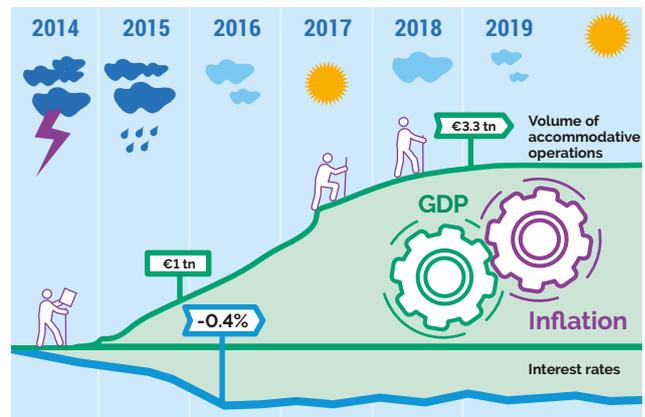
In 2018, the Eurosystem gradually reduced the monthly pace of net asset purchases under the expanded APP, ultimately ending them at the end of the year. Taking into account the latest macroeconomic projections and uncertainties surrounding the inflation outlook, in June 2018 the Governing Council announced that it expects to end net asset purchases under the expanded APP at the end of the year. The Governing Council continued to make net purchases at the monthly pace of €30 billion until the end of September 2018, reducing the pace to €15 billion in October-December. Amid expectations of continued sustainable adjustment in the path of inflation towards the target rate and economic growth acceleration supported by domestic demand, the Eurosystem ended net purchases at the end of December 2018, as intended. From the start of 2019, purchases only include reinvestment, in full, of the principal payments from maturing securities. By reinvesting, the Eurosystem will keep the stock of acquired securities consistent for an extended period of time past the date when the key ECB interest rates will be raised.

The Governing Council provided more information on forward guidance on the key ECB interest rates. In June 2018, the Governing Council announced that it expects the key ECB interest rates to remain at their present levels at least through the summer of 2019 and in any case for as long as necessary to ensure that the evolution of inflation remains aligned with the current expectations of a sustained adjustment

path. In March 2019, in response to revised economic and inflation projections and increased risks, the Governing Council enhanced its forward guidance, announcing that it expects the key ECB interest rates to remain at their present levels at least through the end of 2019.

In March 2019, the Governing Council announced that the Eurosystem will launch a new series of TLTRO. The decision was taken in view of the latest macroeconomic projections and the inflation outlook. The quarterly operations will start in September 2019 and end in March 2021, each with a maturity of two years. They will feature built-in incentives for banks to increase crediting, which will help to preserve favourable bank lending conditions and the smooth transmission of monetary policy to the real economy.

Volume of accommodative monetary policy operations (extended APP and TLTRO) and short-term interest rate evolution



Factual euro area macroeconomic indicators and their March 2019 projections (annual percentage change)

	2018	2019	2020	2021
Real GDP	1.9	1.1	1.6	1.5
HICP	1.7	1.2	1.5	1.6
Unemployment rate	8.2	7.9	7.7	7.5
Compensation per employee	2.2	2.1	2.4	2.6

Monetary policy of the Eurosystem

Measures



The operational framework of the Eurosystem consists of the following set of instruments: open market operations, standing facilities and minimum reserve requirements.



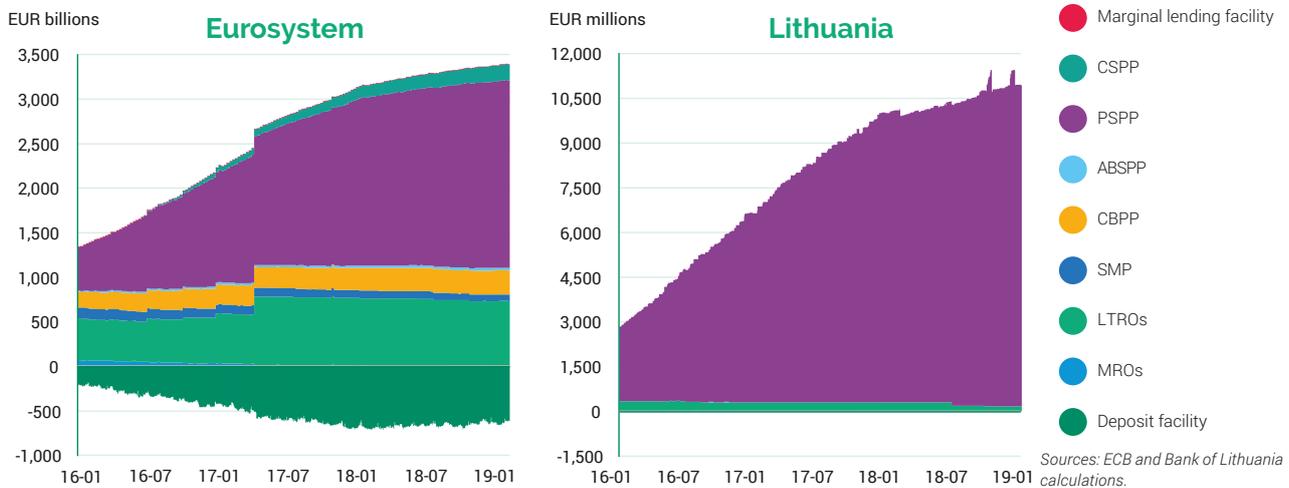
In 2018, the Eurosystem injected into the financial market €240.6 billion, of which €0.9 billion was injected by the Bank of Lithuania.

In 2018, the Eurosystem carried out 113 open market operations via tenders. At the end of 2018, the outstanding amount of funds borrowed by counterparties under MROs was

€8.2 billion, through LTROs (including TLTROs) – €723.8 billion. The latter was lower on a year-on-year basis as counterparties started to repay their TLTRO borrowings early. The Bank of Lithuania counterparties had also made early repayments (€0.1 million), thus the total amount of funds borrowed decreased to €0.2 billion. In the period under review, the Bank of Lithuania counterparties took recourse to the marginal lending facility on several occasions and borrowed, on average, €16.2 million.

Under the expanded APP, which includes the third CBPP, the ABSPP, the CSPP and the PSPP, the Eurosystem increased the securities portfolio held for monetary policy purposes by €272.5 billion – to €2,658.5 billion. In 2018, on account of monthly purchases of the government securities of the Republic of Lithuania and bonds of the European supranational institutions, the Bank of Lithuania increased the securities portfolio by €1.1 billion to €10.8 billion, of which government securities of the Republic of Lithuania account for €1.9 billion, bonds of the European supranational institutions – €8.9 billion. Due to redemptions, the PSPP portfolio saw more significant volatility in February, October and December.

Liquidity-providing and liquidity-absorbing monetary policy operations of the Eurosystem



Minimum reserves, current account holdings, recourse to deposit and marginal lending facilities

Indicator	Region	Volume at the end of the year, EUR	Annual change, %	Annual average, EUR	Highest value, EUR	Lowest value, EUR
Minimum reserves	Eurosystem	1274 billion	2.9	125.2 billion	1274 billion	123.8 billion
	Lithuania	221.7 million	4.7	211.3 million	221.7 million	203.1 million
Current account holdings	Eurosystem	1,299.8 billion	9.6	1,244.5 billion	1,439.6 billion	1,185.8 billion
	Lithuania	5,997.1 million	18.1	4,152.4 million	5,997.1 million	3,183.7 million
Recourse to deposit facility	Eurosystem	613.6 billion	-11.8	659.4 billion	715.1 billion	571.1 billion
	Lithuania	0.0 million	0.0	0.0 million	0.0 million	0.0 million
Recourse to marginal lending facility	Eurosystem	0.1 billion	-83.3	0.1 billion	0.7 billion	0.0 billion
	Lithuania	16.2 million	-	0.0 million	16.2 million	0.0 million

Source: Bank of Lithuania calculations.

Monetary policy of the Eurosystem

Impact



In 2018, the accommodative stance of the Eurosystem's monetary policy continued to exert a positive impact on Lithuania and other euro area economies:

- » Bank funding costs remained historically low.
- » The cost of borrowing in financial markets for governments and corporates fluctuated but remained low as well.
- » Bank lending to the real economy continued to increase.

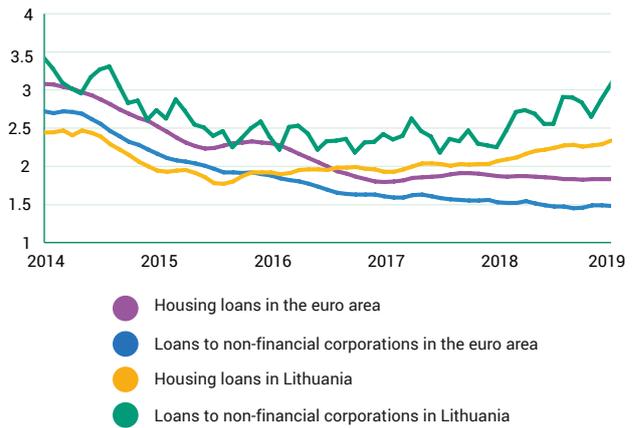
In 2018, short-term interbank lending rates remained broadly unchanged and stood at record low levels. They were close to the ECB deposit facility rate (-0.4%).

Although borrowing conditions for governments and corporates varied, they remained more favourable than in mid-2014. The yields of euro area and Lithuanian government bonds have been decreasing significantly since 2014, when market expectations regarding the adoption of non-standard monetary policy instruments heightened. Later, however, a large share of fluctuations was also driven by other factors. With escalating uncertainty over the new Italian government's policy, the cost of its debt rose substantially in 2018. At the same time, the yields of particularly safe assets, for instance, German bonds, showed a slight downward trend due to increased market uncertainty. In 2018, the yields of Lithuanian government bonds fluctuated within a narrow range and remained almost unchanged. The yields of euro area corporate bonds were broadly in line with those of government bonds – the most significant increase was observed in the borrowing cost for riskier corporations.

The Eurosystem's accommodative monetary policy measures have remained a contributing factor to historically low interest rates in the euro area and Lithuania. Interest rates in the euro area showed no significant changes in 2018, thus remaining at their historical lows. Recently, the average interest rates on new loans in Lithuania (especially those for non-financial corporations) have somewhat increased, remaining above the euro area average. This was likely caused by the worsening competitive environment given the recent increase in concentration in the banking sector. The rate of lending to the private non-financial sector in the euro area and Lithuania remained high: in December 2018, the annual growth rate of loans to households and non-financial corporations in the euro area stood at 3.2% and 3.9% respectively, in Lithuania – at 8.7% and 3.2%.

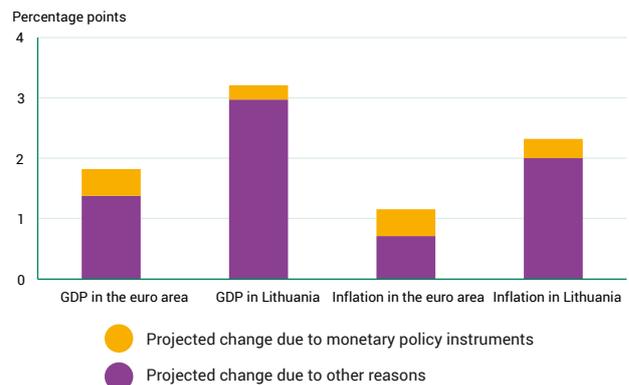
It should be noted that the Eurosystem's accommodative monetary policy contributes to the acceleration of economic growth in Lithuania and the euro area. ECB experts project that in 2016-2019 the Eurosystem's accommodative monetary policy will add 1.7 percentage points to both euro area growth and inflation. The Bank of Lithuania estimates it to translate into

Average interest rates on new MFI housing loans and loans to non-financial corporations



Sources: ECB and Bank of Lithuania calculations.
Note: 3-month moving average.

Projected impact of the Eurosystem's accommodative monetary policy on real GDP growth and inflation in the euro area and Lithuania in 2016-2019 (yearly average)



Sources: ECB, Thomson Reuters Datastream, Bank of Lithuania calculations.

0.9 and 1.3 percentage points for Lithuania respectively. The more pronounced impact on the euro area may be explained by higher debt levels and more developed financial markets. The accommodative policy stimulates Lithuania's economy mainly through the tradable sector – stronger demand in the euro area and depreciation of the euro have opened up more possibilities for the country's exporters.

Macroprudential policy

Analysis of systemic risks

 Imbalances in the Nordic countries and their potential impact on parent banks remain the key risks to Lithuania's financial system.

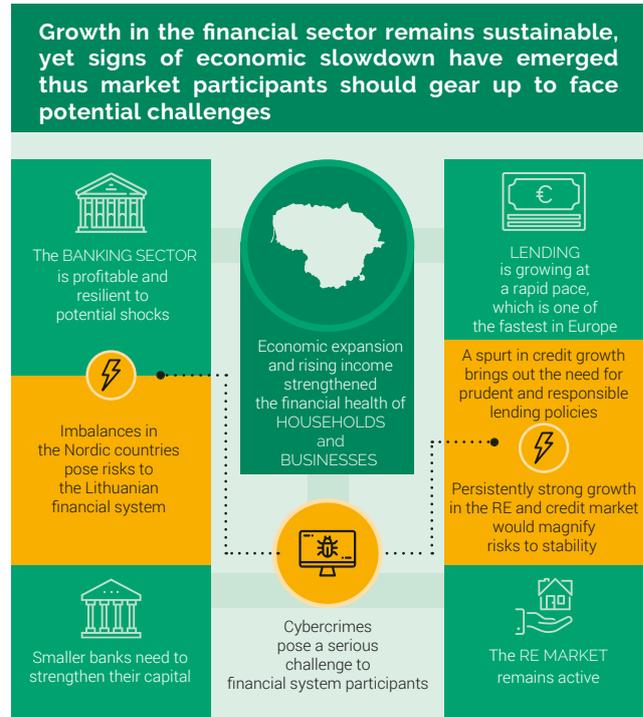
 The rapid growth of the RE market and crediting in Lithuania is yet another systemic risk.

 Cybersecurity risks are not subsiding.

The potential negative impact of imbalances in the Nordic countries on parent banks has remained broadly unchanged over the recent years. Although house prices in Sweden have dropped, while remaining almost unchanged in Norway, uncertainty over house price developments in these countries remains high, hence a scenario of their more rapid decline should not be disregarded. Given that the high household indebtedness in Sweden and Norway continues to grow, the falling house prices could lead to bank losses and an overall economic slowdown or even an economic collapse in these countries.

Nordic banks still finance a rather large share of their business with resources attracted in international financial markets. Tensions in individual regions (e.g. Brexit, trade wars between the US and China) may raise borrowing costs in international markets, making borrowing more expensive for Nordic banks, in which case the costs of lending by subsidiary banks may increase accordingly.

The ongoing rapid growth of housing loans in Lithuania can lead to imbalances in the RE market. Housing loan and RE market activity remains robust. If such a trend were to prevail, the relative indebtedness level would pick up, which would enhance the adverse effects of unfavourable shocks. Expectations regarding the country's economic outlook (including future development of the RE market) remain optimistic. Therefore, the cost of borrowing for house purchase and RE prices are expected to continue on an upward climb. However, this risk



is mitigated by high housing supply, the sustainable financial health of households and macroprudential policy instruments implemented by the Bank of Lithuania.

Given the rising number of cyber attacks, challenges related to cybersecurity are not subsiding. This is especially relevant to Lithuania's financial system participants as they are more and more inclined to provide services online so as to enhance operating efficiency. Challenges related to cybersecurity will remain relevant in the future, yet potential adverse effects are mitigated by new safety measures.

Macroprudential policy

Credit and the real estate market

 Credit in Lithuania continued to grow, mainly stimulated by lending to households.

 Lending to businesses was active, yet growth in the corporate loan portfolio slowed down due to amortisation of individual large-scale loans.

 Growth of the housing loan portfolio was still one of the strongest in Europe.

 Albeit still strong, growth in house prices decelerated.

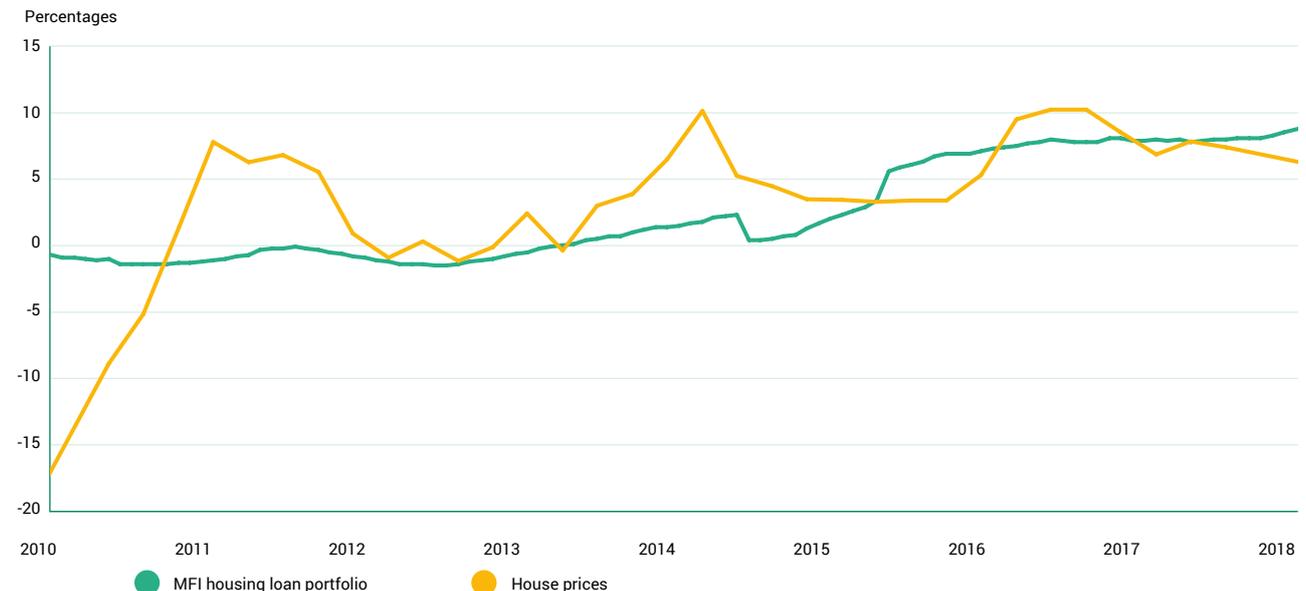
 RE market activity remains at historic highs.

 According to market participant projections, house prices in 2019 will continue rising at a similar pace as last year.

In 2018, crediting in Lithuania remained active – similarly to 2017, the portfolio of loans to the private non-financial sector increased by 6.0%. This was mainly driven by lending to households: the annual growth rate of the portfolio of loans to households increased and reached 8.7% at the end of 2018, reflecting sustained activity in the RE market. The portfolio of loans to non-financial corporations expanded by 3.2% year on year, i.e. somewhat less than in 2017 due to amortisation of individual large-scale loans in the information and communication as well as energy sector.

In 2018, the number of housing transactions increased by 2% and has been the highest over the last decade. Amid heightened activity in the housing market, the annual growth rate of house prices in Lithuania increased and stood at 6.6%, a significant drop compared to 2017. House price dynamics showed pronounced regional heterogeneity: house prices in Vilnius increased by 3.5%, in the remainder of the country – by 9.1%. According to surveys conducted by the Bank of Lithuania, banks and professional RE market participants expect that, in comparison to 2018, house prices in 2019 will increase at a similar rate.

Annual change in the MFI housing loan portfolio and house prices



Source: Bank of Lithuania.

Macroprudential policy

Macroprudential policy instruments



The CCyB rate was increased to 1%.



The Bank of Lithuania identified 4 systemically important financial institutions, which were set additional capital buffers.



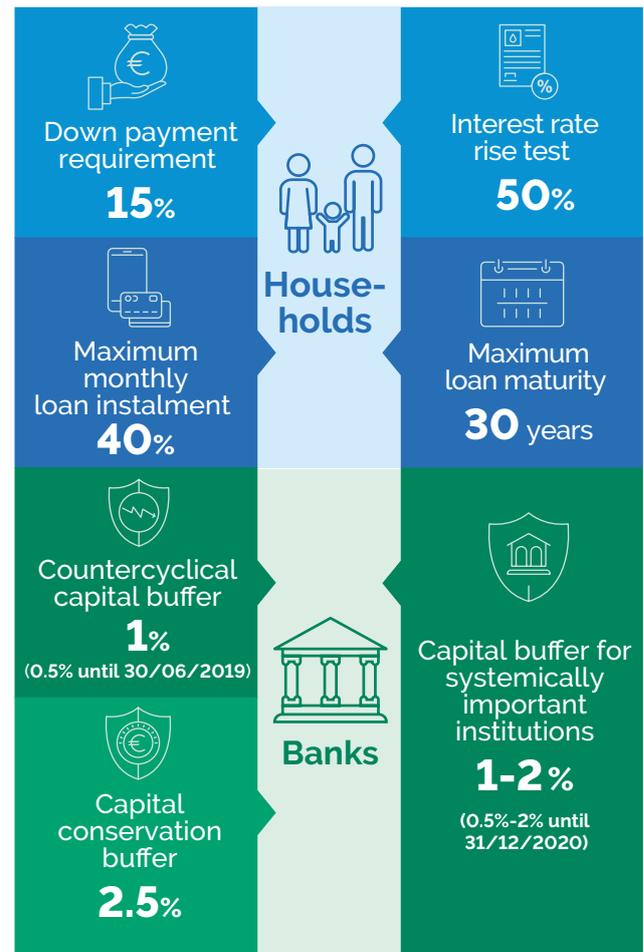
The Bank of Lithuania reviewed its Macroprudential Policy Strategy and extended the list of macroprudential policy instruments

In view of recent credit and RE market trends and seeking to increase the resilience of the financial system, on 20 June 2018 the Bank of Lithuania took the decision to increase the CCyB rate³, which is revised on a quarterly basis, from 0.5% to 1%. The increased CCyB rate will come into effect on 30 June 2019. Until then the CCyB rate of 0.5%, which came into force on 31 December 2018, will remain valid. The countercyclical capital buffer helps strengthen the resilience of the financial system to potential shocks. When faced with shocks or economic recession, the capital requirement might be relaxed, thus allowing credit institutions to maintain sufficient credit supply.

During the 2018 assessment, as the year before, the Bank of Lithuania identified 4 systemically important institutions and set them additional capital buffers. The O-SII capital buffer set for AB SEB bankas, Luminor Bank AB, and Swedbank, AB, remained unchanged at 2%. Since the systemic importance of AB Šiaulių bankas grew, its O-SII capital buffer was increased from 0.5% to 1%; the bank has to accumulate it by 31 December 2020. On 2 January 2019 Luminor Bank AB became the Lithuanian branch of Luminor Bank AS, which is headquartered in Estonia, hence its previously-set O-SII capital buffer is no longer valid.

The Bank of Lithuania continued to actively implement its macroprudential policy mandate. Taking into account macroprudential policy changes in recent years, in 2018 the Bank of Lithuania reviewed its Macroprudential Policy Strategy. The Strategy now defines in more detail recognition

Macroprudential policy instruments implemented in Lithuania



and reciprocity of macroprudential policy instruments applied by other Member States as well as includes an extended list of available macroprudential policy instruments. The key household lending principles and ratios set in the Responsible Lending Regulations remained unchanged.

³ Resolution No 03-105 of the Board of the Bank of Lithuania of 20 June 2018 on the application of the countercyclical capital buffer.

Management of financial assets

Investment policy and composition



In managing financial assets, the Bank of Lithuania seeks to ensure stability of the financial system, create conditions for smooth monetary policy implementation, ensure financial independence and provide a buffer against economic shocks.



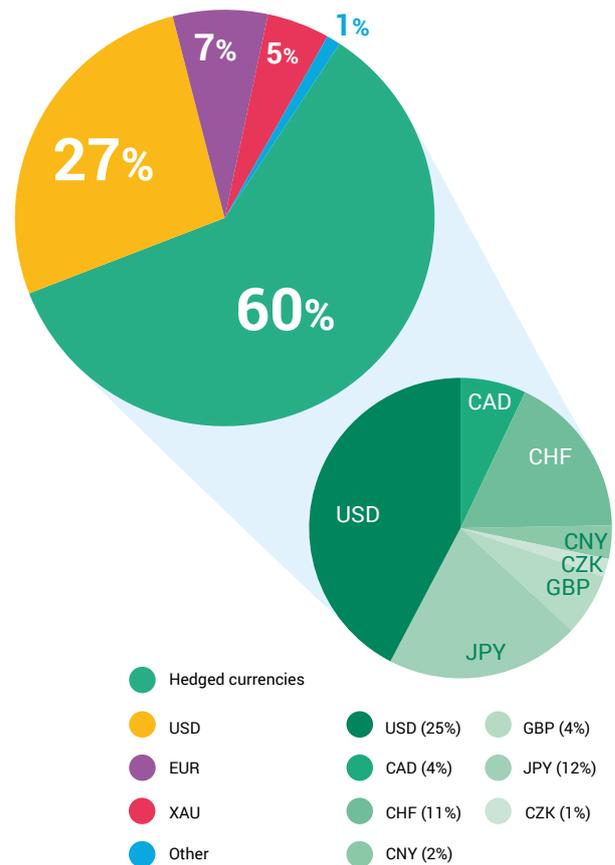
The main bulk of its financial assets is invested in money market instruments and US government bonds. The Bank of Lithuania holds 5.8 tones of gold.

In 2018, the main bulk of the Bank of Lithuania's investments was in euro or other currencies (US dollar, Japanese yen, pound sterling, Czech koruna, Chinese renminbi, Swiss franc, Canadian dollar) with hedged currency risk. Aiming at higher investment diversification, the currency risk of part of investments (in 2018 – 28% on average) was not hedged. The majority of investments with unhedged currency risk were in US dollar.

Security of financial assets is ensured through diversifying investment, concluding transactions with investment-grade rating financial institutions that are of good repute, and investing only in debt securities with an investment grade rating. The investment grade rating assigned to financial institutions and issuers of debt securities by international rating agencies indicates low probability of default on their liabilities. At the end of 2018, the average investment rating was AA-, while 42% of investments were rated AAA (the highest rating).

In terms of financial instruments, the majority of investments made in 2018 were in government bonds and money market instruments. The Bank of Lithuania invested in securities issued by various governments, government agencies, international organisations and municipalities. Money market instruments mainly consisted of deposits in other central banks and international organisations. Lithuania's gold is held at the Bank of England. Under favourable market conditions, gold is invested in gold deposits, thus earning interest, or through gold swaps, i.e. temporarily exchanging gold into other currencies and then investing them.

Average investment composition by currency



Average investment composition



Management of financial assets

Investment goals and results



The Bank of Lithuania invests financial assets with the aim of diversifying risk and increasing expected return over a rolling three-year investment horizon.



The three-year return was 3.21%, or €80.5 million.

The three-year return on the Bank of Lithuania's financial assets not related to monetary policy operations and liabilities was 3.21%, or €80.5 million.

In 2018, the Bank of Lithuania's financial assets not related to monetary policy operations and liabilities amounted to, on average, €4,189 million, while return on these assets in euro (adjusted for exchange rate changes but non-adjusted for gold price changes) reached 0.78%.

The Bank of Lithuania's gold reserves remained unchanged, amounting to 5.8 tones. Due to a leap in the gold market value in the fourth quarter of 2018, return on the gold portfolio was positive and reached 3.49%.

Due to potentially higher returns in the medium term, the Bank of Lithuania tolerates the risk of short-term loss, the size of which, with high probability, should not exceed the risk budget predefined in the investment policy (currently – €150 million). The risk budget is set at a 95% confidence level, which means that €150 million or higher losses may, on the average, be incurred only once over a 20-year period.

In 2018, financial market developments weighed on Bank of Lithuania investment. The increase in the market price of gold and appreciation of the US dollar had a positive effect on investment return. However, the rapid rise in government bond yields across many regions, especially the US, and pessimistic sentiment in equity markets dampened investment results.

Return on investment

Percentages



- Return on financial assets not related to monetary policy operations and liabilities (non-adjusted for exchange rate and gold price changes)
- Return on financial assets not related to monetary policy operations and liabilities (non-adjusted for gold price changes)

Payments

-  The use of services offered via the Bank of Lithuania's payment system CENTROlink increased significantly.
-  CENTROlink started offering instant payment services.
-  The Bank of Lithuania oversees its payment system CENTROlink and a securities settlement system.
-  Together with other central banks, the Bank of Lithuania assessed the T2S platform and changes within RT1.

CENTROlink, a payment system operated by the Bank of Lithuania, offers a full range of SEPA services. CENTROlink users include credit, payment and e-money institutions from both Lithuania and other EEA countries. In 2018, they initiated 11.2 million SEPA credit transfers and received 8.3 million transfers from STEP2. The number of SEPA credit transfers rose 15 times year on year. Over the year, the largest increase was recorded in the number of payments initiated by e-money and payment institutions (160%). In 2018, 34 new payment service providers started using CENTROlink services, which added up to a total of 62 institutions (51 of which were e-money or payment institutions) at the end of the year.

Since August 2018, a few of the payment service providers using CENTROlink started offering instant payments. Instant payments are available 24/7/365; the payer's funds are

immediately transferred to the payee even if they are clients of different payment service providers in different countries. Since its launch, the system's clients initiated more than 250 thousand instant payments.

As a member of the Eurosystem and co-owner of the TIPS platform, the Bank of Lithuania has been ready to provide TIPS-related services since November 2018. TIPS is a TARGET instant payment settlement service offered by Eurosystem central banks. The platform enables reaching different instant payment service providers across Europe.

Together with other Eurosystem central banks, the Bank of Lithuania manages TARGET2, a real time system for gross settlements in euro. The Bank of Lithuania is responsible for a component of this system – the payment system TARGET2-LIETUVOS BANKAS. It is used for urgent payments, payments that implement Eurosystem monetary policy instruments, and the settlement of cash transactions between the Bank of Lithuania and credit institutions. In 2018, TARGET2-LIETUVOS BANKAS processed 64 thousand payments, amounting to a total of €107 billion.

The Bank of Lithuania oversees its payment system CENTROlink and a securities settlement system (VPAS). The Bank of Lithuania regularly monitored the systems and focused on ensuring their effective performance and management of system-related risks.

The Bank of Lithuania, together with the ECB and other Eurosystem central banks, contributes to the reliable and efficient functioning of other payment systems and infrastructures important to Lithuania's market. The central bank participated in a joint assessment of the compliance of TARGET2-Securities – the European securities settlement engine – with the CPSS-IOSCO Principles for Financial Market Infrastructures. Furthermore, together with other central banks, it monitored and assessed changes within the European instant payment system RT1.

Market infrastructure in Lithuania and transactions executed



Payments



The share of residents using payment service packages increased to 67%.



A new payment service comparison tool was introduced in a fee comparison website run by the Bank of Lithuania.



The central bank launched a public consultation on the introduction of additional Open Banking measures in Lithuania.

The Bank of Lithuania revised the maximum fee methodology for the basic payment account, based on which the maximum monthly fee in 2019 was left unchanged (€1.5). The revised methodology foresees that the maximum fee for the basic payment account service is to be set in view of the average fee for payment service packages that are most similar to the basic payment account service. In addition, the determined price cap cannot exceed a certain share of average per capita household consumption expenditure. Payment service packages, which allow to receive various payment services for a fixed fee, are gaining traction. According to the results of a survey commissioned by the Bank of Lithuania, two-thirds of account holders in Lithuania used payment service packages in 2018, compared to a half in 2017.

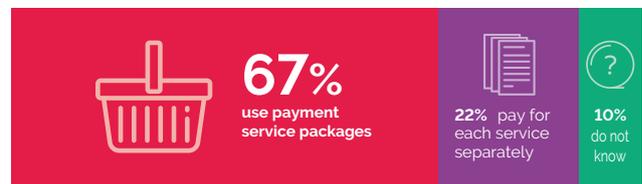
The Bank of Lithuania updated its payment service fee comparison website and introduced a new tool that allows comparing payment service fees and prices of payment service packages. The website now provides the fees for the most often used payment services as well as the composition and prices of payment service packages for various resident groups (youth, seniors, those receiving their salary to the account of a chosen payment service provider). The tool allows comparing the prices of services in various credit institutions using different pricing methods. The comparison website uses standard terms for payment services, which are also used in the Fee Information Document and the Statement of Fees provided by payment service providers. The latter includes all fees paid for using a payment account and payment services during a specified period.

The Bank of Lithuania launched a public consultation on Open Banking in Lithuania. At the end of 2018, the Bank of Lithuania launched a public consultation on the introduction of additional Open Banking measures in Lithuania. During the

consultation, the central bank consulted with the Association of Lithuanian Banks and different FinTech and payment institution associations. Furthermore, representatives of the UK's Open Banking Implementation Entity, leaders in implementing Open Banking, were invited to share their experience and knowledge. The results of the public consultation are available on the Bank of Lithuania [website](#). The Bank of Lithuania is currently actively involved in the work of the ERPB working group on a potential SEPA API Access Scheme that will contribute to further development of Open Banking.

The Bank of Lithuania signed an international Memorandum of Understanding which will contribute to increasing competition between companies processing payment card transactions in the EU. The memorandum on cooperation in implementing a provision of the EU Regulation requiring to separate payment card schemes (VISA, Mastercard) and card payment processing was signed by the competent authorities of the UK, the Netherlands, Denmark, Finland, Czech Republic, Belgium, Italy and Lithuania.

Choice of pricing method for payment services in Lithuania



Source: Survey of residents commissioned by the Bank of Lithuania.



www.lb.lt/ikainiai

Payment service fees and prices of payment service packages can be compared on the Bank of Lithuania's website

Supervision

Financial market

 The number of financial market participants under supervision has been gradually increasing: at the beginning of 2019, the Bank of Lithuania supervised more than 530 market participants whose assets exceeded €46 billion.

 Information on market participants and their operating results as well as reviews on their activities are published on the [Bank of Lithuania website](#).

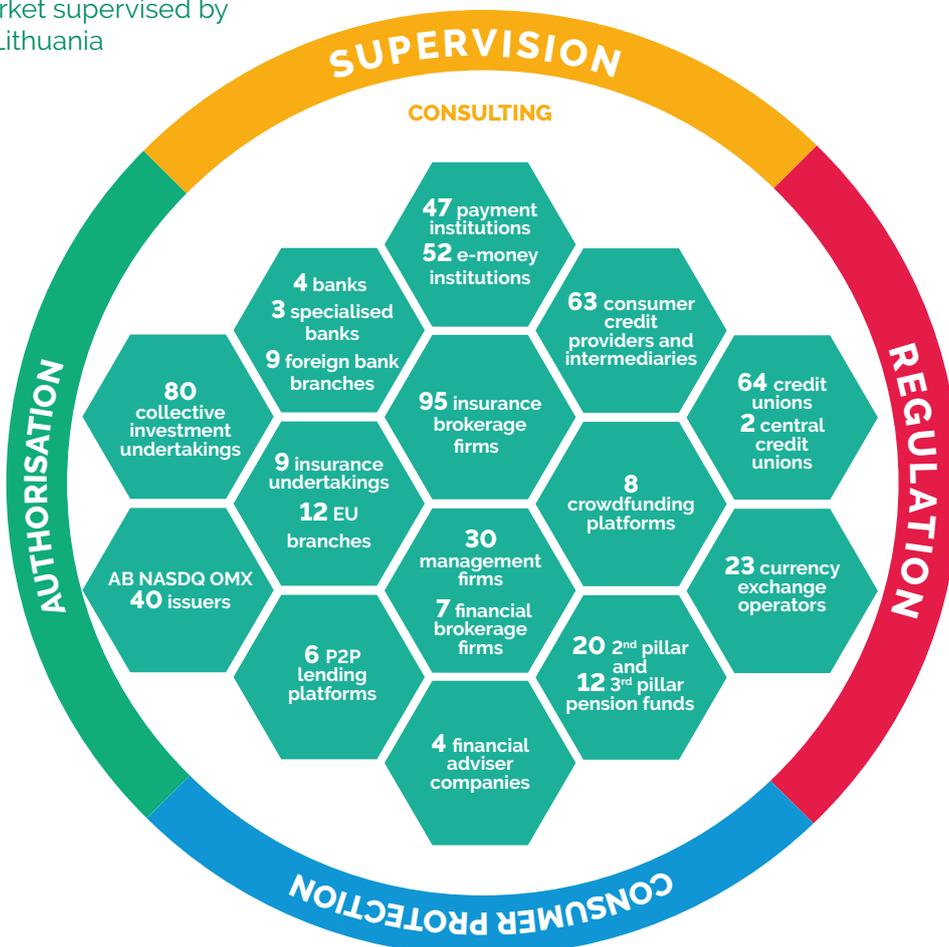
European Merchant UAB, and AB Mano banks (at the beginning of 2019 the first two were not yet in operation). AB Mano banks, which was established after the credit union Mano unija had been issued a specialised bank licence and was subsequently reorganised, became operational on 2 January 2019.

Following the completion of the consolidation process of Luminor Bank AB, its Lithuanian licence was revoked with effect from January 2019. Starting from 2019, its activities have been carried out via the Lithuanian branch of Luminor Bank AS, headquartered in Estonia. The licence of AB Citadele banks was also revoked with effect from January 2019. The bank will carry out its activities as the Lithuanian branch of the Latvian company AS Citadele banka.

In 2018, market participants continued to show avid interest in Lithuanian licences. These were mainly foreign FinTech businesses (companies from the UK and other EU countries, Israel, Asia) as such licences granted authorisation to provide payment services across the EU. In 2018, the number of meetings with potential market participants doubled (exceeding 160). Overall, the Bank of Lithuania issued 34 licences. Based on survey results, the number of applications for licences in 2019 is not expected to decline.

At the end of 2018, 6 banks and 7 foreign bank branches were active in Lithuania, yet the end of the year witnessed some significant changes, which in 2019 will influence the statistics on banks and foreign bank branches. The ECB granted a specialised bank licence to Revolut Bank UAB,

Financial market supervised by the Bank of Lithuania



Supervision

Consultation and inspection of supervised entities

 The Bank of Lithuania provides consultations to market participants within its supervisory competence.

 Seeking to improve the supervisory environment, the Bank of Lithuania consults with financial market participants.

 Financial market participants are informed in advance on the planned regulatory changes.

 The Bank of Lithuania conducts a periodical survey to determine financial market participants' view on the quality of its supervisory practices.



Seeking to create an advanced and attractive regulatory and supervisory environment, since 2017 the Bank of Lithuania has been publishing the deadlines and scope of its routine inspections and investigations.

A survey of financial market participants conducted in 2018 shows that the majority of respondents (65%) are satisfied with the quality of supervision, 84% of them believe that the supervisory measures employed are effective and are fully satisfied in terms of communication with the regulator, while more than half of the surveyed are pleased with the overall consultation process as well as the clarity and effectiveness of the drafted legal acts.

The Bank of Lithuania organises annual meetings with members of the board of banks and insurance companies as well as the management of foreign bank branches and branches of other EU Member State insurance companies in order to discuss annual results, present plans for the next year and intended changes in the regulatory environment. Before or after drafting legal acts, market participants are given presentations so as to inform them on the amendments introduced, consult

them and answer their questions. The majority of consultations are given individually via phone, email or in writing. In 2018, the Bank of Lithuania held more than 30 meetings with compliance officers to discuss relevant regulatory issues related to financial and insurance services (regulation of investment and insurance services, pension system reform, credit service regulation, etc.).

In 2018, the Bank of Lithuania received a number of questions regarding licensed activities, content and structure requirements for licensing documents, requirements applicable to specific activities, exemptions for new market participants, online document submission, etc. Active participants are most often consulted on supervisory reporting.

Within the frame of its consulting activities, the Bank of Lithuania publishes guidelines and recommendations on relevant financial market regulatory issues, thus aiming to provide more clarity on existing legal acts and regulatory expectations in terms of market participants as well as to formulate best market practices.

Supervision

Prudential supervision



In carrying out financial market supervision, the Bank of Lithuania mainly focused on areas exposed to highest risk.



It carried out 11 inspections, conducted 2 on-site visits and revoked 4 licences.



The Bank of Lithuania carried out the annual Supervisory Review and Evaluation Process (SREP).



Under the Solvency II Directive, it conducted an annual comprehensive risk assessment of insurance undertakings.

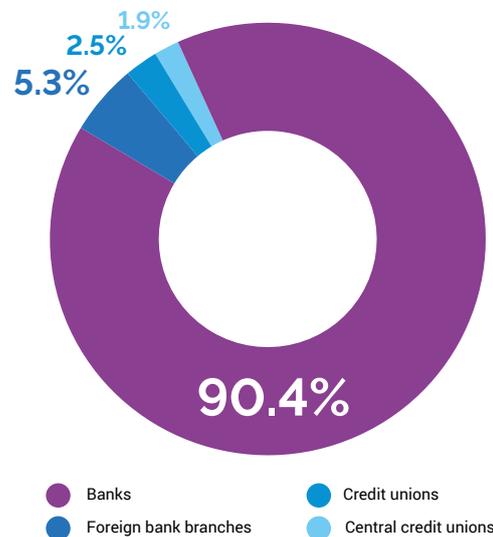
Banks remained stable: as before their assets were mainly comprised of loans, while deposits accounted for the main bulk of their liabilities. The expanding loan portfolio remained the main contributor to growing bank assets and profits. All banks complied with their capital adequacy requirements. In 2018, banks' liquid asset reserves continued to increase, thus, their liquidity level was particularly high.

The insurance market maintained momentum in 2018 – total insurance premiums reached nearly €0.89 billion. Market growth was driven by a 12.2% increase in the non-life insurance sector, whereas the life assurance sector expanded by 7.3%. In terms of insurance premiums, non-life insurance comprised more than 70% of the entire insurance market. Transport insurance accounted for almost two thirds of the non-life insurance portfolio. Unit-linked life assurance accounted for more than 60% of the life assurance portfolio. Insurance undertakings earned more than €42 million. All insurance undertakings were solvent and complied with their solvency capital requirements. Insurance brokerage firms operated at a profit, earning €31 million.

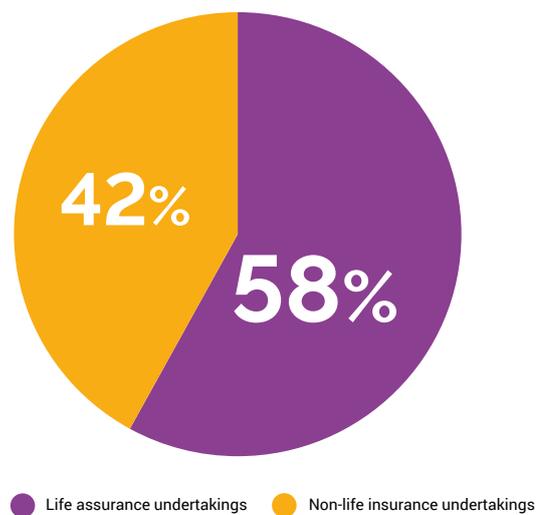
The reformed credit union sector was profitable, credit unions complied with their prudential requirements. Due to reorganisation by merger, the number of credit unions (members of the Lithuanian Central Credit Union) decreased. Credit unions optimised their activities and increased effectiveness, which, in turn, had a positive impact on the sector's results – credit unions earned €3 million in unaudited profits in 2018. Rising profitability

and growing sustainable shares, accounting for 90% of the share capital at the end of 2018, suggest that credit unions' capital base will further increase. Accepted deposits have remained the main source for financing credit union activities.

Banking and credit union sector by assets



Insurance market by assets



Supervision

Licensing



The Bank of Lithuania authorised 28 e-money and payment institutions, 1 credit union, 9 management and investment companies, 2 insurance brokerage firms.



3 specialised bank licences were granted in Lithuania.



The central bank received 4 applications for a specialised bank licence and 1 application for a banking licence.



4 credit unions were permitted to restructure into specialised banks.



3 companies were included in the public lists of crowdfunding and P2P lending platform operators.



The Bank of Lithuania revoked 4 licences (2 payment institution licences and 2 credit union licences).

In 2018, the Bank of Lithuania received 1 application for a banking licence and 4 applications for a specialised bank licence. It is important to note that licences for specialised banks are issued by the ECB.

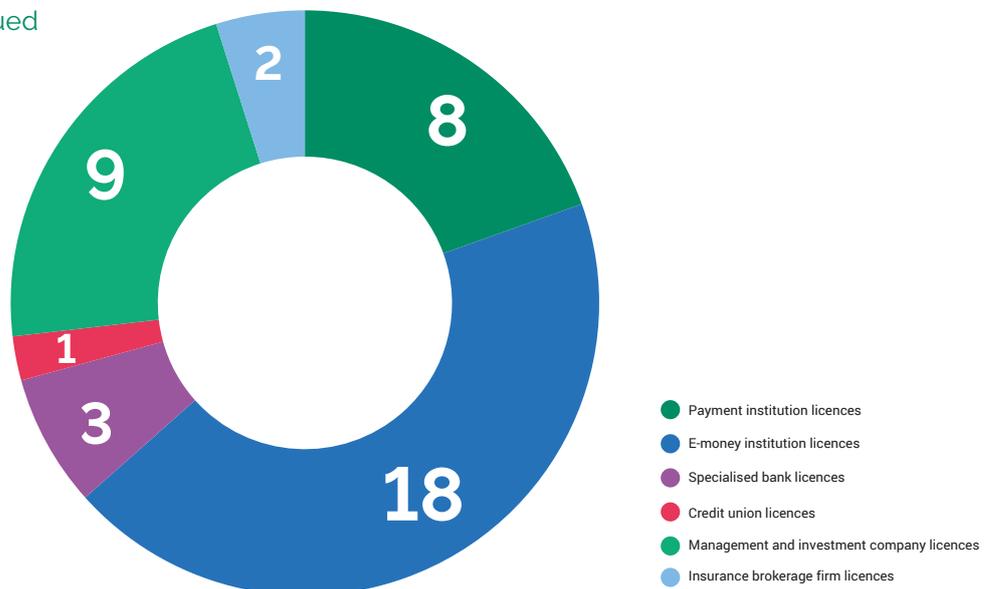
FinTech companies were issued 28 licences in 2018 – almost as much as in 2017 (29 licences). Having met with more than 160 potential market participants to discuss the possibilities of setting up in Lithuania, currently the Bank of Lithuania is assessing more than 60 applications.

With a view to making Lithuania a FinTech hub in the Nordic-Baltic region, the Bank of Lithuania aims at creating a FinTech-friendly environment that would attract new companies and encourage them to incubate new products in the country. The Bank of Lithuania has already developed a one-stop shop, set up a dedicated email for all queries on setting up in Lithuania, allowed foreign citizens to submit documents necessary for obtaining a licence in English, and updated the Lithuanian and English versions of its Licensing Guide. The Bank of Lithuania website has a section dubbed the Newcomer Programme, which in a concise and clear manner presents key information for new market entrants.

In 2018, the central bank developed and launched a regulatory sandbox that will allow companies developing innovative financial products to test their business solutions in a live environment under the guidance and supervision of the Bank of Lithuania. Selection of eligible participants will be based on [certain criteria](#).

The Bank of Lithuania introduced its electronic licensing tool: now all companies are able to take care of the necessary paperwork and procedures electronically.

Licences issued



Supervision

Supervision of financial services



The Bank of Lithuania investigated more than 1,500 complaints and inquiries from natural and legal persons regarding financial service providers' compliance with legislative requirements (in 2017 – more than 700).



38 enforcement measures and binding instructions were imposed for the violation of legal acts regulating financial services.



Access to 11 websites offering illegal investment, insurance or other financial services in Lithuania was blocked.



To assess the situation in the financial services market, the Bank of Lithuania conducted thematic reviews, based on which financial market participants were given recommendations.



Greater attention was paid to consumer credit advertising.

Given the rising popularity of household insurance, **the Bank of Lithuania carried out an analysis of Lithuania's consumer household insurance product market.** The analysis identified risks to household insurance service users (consumers) that may arise throughout the life-cycle of the household insurance product (product supervision and management, product distribution, administration of insured events) and provided recommendations for insurance undertakings to mitigate these risks.

The Bank of Lithuania conducted a desk-based review regarding disclosure of pre-contractual information when concluding mortgage credit agreements. The aim of the review was to assess whether standard information provided to the consumer meets legislative requirements, compliance with time limits laid down in legal acts (e.g. time period for deliberation) and other requirements. The Bank of Lithuania also investigated mortgage credit agreements in order to assess whether they include all required information. Shortcomings identified during the review and examples of best practises were presented to credit providers.

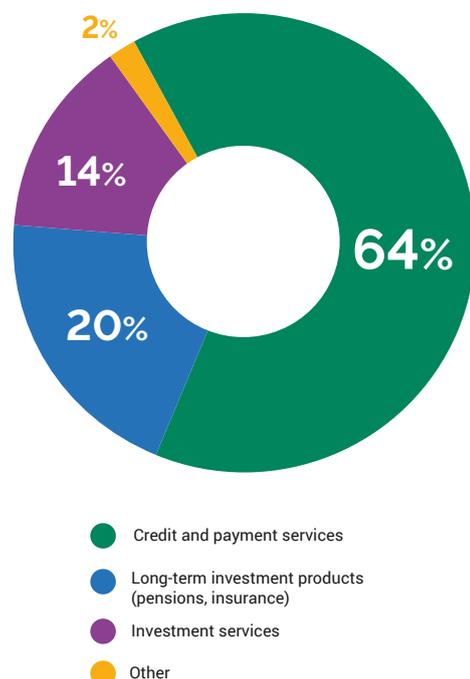
The Bank of Lithuania conducted an e-shop websites review regarding specified payment methods and procedures. Having concluded the investigation, the central bank informed that providers of goods and services have no right to charge consumers a fee for paying with payment cards, via internet banking or using other payment methods, and must return the fee if it has already been charged.

The Bank of Lithuania investigated nearly 20 complaints regarding potentially inadequate consumer credit advertising, conducted 5 related investigations and imposed almost **€190 thousand in fines** for identified breaches of legal acts. The largest fine imposed on a market participant was €150 thousand.

Supervisory actions



Distribution of complaints and inquiries regarding financial services



Supervision

Supervision of financial services



Significant regulatory changes to pension accumulation have come into effect on 1 January 2019.



Amendments to laws regulating the activities of CIUs, which promote the development of capital markets, have come into effect on 1 February 2019.



The Bank of Lithuania took a stand in support of minority shareholders.

shares of foreign alternative CIUs to retail investors in Lithuania, ensure more flexibility in regulating investment company activities, and reduce the administrative burden for CIUs. CIUs for informed investors comprise the majority of investment companies and investment funds currently being established in Lithuania. To this end, the Bank of Lithuania, together with investment managers and representatives of their associations, is standardising documents of such CIUs which will allow streamlining the process of setting up investment companies and funds intended for informed investors.

Repeated offences and disregard for minority shareholders will not be tolerated. At the beginning of 2018, the Bank of Lithuania created a precedent when it imposed fines on two issuers: AB Snaigė was fined €207 thousand for repeatedly failing to comply with the International Financial Reporting Standards (IFRS) and earlier binding instructions, while AB Žemaitijos pienas was fined €158 thousand and given a warning for repeated failure to comply with the IFRS and binding instructions, and inappropriate disclosure of information. The central bank clearly stated that a majority shareholder cannot abuse its position and a management body of a company must act in the best interest of all shareholders and the company as a whole.

Amendments to laws regulating the activities of CIUs that came into effect on 1 February 2019 will simplify licensing and authorisation procedures, increase competition in the depository market, allow the marketing of investment units or

Main changes in the pension accumulation system

 <p>Life-cycle pension funds</p>	<p>The main idea behind life-cycle pension funds is to assume higher risk at the start of accumulation, receiving highest possible investment returns, and reduce the investment risk as the retirement age approaches, thus preserving the accumulated assets. The risky investment portion is adjusted automatically with regard to the age of the pension fund participants.</p>
 <p>Changes in contributions</p>	<p>The old system allowed accumulating under the formula 2%+2%+2% or 2%+0%+0%. Now a contribution to the pension fund accounts for 3% of a participant's wage and an additional government incentive amounting to 1.5% of the average wage. Persons who accumulated under the formula 2%+0%+0% can now choose to gradually increase their contribution (from 1.8% + 0.3% of the average wage in 2019 to 3% + 1.5% of the average wage in 2021).</p>
 <p>Reduced fees</p>	<p>The 2nd pillar pension fund management fee decreased on 1 January 2019. The asset management fee applied to life-cycle pension funds cannot exceed 0.8% (in 2018 – 1%) of the average annual value of a participant's accumulated funds. Subsequently, it will be reduced to 0.65% in 2020 and 0.5% from 2021 onwards.</p>
 <p>Automatic inclusion</p>	<p>Persons under 40 years of age who were not pension accumulation system participants will be automatically included into the system; however, they will be able to opt out upon their request.</p>
 <p>Opportunity to make larger contributions and receive a PIT concession</p>	<p>2nd pillar pension fund participants can make additional voluntary contributions to their fund and be granted a personal income tax (PIT) concession.</p>

Out-of-court settlement of disputes between consumers and financial market participants



In 2018, the Bank of Lithuania settled 535 disputes.



The Bank of Lithuania took 206 decisions regarding the subject matter of a dispute.



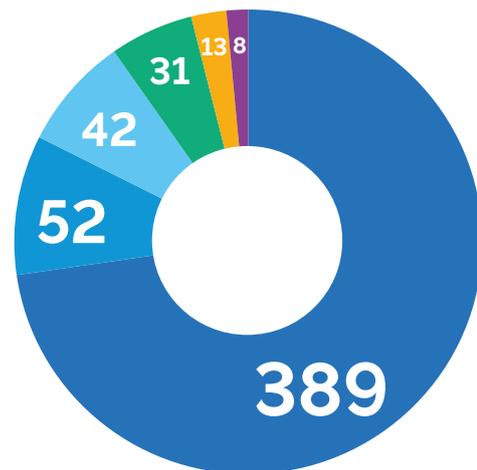
Financial market participants implemented 89% recommendations given by the Bank of Lithuania – the highest number since 2012.



The average duration for dispute settlement was 68 calendar days (in 2017 – 74).

During the reporting period, a total of 35% of Bank of Lithuania decisions was made in favour of consumers, while financial market participants implemented 89% of recommendations given by the Bank of Lithuania (the highest number since 2012). 8 recommendations were not implemented (6 by insurance undertakings, 2 – other financial market participants). The list of depersonalised decisions of the Bank of Lithuania regarding the [subject matter of a dispute](#) and [financial market participants that have not implemented recommendations specified in these decisions](#) is published on the website of the Bank of Lithuania. More information on the settlement of consumer disputes in 2018 is available in the [Report on the Out-of-court Settlement of Consumer Disputes](#).

Disputes by type of financial service



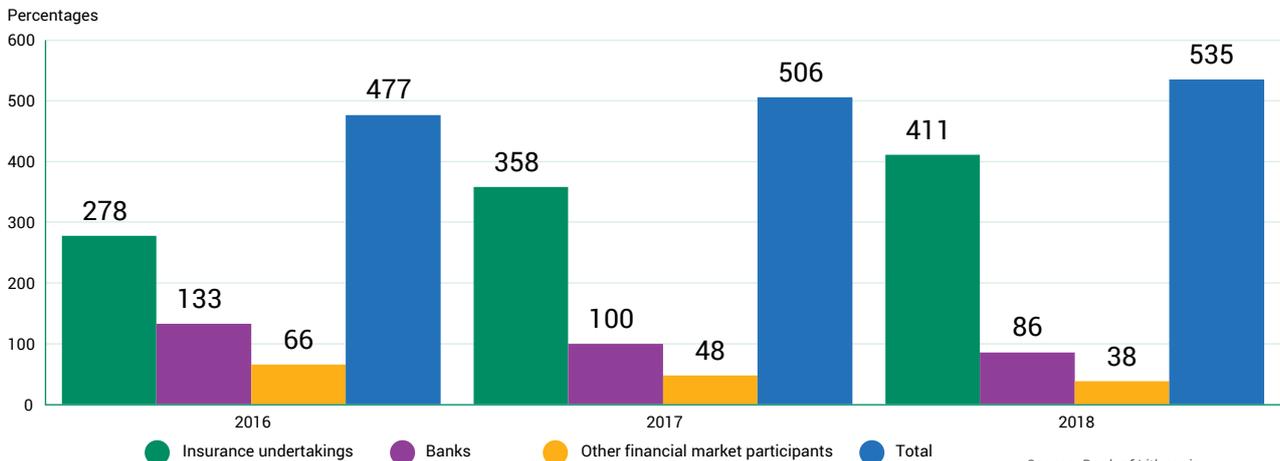
- Non-life insurance
- Payment services
- Credit services
- Life assurance
- Other financial services
- Non-financial services

In 2018, 77% of all disputes settled at the Bank of Lithuania involved insurance undertakings, disputes with banks accounted for 16%, while the remaining 7% involved other financial market participants. As usual, the majority of disputes with insurers were over property insurance (114) and compulsory MTPL insurance (110). 72 disputes arose over land vehicles (other than railway rolling stock) insurance (CASCO). Most disputes in the banking sector generally occurred over payment (46) and credit (26) services.

The Bank of Lithuania always aims at ensuring that the parties to the dispute reach a peaceful settlement. In 2018, 85 disputes ended in peaceful resolution, a year-on-year increase of 12%.

In addition, the Bank of Lithuania organised preventive meetings with individual market participants to discuss the results of out-of-court consumer dispute settlement.

Disputes by financial market participant



Source: Bank of Lithuania.

Bank resolution

 In 2018, the Single Resolution Fund accumulated €24.9 billion in contributions paid by euro area banks.

 The Bank of Lithuania prepared and approved resolution plans covering around 90% of Lithuania's banking sector.

 At the beginning of 2019, the Bank of Lithuania helped to organise and took part in the joint Nordic-Baltic Crisis Simulation exercise. Lessons learned will contribute to improving coordination and decision-making process at the domestic and regional level.

 In the course of the review of the Bank Recovery and Resolution Directive (BRRD) at the Council of the European Union, the Bank of Lithuania formed a position on priority issues and provided expert support for the Ministry of Finance.

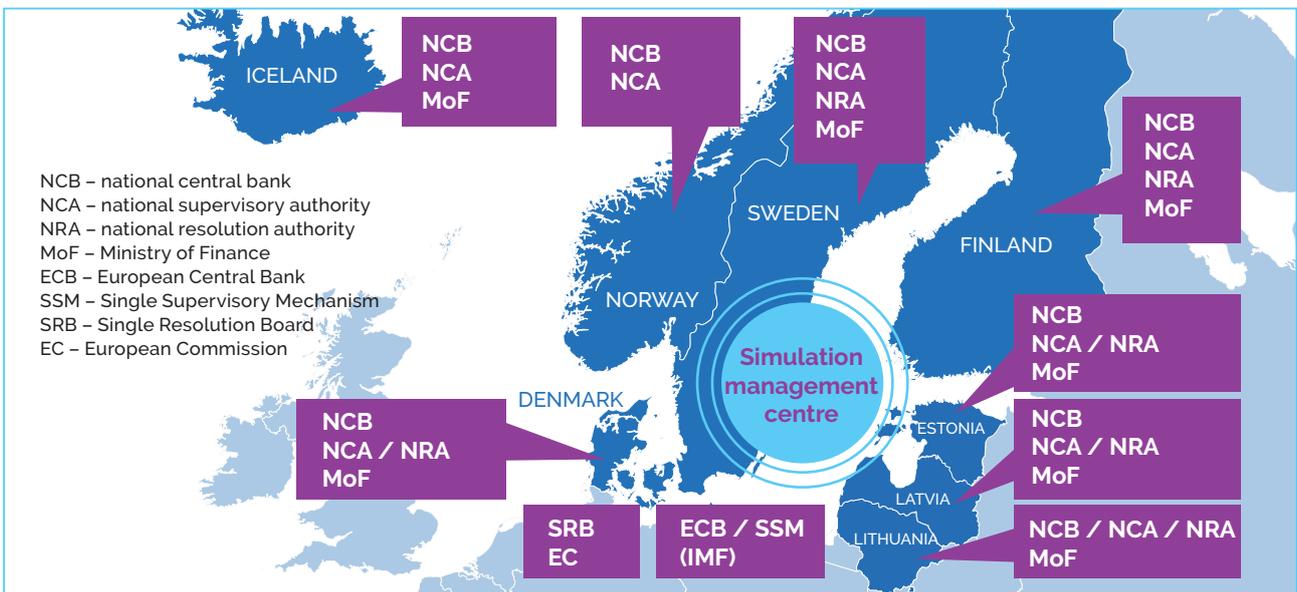
In 2018, the Single Resolution Fund accumulated €24.9 billion in contributions paid by euro area banks. Over the year, banks operating in Lithuania paid €6.6 million in ex-ante contributions (all 19 euro area countries banks – €7.5 billion), which were transferred to the Single Resolution Fund. The target level of the Single Resolution Fund to be reached by 2024 is at least 1% of the amount of covered deposits of all credit institutions within the Banking Union, i.e. €60 billion.

In carrying out its mandate as a resolution authority, the Bank of Lithuania helps to ensure efficient resolution and continuous operation of failing banks without the government's assistance. To this end, in 2018, the Bank of Lithuania prepared and approved the first resolution plans for Lithuanian banks, i.e. AB Šiaulių bankas and UAB Medicinos bankas. Furthermore, together with the Single Resolution Board and the Swedish, Danish, Estonian and Latvian resolution authorities, it prepared resolution plans for other international banking groups. In 2018, resolution plans for Sweden's SEB and Swedbank, Latvia's Citadele and Denmark's Danske banking groups, including subsidiaries operating in Lithuania, were updated. The plans provide for a binding consolidated minimum requirement for own funds and eligible liabilities (MREL), i.e. an additional financial security measure that would ensure sufficient resources for absorbing losses and restoring capital positions for failing banks. The MREL target for subsidiary banks will be set in the coming years.

At the beginning of 2019, the Bank of Lithuania helped to organise and took part in the joint Nordic-Baltic Crisis Simulation exercise. The exercise involved representatives from 31 competent national authorities from Denmark, Estonia, Finland, Iceland, Latvia, Lithuania, Norway, Sweden and competent EU authorities – the European Commission and the Single Resolution Board. The exercise assessed respective Nordic-Baltic authorities' capacities to manage crises and ensure regional cooperation. Lessons learned during the exercise will allow improving interinstitutional cooperation and decision-making processes at the domestic and Nordic-Baltic level.

In 2018, the Bank of Lithuania continued to take an active part in the review of the legal basis of the EU resolution framework – the Bank Recovery and Resolution Directive (BRRD). The Bank of Lithuania provided expert support for the Ministry of Finance in forming the country's position at the Council of the European Union regarding the European Commission's proposal of November 2016 on the implementation of risk mitigating measures in the banking sector. The main focus was given to such issues as imposition of a moratorium, MREL targets for subsidiary banks and the transitional period for their accumulation.

Participants of the 2019 Nordic-Baltic Crisis Simulation exercise



Cash



The value of euro banknotes and coins issued into circulation by the Bank of Lithuania has been increasing at a steady pace.



The Bank of Lithuania exchanged into euro LTL 13.3 million in 2018. As at 31 December 2018, the total value of litas in circulation amounted to LTL 437 million.



It issued into circulation 9 collector and 2 commemorative euro coins as well as a numismatic set of circulation coins.



The Bank of Lithuania was granted more rights to assess the activities of cash handlers – respective amendments are detailed in the Republic of Lithuania Law on the Bank of Lithuania.



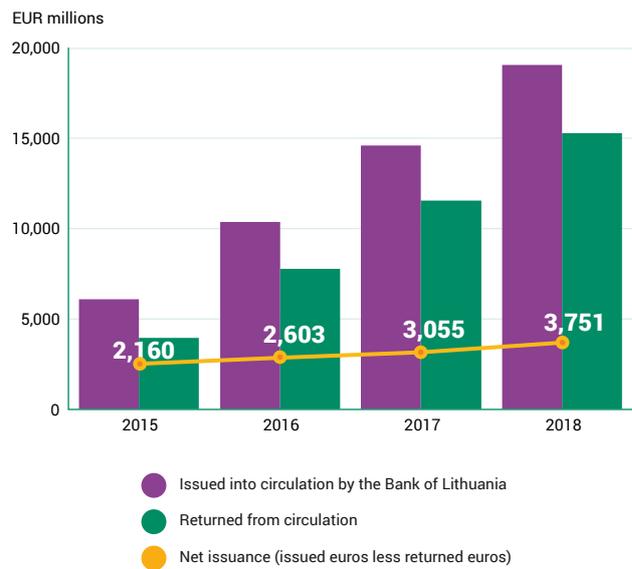
3,134 counterfeit euro banknotes and coins were withdrawn from circulation.

The value of euro banknotes and coins issued into circulation by the Bank of Lithuania has been increasing at a steady pace, which means that cash in Lithuania is still a popular means of payment and store of value. In 2018, the total value of euro banknotes and coins in circulation increased by 23%, to stand at €3,751 million.

In 2018, the ECB unveiled the new €100 and €200 banknotes with enhanced security features. They will enter into circulation on 28 May 2019.

On 26 January 2019, the Bank of Lithuania stopped the issuance

Euro banknotes and coins



of the €500 denomination. It will, however, remain legal tender and can therefore continue to be used as a means of payment for an unlimited period of time.

The Bank of Lithuania issued into circulation 9 collector and 2 commemorative euro coins as well as a numismatic set of circulation coins. Numismatic items commemorate historical events and personalities. Aiming to stay in tune with market needs, at the beginning of 2018, the Bank of Lithuania launched an [e-shop](#) for numismatic items, which has been gaining traction ever since.

3,134 counterfeit euro banknotes and coins were withdrawn from circulation in 2018 (2,728 in 2017). In total, the Bank of Lithuania withdrew from circulation 2,723 counterfeit euro banknotes, 411 counterfeit euro coins and a few counterfeit litas banknotes. The majority of counterfeit notes (89%) were €50 banknotes. In 2018, having received applications from natural and legal persons to exchange worn or damaged currency, the Bank of Lithuania examined the genuineness and acceptability of almost 46 thousand banknotes and coins.

Handling of statistics



Lithuania became the first Baltic State to apply SDDS Plus.



All statistical tasks arising from the ESCB membership were successfully completed.



The availability and visibility of statistics compiled by the Bank of Lithuania were increased.

In 2018, Lithuania adhered to the IMF Special Data Dissemination Standard Plus (SDDS Plus). As a result of the collective efforts between the Bank of Lithuania, the Ministry of Finance and Statistics Lithuania, Lithuania became the sixteenth country in the world and the first among the Baltic States to implement the SDDS Plus initiative, thus contributing to international efforts to enhance data availability, quality,

transparency and reliability. The standard is applied to economic and financial data intended to support financial stability at the national and international levels. Its purpose is to assist IMF member countries with regard to the publication of comprehensive, reliable and comparable statistical data.

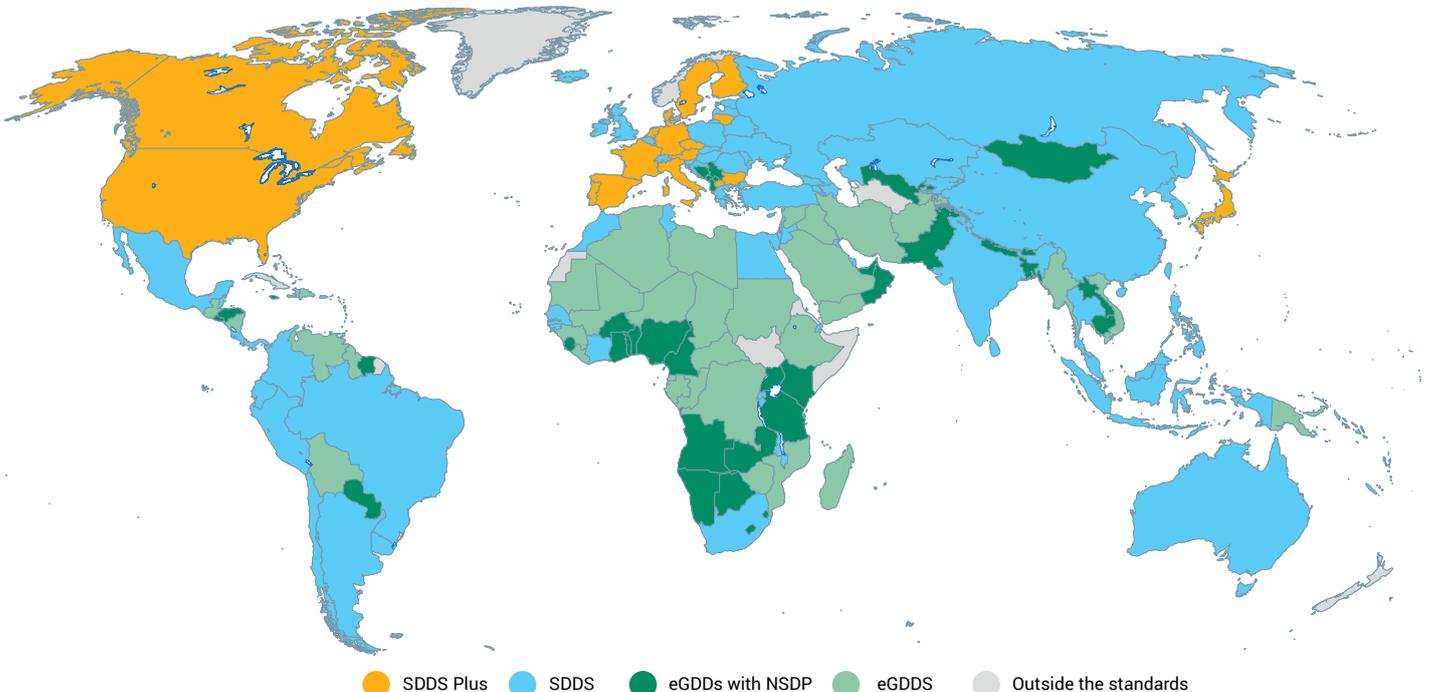
The central bank continued to develop financial statistics and published new statistics, which now also include:

- » aggregated data on 2nd and 3rd pillar pension funds;
- » annual growth rates of MFI loans, securities and deposits;
- » statistics on holdings of securities by certain reporting banking groups;
- » more detailed financial accounts statistics on households (including information on their investment goals), financial assets and liabilities of life and non-life insurance undertakings.

The Bank of Lithuania improved statistical data visualisation and enhanced its visibility.

The Bank of Lithuania website introduced interactive charts which may be flexibly adapted to user needs, while the visibility of statistics compiled by the Bank of Lithuania was increased through social networking tools.

SDDS Plus implementation across the world



Note: SDDS Plus – Special Data Dissemination Standard Plus, SDDS – Special Data Dissemination Standard, eGDDs – enhanced General Data Dissemination System, NSDP – National Summary Data Page.

Source: IMF (<https://dsbb.imf.org>).

Treasury agent

Administration of the accounts of the State Treasury and other institutions

 The Bank of Lithuania administered euro and foreign currency accounts of the Ministry of Finance, European Commission and World Bank Group.

 It executed 448 thousand credit transfers, amounting to €18.5 billion.

 Having assessed optimisation strategies for payment processes related to the State Treasury management, the joint working group created by the Bank of Lithuania and the Ministry of Finance proposed to consolidate public funds.

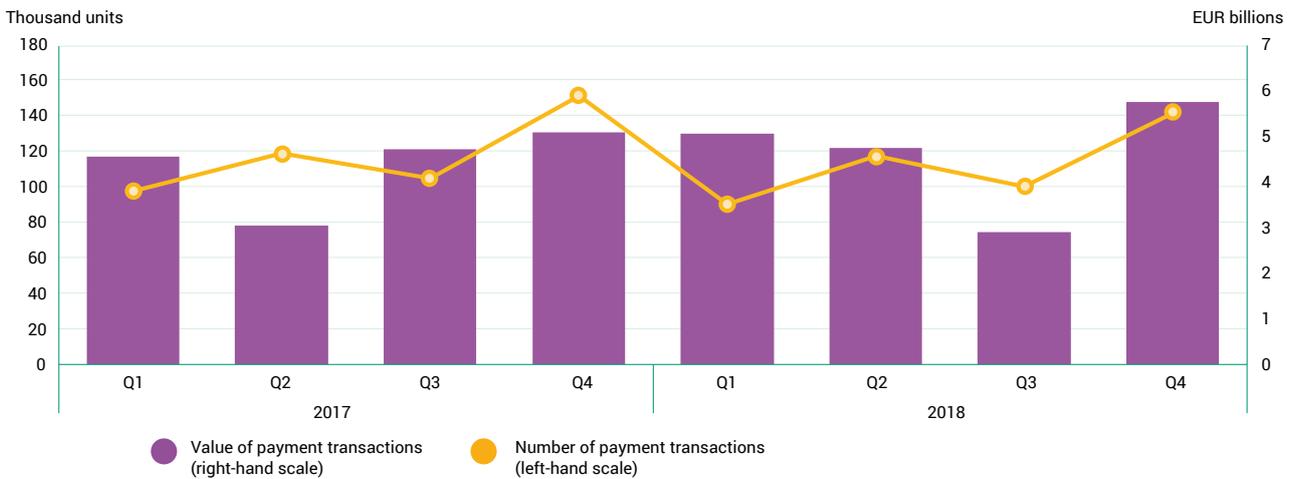
set forth by the State Treasury Law of the Republic of Lithuania and other legal acts. In addition, the Bank of Lithuania managed euro accounts of EU institutions and international financial institutions (hereinafter – other institutions). Monetary resources in the State Treasury accounts managed by the Ministry of Finance made up the largest share of funds held in all accounts.

As at 31 December 2018, the Bank of Lithuania administered 67 accounts of the State Treasury and other institutions (as at 31 December 2017 – 65). These accounts were opened and administered at the Bank of Lithuania in accordance with the legal acts of the Republic of Lithuania, the Bank of Lithuania and the ECB.

The following banking services are offered to the State Treasury and other institutions: payment services, foreign exchange transactions, account statements and other reporting services. In 2018, the Bank of Lithuania executed 448 thousand credit transfer instructions of the Ministry of Finance and other institutions; their total value amounted to €18.5 billion.

Having assessed optimisation strategies for payment processes related to the State Treasury management, the joint working group created by the Bank of Lithuania and the Ministry of Finance proposed to consolidate public funds and create a system that would allow (i) managing state payment processes more efficiently, (ii) upgrading Treasury information systems to ensure better management of public funds and (iii) optimising other related processes in light of current technology advancements. The consolidation process will cover local ministries, budgetary institutions, non-budgetary funds and funds of funds.

Acting as a State Treasury agent under the Republic of Lithuania Law on the Bank of Lithuania, **in 2018 the Bank of Lithuania administered euro and foreign currency accounts of the State Treasury.** The state monetary resources held in these accounts are managed by the Ministry of Finance. The resources are accumulated and used in accordance with the procedure



Organisation of activities

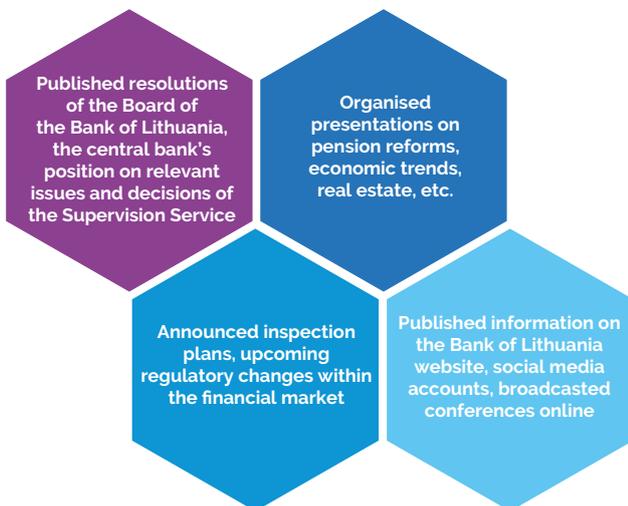
Staff and working environment

 The employees of the Bank of Lithuania are specialists that have high-level professional and academic qualifications and excellent analytical skills.

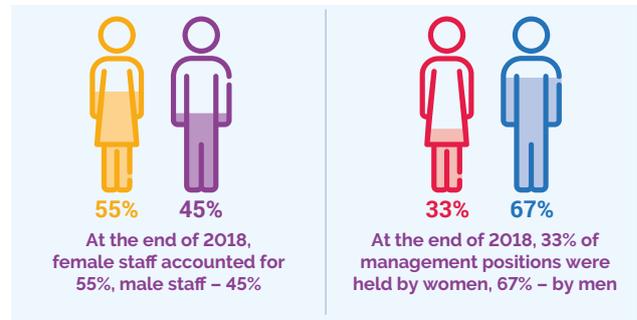
 On 31 December 2018, the number of actual staff positions at the Bank of Lithuania stood at 583.⁴

 In 2018, the overall staff turnover rate stood at 12%, 7% of which accounted for voluntary turnover.

 The Bank of Lithuania employees can work remotely, part-time or have flexible working hours.



The Bank of Lithuania employees improved their competence in the field of central banking, exchanged ideas and shared best practices with ECB experts. They also represented the Bank of Lithuania in international forums, cooperated with foreign institutions and their representatives. In 2018, nine Bank of Lithuania employees had a unique opportunity to work at the ECB under fixed-term contracts, one employee was appointed as Advisor to the Executive Director at the IMF for a 3-year term. Moreover, the Bank of Lithuania had its representative at the Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism. One staff

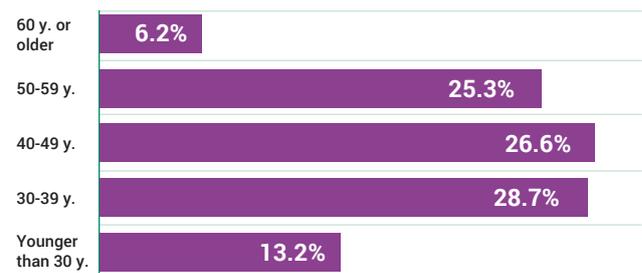


member took part in the Schuman Programme, which is aimed at encouraging short-term (6–9 months) mobility among the European central banks, gaining international experience and contributing to the activities of other European central banks.

In 2018, the Bank of Lithuania continued to strengthen and develop its employees' management and leadership competences and implemented practical tools to make its activities more efficient. The Bank of Lithuania continued its management development programme and trainings on organisational culture: during the annual Management Day, staff members in management positions discussed the role of management and the importance of its decisions in achieving organisational results, developing organisational culture and enhancing staff competences. In order to increase operational efficiency, two services of the Bank of Lithuania launched a pilot project for the implementation of the Asaichi system. Safety, health, civil and fire-prevention instructions and tests were transferred to a local e-learning platform.

The organisational structure of the Bank of Lithuania remained largely unchanged. The Bank of Lithuania has four services, namely the Banking Service, the Economics and Financial Stability Service, the Supervision Service and the Organisation Service. Expanding research capacities in both applied and basic research falls under the domain of the Centre for Excellence in Finance and Economic Research. The Bank of Lithuania's organisational structure also includes four autonomous departments and four autonomous divisions. The Banking Service was restructured in 2018 with the aim to mobilise market infrastructure professionals in a single structural unit, thus ensuring the efficient development of a competitive and advanced payments market in Lithuania.

Staff distribution by age



⁴ The number does not include 19 staff members who were on maternity/paternity leave and 9 employees who were on unpaid leave during their work at other institutions.

Research activities



 Economic research at the Bank of Lithuania is primarily conducted at the Center for Excellence in Finance and Economic Research (CEFER) and the Applied Macroeconomic Research Division (TMTS).

 Research carried out at TMTS plays a notable role in the decision-making process of the central bank.

 The aim of CEFER is to raise the quality of economic and financial research and encourage high-level discussion on relevant economic and financial issues.

-  Main fields of expertise:
- » Macroeconomic modelling
 - » International finance and macrofinance
 - » Impact of debt on the economy and households
 - » Labour economics and reform assessment
 - » Dynamic Stochastic General Equilibrium models
 - » Household consumption and income inequality

Quality economic and financial research. The joint initiative of CEFER, Vilnius University and Kaunas University of Technology helped to attract to the Bank of Lithuania PhD researchers from the leading US and European universities. CEFER aims at raising the quality of economic and financial research, encouraging high-level discussions on economic and financial issues and becoming the hub of economic and financial sciences in the Baltic region.

Top-tier international publications. In 2018, CEFER and TMTS published 13 working and discussion papers as well as 17 publications, some of which were featured in high-level international journals, such as Journal of Finance, Contemporary Economic Policy, Structural Change and Economic Dynamics, Quarterly Review of Economics and Finance, Economic Systems.

High-level conferences, seminars, workshops and research clusters across the Baltics. The Bank of Lithuania was one of the organisers of the first (inaugural) Baltic Economic Conference, which was held in Vilnius in June 2018. In a joint effort with the Central Bank Research Association, the National Bank of Poland and the Centre for Economic Policy Research, the central bank also organised a high-level biennial conference on Economic Spillovers in Warsaw (it received over 100 applications from world-renowned economists). The Bank of Lithuania has been actively involved in joint exchange programmes and discussions with researchers from other Baltic central banks. CEFER is heavily engaged in the organisation of the International Panel Data Conference which will take place in Vilnius in 2019 and that was organised in Seoul (South Korea) in 2018; this year 135 applications have already been received from all over the world.

Promotion of research in economics and finance. To this end, the Bank of Lithuania hosts the Visiting Researcher Programme, organises the invited speaker research seminar series, gives non-technical research seminars open not only for central bank staff but also to the general public, external researchers and experts. To encourage high-quality research, the Bank of Lithuania also grants two awards for economic research activities: Vladas Jurgutis Award (€10 thousand) and the Bank of Lithuania Award for Dissertation in the Field of Economics (€5 thousand). In 2019, they will be awarded for the best research works submitted to the Bank of Lithuania in 2018: the experimental studies on various forms of labour remuneration, and research on the impact of strategic behaviour on investors and asset pricing.

Improvement of education, lectures and updated study programmes. In cooperation with TMTS and Vilnius University, CEFER created a bachelor's programme in Quantitative Economics. This is the first programme in Lithuania that offers a unique blend of mathematics, statistics, economics and data science. Out of 100 applicants, 35 students were selected for an interview and enrolled in the programme. The joint programme promotes education transcending national borders, allows talented youth to stay in Lithuania, and prepares a new generation of analysts able to combine economic intuition, data analytics as well as mathematical and quantitative skills in economics modelling. It will also add to the pool of high-skilled workers in Lithuania. In addition, CEFER took the initiative to organise joint PhD courses, various seminars and workshops aimed at increasing the competence of researchers working at Lithuanian universities.

Research on household finance and consumption. In 2018, TMTS conducted the first representative survey in Lithuania on household assets and finances. The total survey sample included nearly 1,700 Lithuanian households, providing information on almost 3,000 individuals. The survey results will allow specialists to assess household assets, liabilities, income and consumption, their correlations and distributions. Since analogous research is conducted in other European countries, Lithuania's results will be comparable on a Eurosystem level. The analysed data will enable specialists to assess income and, most importantly, asset inequality, reasons behind it, financial resilience of households in the event of an economic downturn, and potential future developments of these variables.

Other important events during the reporting period



In 2018, a consortium of the national central banks of Germany, Lithuania and Poland kicked off the EU Twinning project 'Strengthening the National Bank of Belarus'.



Organised by the ECB and the Bank of Lithuania, the European Cultural Days showcased Lithuania's cultural heritage.



The Bank of Lithuania held an Open Day event at its premises in Kaunas.

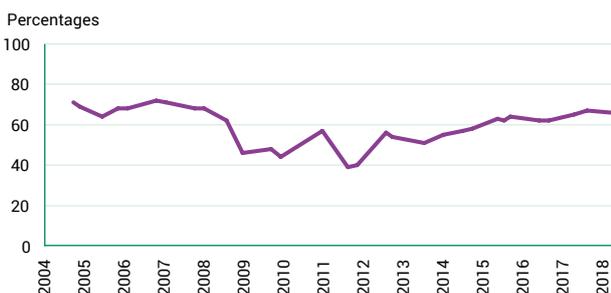


The Bank of Lithuania was announced the winner of Central Banking's first Catalyst Award.

The primary channel for information on the Bank of Lithuania and its activities is its [website](#) (6,826,671 pageviews in 2018). The central bank's presence on social media platforms has been increasing further (reach statistics for 2018: Facebook – over 2 million users, LinkedIn – more than 0.6 million users, Twitter – 245 thousand users).

In January 2018, a consortium of the national central banks of Germany, Lithuania and Poland started implementing the EU Twinning project 'Strengthening the National Bank of Belarus'. The project aims to enhance the capacity of the National Bank of the Republic of Belarus to effectively pursue its core responsibilities in the field of financial stability, banking supervision, payment systems, consumer protection and communication policy. With a budget of €1.15 million, the project is set to run for 18 months, counting on the expertise of the Bundesbank as the main partner and the central banks of Poland and Lithuania as junior partners. First of its kind in Belarus, it is also the first EU Twinning Project to the implementation of which the Bank of Lithuania contributes.

Public confidence in the Bank of Lithuania



Two major events held in Lithuania and abroad – the European Cultural Days in Frankfurt am Main and the Open Days at the Bank of Lithuania premises in Kaunas – commemorated the centenary of the restoration of Lithuania's statehood.

Organised since 2003, the European Cultural Days of the ECB provide an opportunity for Member States to showcase their cultural gems, while residents and visitors of Frankfurt am Main can learn more about the varied array of cultures and celebrate this 'unity in diversity'. The 2018 European Cultural Days celebrated Lithuania's cultural heritage. The programme of the event was compiled by the Bank of Lithuania and the ECB. The three concerts given by Lithuanian and German performers received a great deal of attention in Germany.



In the Old Opera House in Frankfurt (left to right): Uwe Becker, Mayor of Frankfurt am Main, Mario Draghi, President of the ECB, Martynas Stakionis, Conductor of the Lithuanian Chamber Orchestra and Vitas Vasiliauskas, Chairman of the Board of the Bank of Lithuania

On 27 October 2018, the unique interwar building of the Bank of Lithuania in Kaunas opened its doors to the city residents and visitors. They were invited to attend public discussions on the history of the Bank of Lithuania, watch documentaries and test their knowledge in quizzes. Re-established on 1 March 1990, the Bank of Lithuania continues the traditions of the country's central bank that operated during the interwar period. The second Open Day event in Kaunas was dedicated to the centenary of the restoration of Lithuania's statehood and attracted over 3,000 visitors.

On 6 September 2018, the Bank of Lithuania was announced winner of the first Catalyst Award in the FinTech & RegTech Global Awards 2018 organised by Central Banking, an international journal on the world's central banks. The awards ceremony was held in Singapore, one of the most important global financial centres, and ran in unison with the central banking global summit, which focused on FinTech and supervisory challenges.

The judging panel was impressed with the Bank of Lithuania's broad-based approach to FinTech, and particularly with its achievements in creating a FinTech-friendly environment. The Catalyst Award is aimed at acknowledging a technology incubator, sandbox, accelerator or equivalent which has furthered the development of FinTech and/or RegTech in the central banking and financial fields.



LIETUVOS BANKAS
EUROSISTEMA

Annual Financial Statements of the Bank of Lithuania

2018

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INDEPENDENT AUDITOR'S REPORT

To the Seimas of the Republic of Lithuania

Opinion

We have audited the accompanying financial statements of the Bank of Lithuania (hereinafter the Bank), which comprise the balance sheet as at 31 December 2018, the profit and loss account for the year then ended and notes to the financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying Bank's financial statements give a true and fair view of the financial position of the Bank as at 31 December 2018 and its financial performance for the year then ended in accordance with Guideline (EU) 2016/2249 of the European Central Bank (ECB) on the legal framework for accounting and financial reporting in the European System of Central Banks (ECB/2016/34) adopted by the Governing Council of the ECB, the Law on the Bank of Lithuania and the Accounting Policy of the Bank approved by the Board of the Bank of Lithuania.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the financial statements* section of our report. We are independent of the Bank in accordance with the International Ethics Standards Board for Accountants' *Code of Ethics for Professional Accountants* (IESBA Code) together with the requirements of the Law on Audit of the financial statements of the Republic of Lithuania that are relevant to the audit in the Republic of Lithuania, and we have fulfilled our other ethical responsibilities in accordance with the Law on Audit of the financial statements of the Republic of Lithuania and the IESBA Code. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other matter

The financial statements of the Bank for the year ended 31 December 2017 were audited by another auditor who expressed an unmodified opinion on them on 3 April 2018.

Responsibilities of management and those charged with governance for the financial statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with Guideline (EU) 2016/2249 of the European Central Bank (ECB) on the legal framework for accounting and financial reporting in the European System of Central Banks (ECB/2016/34) adopted by the Governing Council of the ECB, the Law on the Bank of Lithuania and the Accounting Policy of the Bank approved by the Board of the Bank of Lithuania, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Bank's financial reporting process.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional skepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Bank to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

UAB ERNST & YOUNG BALTIC
Audit Company's license No. 001335



Jonas Akelis
Auditor's license
No. 000003

19 April 2019

Balance Sheet of the Bank of Lithuania

EUR thousands

	Notes	31 December 2018	31 December 2017
ASSETS			
1. Gold and gold receivables	1	209,811	202,484
2. Claims on non-euro area residents denominated in foreign currency		5,461,691	4,003,379
Receivables from the IMF	2	200,940	163,092
Balances with banks and security investments, external loans and other external assets	3	5,260,751	3,840,288
3. Claims on euro area residents denominated in foreign currency	4	71,990	9
4. Claims on non-euro area residents denominated in euro	5	1,006	8,934
5. Lending to euro area credit institutions related to monetary policy operations denominated in euro	6	189,166	303,000
Main refinancing operations		-	-
Longer-term refinancing operations		173,000	303,000
Fine-tuning reverse operations		-	-
Structural reverse operations		-	-
Marginal lending facility		16,166	-
Credits related to margin calls		-	-
6. Other claims on euro area credit institutions denominated in euro	7	360	12,077
7. Securities of euro area residents denominated in euro		11,641,412	10,265,899
Securities held for monetary policy purposes	8	10,755,562	9,699,423
Other securities	9	885,850	566,476
8. General government debt denominated in euro		-	-
9. Intra-Eurosystem claims		3,446,946	3,803,146
Participating interest in the ECB	10	207,183	207,183
Claims equivalent to the transfer of foreign reserves	11	239,454	239,454
Net claims related to the allocation of euro banknotes within the Eurosystem	12	3,000,309	3,356,508
Other claims within the Eurosystem (net)		-	-
10. Items in course of settlement		-	-
11. Other assets		161,939	179,639
Tangible and intangible fixed assets	13	29,668	30,781
Other financial assets	14	4,368	3,355
Off-balance-sheet instruments revaluation differences	15	55,324	71,336
Accruals and prepaid expenses	16	70,200	71,466
Sundry	17	2,380	2,702
TOTAL ASSETS		21,184,321	18,778,567

Balance Sheet of the Bank of Lithuania

EUR thousands

	Notes	31 December 2018	31 December 2017
LIABILITIES			
1. Banknotes in circulation	18	6,648,124	6,321,866
2. Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	19	6,016,113	5,077,380
Current accounts (covering the minimum reserve system)		5,997,113	5,077,380
Deposit facility		-	-
Fixed-term deposits		-	-
Fine-tuning reverse operations		-	-
Deposits related to margin calls		19,000	-
3. Other liabilities to euro area credit institutions denominated in euro	20	-	1,200
4. Debt certificates issued		-	-
5. Liabilities to other euro area residents denominated in euro	21	1,011,590	1,868,929
General government		893,165	1,840,777
Other liabilities		118,425	28,153
6. Liabilities to non-euro area residents denominated in euro	22	123,074	11,400
7. Liabilities to euro area residents denominated in foreign currency	23	216,245	224,770
8. Liabilities to non-euro area residents denominated in foreign currency	24	47,475	31,936
9. Counterpart of special drawing rights allocated by the IMF	2	166,800	162,985
10. Intra-Eurosystem liabilities		5,728,138	3,985,282
Net liabilities related to the allocation of euro banknotes within the Eurosystem		-	-
Other liabilities within the Eurosystem (net)	25	5,728,138	3,985,282
11. Items in course of settlement	26	3,691	21,469
12. Other liabilities		319,155	270,813
Off-balance-sheet instruments revaluation differences	15	78,275	47,626
Accruals and income collected in advance	27	17,409	9,025
Sundry	28	223,472	214,162
13. Provisions	29	123,554	106,895
14. Revaluation accounts	30	281,606	217,327
15. Capital	31	465,146	444,389
Authorised capital		60,000	60,000
Reserve capital		405,146	384,389
16. Profit for the year	42	33,610	31,926
TOTAL LIABILITIES		21,184,321	18,778,567

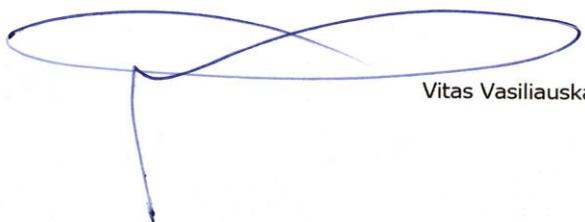
Profit and Loss Account of the Bank of Lithuania

EUR thousands

	Notes	2018	2017
Interest income		120,513	64,810
Interest expense		(40,343)	(6,504)
1. Net interest income	32	80,171	58,306
Realised gains (losses) arising from financial operations		(25,544)	6,125
Write-downs on financial assets and positions		(23,527)	(50,406)
Transfer to provisions for risks		(16,000)	-
2. Net result of financial operations, write-downs and risk provisions	33	(65,071)	(44,281)
Fees and commissions income		7,426	7,091
Fees and commissions expense		(3,049)	(1,852)
3. Net income from fees and commissions	34	4,377	5,239
4. Income from equity instruments	35	20,685	10,900
5. Net result of pooling of monetary income	36	25,007	34,670
6. Other income	37	3,078	1,216
TOTAL NET INCOME		68,247	66,050
7. Staff costs	38	(16,403)	(16,317)
8. Administrative expenses	39	(9,853)	(8,449)
9. Depreciation of tangible and intangible fixed assets	13	(4,280)	(2,997)
10. Banknote production services	40	(1,837)	(2,307)
11. Other expenses	41	(2,264)	(4,054)
PROFIT FOR THE YEAR	42	33,610	31,926

The Annual Financial Statements for 2018 of the Bank of Lithuania were approved on 4 April 2019 by Resolution No 03-75 of the Board of the Bank of Lithuania.

Chairman of the Board



Vitas Vasiliauskas

Director of the Accounting Department
Organization Service



Lina Našlėnienė

Explanatory notes

1. BASIS FOR PREPARATION AND PRESENTATION OF THE ANNUAL FINANCIAL STATEMENTS

As of 1 January 2015, Lithuania is a member of the euro area.

The financial accounting of the Bank of Lithuania is managed and the Annual Financial Statements are prepared in accordance with Guideline (EU) 2016/2249 of the European Central Bank (ECB) on the legal framework for accounting and financial reporting in the European System of Central Banks (ECB/2016/34), adopted by the Governing Council of the ECB (hereinafter 'Accounting Guideline'), the Law on the Bank of Lithuania and the Accounting Policy approved by the Board of the Bank of Lithuania. If a specific accounting treatment is not laid down in the Accounting Guideline and the Accounting Policy of the Bank of Lithuania and in the absence of decisions and instructions to the contrary by the ECB, the Bank of Lithuania shall follow the principles of the International accounting and financial reporting standards as adopted by the European Union (EU).

Due to rounding, the totals included in the Balance Sheet, Profit and Loss Account and Notes of the Bank of Lithuania may not equal the sum of the individual figures.

2. ACCOUNTING POLICY

2.1. GENERAL PRINCIPLES

In managing financial accounting, the Bank of Lithuania follows the following basic accounting assumptions: going concern basis, accrual principle, post-balance sheet events.

The qualitative characteristics in drawing up the financial statements of the Bank of Lithuania are as follows: economic reality and transparency, prudence, materiality, consistency and comparability.

Gold, marketable securities and other on-balance-sheet and off-balance-sheet assets and liabilities that comprise financial assets (hereinafter 'financial items') in financial accounting are recorded at acquisition cost (transaction price), and in the Annual Financial Statements are presented at market price (except for debt securities valued at amortised cost and non-marketable equity instruments presented as other financial assets). The results arising from revaluation of gold, marketable debt and equity securities, including exchange traded fund units (on a code-by-code basis) and derivatives (on an item-by-item basis) at market prices are accounted for separately.

In the Annual Financial Statements, financial items denominated in foreign currency are presented in euro at market rates.¹ Results arising from revaluation of foreign currency (on a currency-by-currency basis) at market rates are accounted for separately.

For recognition of unrealised revaluation results, the Bank of Lithuania uses asymmetric approach established in the Accounting Guideline. Pursuant to this approach, unrealised revaluation loss arising at the end of the financial year from revaluation of a separate financial item at market price or market rate and exceeding previous unrealised revaluation gain registered in a corresponding revaluation account is recognised as the expense of the reporting financial year. Unrealised loss taken to Profit and Loss Account cannot be reversed in subsequent years against new revaluation gain of the same financial item resulting from changes in market price and market rate or offset by the revaluation gain of another type of financial item.

Unrealised revaluation gain arising at the end of the financial year from the revaluation of a separate financial item at market price and market rate is presented in revaluation accounts.

The average rate and average price method is used in order to compute the acquisition costs for gold, securities and foreign currency. Such acquisition costs are used for the purpose of calculating the realised and unrealised results.

¹ Market rate – euro and foreign currency reference rate, based on the daily concertation procedure between central banks within and outside the ESCB, published by the ECB.

Income and expense are recognised in the accounting period in which they are earned or incurred and not in the period in which they are received or paid. Income and expense in foreign currency are recognised in euro at market rates prevailing on the day of their recognition in accounting; they influence a respective foreign currency position on that date.

2.2. FOREIGN CURRENCY

The market rates of the euro and foreign currency with which the Bank of Lithuania holds material positions

Foreign currency per euro

Currency	Code	31 December 2018	31 December 2017	Change (%)
Swiss franc	CHF	1.12690	1.17020	-3.7
US dollar	USD	1.14500	1.19930	-4.5
Chinese yuan	CNY	7.87510	7.80440	0.9
British pound	GBP	0.89453	0.88723	0.8
Special drawing rights (SDR)	XDR	0.82277	0.84203	-2.3
Canadian dollar	CAD	1.56050	1.50390	3.8
Czech Koruna	CZK	25.7240	25.5350	0.7

The average rate of foreign currency is recalculated on a daily basis in consideration of an increase of a respective foreign currency position and of the average costs of all purchases (if the position is long), or of all sales (if the position is short) of the same foreign currency made during the day. When the foreign currency position decreases – the realised result is calculated.

The allocation of the Bank of Lithuania's net assets (liabilities) by foreign currency is disclosed in Note 44 'Assets and liabilities of the Bank of Lithuania by foreign currency'.

In the event of the recognition of unrealised revaluation loss on a separate foreign currency at year-end, the average rate of that currency is correspondingly adjusted to the market rate on the last business day of the financial year.

2.3. GOLD

In the Annual Financial Statements, gold is presented in euro at the market price of one Troy ounce, prevailing on the last business day of the financial year.

In the event of the recognition of unrealised revaluation loss on gold at year-end, the average cost of gold is correspondingly adjusted to the gold market price prevailing on the last business day of the financial year.

Transactions related to gold swaps are accounted for in the same way as repurchase agreements.

2.4. MARKETABLE SECURITIES

Marketable debt and equity securities are recorded in on-balance-sheet accounts at acquisition cost on the settlement date.

Securities held for monetary policy purposes, as well as debt securities classified as held-to-maturity, are presented in the Balance Sheet at amortised cost subject to impairment. Other marketable securities are presented in the Balance Sheet either at the mid-market prices (87% of the fair value as at 31 December 2018) or on the basis of the relevant yield curve (13% of the fair value as at 31 December 2018) prevailing on the last business day of the financial year. Revaluation results of securities related with changes of the market price of securities and the market rate of the foreign currency are presented in separate revaluation accounts.

The average price of each issue of securities is recalculated at the end of the business day in consideration of all purchases of the same issue of securities made during the day and their average acquisition costs. Realised gain (loss) for the same day sales of these securities is calculated according to this new average cost.

A coupon purchased together with debt securities is presented in a separate Balance Sheet item as other assets and is not included in the acquisition cost of the securities.

Dividends, bought together with equity securities, are included in the acquisition cost of the securities. Dividends bought in the period after the dividend receivable is announced are presented in a separate Balance Sheet item as other assets.

The difference between the debt security acquisition cost and its par value – discount or premium – is recognised as income or expense according to the straight-line method on a daily basis from the settlement date of the purchase transaction to the maturity date or settlement date of the sale transaction. The nominal

value of inflation-linked securities is indexed to the inflation index on a daily basis from the settlement date of the purchase transaction to the maturity date or settlement date of the sale transaction. The nominal value change is recognised as interest income or expense.

Discount on non-coupon bearing debt securities is amortised according to the internal rate of return (IRR), and discount or premium on coupon bearing debt securities is amortised according to the straight-line method.

If at the end of the financial year unrealised revaluation loss on valuation of a separate issue of securities is recognised as expense, the average cost of such issue of securities is adjusted according to its market price prevailing on the last business day of the financial year.

2.5. NON-MARKETABLE EQUITY INSTRUMENTS

Non-marketable equity instruments are long-term investments in equity instruments held for the specific purposes of the Bank of Lithuania in order to participate in the activities of a specific enterprise whose equity instruments are non-marketable and their price is not quoted in the market. They are recorded at acquisition cost subject to impairment.

2.6. INCOME AND EXPENSE

In the Profit and Loss Account, interest on a separate financial item or instrument is presented on a net basis (interest income is netted against interest expense on the same financial item or instrument).

Realised income and expense related to sold foreign currency, gold and securities are recognised in the income and expense accounts. Such income and expense are calculated considering the average rate or average price of the corresponding financial item.

Unrealised revaluation gain of financial items is not recognised as income and is presented in revaluation accounts. Unrealised revaluation loss, exceeding previous revaluation gain related to the corresponding financial item, is recognised as expense at the end of the financial year.

Impairment losses are recognised as expense and are not reversed in subsequent years unless the impairment decreases and this decrease can be related to an observable event that occurred after the impairment was first recorded.

Dividends of marketable equity securities are booked upon their announcement, while dividends of non-marketable equity instruments are booked upon having been settled or having received a notification on their distribution.

2.7. REVERSE TRANSACTIONS

Reverse transactions are operations whereby the Bank of Lithuania buys or sells assets under a repurchase agreement or conducts credit operations against collateral.

Repurchase agreements are presented as collateralised deposits of the counterparty on the liabilities side of the Balance Sheet, while the financial asset that has been given as collateral (sold and repurchased under these agreements) remains on the asset side of the Balance Sheet for the period of transactions. Collateral provided in the form of cash is presented on the asset side of the Balance Sheet.

Reverse repurchase agreements are presented as collateralised loans on the asset side of the Balance Sheet. The collateral acquired (bought with a subsequent sale under these agreements) is not reported in the Balance Sheet and is not revalued during the transaction period. Collateral received in the form of cash is presented on the liabilities side of the Balance Sheet.

The difference between the purchase and repurchase price of the collateral acquired under reverse repurchase and repurchase agreements is recognised on a daily basis as interest income or expense over the remaining duration of the transaction.

Seeking to support bond and repurchase agreement market liquidity, the Bank of Lithuania, together with the ECB and other Eurosystem national central banks (NCBs), lends securities purchased under the public sector purchase programme. The Bank of Lithuania lends securities via its lending agent, as well as under the fail mitigation programme and the strategic lending programme provided by its securities depository. In the case of security lending transactions, the securities remain on the asset side of the Balance Sheet for the throughout the duration of transactions.

2.8. FOREIGN EXCHANGE TRANSACTIONS

Foreign currency to be received or paid, under foreign exchange spot, forward and swap transactions, influences a respective foreign currency's position on the trade date and is recorded in off-balance-sheet accounts from the trade date to the settlement date.

The difference in the value at the spot and forward rates of the foreign exchange forward and swap transactions is recognised as interest income or expense and is accrued on a daily basis over the remaining duration of the transaction.

Non-deliverable foreign exchange forwards are recorded in the off-balance-sheet accounts from the trade date to the maturity date at notional amount based on the forward exchange rate. In the Balance Sheet, the value of these transactions is presented at market prices prevailing on the last business day of the financial year. Unrealised loss recognised as expense at the end of the financial year is presented as off-balance-sheet instruments revaluation difference on the Balance Sheet liabilities side. The difference between the forward rate and the spot rate at the settlement date of the transaction, taking into account any accumulated impairment losses, is recognised as realised income or expense.

2.9. FORWARD TRANSACTIONS IN SECURITIES

Forward purchases or sales of securities are recognised in off-balance-sheet accounts from the trade date to the settlement date at the forward price of the transaction. In the Balance Sheet, the value of these transactions is presented at the forward market price prevailing on the last business day of the financial year.

On the settlement date of forward transactions in securities, the purchases or sales of the securities are recorded on the on-balance-sheet accounts at the actual market price, and the difference between this price and the forward price of the transaction is recognised as realised income or expense.

2.10. INTEREST RATE TRANSACTIONS

Interest rate futures are recorded in off-balance-sheet accounts at the nominal value of contracts from the trade date to the closing or maturity date. Daily changes in the variation margin of these contracts are recognised as realised income or expense.

Interest rate swaps are recorded in off-balance-sheet accounts at contractual amount from the trade date to the closing or maturity date. In the Balance Sheet, the value of these transactions is presented at market prices, prevailing on the last business day of the financial year. Unrealised loss recognised as expense at the end of financial year is presented as off-balance-sheet instruments revaluation difference on the Balance Sheet liabilities side and is subject to straight-line amortisation till the maturity date of the transaction. Interest income and interest expense is accrued on a daily basis over the remaining duration of the transaction.

2.11. TANGIBLE AND INTANGIBLE FIXED ASSETS

Tangible fixed assets include such tangible assets whose useful life is longer than one year and whose acquisition cost (including VAT) is no less than EUR 2,000. Intangible fixed assets include items without physical substance whose useful life is no less than one year and whose acquisition cost is no less than EUR 2,000. Tangible and intangible fixed assets are recorded in the Balance Sheet at cost less accumulated depreciation (amortisation) and are subject to impairment. Internally generated tangible and intangible assets are recorded as fixed assets if they comply with the recognition criteria. The initial cost of such assets consists of the direct staff cost, the cost of assets and services acquired or depreciated (amortised) in order to develop the assets. The fixed assets under construction, pieces of art, museum stocks and tangible assets included in the list of cultural valuables (excluding buildings) are not depreciated (amortised). Depreciation (amortisation) of other fixed assets is calculated on a straight-line basis over the expected useful life of the assets.

Useful lives of tangible and intangible fixed assets

Fixed assets	Years
Tangible assets	
Buildings	33-59
Cash processing equipment	5-15
Computer equipment	3-7
Other assets (furniture, office equipment and other)	5-30
Intangible assets	3-10

The residual depreciation (amortisation) period is reviewed having assessed that the useful life of the fixed assets have changed significantly.

If there are indications that the value of real estate has declined significantly, at the end of the financial year, the acquisition cost of such assets is reduced by the amount of impairment loss.

When fixed assets are sold, the difference between the value of sale and the value presented in the Balance Sheet is recognised as income or expense.

Maintenance and repair costs of fixed assets are recognised as an expense at the time they are incurred.

2.12. BANKNOTES AND COINS IN CIRCULATION

The euro area NCBs and the ECB, which together comprise the Eurosystem, issue euro banknotes.² The total value of euro banknotes in circulation is allocated to the Eurosystem NCBs on the last business day of each month in accordance with the banknote allocation key.³

The ECB is allocated a share of 8% of the total value of euro banknotes in circulation, whereas the remaining 92% is allocated to NCBs according to the Eurosystem capital key. The share of banknotes allocated to each NCB is disclosed in their Balance Sheet under liability item 'Banknotes in circulation'.

The difference between the value of euro banknotes allocated to each NCB in accordance with the banknote allocation key and the value of euro banknotes that it actually puts into circulation is presented as remunerated intra-Eurosystem balance.⁴ The remuneration of this balance is calculated at the latest available marginal interest rate used by the Eurosystem in its tenders for the main refinancing operations⁵.

The interest income or expense on this balance is disclosed in the Profit and Loss Account item 1 'Net interest income' (see Note 32 'Net interest income').

Seeking to avoid fluctuations in monetary income after new members join the Eurosystem, the net intra-Eurosystem balances arising from the allocation of euro banknotes are adjusted by the compensatory amount, which is applied for the new entrants from the EUR adoption year and gradually reduced over the following five years. For the Bank of Lithuania, the period for which the above-mentioned adjustments are applicable will terminate on 31 December 2020. As of 1 January 2021, the interest income will be calculated on the whole position of the net claims related to the allocation of euro banknotes.

The nominal value of euro circulation coins issued into circulation by the Bank of Lithuania is presented in the Balance Sheet item 12 'Other liabilities' (see Note 28 'Sundry').

The nominal value of litas⁶ banknotes and litas circulation coins issued into circulation by the Bank of Lithuania and not returned from circulation after the euro adoption is presented in the Balance Sheet item 12 'Other liabilities'.

The sale price (excluding VAT) of collector euro coins and other numismatic valuables is recognised as income.

The cost of printing banknotes and minting coins, as well as other expenses associated with the issue of banknotes and coins into circulation, are recorded as expenses when incurred, irrespective of when the coins and banknotes were put into circulation.

2.13. PROVISIONS FOR COVERING FINANCIAL RISKS AND LIABILITIES

Provisions for expected foreign exchange rate, interest rate, gold price and credit risks (hereinafter 'provisions for risks') are formed by the Board of the Bank of Lithuania, in order that the Bank of Lithuania would have sufficient financial resources to offset the negative change in value arising from the financial assets, including the financial assets acquired in connection with monetary policy operations of the Eurosystem, as well as the financial liabilities related to the management of these assets, and in such way safeguard the Bank of Lithuania's capital and the real value of financial assets.

These provisions are formed according to the rules established by the Board of the Bank of Lithuania. The aim of these provisions is to cover the assessed level of risk, which is set in accordance with the risk assessment methodology approved by the Governing Council of the ECB. The expected shortfall at a 99% confidence level (ES99%) is used to define the target amount of risk provisions. Provisions for risks may be used for the coverage of all or part of the net expenses related to financial assets operations (realised result, unrealised revaluation loss and impairment of the financial assets).

² ECB Decision of 13 December 2010 on the issue of euro banknotes (recast) (ECB/2010/29), OJ L 35, 9.2.2011, p. 26, as amended.

³ Banknote allocation key means the percentages that result from taking into account the ECB's share in the total euro banknote issue and applying the subscribed capital key to the NCBs' share in such total.

⁴ ECB Decision of 3 November 2016 on the allocation of monetary income of the national central banks of Member States whose currency is the euro (recast) (ECB/2016/36), OJ L 347, 20.12.2016, p. 26.

⁵ The marginal interest rate used by the Eurosystem in its tenders for the main refinancing operations was 0% in 2017 and 2018.

⁶ The national currency used as legal tender until the adoption of the euro.

Provisions for termination benefits, payable for staff who will qualify for the state social insurance pension while working at the Bank of Lithuania, are assessed using actuary calculations. Their value is determined as termination benefits earned by the employee upon retirement and calculated based on the employee change dynamics and wage growth preconditions, discounted at using the long-term lending interest rates in the Republic of Lithuania.

Other provisions for liabilities, such as provisions for wages and salaries payable for annual leave, provisions for termination benefits or provisions related to the exchange of litas banknotes and coins, are not discounted due to the relatively short period from the formation of these provisions to their use.

Provisions for risks and liabilities are formed as at year-end and recognised as expense.

3. FINANCIAL RISK MANAGEMENT

3.1. MANAGEMENT OF FINANCIAL RISK RELATED TO MONETARY POLICY OPERATIONS

The risk related to monetary policy assets and operations is managed within the Eurosystem on an integral basis. The Bank of Lithuania takes part in this risk management process via its representative in the Risk Management Committee of the ECB, which is responsible for the management of financial risk related to monetary policy operations and investment of foreign reserves of the ECB.

Credit, market and liquidity risks are the key risks encountered in conducting monetary policy operations. Credit operations conducted by the Eurosystem are mainly exposed to credit risk, arising from potential default of counterparty. To manage the counterparty's credit risk, credibility requirements for counterparties, with which these operations can be executed, are established and monetary policy operations are conducted only against collateral. Collateral should match the established requirements for suitability and other risk management instruments. In case of insolvency of the counterparty, the Eurosystem will face collateral issuer's or debtor's credit risk, market risk arising from the changes in collateral market value and liquidity risk (particularly if the Eurosystem wanted to sell a large part of asset position).

To mitigate the risk of securities purchase operations, requirements for securities, which can be acquired by the Eurosystem under adopted securities purchase programmes, and limits on their acquisition are set.

The Bank of Lithuania ensures, that financial institutions registered in Lithuania and participating in monetary policy operations as well as collateral provided under monetary policy operations would match established requirements, and controls fulfilment of established risk limits.

3.2. MANAGEMENT OF FINANCIAL RISK RELATED TO THE INVESTMENT OF THE BANK OF LITHUANIA

Investments made by the Bank of Lithuania, not related to monetary policy operations, are mainly exposed to financial risks, such as market (foreign exchange rate, equity securities and gold price, interest rate), credit, liquidity and settlement risks.

Value-at-risk is the basic tool for the evaluation and management of market risk of investment portfolio which is the largest part of financial assets, not related to monetary policy operations. This indicator, also called as the risk budget, is calculated for one year period at 95% confidence level and cannot exceed EUR 150 million. The application of the risk budget ensures integral management of market risk, more flexible use of various investment strategies as well as one indicator for the overall assessment of both equity and debt securities risk. The model used for the calculation of value-at-risk considers past patterns and forecasted macroeconomic environment. As at 31 December 2018, the risk value of investment portfolio amounted to EUR 101 million (the same as at 31 December 2017).

In pursuit of a credible risk management system, other market risk management instruments are combined with the risk budget instrument.

For managing foreign exchange rate risk related to financial assets, which do not correspond to liabilities in foreign currencies, limits for open currency positions (except for a separate reserve portfolio denominated in US dollars whose exchange rate risk is not hedged) are established. As at 31 December 2018, the risk value of reserve portfolio amounted to EUR 124 million – an increase of EUR 45 million, compared with the previous year.

Exchange rate risk related to financial assets corresponding to liabilities in foreign currencies is eliminated by investing in the currency of liabilities. For managing foreign exchange rate and interest rate risks, the Bank of Lithuania widely uses financial derivatives.

Credit risk is managed by dealing only with reliable financial institutions, investing only in investment grade financial instruments. Taking into account the credibility of counterparty or issuer, limits on the liabilities to the Bank of Lithuania by issuers, counterparties and their groups are established. These limits help to diversify credit risk.

Seeking to ensure the liquidity of financial assets, which do not correspond to liabilities in foreign currencies, a part of such financial assets is invested in very safe and liquid government debt securities. Liquidity risk related to financial assets that are linked to liabilities is managed by combining the duration of liabilities and corresponding investments.

The following instruments are applied to diminish settlement risks: the delivery-versus-payment principle, matching of debt and credit turnovers, ISDA Master Agreement.

Appropriate investment allocation plays an important role in financial risk management seeking to reduce the concentration of investment. In 2018, the Bank of Lithuania ensured diversification of investments by investing in debt securities of nine countries and more than thirty issuers. The Bank of Lithuania also invests in exchange traded funds linked to well-diversified equity and debt securities market indexes.

All financial derivatives are included in the measurement of the market and credit risk of the Bank of Lithuania's financial assets investment.

4. FINANCIAL ACCOUNTING PRINCIPLES ON OPERATIONS RELATED TO PARTICIPATION IN THE EUROSISTEM

This chapter covers the accounting principles of claims and liabilities as well as income, and expenses arising from operations related to participation in the Eurosystem.

4.1. PARTICIPATING INTEREST IN ECB CAPITAL

Shares of the NCBs in the subscribed capital of the ECB depend on the established key for ECB capital subscription, which is adjusted, in accordance with the provisions of the Statute of the European System of Central Banks (hereinafter 'ESCB') and of the ECB, every five years and every time when a new Member State joins the EU, on the basis of population and GDP data provided by the European Commission.

Participating interest of NCBs of the EU Member States in the ECB capital

NCB	Capital key as at 31 December 2018, %	Paid-up capital as at 31 December 2018, EUR	Eurosystem capital key as at 31 December 2018, %
Nationale Bank van België / Banque Nationale de Belgique	2.4778	268,222,025	3.52003
Deutsche Bundesbank	17.9973	1,948,208,997	25.56743
Eesti Pank	0.1928	20,870,614	0.27390
Banc Ceannais na hÉireann / Central Bank of Ireland	1.1607	125,645,857	1.64892
Bank of Greece	2.0332	220,094,044	2.88842
Banco de España	8.8409	957,028,050	12.55961
Banque de France	14.1792	1,534,899,402	20.14334
Banca d'Italia	12.3108	1,332,644,970	17.48904
Central Bank of Cyprus	0.1513	16,378,236	0.21494
Latvijas Banka	0.2821	30,537,345	0.40076
Lietuvos bankas	0.4132	44,728,929	0.58700
Banque centrale du Luxembourg	0.2030	21,974,764	0.28839
Bank Ċentrali ta'Malta / Central Bank of Malta	0.0648	7,014,605	0.09206
De Nederlandsche Bank	4.0035	433,379,158	5.68748
Oesterreichische Nationalbank	1.9631	212,505,714	2.78883
Banco de Portugal	1.7434	188,723,173	2.47672
Banka Slovenije	0.3455	37,400,399	0.49083
Národná banka Slovenska	0.7725	83,623,180	1.09743
Suomen Pankki – Finlands Bank	1.2564	136,005,389	1.78487
Subtotal for euro area NCBs	70.3915	7,619,884,851	100.00000

Българска народна банка (Bulgarian national bank)	0.8590	3,487,005	-
Česká národní banka	1.6075	6,525,450	-
Danmarks Nationalbank	1.4873	6,037,512	-
Hrvatska narodna banka	0.6023	2,444,963	-
Magyar Nemzeti Bank	1.3798	5,601,129	-
Narodowy Bank Polski	5.1230	20,796,192	-
Banca Națională a României	2.6024	10,564,124	-
Sveriges Riksbank	2.2729	9,226,559	-
Bank of England	13.6743	55,509,148	-
Subtotal for non-euro area NCBs	29.6085	120,192,083	-
Total	100.0000	7,740,076,935	100.00000

The contribution of the Bank of Lithuania to ECB capital is presented in Note 10 'Participating interest in the ECB'.

4.2. FOREIGN RESERVES TRANSFERRED TO THE ECB

Pursuant to Article 48 and Article 30 of the Statute of the ESCB and of the ECB, the NCBs, when joining the Eurosystem, transfer their share of foreign reserves to the ECB, applying the ratio of the number of shares subscribed by the NCB concerned and the number of shares already paid up by the other NCBs.

The ECB's Intra-Eurosystem liabilities to the euro area, equivalent to the transfer of foreign reserves by the NCBs, comprised the amount of EUR 40,793 million. The share of foreign reserve assets, transferred to the ECB by the Bank of Lithuania, is reported under 'Claims equivalent to the transfer of foreign reserves' (see Note 11).

The remuneration of foreign reserves transferred to the ECB (except for the gold component) is calculated daily, at the latest available marginal interest rate used by the Eurosystem in its tenders for main refinancing operations.⁷

4.3. LENDING TO EURO AREA CREDIT INSTITUTIONS DENOMINATED IN EURO

Main refinancing operations. These are executed through liquidity providing reverse transactions with a weekly frequency and a maturity of one week, normally by means of standard tenders. These operations play a key role in achieving the aims of the steering interest rate, managing market liquidity and signalling the monetary policy stance.

Longer-term refinancing operations. These operations aim to provide counterparties with additional longer-term refinancing. In 2018, operations with maturity of 3 months were conducted. Additionally, in 2016 the Governing Council of the ECB introduced a series of four targeted longer-term refinancing operations. These operations have a four-year maturity, with a possibility of full or partial repayment after two years. According to the decisions taken by the Governing Council of the ECB, the final interest rate applicable to each targeted longer-term refinancing operation depended on the lending behaviour of the counterparties for the period between 1 February 2016 and 31 January 2018 and would be between the main refinancing operations rate and the deposit facility rate at the time of the allotment. Given that the actual rate only became known in 2018 and a reliable estimate was not possible until this time, the deposit facility rate was used for calculating the interest for these targeted longer-term refinancing operations up to the end of 2017, as this was deemed a prudent approach. The difference between the deposit facility rate and the actual rate for that period was recognised as interest income in 2018.

Fine-tuning reverse operations. They aim to regulate the market liquidity situation and steer interest rates, particularly to smooth the effects on interest rates caused by unexpected market fluctuations. Owing to their nature, they are executed on an *ad hoc* basis.

Structural reverse operations. These are reverse open-market transactions through standard tenders to enable the Eurosystem to adjust its structural liquidity position *vis-à-vis* the financial sector.

Marginal lending facility. The marginal lending facility is a standing facility provided by the Eurosystem, which may be used by counterparties to obtain overnight liquidity from NCBs at a pre-specified interest rate against eligible assets.

⁷ The marginal interest rate used by the Eurosystem in its tenders for the main refinancing operations was 0% in 2017 and 2018.

Credits related to margin calls. They refer to cash paid to counterparties in those instances where the market value of the collateral exceeds an established trigger point implying an excess of collateral with respect to outstanding monetary policy operations.

As at 31 December 2018, the total Eurosystem NCB's holding of monetary policy assets amounted to EUR 734,382 million (as at 31 December 2017 – EUR 764,310 million). The share of monetary policy assets held by the Bank of Lithuania is presented in Note 6 'Lending to euro area credit institutions related to monetary policy operations denominated in euro'.

Losses can only materialise if both the counterparty fails and the recovery of funds received from the resolution of the collateral provided by the counterparty is not sufficient. For specific collateral, which can be accepted by the NCBs at their own discretion, risk sharing has been excluded by the Governing Council of the ECB.

4.4. SECURITIES HELD FOR MONETARY POLICY PURPOSES

As at 31 December 2018, the securities held by the ECB and NCBs amounted to EUR 2,651,281 million (as at 31 December 2017 – EUR 2,386,012 million); they were acquired within the scope of three covered bond purchase programmes, the Securities Markets Programme, the asset-backed securities purchase programme, the public sector purchase programme⁸ and the corporate sector purchase programme.

In 2018 the Eurosystem continued its securities purchases under the expanded asset purchase programme⁹. This programme includes the third covered bond purchase programme, the asset-backed securities purchase programme, the public sector purchase programme and the corporate sector purchase programme.

The monthly pace of combined net asset purchase programme purchases by the NCBs and the ECB was EUR 30 billion on average until September 2018 and EUR 15 billion from October 2018 until the end of the year when the net purchases ended. The Governing Council of the ECB intends to continue reinvesting, in full, the principal payments from maturing securities purchased under the asset purchase programme for an extended period of time past the date when it starts raising the key ECB interest rates, and in any case for as long as necessary to maintain favourable liquidity conditions and an ample degree of monetary accommodation.

Securities purchased under all of these programmes are valued on an amortised cost basis subject to impairment. In accordance with Article 32.4 of the Statute of the ESCB and of the ECB, losses from holdings of securities purchased under the third covered bond purchase programme, the Securities Markets Programme and the corporate sector purchase programme, as well as securities of supranational organisations purchased under the public sector purchase programme (totalling EUR 710,867 million as at 31 December 2018), if they were to be materialised, are shared in full by the Eurosystem NCBs, in proportion to the prevailing Eurosystem capital key. Losses from holdings of securities purchased under the first and second covered bond purchase programmes, as well as securities of governments purchased under the public sector purchase programme are covered by the NCBs concerned.

The Governing Council of the ECB assesses on a regular basis the financial risks associated with the securities held under all these programmes. Annual impairment tests are conducted on the basis of the estimated recoverable amounts as at the year-end. Upon assessing that the value of a security is impaired, in accordance with the prudence principle, a provision against losses in monetary policy operations is established. Impairment losses materialising from securities held for monetary policy purposes, which are proportionally shared in full by all the Eurosystem NCBs, are recognised as part of net result of monetary income's pooling (see Note 29 'Provisions' and Note 36 'Net result of pooling of monetary income').

The value of securities holdings of the Bank of Lithuania is presented in Note 8 'Securities held for monetary policy purposes'.

4.5. LIABILITIES TO EURO AREA CREDIT INSTITUTIONS, RELATED TO MONETARY POLICY OPERATIONS DENOMINATED IN EURO

Current accounts (covering the minimum reserve system). These are the balances on the current accounts of credit institutions with NCBs that are required to hold minimum reserves.

Deposit facility. Deposit facility is a liquidity absorbing standing facility provided by the Eurosystem, which counterparties can use to make overnight deposits with NCBs at the pre-specified rate.

Fixed-term deposits. These liabilities relate to liquidity-absorbing fine-tuning operations for a fixed term and with a fixed rate of interest.

⁸ Decision ECB/2015/10 of 4 March 2015 on a secondary markets public sector asset purchase programme, OJ L 121, 14.5.2015, p. 20.

⁹ Further information on the asset purchase programme is available at the [ECB's website](#).

Fine-tuning reverse operations. Fine-tuning reverse operations are liquidity-absorbing reverse operations used to offset high liquidity imbalances.

Deposits related to margin calls. They refer to cash received from counterparties in those instances where the market value of the collateral has fallen below an established trigger point implying a shortfall of collateral to cover the outstanding monetary policy operations.

4.6. PARTICIPATION IN TARGET2

Cross-border payments in the EU settled in TARGET2¹⁰ give rise to bilateral balances in the TARGET2 accounts of EU central banks. These bilateral balances are netted out and then assigned to the ECB on a daily basis, leaving each NCB with a single net bilateral position *vis-à-vis* only the ECB. Intra-Eurosystem balances of the Bank of Lithuania *vis-à-vis* the ECB arising from TARGET2 are disclosed under the Balance Sheet items 'Other claims within the Eurosystem (net)' or 'Other liabilities within the Eurosystem (net)'.

4.7. ALLOCATION OF MONETARY INCOME

Monetary income of the Eurosystem, accruing to the NCBs in the performance of the ESCB's monetary policy functions, is calculated and allocated among the NCBs at the end of each financial year in proportion to their Eurosystem capital key in accordance with Article 32 of the ESCB and of the ECB.

The amount of the Eurosystem NCBs' monetary income is determined by measuring actual income, which it derives from the earmarkable assets held against its liability base.

The earmarkable assets consist mainly of the following items: lending to euro area credit institutions related to monetary policy operations denominated in euro; securities held for monetary policy purposes; intra-Eurosystem claims equivalent to the transfer of foreign reserves to the ECB; net intra-Eurosystem claims resulting from TARGET2 transactions; net intra-Eurosystem claims related to the allocation of euro banknotes within the Eurosystem; accrued interest on monetary policy operations, the maturity of which is one year or longer; a limited amount of each NCBs' gold holdings in proportion to each NCBs' capital key share.

The liability base consists mainly of the following items: banknotes in circulation; liabilities to euro area credit institutions related to monetary policy operations denominated in euro; net intra-Eurosystem liabilities resulting from TARGET2 transactions; net intra-Eurosystem liabilities related to the allocation of euro banknotes within the Eurosystem.

Interest paid on the liability base items and (or) on the earmarkable assets items is deducted from NCB's monetary income derived from these items. The difference between the NCBs' earmarkable asset value and its liability base value shall be offset by applying the difference of the latest available marginal rate for the Eurosystem's main refinancing operations¹¹. Furthermore, for monetary income calculation purposes, gold is considered to generate no income, and securities held for monetary policy purposes under both Decision ECB/2009/16 on the implementation of the covered bond purchase programme and Decision ECB/2011/17 on the implementation of the second covered bond purchase programme, as well as government securities under Decision ECB/2015/10 on the implementation of a secondary markets public sector asset purchase programme are considered to generate income at the latest available marginal interest rate used by the Eurosystem in its tenders for main refinancing operations.

After pooling of the annual monetary income of the Eurosystem and reallocation to NCBs in proportion to their subscribed capital keys, the differences between the NCBs' pooled monetary income and allocated in proportion to the Eurosystem capital key are settled among the NCBs' via TARGET2. The net result arising from the reallocation of monetary income for the Bank of Lithuania is disclosed in Note 36 'Net result of pooling of monetary income'.

4.8. MANAGEMENT OF NET FINANCIAL ASSETS

The Agreement on Net Financial Assets is an agreement between the Eurosystem NCBs and the ECB which sets the maximum amount of net financial assets of each NCB and the ECB held for non-monetary policy purposes and its management. The net financial assets covered by the agreement are mainly formed using liability base funds received from monetary policy operations that are temporarily free from performing monetary policy operations at that time (see section 4.7 of the Accounting Policy 'Allocation of monetary income'). Such assets are usually comprised of gold and foreign currency reserves, investments in euro.

The Bank of Lithuania determines the amount of financial assets, taking into consideration market conditions as well as investment opportunities and restrictions; however, the average amount of financial assets cannot be above the maximum amount of net financial assets set in accordance with the agreement, i.e.

¹⁰ The Trans-European Automated Real-time Gross settlement Express Transfer system.

¹¹ The marginal interest rate used by the Eurosystem in its tenders for main refinancing operations was 0% in 2017 and 2018.

EUR 5,856 million. In 2018, as in 2017, the amount of net financial assets of the Bank of Lithuania met the provisions of the Agreement.

4.9. THE ECB PROFIT DISTRIBUTION

Unless otherwise decided by the Governing Council of the ECB, the ECB distributes seigniorage income, which arises from the 8% share of euro banknotes allocated to the ECB, as well as the income arising from the securities acquired under securities programmes (the securities markets programme, the third covered bond purchase programme, the asset-backed securities purchase programme and the public sector asset purchase programme), by means of an interim distribution of profit in January of the following year.¹² It is distributed in full, unless it exceeds the ECB's net profit for the year, and is subject to any decisions by the Governing Council of the ECB to make transfers to the provisions for foreign exchange rate, interest rate, credit and gold price risks. The result from ECB interim profit distribution is recorded by the euro zone NCBs as income of the financial year when this income was accrued, not received.

After the Governing Council approves the ECB annual accounts, the remaining profit is distributed to the shareholders of the ECB in proportion to the Eurosystem capital key pursuant to Article 33 of the Statute of the ESCB and of the ECB. The result from the ECB final profit distribution is recorded by the NCBs as income of the financial year when this income was received.

The received distribution of the ECB profit is disclosed in the Profit and Loss Account item 4 'Income from equity instruments' (see Note 35 'Income from equity instruments').

5. POST-BALANCE SHEET EVENTS

Pursuant to Article 29 of the Statute of the ESCB and of the ECB, shares of the NCBs in the subscribed capital of the ECB are adjusted every five years on the basis of population and GDP data provided by the European Commission. The most recent such adjustment took effect on 1 January 2019.

Consequently, the Bank of Lithuania's share in the subscribed capital of the ECB decreased by 0.0073 percentage point and amounts to 0.4059% as of 1 January 2019. The Eurosystem capital key of the Bank of Lithuania decreased by 0.00396 percentage point and amounts to 0.58304%.

Given the decrease of the Bank of Lithuania's share in the paid-up capital of the ECB, EUR 790 thousand from the contribution to the ECB capital was repaid to the Bank of Lithuania on 1 January 2019 and the Bank of Lithuania's Balance Sheet item 'Participating interest in the ECB' decreased to EUR 206,393 thousand.

The adjustment to the ECB capital key entailed a change in the Bank of Lithuania's claims equivalent to the transfer of foreign reserves; the respective Balance Sheet item decreased by EUR 4,230 thousand to EUR 235,223 thousand.

In addition, given the adjustment of the banknote allocation key on 1 January 2019, the Bank of Lithuania's share in the allocation of euro banknotes in the Eurosystem was changed.

6. NOTES ON THE BALANCE SHEET

NOTE 1. GOLD AND GOLD RECEIVABLES

	31 December 2018	31 December 2017
Gold holdings in		
Troy ounces	187,171	187,159
Kilograms	5,822	5,821
Price per one Troy ounce, EUR	1,120.961	1,081.881
Value of gold, EUR thousands	209,811	202,484

The gold held by the Bank of Lithuania as at 31 December 2018, the same as at 31 December 2017, was invested in gold swaps.

Compared to 2017, gold holdings in 2018 slightly increased due to differences in weight of gold bars arising from settlements of gold investment transactions.

The overall increase in the value of gold was caused by the rise in the gold price in financial markets in 2018.

¹² Decision ECB/2014/57 of 15 December 2014 on the interim distribution of the income of the European Central Bank (recast), OJ L 53, 25.2.2015, p. 24., as amended.

NOTE 2. RECEIVABLES FROM THE IMF

EUR thousands

	31 December 2018	31 December 2017
Balance in the SDR account with the IMF	166,867	163,051
Reserve tranche position in the IMF	34,073	41
Lithuania's quota in the IMF	536,724	524,447
Balance in the IMF account No 1 with the Bank of Lithuania	(502,651)	(1,343)
Promissory notes of the government of the Republic of Lithuania	-	(523,062)
Total	200,940	163,092

The major part of the SDR balance in the SDR account with the IMF, managed by the Bank of Lithuania, is comprised of SDR 137,239 thousand, allocated to the Republic of Lithuania by the IMF in 2009, the counterpart (EUR 166,800 thousand) of which is disclosed under the Balance Sheet of the Bank of Lithuania liability item 9 'Counterpart of special drawing rights allocated by the IMF'. The Bank of Lithuania receives interest on balance in the SDR account with the IMF and pays interest on SDR allocated to the Republic of Lithuania by the IMF.

The increase in the euro equivalent value of the SDR balance in the SDR account with the IMF was due to the appreciation of the SDR against the euro in 2018.

The Bank of Lithuania performed the function of the depository of IMF funds until the end of 2017. Pursuant to Law No XIII-877 of the Republic of Lithuania on the membership of the Republic of Lithuania in the International Monetary Fund of 12 December 2017, the Bank of Lithuania took over the functions of the fiscal agency of the IMF from the Ministry of Finance of the Republic of Lithuania in the beginning of 2018 and since then has carried out financial operations of the IMF on behalf the Republic of Lithuania using financial assets of the Bank of Lithuania. In implementing this Law, the Bank of Lithuania took over the rights and liabilities related to the performance of the fiscal agency's functions of the IMF on 8 February 2018. The rights are reflected by the Lithuania's quota in the IMF which belongs to the Republic of Lithuania and represents its participation and voting power within the IMF. The liabilities to the IMF which were ensured until 31 December 2017 by promissory notes issued by the government of the Republic of Lithuania, are presented by the Bank of Lithuania as the balance in the IMF account No 1 with the Bank of Lithuania.

The increase in the reserve tranche position in the IMF as at 31 December 2018, compared to 31 December 2017, was due to participation in the Financial Transactions Plan. The Bank of Lithuania receives interest on funds transferred under the Financial Transactions Plan.

NOTE 3. BALANCES WITH BANKS AND SECURITY INVESTMENTS, EXTERNAL LOANS AND OTHER EXTERNAL ASSETS DENOMINATED IN FOREIGN CURRENCY

This Balance Sheet item consists of the Bank of Lithuania's balances with credit institutions, investments in securities and reverse repurchase agreements of non-euro area residents denominated in foreign currency.

EUR thousands

	USD	JPY	CZK	CHF	GBP	Other	Total
31/12/2018							
Balances in current accounts	2,159	1,489,268	641,126	320,851	1,525	3,373	2,458,302
Debt securities	1,885,517	-	-	-	191,890	240,667	2,318,074
Marketable equity securities	482,978	-	-	-	-	-	482,978
Reverse repurchase agreements	1,397	-	-	-	-	-	1,397
Total	2,372,051	1,489,268	641,126	320,851	193,415	244,040	5,260,751
31/12/2017							
Balances in current accounts	1,810	580,517	502,696	835,528	1,736	778	1,923,064
Debt securities	1,231,790	-	-	-	156,341	281,190	1,669,321
Marketable equity securities	247,152	-	-	-	-	-	247,152
Reverse repurchase agreements	750	-	-	-	-	-	750
Total	1,481,503	580,517	502,696	835,528	158,077	281,967	3,840,288

The Bank of Lithuania manages financial investments using funds temporarily free from performing the single monetary policy (see section 4.8 of the Accounting Policy).

The balances in current accounts denominated in Japanese yen increased due to short-term transactions conducted so as to benefit from favourable conditions in the money market at year-end.

In 2018, the Bank of Lithuania increased investments in debt securities and in exchange traded fund units, replicating corporate debt security indexes, denominated in US dollars. The currency risk of the reserve portfolio and the share of investment portfolio denominated in US dollars is not hedged and, therefore, substantial fluctuations in these investments' value in euros are possible.

Breakdown of balances with banks and security investments, external loans and other external assets by the economic area of residence of the issuer and counterparty

EUR thousands	31 December 2018	31 December 2017
USA	2,263,812	1,434,638
Japan	1,510,516	601,885
Non-euro area EU Member States	810,996	633,819
Switzerland	320,851	835,528
Canada	197,674	229,227
China	88,400	85,456
Korea	47,816	-
Other countries	20,685	19,734
Total	5,260,751	3,840,288

NOTE 4. CLAIMS ON EURO AREA RESIDENTS DENOMINATED IN FOREIGN CURRENCY

EUR thousands	USD	CAD	Other	Total
31/12/2018				
Balances in current accounts	60	61	49	170
Debt securities	71,820	-	-	71,820
Total	71,880	61	49	71,990
31/12/2017				
Balances in current accounts	9	0	0	9
Total	9	0	0	9

NOTE 5. CLAIMS ON NON-EURO AREA RESIDENTS DENOMINATED IN EURO

This Balance Sheet item consists of the Bank of Lithuania's balances in current accounts with non-euro area residents denominated in euro.

In 2018 the part of balances in current accounts that amounted to EUR 900 thousand was provided as collateral to the counterparty in the form of cash to ensure the discharge of the Bank of Lithuania obligations under transactions outstanding (in 2017 – EUR 6,700 thousand).

NOTE 6. LENDING TO EURO AREA CREDIT INSTITUTIONS RELATED TO MONETARY POLICY OPERATIONS DENOMINATED IN EURO

EUR thousands	31 December 2018	Conducted (repaid) in 2018	31 December 2017
Longer-term refinancing operations	173,000	(130,000)	303,000
Marginal lending facility	16,166	16,166	-
Total	189,166	(113,834)	303,000

Descriptions of these operations are presented in section 4.3 of the Explanatory Notes 'Lending to euro area credit institutions denominated in euro'.

In 2018 no impairment losses from these monetary policy operations were incurred by the Bank of Lithuania.

NOTE 7. OTHER CLAIMS ON EURO AREA CREDIT INSTITUTIONS DENOMINATED IN EURO

This item consists of the Bank of Lithuania's balances in current accounts with credit institutions which do not relate to monetary policy operations. As at 31 December 2018, the balances in current accounts amounted to EUR 360 thousand (as at 31 December 2017 – EUR 12,077 thousand).

NOTE 8. SECURITIES HELD FOR MONETARY POLICY PURPOSES

This item consists of the Republic of Lithuania government and supranational securities acquired by the Bank of Lithuania within the scope of the public sector purchase programme (see section 4.4. of the Explanatory Notes 'Securities held for monetary policy purposes').

EUR thousands

Public sector purchase programme	31 December 2018		31 December 2017	
	Amortised cost	Market value	Amortised cost	Market value
The Republic of Lithuania government securities	1,847,379	1,859,293	1,720,641	1,743,946
Supranational securities	8,908,182	8,937,537	7,978,782	7,994,057
Total	10,755,562	10,796,829	9,699,423	9,738,003

The market value of the securities presented in the table is not recorded on the Balance Sheet or in the Profit and Loss Account but is provided for presentation purposes only.

As a result of an impairment test conducted as at 31 December 2018 on securities purchased under the public sector purchase programme, the Governing Council of the ECB decided that all future cash flows on these securities were expected to be received, therefore no impairment losses from securities held by the Bank of Lithuania were incurred in 2018.

NOTE 9. OTHER SECURITIES

The Bank of Lithuania's investments in debt and marketable equity securities by euro area residents, presented in this item were marked to market in 2018 and 2017.

EUR thousands

	31 December 2018	31 December 2017
Debt securities	184,176	22,871
Marketable equity securities	701,674	543,605
Total	885,850	566,476

Marketable equity securities are investments in exchange traded fund units, replicating corporate debt or equity securities indexes.

As at 31 December 2018, holdings of both debt and marketable equity securities increased due to implementation of active investment decisions.

NOTE 10. PARTICIPATING INTEREST IN THE ECB

EUR thousands

	31 December 2018	31 December 2017
Contribution of the Bank of Lithuania to the ECB capital	44,729	44,729
Contribution of the Bank of Lithuania to the reserves of the ECB and to provisions, equivalent to reserves	162,454	162,454
Total	207,183	207,183

With effect from 1 January 2015, the share of the Bank of Lithuania in the subscribed and paid-up capital of the ECB comprises 0.4132% or EUR 44,729 thousand.

The Bank of Lithuania, pursuant to Article 48.2 of the Statute of the ESCB and of the ECB, has contributed to the reserves of the ECB and to provisions, equivalent to reserves, EUR 162,454 thousand.

NOTE 11. CLAIMS EQUIVALENT TO THE TRANSFER OF FOREIGN RESERVES

Upon joining the Eurosystem, the Bank of Lithuania, pursuant to Article 48.1 of the Statute of the ESCB and of the ECB, transferred its share of foreign reserves to the ECB.

Claims equivalent to the transfer of foreign reserves of the Bank of Lithuania, shown in this Balance Sheet item, comprise EUR 239,454 thousand. These claims were determined by multiplying the amount of the foreign reserves already transferred to the ECB at historical exchange rates (31 December 1998) by the ratio

between the number of shares subscribed by the NCB concerned and the number of shares already paid up by the other NCBs.

NOTE 12. NET CLAIMS RELATED TO THE ALLOCATION OF EURO BANKNOTES WITHIN THE EUROSYSYEM

This item presents the claim of the Bank of Lithuania to the Eurosystem, related to the allocation of euro banknotes within the Eurosystem (see section 2.12 of the Explanatory Note 'Banknotes and coins in circulation' and Note 18 'Banknotes in circulation'). As at 31 December 2018, compared to 31 December 2017, these net claims of the Bank of Lithuania decreased by EUR 356,199 thousand or 11% due to a higher increase in the nominal value of the banknotes put into circulation by the Bank of Lithuania (23%) compared to the rise in the nominal value of banknotes in circulation in the entire Eurosystem (5%).

NOTE 13. TANGIBLE AND INTANGIBLE FIXED ASSETS

EUR thousands

	Tangible assets				Intangible assets (including assets under construction)	Total
	Buildings and construction in progress	Cash processing equipment (including assets under construction)	Computer equipment (including assets under construction)	Other tangible assets (including assets under construction)		
Acquisition cost as at 31 December 2017	36,313	5,829	11,533	7,899	9,749	71,322
Additions in 2018	18	51	1,181	110	1,952	3,312
Disposals in 2018	-	(15)	(192)	(107)	-	(314)
Acquisition cost as at 31 December 2018	36,331	5,865	12,523	7,902	11,700	74,320
Accumulated depreciation as at 31 December 2017	(15,226)	(4,944)	(9,201)	(6,297)	(4,872)	(40,541)
Depreciation in 2018	(2,180)	(195)	(916)	(106)	(1,028)	(4,426)
Depreciation of disposed assets in 2018	-	15	192	107	-	314
Accumulated depreciation as at 31 December 2018	(17,406)	(5,124)	(9,926)	(6,296)	(5,900)	(44,652)
Net carrying amount as at 31 December 2018	18,924	741	2,597	1,605	5,800	29,668
Net carrying amount as at 31 December 2017	21,086	885	2,332	1,602	4,877	30,781

The significant impact on the increase (EUR 1,403 thousand) of intangible fixed assets in 2018 had the recognition of six intangible asset items internally generated by way of projects. A part of this cost (EUR 145 thousand) was comprised of the depreciation of the assets used for these projects, therefore, depreciation of tangible and intangible fixed assets presented in the Profit and Loss Account is lower than depreciation accumulated during 2018.

In 2017, the Board of the Bank of Lithuania made a decision to implement the renovation project of the Bank of Lithuania's premises situated in Vilnius, Žirmūnų g. 151. During the implementation of this project, part of the premises will be dismantled in 2019. The useful life of the part of the premises to be dismantled was reduced to the date of derecognition (31 December 2018), thus the depreciation of this building increased by EUR 1,312 thousand in 2018 (in 2017 – by EUR 547 thousand).

The Bank of Lithuania has not concluded any transactions with the mortgage of tangible assets of the Bank of Lithuania.

NOTE 14. OTHER FINANCIAL ASSETS

This item presents the Bank of Lithuania's investments in non-marketable equity instruments, the price of which is not quoted in the market, as well as the Bank of Lithuania's balances in current accounts with euro area residents (non-credit institutions) denominated in euro.

EUR thousands

	31 December 2018	31 December 2017
Bank for International Settlements shares	3,334	3,334
Balances in current accounts	934	-
SWIFT shares	100	21
Total	4,368	3,355

The Bank of Lithuania is a member of the Bank for International Settlements (BIS), with 1,070 shares, the acquisition cost of which is EUR 3,334 thousand and the nominal value per share is SDR 5,000. The Bank of Lithuania received EUR 304 thousand in dividends for these BIS shares in 2018 (EUR 394 thousand in 2017).

In 2018, The Bank of Lithuania additionally acquired 17 SWIFT shares for EUR 79 thousand. As at 31 December 2018, the Bank of Lithuania held 24 SWIFT shares with the acquisition cost of EUR 100 thousand. Dividends are not paid for these shares.

NOTE 15. OFF-BALANCE-SHEET INSTRUMENTS REVALUATION DIFFERENCES

These items represent the revaluation of foreign currency to be paid and received under foreign exchange transactions due to changes in the market rates and the revaluation of non-deliverable foreign exchange forward transactions, interest rate swaps and forward transactions in securities due to market price movements.

EUR thousands

	31 December 2018		31 December 2017	
	Positive differences	Negative differences	Positive differences	Negative differences
Foreign exchange transactions	54,012	75,733	62,888	30,461
Non-deliverable foreign exchange forwards	959	2,010	6,122	16,170
Interest rate swaps	348	526	2,325	996
Forward transactions in securities	3	5	-	-
Total	55,324	78,275	71,336	47,626

NOTE 16. ACCRUALS AND PREPAID EXPENSES

EUR thousands

	31 December 2018	31 December 2017
Accrued interest income	61,855	64,439
On securities held for monetary policy purposes	44,320	49,428
On financial derivatives	8,548	8,569
On other securities	7,910	5,258
On accounts and deposits	1,075	1,183
Other accrued interest	3	-
Debt securities coupon payment purchased	7,083	5,837
Prepaid expenses	1,261	1,191
Total	70,200	71,466

NOTE 17. SUNDRY

EUR thousands

	31 December 2018	31 December 2017
Dividends receivable	1,395	540
Short-term assets	540	466
Loans to the staff of the Bank of Lithuania	370	416
Advances and other receivables	76	1,279
Total	2,380	2,702

Dividends receivable are dividends of marketable equity securities that are recognised as income on their announcement day but not received yet.

NOTE 18. BANKNOTES IN CIRCULATION

EUR thousands

	31 December 2018	31 December 2017
Euro banknotes issued by the Bank of Lithuania	3,647,815	2,965,358
Adjustment for banknote allocation in the Eurosystem	3,578,452	3,906,279
The ECB's share of euro banknotes in circulation	(578,143)	(549,771)
Total	6,648,124	6,321,866

This item consists of the Bank of Lithuania's share of total euro banknotes in circulation according to the banknote allocation key (see section 2.12 of the Explanatory Notes 'Banknotes and coins in circulation'). As at 31 December 2018, the banknote allocation key was 0.54%. The nominal value of euro banknotes actually issued by the Bank of Lithuania in 2018 increased by 23%. As this was less than the allocated amount, the difference of EUR 3,300,309 thousand (compared to EUR 3,356,508 thousand as at 31 December 2017) is shown under the asset sub-item 'Net claims related to the allocation of euro banknotes within the Eurosystem' (see Note 12).

NOTE 19. LIABILITIES TO EURO AREA CREDIT INSTITUTIONS RELATED TO MONETARY POLICY OPERATIONS DENOMINATED IN EURO

EUR thousands

	31 December 2018	Conducted in 2018	31 December 2017
Current accounts (covering the minimum reserve system)	5,997,113	-	5,077,380
Deposits related to margin calls	19,000	53,800	-
Total	6,016,113	53,800	5,077,380

The minimum reserve balances have been remunerated at the latest available marginal interest rate used by the Eurosystem in its tenders for main refinancing operations¹³. The reserves held in excess of the minimum requirements are remunerated at a lower rate of either 0% or the deposit facility rate.

Descriptions of liquidity absorbing monetary policy operations are presented in the Explanatory Notes, section 4.5. 'Liabilities to euro area credit institutions related to monetary policy operations denominated in euro'.

NOTE 20. OTHER LIABILITIES TO EURO AREA CREDIT INSTITUTIONS DENOMINATED IN EURO

As at 31 December 2018, the Bank of Lithuania had no other liabilities to the euro area credit institutions denominated in euro. As at 31 December 2017, this item presented collateral in the form of cash, whereby the counterparty ensured the discharge of its obligations towards the Bank of Lithuania under transactions outstanding (EUR 1,200 thousand).

NOTE 21. LIABILITIES TO OTHER EURO AREA RESIDENTS DENOMINATED IN EURO

This item contains the balances on the current accounts of euro area residents with the Bank of Lithuania denominated in euro.

EUR thousands

	31 December 2018	31 December 2017
Liabilities to the general government	893,165	1,840,777
Other liabilities	118,425	28,153
Total	1,011,590	1,868,929

The increase of other liabilities is related to the rise in the number of non-credit institution sector participants in the payment system CENTROLINK operated by the Bank of Lithuania (i.e. payment and e-money institutions).

NOTE 22. LIABILITIES TO NON-EURO AREA RESIDENTS DENOMINATED IN EURO

This item presents balances in current accounts of the non-euro area participants of the payment system CENTROLINK operated by the Bank of Lithuania (i.e. payment and e-money institutions) and international institutions with the Bank of Lithuania denominated in euro.

¹³ The marginal interest rate used by the Eurosystem in its tenders for the main refinancing operations was 0% in 2017 and 2018.

EUR thousands

	31 December 2018	31 December 2017
Balances in current accounts	122,274	11,400
Other liabilities	800	-
Total	123,074	11,400

The increase of balances in current accounts is related to the rise in the number of the non-credit institution sector participants in the payment system CENTROLINK operated by the Bank of Lithuania (i.e. payment and e-money institutions).

NOTE 23. LIABILITIES TO EURO AREA RESIDENTS DENOMINATED IN FOREIGN CURRENCY

This item shows gold swaps and repurchase agreements in foreign currency concluded by the Bank of Lithuania with euro area financial sector residents, as well as liabilities to the general government, the main part of which consists of balances in current accounts of government institutions in foreign currency.

EUR thousands

	USD	CAD	CHF	XDR	Total
31/12/2018					
Liabilities to the financial sector	216,062	-	-	-	216,062
Gold swaps	216,062	-	-	-	216,062
Liabilities to the general government	184	-	-	-	184
Total	216,245	-	-	-	216,245
31/12/2017					
Liabilities to the financial sector	171,080	28,007	25,445	-	224,531
Repurchase agreements	-	28,007	-	-	28,007
Gold swaps	171,080	-	25,445	-	196,525
Liabilities to the general government	198	-	-	41	238
Total	171,277	28,007	25,445	41	224,770

NOTE 24. LIABILITIES TO NON-EURO AREA RESIDENTS DENOMINATED IN FOREIGN CURRENCY

This item presents repurchase agreements concluded by the Bank of Lithuania with non-euro area residents and other liabilities in foreign currency with a total value of EUR 47,475 thousand as at 31 December 2018 (compared to EUR 31,936 thousand as at 31 December 2017).

NOTE 25. OTHER LIABILITIES WITHIN THE EUROSISTEM (NET)

EUR thousands

	31 December 2018	31 December 2017
Balance in TARGET2 account	5,760,679	4,026,154
Distribution of monetary income	(25,548)	(35,074)
Interim distribution of the ECB profit	(6,993)	(5,798)
Total	5,728,138	3,985,282

Other liabilities within the Eurosystem include (1) Intra-Eurosystem balance (net) of the Bank of Lithuania *vis-à-vis* the ECB in respect of the transfers through TARGET2 by the ESCB national central banks and the ECB; (2) the position *vis-à-vis* the ECB in respect of monetary income redistribution's amount receivable (see Note 36 'Net result of pooling of monetary income'); (3) the Bank of Lithuania's position *vis-à-vis* the ECB in respect of any amounts receivable or refundable, including the amount due to the Bank of Lithuania in respect of the ECB's interim profit distribution (see Note 35 'Income from equity instruments').

NOTE 26. ITEMS IN COURSE OF SETTLEMENT

As at 31 December 2018, this item consisted of cash management operations with commercial banks in the course of settlement (EUR 3,691 thousand). As at 31 December 2017, the balance of this item consisted of the marketable equity securities' purchase transactions (EUR 11,869 thousand) and cash management operations with commercial banks in the course of settlement (EUR 9,600 thousand).

NOTE 27. ACCRUALS AND INCOME COLLECTED IN ADVANCE

EUR thousands

	31 December 2018	31 December 2017
Accrued interest expenses	16,292	7,754
On financial derivatives	14,922	5,865
On monetary policy operations	1,359	1,852
Other accrued interest expenses	10	37
Other accrued expenses	1,074	1,226
Income collected in advance	43	45
Total	17,409	9,025

The increase in accrued interest expenses on financial derivatives resulted due to the increased accrued interest expenses on foreign exchange forward and swap transactions (as at 31 December 2018, the balance of these items amounted to EUR 9,961 thousand, as at 31 December 2017 – EUR 3,162 thousand).

NOTE 28. SUNDRY

EUR thousands

	31 December 2018	31 December 2017
Litas banknotes in circulation	87,443	91,190
Euro coins in circulation	103,397	90,092
Litas coins in circulation	32,095	32,182
Sundry	537	697
Total	223,472	214,162

NOTE 29. PROVISIONS

EUR thousands

	31 December 2018	31 December 2017
Provisions for risks (see the Explanatory Notes, section 2.13 'Provisions for covering financial risks and liabilities')	118,420	102,420
Provisions for unrealised impairment loss of monetary policy operations established by the ECB	946	404
Provisions for liabilities related to	4,188	4,070
Termination benefits, payable to staff who will qualify for the state social insurance pension while working at the Bank of Lithuania	1,726	1,814
Wages and salaries payable for annual leave	1,914	1,675
Termination benefits to the members of the Board as provided in the Law on the Bank of Lithuania	172	158
Termination benefits by agreements payable to the staff in the subsequent financial year	-	7
Provisions for exchanging derecognised litas banknotes and coins	376	417
Total	123,554	106,895

In 2018, the Board of the Bank of Lithuania, based on risk assessment, made a decision to form additional risk provisions amounting to EUR 16,000 thousand (no additional provisions for risks were formed in 2017).

As a result of the impairment test conducted on its securities held under the corporate sector purchase programme as at 31 December 2018, the Governing Council of the ECB has deemed it appropriate to establish a provision of EUR 161,075 thousand against credit risk losses in monetary policy operations. In accordance with Article 32.4 of the Statute of the ESCB and of the ECB, losses from the aforementioned securities' holdings are shared in full by the Eurosystem NCBs in proportion to their prevailing Eurosystem capital key. As a result, a provision of EUR 946 thousand equal to the Eurosystem capital key of the Bank of Lithuania was created. This provision was recognised as part of the result of monetary income pooling (see Note 36 'Net result of pooling of monetary income'). Accordingly, the Bank of Lithuania dissolved the provisions created in 2017 that amounted to EUR 404 thousand and in such way covered realised losses caused by the sale of the impaired securities.

Provisions for the exchange of derecognised litas banknotes and coins are the provisions, formed in 2014, for covering the nominal value of derecognised litas banknotes and coins, which may be returned to the Bank of

Lithuania for exchange into euro. The share of these provisions amounting to EUR 40 thousand was used in 2018 (compared to EUR 67 thousand in 2017).

As at 31 December 2018, the Bank of Lithuania was a defendant or co-respondent in four legal proceedings related to financial market supervision performed by the Bank of Lithuania. Because of the low probability of settlement of the claims brought against the Bank of Lithuania or their low relevance, no provisions were formed for these claims.

NOTE 30. REVALUATION ACCOUNTS

Revaluation accounts represent unrealised revaluation gains of foreign currency, debt and marketable equity securities, as well as off-balance-sheet financial instruments. Unrealised revaluation gains of financial items, which built up before joining the euro area, are shown separately from other revaluation gains.

EUR thousands

	31 December 2018	31 December 2017
Revaluation accounts		
Pre-system unrealised gains	164,456	164,456
Foreign currency	67,135	2
Gold	27,647	20,332
Debt securities	12,249	2,449
Equity securities	8,808	21,641
Financial derivatives	1,311	8,447
Total	281,606	217,327

Unrealised revaluation losses, recognised as expenses at the end of 2018 are presented in Note 33. 'Net result of financial operations, write-downs and risk provisions'.

NOTE 31. CAPITAL

Statement of changes in equity for 2018

EUR thousands

	31 December 2018	2017 profit distribution	31 December 2017
Capital			
Authorised capital	60,000	–	60,000
Reserve capital	405,146	20,757	384,389
Total	465,146	20,757	444,389

The authorised capital of the Bank of Lithuania amounts to EUR 60,000 thousand and is fully formed.

Pursuant to the Law on the Bank of Lithuania, the Bank of Lithuania's reserve capital must not be lower than five amounts of its authorised capital and can be increased from the Bank of Lithuania's profit by an independent decision of the Board of the Bank of Lithuania, adopted taking into account risks and their likely impact. Reserve capital is used for the Bank of Lithuania's loss absorption.

In 2015, the Board of the Bank of Lithuania made a decision to increase the reserve capital up to a specified amount, providing that the annual rate of increase shall be proportionally close to the Bank of Lithuania's projected Republic of Lithuania GDP in the medium-term (calculated in comparative prices) annual average growth.

7. NOTES ON THE PROFIT AND LOSS ACCOUNT

NOTE 32. NET INTEREST INCOME

EUR thousands

	2018		2017	
	Interest income	Interest expense	Interest income	Interest expense
Monetary policy operations	57,927	(332)	37,028	(1,229)
Securities held for monetary policy purposes	41,901	-	26,782	-
Current accounts (covering the minimum reserve system)	15,992	-	10,244	-
Deposits related to margin calls	34	-	2	-
Longer-term refinancing operations	-	(332)	-	(1,229)
Debt securities	56,328	-	19,428	-
Balances in current accounts with the Bank of Lithuania	5,676	-	6,885	-
Interest rate swaps	483	-	-	(502)
Repurchase agreements	-	(3,050)	-	(2,243)
The Bank of Lithuania's balances in current accounts	-	(3,268)	-	(352)
Gold swaps	-	(4,501)	-	(2,178)
Foreign exchange transactions	-	(29,192)	1,349	-
Other	99	-	120	-
Total interest income (expense)	120,513	(40,343)	64,810	(6,504)
Net interest income	80,171		58,306	

In 2018, the net interest income increased by EUR 21,865 thousand, compared to 2017, mainly due to the growth in net interest income from debt securities and monetary policy operations. This growth was related to the increase in interest rates of debt securities denominated in US dollars, purchase of securities under the public sector purchase programme (see Note 8 'Securities held for monetary policy purposes') and still negative deposit facility rate (-0.4%).

The net interest income decreased due to the significantly higher interest expense on foreign exchange transactions. The volume of these foreign exchange hedging transactions increased due to the growth of investments in US dollar denominated debt securities with hedged currency risk; furthermore, the price for these transactions was higher, following the differences between interest rates in the US and European markets.

NOTE 33. NET RESULT OF FINANCIAL OPERATIONS, WRITE-DOWNS AND RISK PROVISIONS

This item includes (a) net income (expense) related to the sale transactions of financial instruments, gold and foreign currency; (b) write-downs of financial items, which consist of unrealised revaluation loss as a result of the decline in market prices and rates on 31 December 2018 as compared to the average prices and rates of these items; and (c) additional provisions for foreign exchange rate, interest rate, gold price and credit risks, formed, by a decision of the Board of the Bank of Lithuania, based on the assessment of the level of accounting risk assumed.

EUR thousands

	2018	2017
Net realised gains (losses) arising from	(25,544)	6,125
Transactions in securities	(18,525)	3,215
Transactions in gold and foreign currency	(8,348)	(888)
Interest rate derivatives	1,329	3,798
Write-downs on financial items	(23,527)	(50,406)
Securities	(20,969)	(9,192)
Financial derivatives	(2,542)	(17,166)
Foreign currency	(16)	(24,048)
Transfers to provisions for risks	(16,000)	-
Net result of financial operations, write-downs and risk provisions	(65,071)	(44,281)

NOTE 34. NET INCOME FROM FEES AND COMMISSIONS

EUR thousands

	2018	2017
Fees and commissions income	7,426	7,091
Contributions of supervised financial market participants	5,922	5,554
Settlement services	705	617
Security lending	451	559
Other services	348	362
Fees and commissions expense	(3,049)	(1,852)
Financial instruments	(2,761)	(1,552)
Other	(288)	(300)
Net income from fees and commissions	4,377	5,239

Pursuant to the Law on the Bank of Lithuania, the costs of financial market supervision are funded by the contributions of supervised financial market participants and own funds of the Bank of Lithuania. In 2018, the Bank of Lithuania collected contributions amounting to EUR 5,617 thousand to cover the costs of financial market supervision (in 2017 – EUR 5,260 thousand).

In 2015, the Bank of Lithuania was assigned the function of financial institutions resolution. In 2018, the Bank of Lithuania collected the contributions of financial market participants amounting to EUR 305 thousand to finance the activity of the financial sector resolution authority (in 2017 – EUR 293 thousand).

In 2018, Fees and commissions expense grew mainly due to more fees paid in relation to interest rate futures.

NOTE 35. INCOME FROM EQUITY INSTRUMENTS

EUR thousands

	2018	2017
Dividend income from marketable equity securities	11,703	3,377
Income from distribution of the ECB profit	8,678	7,130
Dividend income from non-marketable equity securities	304	394
Total	20,685	10,900

In 2018, income from equity instruments increased due to the growth of investments in marketable equity securities denominated in US dollars and an increase in dividend yields.

Following a decision of the Governing Council of the ECB, the amount due to the euro area NCBs in 2018, with respect to the ECB's interim profit distribution, was EUR 1,191,362 thousand. The amount due to the Bank of Lithuania (EUR 6,993 thousand) was recognised as income of 2018. The result from the ECB final profit distribution of 2017 was also recognised as income of 2018 (see section 4.9 of the Explanatory Notes 'Distribution of the ECB profit').

NOTE 36. NET RESULT OF POOLING OF MONETARY INCOME

EUR thousands

	2018	2017
Net monetary income pooled by the Bank of Lithuania	(47,753)	(28,240)
Net monetary income reallocated to the Bank of Lithuania	71,653	63,332
Adjustment for the monetary income of previous years	1,649	(18)
The Bank of Lithuania's share in the provision against losses in monetary policy operations (see Note 29 'Provisions').	(946)	(404)
Reversal of income of the Bank of Lithuania's share in the provisions against losses in monetary policy operations of previous years	404	-
Net result of pooling of monetary income	25,007	34,670

NOTE 37. OTHER INCOME

EUR thousands

	2018	2017
Income from sale of collector coins and other numismatic items	2,820	899
Other miscellaneous income	258	317
Total	3,078	1,216

In 2018, an increase in income from sale of collector coins and other numismatic items was caused by the increased issue of collector coins (including gold coins) dedicated to the 100th anniversary of the restoration of Lithuania's independence.

NOTE 38. STAFF COSTS

EUR thousands

	2018	2017
Expenses on wages and salaries	12,151	11,461
To the members of the Board	383	351
To the heads of structural divisions	1,013	904
To other staff of the Bank of Lithuania	10,755	10,206
Other emoluments	306	402
Contributions to the State Social Insurance Fund	3,787	3,623
Expenses on (income from) provisions related to liabilities to the staff	158	830
Total	16,403	16,317

Pursuant to the Law on the Bank of Lithuania, the Board of the Bank of Lithuania consists of: the Chair, two Deputy Chairs, and two Members.

As at 31 December 2018, four Services, four autonomous Departments and four autonomous Divisions operated in the Bank of Lithuania. As at 31 December 2018, the Bank of Lithuania employed 583 staff members (at the end of 2017 – 591) of which 40 (at the end of 2017 – 38) worked under a fixed-term labour contract. In addition, 28 employees were on parental leave or unpaid leave for the term of their contracts with the ECB and the IMF (at the end of 2017 – 24).

In 2018, an increase in expenses on wages and salaries was caused by the growth of wages and salaries.

In 2018, the part of staff costs that amounted to EUR 353 thousand (in 2017 - EUR 460 thousand) were included in the initial costs of the intangible asset items internally generated by the way of projects (see section 2.11 of the Explanatory Notes and Note 13 'Tangible and intangible fixed assets') and are not presented in this item.

NOTE 39. ADMINISTRATIVE EXPENSES

EUR thousands

	2018	2017
Administrative expenses		
Tangible assets maintenance	3,012	3,024
Information system maintenance and information acquisition	2,088	1,346
Participation in international organisations fees	1,275	1,196
Business trips	846	802
Equipment and office supply	684	431
Training of the staff	444	378
Mail and telecommunication	343	264
Communication	283	299
Other	878	710
Total	9,853	8,449

NOTE 40. BANKNOTE PRODUCTION SERVICES

The Bank of Lithuania participates in the production of euro banknotes together with other NCBs of the euro area. The Governing Council of the ECB sets the denominations of euro banknotes and their quantities that must be produced each year from euro area NCB funds. In 2018, the Bank of Lithuania incurred euro banknote production expenses (amounting to EUR 1,837 thousand) that were necessary to supplement the Eurosystem's strategic reserve (in 2017 – EUR 2,307 thousand).

NOTE 41. OTHER EXPENSES

EUR thousands

	2018	2017
Collector and commemorative coin minting expenses	2,084	579
Euro circulation coin minting expenses	120	3,434
Cash circulation expenses	53	41
Other miscellaneous expenses	7	0
Total	2,264	4,054

NOTE 42. PROFIT DISTRIBUTION

Pursuant to Article 23 of the Law on the Bank of Lithuania, profit (loss) is distributable (coverable) as follows:

- 1) net distributable profit (loss), which consists of the profit (loss) for the last financial year and undistributed profit (if any) carried over from the previous financial periods, is distributed (covered) after the end of the financial year;
- 2) net distributable loss shall be covered from the reserve capital of the Bank of Lithuania. When the reserve capital is not sufficient to cover the net distributable loss, the remaining uncovered losses are carried forward to be covered by the distributable profit of the succeeding financial years;
- 3) net distributable profit shall be allocated in the following sequence:
 - to cover the uncovered loss carried forward;
 - for the authorised capital up to the amount specified in the Law on the Bank of Lithuania;
 - for the reserve capital up to the amount independently established by the decision of the Board of the Bank of Lithuania, taking into account the potential impact of risks; however, this capital shall not be less than five amounts of the authorised capital of the Bank of Lithuania;
 - to the State Budget as the profit contribution of the Bank of Lithuania. This contribution shall not exceed the amount corresponding to 70% of the calculated average of the profit (loss) of the Bank of Lithuania of the last three financial years.

The surplus of the distributable profit after allocation shall be carried forward as undistributed profit and shall be distributed in subsequent financial years.

Profit distribution

EUR

	2018	2017	2016
Profit distribution			
Allocation to the reserve capital of the Bank of Lithuania	20,905,554	20,757,026	15,493,621
Transfer to the state budget	12,704,656	11,169,059	11,510,168
Total	33,610,210	31,926,085	27,003,790

8. OTHER NOTES

NOTE 43. DERIVATIVES

As at 31 December 2018, the Bank of Lithuania had outstanding foreign exchange swaps, foreign exchange forwards, non-deliverable foreign exchange forwards, interest rate futures, interest rate swaps and forward transactions in securities. All these transactions were conducted in the context of the management of the Bank of Lithuania's financial assets (excluding monetary policy operations) and are presented in the off-balance sheet accounts.

Foreign exchange swaps and foreign exchange forwards

EUR thousands

	31 December 2018	31 December 2017
Claims	8,226,540	6,549,820
Liabilities	8,226,540	6,549,820

Non-deliverable foreign exchange forwards

EUR thousands

	31 December 2018	31 December 2017
Notional claims	337,792	519,879
Notional liabilities	338,357	530,287

Interest rate futures

EUR thousands

	31 December 2018	31 December 2017
Notional claims	12,302,559	2,254,127
Notional liabilities	9,070,379	4,429,584

Interest rate swaps

As at 31 December 2018, the contractual amount of interest rate swaps amounted to EUR 341,419 thousand (as at 31 December 2017 – EUR 680,187 thousand).

Forward transactions in securities

EUR thousands

	2018	2017
Claims	10,027	-
Receivable amounts	4,191	-
Receivable securities	5,836	-
Liabilities	10,027	-
Payable amounts	5,836	-
Payable securities	4,191	-

NOTE 44. ASSETS AND LIABILITIES OF THE BANK OF LITHUANIA BY FOREIGN CURRENCY

EUR thousands

	USD	CNY	XDR	GBP	CHF	CZK	Other
31/12/2018							
On-balance sheet assets	2,499,438	97,451	200,968	195,142	321,645	644,217	1,650,654
On-balance sheet liabilities	233,502	3,456	166,800	48,806	9,854	1,846	68,311
NET ON-BALANCE SHEET ASSETS (LIABILITIES)	2,265,936	93,995	34,168	146,336	311,791	642,372	1,582,343
Net off-balance sheet assets (liabilities) included into currency position	(888,418)	(379,058)	-	(143,357)	(313,158)	(641,686)	(1,582,551)
NET ASSETS (LIABILITIES)	1,377,518	(285,063)	34,168	2,979	(1,367)	685	(208)
31/12/2017							
On-balance sheet assets	1,500,226	86,626	163,092	158,945	841,083	503,176	836,695
On-balance sheet liabilities	244,438	646	163,026	2,676	25,445	10,633	34,181
NET ON-BALANCE SHEET ASSETS (LIABILITIES)	1,255,788	85,980	66	156,269	815,639	492,543	802,514
Net off-balance sheet assets (liabilities) included into currency position	(246,906)	(126,285)	-	(154,341)	(814,846)	(492,412)	(801,726)
NET ASSETS (LIABILITIES)	1,008,882	(40,305)	66	1,928	793	131	788



Collector and commemorative coins issued into circulation in 2018

» More information is available [here](#).

Resolutions adopted by the Board of the Bank of Lithuania in 2018

- » The Bank of Lithuania took active legislative actions, adopting regulatory Bank of Lithuania legal acts.
- » The Board of the Bank of Lithuania adopted 154 resolutions regulating activities of banks and other financial market participants; they are made publicly available on the [Register of Legal Acts](#).

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