

# CNB CZECH NATIONAL BANK



Annual  
Report  
2014





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NATIONAL  
BANK

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# MANDATE OF THE CZECH NATIONAL BANK

- **to maintain price stability,**
  - **to maintain financial stability and see to the sound operation of the financial system in the Czech Republic,**
  - **to issue banknotes and coins, manage the circulation of currency and administer clearing between banks,**
  - **to supervise the entities operating on the financial market.**
- 
- Through *monetary policy* we seek to preserve price stability, i.e. low and stable inflation. Through *macroprudential policy* we foster financial stability and resilience of the financial system, which are necessary conditions for the maintenance of price stability. Through the joint action of monetary policy and macroprudential policy, we contribute to maintaining confidence in the value of the Czech koruna and safeguarding the stability of the macroeconomic environment.
  - By *supervising the financial market and creating prudential rules and rules of conduct towards clients* we protect the clients of persons and institutions carrying on business on the financial market.
  - By *managing the interbank payment system and issuing banknotes and coins* we ensure smooth payments and cash circulation.
  - As the *bank of the state*, we provide banking services to the state and the public sector.
  - In line with our primary objective, we *manage international reserves with professional care*.
  - We are a *part of the European System of Central Banks* and contribute to the fulfilment of the ESCB's objectives and tasks.

## → WHAT WE BUILD ON

### → INDEPENDENCE

Broad independence of the central bank is a key condition for successful implementation of monetary policy, i.e. for sustained non-inflationary growth of the economy, as well as for objective supervision of the financial market.

### → OPENNESS AND CREDIBILITY

A high degree of independence must go hand in hand with a high degree of accountability to the public for fulfilling our objectives. We inform the public and their elected representatives regularly and openly about our objectives and their fulfilment and about our opinions, plans and predictions. This makes our actions comprehensible, predictable and therefore credible.

### → PROFICIENCY

Proficient and competent employees are vital if the CNB is to succeed in enhancing its reputation as a credible and open institution at home and on the international stage.

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# THE YEAR AT A GLANCE

- Czech economic growth accelerated in 2014, aided significantly by easy monetary policy. Although the direct risk of deflation associated with a slump in domestic demand was averted, inflation was below the lower boundary of the CNB's tolerance band throughout the year, dropping to almost zero towards the year-end. This was due to subdued inflation abroad and a decline in global oil prices. These factors also led to the inflation forecasts being gradually lowered.
- The Bank Board repeatedly extended the CNB's one-sided exchange rate commitment of CZK 27 to the euro in 2014 and early 2015 in response to actual and expected inflation. It also expressed its readiness to move the commitment to a weaker level if there were to be a long-term increase in deflation pressures capable of causing a slump in domestic demand, renewed risks of deflation in the Czech economy and a systematic decrease in inflation expectations.
- Governor Miroslav Singer won the Central Bank Governor of the Year in Europe award for 2014. He received the award in January 2014 from the prestigious monthly magazine *The Banker* published by the Financial Times Group. According to the magazine's editorial board, the award is an expression of the confidence of international financial markets in the CNB and its conduct of monetary policy.
- The President of the Czech Republic appointed Jiří Rusnok as a member of the CNB Bank Board with effect from 1 March 2014.
- The Czech financial sector remains sufficiently stable and is financially strong and ready to comply with the new European regulatory rules, as summed up in the tenth Financial Stability Report 2013/2014.
- The CNB revoked the credit union licence of WPB Capital due to an artificial increase in WPB Capital's capital funded from the credit union's funds granted in the form of loans, the acquisition of prohibited types of securities and the circumvention of exposure limits. The decision became final and conclusive on 24 June 2014.
- The CNB completed the gradual transformation of its branch network into a more efficient and effective organisation. Its branches in České Budějovice, Plzeň and Ústí nad Labem were converted into regional offices. The reorganisation will save the CNB tens of millions of koruna a year in operating expenses.
- In connection with the transposition of EU banking directives, in particular Directive 2014/59/EU of the European Parliament and of the Council establishing a framework for the recovery and resolution of credit institutions and investment firms, the CNB established a Resolution Department as of 1 November 2014.
- In their *Assessment of the Fulfilment of the Maastricht Convergence Criteria and the Degree of Economic Alignment of the Czech Republic with the Euro Area*, the Czech National Bank and the Ministry of Finance recommended that the Czech government should not set a target date for adopting the euro and thus should not attempt to enter ERM II during 2015.





# GOVERNOR'S FOREWORD



In the economic area, 2014 was shaped by the Bank Board's decision of November 2013 to weaken the koruna. This move was aimed at averting the real threat of deflation, attaining the inflation target earlier and helping the economy to recover faster. Our monetary policy focus was unchanged by the weakening of the koruna. The monetary policy objective is to ensure price stability, as it has always been. The only change was that the necessary monetary policy easing was achieved by means of the exchange rate instead of interest rates, which had been lowered to technical zero in November 2012.

It became even clearer during 2014 that the Czech economy was experiencing the expected and desired turnaround. The role of driver of growth was assumed increasingly by domestic demand instead of net exports. A recovery was recorded not only by household consumption, but also by private investment, which had been very subdued in previous years. The profitability of companies rose substantially in a short period of time and the improving growth prospects of the corporate sector started to translate into growth in employment, growth in the number of job vacancies and a decline in unemployment. The improving labour market situation boosted households' expectations and encouraged them to save less and spend more. Retail sales recorded a pronounced recovery focused on purchases of durable goods, especially cars. Industry expanded at a solid pace, with insufficient demand becoming a smaller and smaller constraint. The construction industry also emerged from a several-year recession.

However, the weakening of the koruna was not the sole cause of the Czech economic recovery. Two other major factors played a role. The first was a recovery in external demand, although this external stimulus boosted domestic growth less than we had expected at the end of 2013. And the second was the completion of the domestic fiscal consolidation process, which had held back the Czech economy quite significantly in previous years.

As the primary aim of weakening the koruna was to increase inflation, the central bank monitored price movements particularly closely. Following many years of year-on-year decline, adjusted inflation excluding fuels started to rise again, with the pace of this growth steadily increasing as the year progressed. Thanks mainly to this, headline inflation remained positive, albeit at very low levels – well below the 2% inflation target and our end-2013 forecasts. The lower-than-expected rise in inflation was due to much more subdued inflation abroad than we had originally assumed. Our analyses show that if we had not weakened the koruna, the Czech economy would have been in deflation for two years by now and annual headline inflation would have dropped to around -2%.

The Bank Board extended the asymmetric exchange rate commitment of CZK 27 to the euro several times in 2014 in response to actual and expected inflation. At the end of the year, as a result of gradually intensifying disinflationary pressures, it expressed its readiness to move the exchange rate commitment to a weaker level if there were to be a long-term increase in deflation pressures capable of causing a slump in domestic demand, renewed risks of deflation in the Czech economy and a systematic decrease in inflation expectations.

To sum up, the Czech economy changed almost beyond recognition in 2014. Most major economic statistics turned positive and the foundations of the recovery strengthened in almost all areas. The Czech economy also improved significantly in various international comparisons,

where it had performed rather poorly in 2013. So, more than one year on, our decision to weaken the koruna turned out to be not only beneficial, but also even more necessary than it had seemed in November 2013.

The use of the exchange rate as an additional monetary policy instrument led to changes in our external communication policy and practice. After evaluating public reaction to the weakening of the koruna we strengthened direct communication with target groups and brought in new tools and means of communication. We launched the *čnBlog* on our website, where we post articles written by CNB Bank Board members and experts. We also introduced roundtable discussions, to which we invite business leaders, economic analysts and representatives of the academic community in various regions. Roundtables were held in Ostrava in February, in Plzeň in April and in Hradec Králové in September. These meetings served their purpose, giving business people an opportunity to better understand the reasons which led us to weaken the koruna and giving us an insight into the microeconomic impacts of our monetary policy.

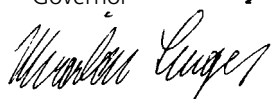
Turning to the internal workings of the central bank, the Bank Board underwent a change in line-up in 2014. The six-year term of office of Board Member Eva Zamrazilová expired at the end of February. She was replaced by Jiří Rusnok with effect from 1 March.

We also continued the streamlining measures commenced in previous years. At the end of June, we completed the gradual transformation of our branch network into a more efficient and effective organisation. Our branches in České Budějovice, Plzeň and Ústí nad Labem were converted into regional offices, which continue to provide the state, the public and other non-bank clients with a full range of services. The modus operandi of the branches in Brno, Hradec Králové, Ostrava and Praha were unchanged. All our offices outside Prague remained involved in supervising the financial market. The central bank thus retains a full presence in all seven regions of the Czech Republic. The reorganisation of the branch network will save us tens of millions of koruna a year in operating expenses. The changes included trimming the total number of job positions. As of 31 December 2014 the CNB had 1,321 employees, a decrease of 59 compared to the end of 2013. Despite that, the reorganisation allowed us to recruit more staff in the areas of consumer protection in the financial market and supervision of the financial market.

The organisational and personnel changes affected not only the branches, but also some departments of the bank. A new Executive Director of the General Secretariat was appointed on 1 July, the previously independent Communications Department was integrated into the General Secretariat at the beginning of December, and a Resolution Department was established at the start of November. Other organisational changes laid the groundwork for hiring more staff, especially in supervisory departments.

In 2014, we again issued five CZK 200 silver commemorative coins, one CZK 500 silver coin and two CZK 5,000 gold coins from a five-year cycle featuring technically, architecturally or historically interesting bridge structures in the Czech Republic. At the end of October we unveiled a new schedule of issuance for commemorative coins in 2016–2020. This will consist of two thematic cycles. The cycle of ten CZK 5,000 gold coins will commemorate castles of the Czech Republic. The cycle of CZK 500 silver coins will have a unifying theme of anniversaries relating to the foundation of the Czechoslovak Republic.

Miroslav Singer  
Governor



## **SEVEN**

The supreme governing body of the Czech National Bank is the Bank Board of the Czech National Bank. It sets monetary and macroprudential policy and the instruments for implementing those policies. It decides upon the fundamental monetary and macroprudential policy measures of the Czech National Bank and measures in the area of financial market supervision. The Bank Board has seven members. Its members are the Governor, two Vice-Governors and four other Bank Board members. All Bank Board members are appointed by the President of the Czech Republic for a maximum of two six-year terms.





# THE BANK BOARD

# THE BANK BOARD



## **The Bank Board as of 31 December 2014**

Pavel Řežábek, Kamil Janáček, Lubomír Lízal, Jiří Rusnok  
Mojmír Hampl, Miroslav Singer, Vladimír Tomšík

The Bank Board is the supreme governing body of the Czech National Bank. Its members are the Governor, two Vice-Governors and four other Bank Board members. Bank Board members are appointed and recalled by the President of the Czech Republic. They are appointed for a term of six years. No one may hold the position of Bank Board member more than twice.

Membership of the Bank Board is incompatible with the position of member of a legislative body, member of the Government and membership of the governing, supervisory or inspection bodies of other banks or commercial undertakings, and the performance of any independent gainful occupation, except for scientific, literary, journalistic, artistic and pedagogical activities and except for management of own assets. Membership of the Bank Board is incompatible with any activity which might cause a conflict of interest.

The Bank Board sets monetary and macroprudential policy in line with the CNB's primary objective, namely to maintain price stability, and in line with the task of maintaining financial stability, and sets the instruments for implementing those policies. It decides upon fundamental monetary and macroprudential policy measures and lays down principles for CNB transactions. It decides on key measures relating to financial stability, financial market supervision and cash and non-cash money circulation. It sets the CNB's overall development strategy and rules for the CNB's involvement in the activities of the EU, the European System of Central Banks (ESCB) and the European Systemic Risk Board (ESRB) and its cooperation with international financial institutions. It decides on the bank's organisational structure and the powers and responsibilities of the organisational units at its headquarters and branches. It also approves the CNB's budget and financial management principles.

The Governor, or, in his absence, a Vice-Governor nominated by him, chairs the meetings of the Bank Board. The Bank Board acts by a simple majority of the votes cast.

## **TWO THOUSAND AND FOURTEEN**

Czech economic growth accelerated, aided significantly by easy monetary policy, and the direct risk of deflation associated with a slump in domestic demand was averted. The Czech financial sector remained strong and ready to comply with new European regulatory rules.





# THE CNB IN 2014

# THE CNB IN 2014

## → MONETARY POLICY AND STATISTICS

### → Monetary policy and economic developments

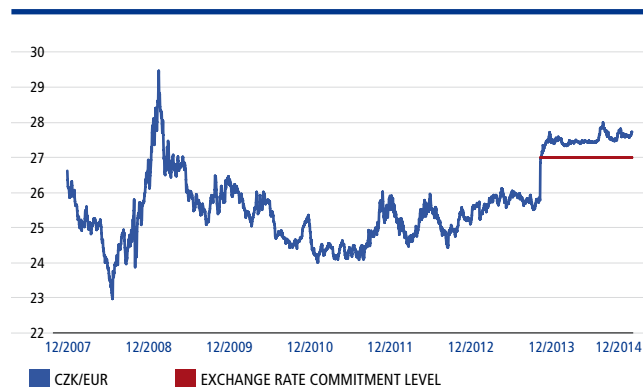
The primary monetary policy objective as laid down in the Act on the CNB is to maintain price stability. Since January 1998, the CNB has been achieving this under an inflation targeting regime in which it tries to keep inflation close to a declared target, defined as year-on-year consumer price index growth of 2% with a tolerance band of  $\pm 1$  percentage point.

The Czech economy went through a lengthy economic recession in 2012–2013 owing to weak external and in particular domestic demand, reflecting budget consolidation and low household and business confidence. The labour market situation deteriorated. There was a risk that inflation would turn negative at the start of 2014 after the effect of tax changes faded away and that deflationary expectations would emerge, leading to a halt in the nascent economic recovery or even a renewed economic downturn. All this was going on in a situation where monetary policy interest rates were at technical zero and the room for using standard monetary policy instruments had thus been exhausted. In November 2013, the CNB, in line with its previous communication, started to use the exchange rate of the koruna as an additional instrument for easing monetary policy. The one-sided commitment means that the CNB is ready to prevent excessive appreciation of the koruna below CZK 27 to the euro by intervening in the foreign exchange market, while allowing the koruna's exchange rate to float on the weaker side of this level.

Following the announcement of the exchange rate commitment the koruna quickly depreciated beyond the exchange rate commitment level. It then soon stabilised close to CZK 27.50 to the euro, which suggests that the exchange rate commitment quickly established a strong degree of credibility. The exchange rate stayed at this level (with minor deviations) throughout 2014 with no need for interventions by the CNB.

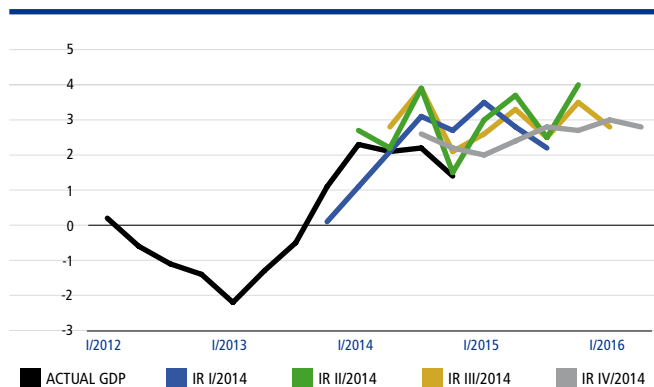
The Czech economy benefited from the weakening of the exchange rate. The economy grew by 2% in 2014. In addition to easy monetary policy, the growth was due to the unwinding of the restrictive effect of domestic fiscal policy and, to a lesser extent, to a recovery in external demand. The weakening of the koruna's exchange rate boosted not only export growth, but also growth in domestic investment and consumption, as firms and households stopped deferring their expenditure. The economic recovery positively affected the labour market through a rise in employment, a decline in the number of unemployed persons and renewed wage growth in the corporate sector.

The exchange rate of the koruna against the euro



GDP forecasts

(in %)



The GDP forecasts compiled by the CNB in 2014 predicted continued economic growth in 2015 and 2016 and differed very little from each other. Only in the second half of last year did the forecasts lower the GDP growth outlook for 2015 as a result of observed and, for the next few quarters, expected lower growth in external demand.

At the start of 2014, headline inflation dropped sharply to a level well below the lower boundary of the tolerance band around the CNB's target. This was due mainly to the fading out of VAT changes implemented the previous year and to a decline in administered prices. On the other hand, adjusted inflation excluding fuels – the measure of core inflation – turned positive for the first time in almost five years. This was due primarily to rapid dissipation of the anti-inflationary effect of the domestic economy, renewed wage growth and an increase in import prices. All these effects reflected, among other things, the weakened exchange rate of the koruna. Headline inflation thus edged up temporarily during 2014.

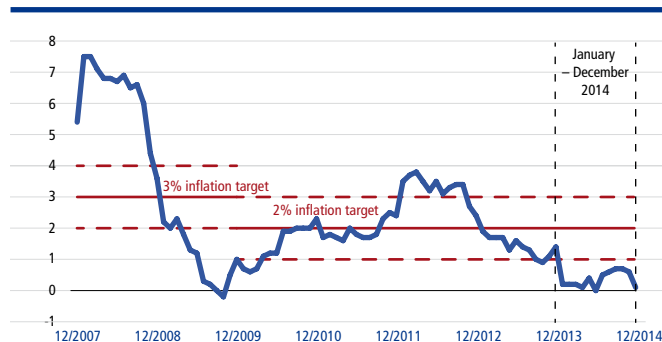
By contrast, the deflationary tendencies in the euro area deepened further last year, dampening growth in import prices and thus counteracting a rise in domestic inflation. Global oil prices declined significantly at the end of the year. As a result, fuel prices started to decline in year-on-year terms in December. Food prices also began to fall year on year owing to a previous decline in global prices of agricultural commodities and a ban on imports to Russia. Overall, this pushed headline inflation back down almost to zero.

The subdued external inflation and the decline in global commodity prices led to a gradual decrease in the inflation forecasts during 2014. While the winter forecast (Inflation Report I/2014) predicted that inflation would return to the target at the end of 2014 and rise temporarily to the upper boundary of the tolerance band at the start of 2015, the autumn forecast (Inflation Report IV/2014) foresaw inflation being in the lower half of the tolerance band throughout 2015 and returning to the target at the start of 2016. The inflation outlook was lowered despite the fact that the koruna's exchange rate was rather weaker than the level of the exchange rate commitment and the fact that the duration of the commitment was extended.

The actual and expected inflation developments resulted last year in a need to ease monetary policy further. In the regime of using the exchange rate as an additional monetary policy instrument, this can be achieved in two ways: (i) by extending the duration of the exchange rate commitment or (ii) by moving the level of the commitment. In 2014, the CNB chose the former option, as the Bank Board extended the CNB's exchange rate commitment in several steps. At its first monetary policy meeting in 2015 (held in February), the Bank Board stated that the CNB would not discontinue the use of the exchange rate as a monetary policy instrument before the second half of 2016. At the same time, it extended the time for

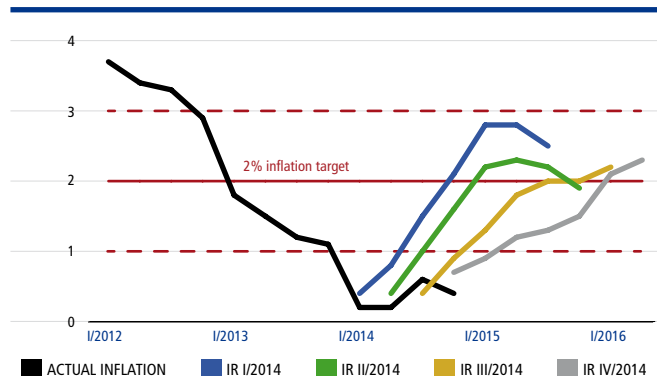
**Fulfilment of the inflation target**

(in %)



**Inflation forecasts**

(in %)



which monetary policy rates would be left at technical zero. In December 2014 and again in February 2015, the Bank Board also made any shift of the exchange rate commitment to a weaker level conditional on there being a long-term increase in deflation pressures capable of causing a slump in domestic demand, renewed risks of deflation in the Czech economy and a systematic decrease in inflation expectations.

More than one year on, it can be stated that the CNB Bank Board's November 2013 decision to start using the exchange rate as another instrument for easing monetary policy served its purpose, as it helped to avert the threat of long-term deflation associated with a slump in domestic demand. The pass-through of the weakened exchange rate to the Czech economy has so far been in line with the CNB's expectations, although it is occurring amid a much stronger-than-expected anti-inflationary effect of the external environment.

More detailed information on economic developments and monetary policy implementation can be found in the quarterly Inflation Reports available on the CNB website (*Monetary policy > Inflation reports*).

At the end of 2014, the CNB in cooperation with the Ministry of Finance prepared for the government the regular *Assessment of the Fulfilment of the Maastricht Convergence Criteria and the Degree of Economic Alignment of the Czech Republic with the Euro Area*. This document, which is available on the CNB website, resulted in a recommendation that the government not set a target date for adopting the euro and thus not attempt to enter ERM II during 2015. This recommendation was based on a number of factors. These included uncertainty regarding future economic growth in the euro area, as the economic recovery there is still fragile and the risk of the euro area economy falling into deflation and slipping back into recession persists. The preparedness of the Czech Republic itself to adopt the euro has improved compared to previous years. The country is compliant with all the Maastricht criteria except for ERM II participation, and will continue to be compliant in the medium term as well. However, in order to make fulfilment of the criteria sustainable and to further increase the overall economic preparedness for euro adoption, it is necessary to strengthen the fiscal framework and concentrate on compliance with the medium-term budgetary objective beyond 2015. At the same time, it is appropriate to strengthen public finance sustainability in connection with population ageing. Last but not least, it is also desirable to take measures to increase the flexibility of the labour market and reduce administrative barriers to entrepreneurship.

## → Statistics

Besides performing its standard role of providing a high-quality database for the needs of the CNB, the Czech Statistical Office, European and international institutions, and the public, CNB Statistics faced new challenges both within the CNB and internationally.

As regards data production methodology, the work of CNB Statistics was focused on six main areas in 2014: financial account statistics, external statistics (the balance of payments and the international investment position), monetary and financial statistics, government financial statistics, securities statistics and general economic statistics. Full compatibility with ESA 2010 was attained in the case of quarterly financial accounts statistics, and the guideline of the ECB on the statistical reporting requirements of the ECB in the field of quarterly financial accounts was implemented in full. In the field of external statistics, the main objective – implementation of the sixth edition of the IMF's Balance of Payments Manual – was achieved. Since October 2014 (in coordination with the publication of national accounts under ESA 2010), the balance of payments and the international investment position have been published in accordance with the updated guideline of the ECB on the statistical reporting requirements of the ECB in the field of balance of payments and international investment position statistics, and the international

reserves template. New statistical standards were also associated with the successful changeover to the new SDMX (Statistical Data and Metadata eXchange) technical standard for statistical data exchange vis-à-vis international organisations. Monetary and financial statistics (MFS) are another important area. The CNB implemented the requirements of the new ECB regulation and guideline on payment systems statistics into its reporting system. In the preparation of statistics on insurance corporations it completed the implementation of the ECB regulation on statistical reporting requirements by insurance corporations. It also worked in cooperation with the ECB in the preparation of RIAD, a European register of organisations. Cooperation with CNB Supervision and, via the ECB, with a new ECB unit engaged in supervisory data production was a new large area of activity in the field of MFS. The CNB also implemented the new ECB guideline on government finance statistics, which was a priority for 2014 in this area. Data were reported in accordance with this guideline and with ESA 2010 for the first time in October 2014. Securities statistics were focused on ensuring full operation of the European Security Holdings Statistics Database (SHSDB). Fully harmonised data for the end-2013 reference period were reported for the first time in March 2014.

Moreover, 2014 was the year when CNB Statistics had to start tackling two important long-term tasks. The first involves the creation of a new SDAT universal data collection system. Procurement documents for this system, which is to replace the existing information system in 2018, were prepared throughout the year in close cooperation with the Monetary and Statistics Department, the Financial Market Regulation and International Cooperation Department and the Information Systems Department. The new system will comprehensively cover the collection, primary processing and storage of statistical and supervisory data. The second task involves the gradual implementation of a national integrated statistical system, i.e. the integration of statistical and supervisory data into a single “data production” system in cooperation with the CNB’s supervisory units.

## → FINANCIAL STABILITY

Maintaining financial stability and seeing to the sound operation of the financial system in the Czech Republic are among the CNB’s primary objectives. The CNB identifies, monitors and assesses risks jeopardising the stability of the financial system. By preventing or mitigating these risks, the CNB contributes by means of its powers to the resilience of the financial system and the maintenance of financial stability and thus creates macroprudential policy. It provides information about the conduct of this policy on its website (*Financial stability > Macroprudential policy*).

The scope of macroprudential policy was substantially extended last year through the implementation of new regulatory rules for the credit institutions sector (the introduction of CRD IV and CRR). These rules gave the CNB the power to instruct all banks to maintain additional capital buffers on top of the basic requirements. The first of these is the capital conservation buffer. Instead of phased introduction, the CNB opted for immediate introduction of the full buffer (2.5%) as from August 2014.

In reaction to the Basel III regulatory framework, CRD IV introduced another important macroprudential instrument into EU regulatory practice: a countercyclical capital buffer. This instrument is intended to increase the resilience of the financial system to risks associated with strong fluctuations in lending. Banks are meant to create such a buffer at times of excessive credit growth. The CNB will announce the countercyclical capital buffer rate on a quarterly basis. Given the subdued lending growth and the absence of related risks, the two decisions made in 2014 resulted in the setting of this buffer at zero.



In October 2014, the CNB required the four banks assessed as being the most systemically important ones to maintain a capital buffer to cover systemic risk. These are banks whose potential destabilisation could undermine confidence in the banking sector's ability to provide its services effectively. This, in turn, could have serious adverse effects on the financial system and the Czech economy as a whole. The CNB will revise the set of banks required to maintain the systemic risk buffer and the buffer rates to be applied by them at least once every two years.

The main tool used to communicate with the public in the financial stability area is the Financial Stability Report. The CNB publishes this report on its website (*Financial stability > Financial stability reports*) and also provides information about its content at a press conference given by the CNB Governor and at a special seminar. In accordance with the law, it also submits the report to the Chamber of Deputies (the lower house of the Czech Parliament).

The Financial Stability Report above all aims to identify new risks arising from domestic economic developments and the external environment. Another key objective is to assess the ability of the domestic financial system to withstand the impacts of adverse economic shocks using stress tests of banks, insurance companies and pension funds. As in the past, the 2013/2014 Financial Stability Report, published in June 2014, assessed the resilience of the Czech financial sector as being high; a decline in economic activity due to adverse developments abroad and a related potential increase in credit risk were identified as the main risk scenario. Deflation pressures were also assessed as a major risk factor. The report also contains macroprudential policy recommendations and information about the CNB's plans to introduce new instruments for reducing sources of systemic risk.

Analyses of risks to financial stability and proposals for macroprudential policies are discussed internally at the Bank Board's regular meetings on financial stability issues. At the European level, the Governor and a Vice-Governor actively participate in the regular meetings of the General Board of the ESRB. CNB experts are involved in the Advisory Technical Committee (ATC) and its working groups and in the Regional Consultative Group of the Financial Stability Board established by the G20. Within the Basel Committee on Banking Supervision (Basel Consultative Group), the CNB was actively involved in the preparation of an impact analysis of the new Basel III global regulatory rules for banks in small and emerging economies.



## → FINANCIAL MARKET SUPERVISION

By law, the CNB is the supervisor of the financial market in the Czech Republic. To the extent stipulated in legal rules, the CNB supervises entities operating on the financial market, lays down rules for their business to safeguard the stability of the financial system and systematically regulates, supervises and, where appropriate, issues penalties for non-compliance with these rules. The CNB is part of the European System of Financial Supervision and works in cooperation with the European Systemic Risk Board and the European Supervisory Authorities. The CNB provides detailed information about financial market supervision in its annual Financial Market Supervision Report – see *CNB > Supervision, regulation > Aggregate information on the financial sector > Financial market supervision reports*.

### FINANCIAL MARKET REGULATION

The CNB sought to constructively influence the legislative process ongoing in the EU in the financial market area and contributed to changes in the regulatory framework in the Czech Republic. In particular, it worked in partnership with the Ministry of Finance in preparing draft legislation in the financial market area and other laws regulating the business of financial institutions and other entities subject to regulation and supervision. It prepared a number of decrees and explanatory and methodological opinions interpreting the application of regulatory requirements pertaining to financial market participants.

Amendments to the Act on Banks, the Act on Credit Unions, the Capital Market Undertakings Act, the Act on the CNB, and the Building Savings Schemes Act transposing CRD IV and adapting to CRR represented a fundamental legislative change. These amendments introduce, among other things, capital buffers, crisis management frameworks and duties of institutions to have recovery plans in place. The amendment to the Act on Credit Unions, setting, among other things, an upper limit on the total assets of a credit union and regulating the link between the size of membership contributions and remunerated deposits, represented a major change in terms of strengthening the stability of the credit union sector.

### EUROPEAN REGULATION

Intensive work on new European financial market regulations continued at the level of the European Commission, the Council and the European Parliament. The CNB prepared relevant opinions on an ongoing basis and its representatives actively promoted the CNB's positions in EU committees and working groups.

June 2014 saw the promulgation of the directive establishing a framework for the recovery and resolution of credit institutions and investment firms (BRDD) and the directive on deposit guarantee schemes (DGSD), which requires Member States to establish deposit guarantee schemes financed from contributions paid in advance, taking into account the risk profile of individual credit institutions.

An agreement was reached among EU Member States, the European Parliament and the Commission regarding the establishment of a Single Resolution Mechanism (SRM), the second pillar of the banking union, including an inter-governmental agreement on the transfer and mutualisation of contributions to the Single Resolution Fund and an implementing regulation determining the contributions to be paid by banks. The CNB's comments on the second pillar of the banking union mainly concerned the legal basis for establishing the SRM, the management and decision-making process within this mechanism and the position of participating and non-participating EU countries.

An amendment to the directive on standard collective investment funds (UCITS V) was promulgated in August 2014. This directive regulates the functioning of standard funds and also contains a number of powers for the Commission to adopt implementing measures. In the discussion, the CNB made a number of unsuccessful comments concerning, among other things, the large number of implementing measures to be adopted as delegated acts.

Positive changes were accepted in the discussion of a proposal for a regulation on indices used as benchmarks in financial instruments and financial contracts. Some cumbersome duties were deleted, the impacts regarding the possible use of benchmarks from third countries were limited and the number of delegated acts of the Commission was reduced to some extent. The discussions will continue in 2015.

Within the European supervisory authorities, the CNB was also actively involved in the preparation of a number of implementing measures (for CRD IV and CRR, for BRRD, for Solvency II, for MiFID II and for CSDR – a regulation on improving securities settlement in the EU and on central securities depositories) and in the preparation of draft guidelines, most notably for CRD IV. The European supervisory authorities issued a total of 36 guidelines in 2014.

## INTERNATIONAL COOPERATION

The large number of legislative proposals issued by the European Commission significantly expanded the workload of the European supervisory authorities – the European Banking Authority (EBA), the European Securities and Markets Authority (ESMA), the European Insurance and Occupational Pensions Authority (EIOPA) and the European Systemic Risk Board (ESRB). As a result of the debt and banking crisis in some euro area countries, work continued on institutional and structural changes in the supervision of the EU banking sector, including the commencement of preparations for potential bank resolution.

Preparations for the launch of the first pillar of the banking union, the Single Supervisory Mechanism (SSM), also continued. The ECB assumed responsibility for direct supervision of banks on 4 November 2014. This was preceded by a comprehensive assessment of 130 banks conducted by the ECB in cooperation with national supervisory authorities, and also by a bank stress testing exercise conducted by the EBA. Aided significantly by the CNB, the Ministry of Finance drew up an impact study on the Czech Republic's participation in the banking union. Among other things, this study identified potential risks to the Czech Republic and contained a draft government decision on further action in this matter.

CNB representatives were actively involved in the work of the EBA, ESMA and EIOPA at board of supervisors, standing committee and working group level. CNB experts prepared numerous analyses and opinions on documents submitted for oral discussions as well as on documents circulated by the secretariats of European institutions for approval in written procedures. Key activities also included participation in discussions and cooperation with relevant coordinators within the ECOFIN Council and its structures and also participation in the plenary meeting of the Council of Europe's MONEYVAL Committee. Turning to other international institutions and associations, the CNB was involved, among other things, in the OECD Committee on Financial Markets, the Basel Committee on Banking Supervision, the International Organisation of Pension Supervisors (IOPS) and the International Organization of Securities Commissions (IOSCO).

As for cooperation with partner supervisory authorities the CNB was involved in ten colleges for European banking groups and one group with a US headquarters. As a consolidating supervisory authority, it initiated the establishment of one supervisory college.



It was also actively involved in the meetings of supervisory colleges for international insurance groups. In the capital market, the CNB continued to work in partnership with other supervisory authorities on the basis of IOSCO and ESMA multilateral memoranda of understanding.

## LICENSING, APPROVAL AND AUTHORISATION ACTIVITIES IN THE FINANCIAL MARKET AREA

As the financial market supervisory authority, the CNB issues authorisations (licences) to the majority of entities providing services on the financial market. In this context, it also issues other permissions or approvals, for example approvals of securities prospectuses and approvals of the publication of takeover bids. In these cases, the CNB acts as an administrative authority.

No new banking licences were granted in 2014. A total of 23 domestic banks and 11 credit unions were subject to CNB supervision. WPB Capital, spořitelní družstvo closed down as a result of a CNB decision to revoke its credit union licence. As of the end of 2014 the CNB was also supervising 32 domestic insurance companies (excluding the Czech Insurers' Bureau), one reinsurance company and, to a limited extent, 20 branches of foreign insurance companies.

At the end of 2014, the CNB registered 33 holders of investment firm licences. No new licences were granted and two licences expired in 2014.

In the area of securities issues and regulated markets, securities of four issuers were newly admitted to trading on a regulated market (bonds in three cases, shares in one case). By contrast, securities of six issuers were excluded (three cases involved bonds excluded owing to redemption).

### Statistics on administrative proceedings conducted in 2014

	<i>No. of administrative proceedings continuing from 2013</i>	<i>No. of administrative proceedings opened in 2014</i>	<i>No. of administrative proceedings closed</i>
Credit institutions	13	57	59
Insurance sector	9	78	78
Pension management companies and funds	5	47	50
Accredited entities	0	2	2
Management companies and investment funds	8	134	103
Investment services providers	5	185	181
Payment institutions	2	4	2
Electronic money institutions	0	0	0
Processors of domestic banknotes and coins	0	0	0
Securities issues and regulated markets	4	42	40

## FINANCIAL MARKET SUPERVISION

In its off-site surveillance work, the CNB continuously monitors the activity and financial performance of individual financial market entities and assesses the evolution of the market as a whole and its segments. The CNB's supervisory work involves checking compliance with the relevant legal rules and compliance with prudential rules, regularly assessing the financial condition of individual regulated entities and checking compliance with the rules of professional care.

In the area of banking supervision, which comprises supervision of banks, building societies, credit unions and, under a simplified regime, foreign bank branches, the CNB – given the persisting uncertainties in the global economy – concentrated primarily on the credit portfolio quality, capital adequacy, liquidity and overall performance of banks and their consolidated groups. It also closely monitored the implementation of revised prudential rules associated with CRD IV and CRR. Banks submitted gradually supplemented and revised versions of their recovery plans to supervisors for assessment in compliance with the BRRD requirements.

The CNB, in cooperation with selected banks, continued to implement the joint bank stress testing project. The tests confirmed the good resilience of banks, as their capital adequacy ratio stayed above the regulatory minimum by a sufficient margin even in the adverse scenario. In addition to these bottom-up tests, the CNB conducts half-yearly stress tests of the entire banking sector (top-down tests), the results of which are regularly published on the CNB website (*CNB > Financial stability > Stress testing*).

Despite its relatively small market share, the credit unions sector is subject to intensive CNB supervision. A substantial proportion of supervisory capacity is devoted to this sector in on-site examinations and off-site surveillance. CNB supervision was focused in particular on assessing the current situation and developments in individual credit unions and on resolving their problems, primarily with respect to the specific risks undertaken by individual institutions.

Prudential supervision of insurance companies is based on regularly assessing their financial condition and their compliance with prudential rules, as well as on the imposition of remedial measures. Economic and insurance technical indicators are assessed on the basis of regularly submitted reports. Insurance companies that belong to insurance groups are also subject to supplementary supervision of insurance companies in groups. During information-gathering visits, the discussions covered the readiness of insurance companies for the Solvency II requirements as well as their current financial and business situation and strategies.

Another round of stress tests of selected insurance companies confirmed that the sector as a whole has sufficient capital and is resilient to significant changes in risk factors. In 2015, the stress tests will be conducted fully in accordance with Solvency II principles.

In the capital market area, the CNB supervises investment firms, investment intermediaries, markets in investment instruments, management companies and investment funds, pension management companies and other entities operating in the capital market. In the investment firms sector, the CNB continuously assessed compliance with information and disclosure duties. It inspected compliance with exposure limits and checked capital adequacy calculations and guarantee fund contribution calculations.

In the area of pension management companies and funds managed by them, supervision concentrated mainly on assessment of their compliance with statutory limits (particularly for the value of assets), their financial performance, compliance with the rules of professional care and compliance with other regulatory limits. The attention of professional care supervisors in the area of supplementary pension savings focused on issues relating to the expiration

of supplementary pension insurance following participants' applications for the payment of benefits. As regards retirement savings, attention was paid to processes relating to the making of contracts and also to subsequent acts during and after the registration of contracts with the administrator of the Central Contract Register.

## ENFORCEMENT

In 2014, activity in the enforcement area consisted mainly in investigating petitions for the opening of administrative proceedings, making decisions on the opening of administrative proceedings or the deferral of cases, and conducting first-instance administrative proceedings, within which fines and remedial measures were imposed, licences revoked and registrations cancelled. In addition to conducting administrative proceedings with supervised entities, the CNB conducts administrative proceedings with entities that provide financial market services without having the relevant licence in financial market sectors where the law enables penalties to be imposed for the carrying on of unauthorised business. Final decisions in the capital market area are published on the CNB website (*Supervision > Conduct of supervision > Final administrative decisions*). Sanctions imposed on insurance intermediaries are entered in the Register of Insurance Intermediaries.

### Statistics on administrative penalty proceedings conducted in 2014

	<i>No. of administrative penalty proceedings opened</i>	<i>No. of administrative penalty proceedings closed</i>	<i>Total fines imposed (in CZK thousands)</i>
Supervision of credit institutions	3	4	–
Capital market supervision	19	26	10,590
Insurance supervision	28	34	2,875
Violation of the Act on Bureau-de-change Activity	9	6	625
Consumer protection	1	2	200
Payment system	5	3	610

## CENTRAL CREDIT REGISTER

The Central Credit Register (CCR) is an information system administered by the CNB since 2002 which enables banks and foreign bank branches operating in the Czech Republic to share information on the credit commitments and payment discipline of businesses. The CCR data play an ever more significant role in European cooperation and will also play a role in the collection of granular credit data by the European System of Central Banks within the AnaCredit project.

### Main operational characteristics of the CCR

	2011	2012	2013	2014
Number of registered borrowers	576,583	609,503	611,885	621,716
of which: natural persons (entrepreneurs)	330,372	345,243	339,730	338,394
legal entities	246,211	264,260	272,155	283,322
Total volume of loans outstanding (CZK billions)	1,290	1,328	1,508	1,559
Number of CCR application users	2,569	2,767	2,836	2,151
Ad hoc enquiries about credit commitments (thousands per year)	215	184	234	285
Number of enquiries about client credit commitments in monthly reports (thousands per year)	3,198	3,843	3,759	4,300
Number of extracts made for clients per year	514	490	520	499

## → Consumer protection

In accordance with its legal powers, the Consumer Protection Department receives and investigates submissions from the public regarding consumer issues, including compliance with selected obligations under the Payment Systems Act and the Consumer Credit Act.

A total of 1,230 complaints were received in 2014. Of these, 448 pertained to banking products. Most of these complaints related to payments and fees. The most common ones concerned time limits for the execution of payment transactions, fees associated with payments abroad and settlement of complaints linked with card payments. Banks' bonus campaigns remain a problem. Consumers often do not understand the conditions of these campaigns and ask for bonuses without being aware of all the conditions they have to meet to obtain them. The provision of loans or credit line increases to low-income persons, disabled people and pensioners, where loan repayments exceed what they can afford, were often subject to complaints.

A total of 427 complaints concerned the insurance sector. Complaints regarding pre-contract information and fees dominated. Other common complaints related to the provision of false information and insufficient information by employees of insurance companies, delays in the settlement of claims and the provision of insufficient pre-contract information. Other submissions concerned inactivity of insurance intermediaries in dealing with complaints and issues of potential damage caused to consumers by the conduct of insurance intermediaries' representatives when selling insurance and investment products.

The CNB investigated 46 complaints regarding the capital market. Most of them concerned investment losses, with consumers claiming that they had not been sufficiently warned of the risks associated with investing, that they had not been offered stop loss and stop limit hedging tools, and that they had requested a guaranteed rate of return.

The number of complaints concerning non-bank foreign exchange entities continued to rise. A total of 185 were received last year. Exchange rates remain the most prevalent problem. Bureaux-de-change in the centre of Prague offer rates of between CZK 15 and 20 to the euro. Foreigners, and often locals as well, do not expect such a rate and ask for transactions to be cancelled after they have been concluded. Bureaux-de-change almost always refuse to do so once the customer has signed the pre-contract information.

A total of 51 complaints pertaining to non-bank consumer credit providers were received. However, these entities are subject to CNB supervision only if the credit is provided via a credit card. A total of 73 complaints pertained to consumer protection in general.

Seven on-site examinations were conducted or commenced in 2014, five of which concerned insurance intermediaries, one an insurance company and one a bureau-de-change operator. As regards insurance, the most frequent shortcomings were detected in the area of informing customers about the nature of life insurance associated with investment in funds or some other type of insurance and in the area of fee policies.

## → RESOLUTION

In connection with the transposition of EU banking directives (in particular Directive 2014/59/EU of the European Parliament and of the Council establishing a framework for the recovery and resolution of credit institutions and investment firms), the CNB established a Resolution Department. On the coming into effect of the Recovery and Resolution Act, the CNB will assume new responsibilities in the area of resolution and will become the national resolution authority. The CNB will be independent in this new role. Within the CNB, the resolution area is separated from, and independent of, other units.

The CNB's main resolution tasks will include the preparation and regular review of resolution plans, the calculation of contributions to the Resolution Fund and, for some entities, the specification of the extent to which they will have to maintain capital and eligible liabilities which can be used, among other things, for potential recapitalisation (the "MREL" indicator).

The main purpose of this new legislation is to ensure that the costs of any failure of a systemically important bank are borne primarily by its shareholders and creditors, not by taxpayers. Practical steps are to be taken to safeguard the stability of the financial system, including its key functions, its resilience to crisis and its ability to respond to any event of a systemic nature with minimal use of public money. Cooperation between the CNB and the Ministry of Finance, or the government, will be necessary in some cases. Any provision of state aid would be subject to approval by the European Commission. In any event, the application of resolution tools is conditional on the public interest criterion being met.

## → CURRENCY AND PAYMENTS

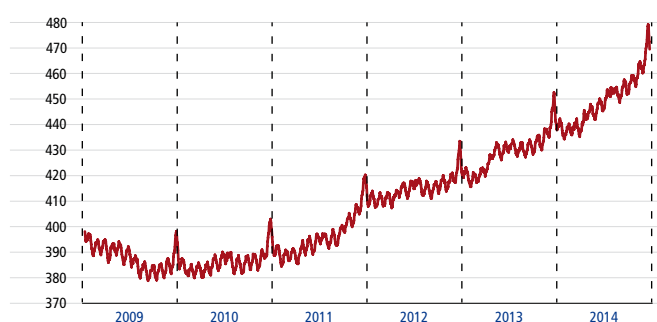
### → Currency in circulation

Under the Act on the CNB, the CNB has the exclusive right to put banknotes and coins, including commemorative coins, into circulation and to manage the circulation of currency. Cash circulation, together with the rights and duties of the CNB, banks, legal entities and natural persons, is regulated by Act No. 136/2011 Coll., on the Circulation of Banknotes and Coins.

The value of currency in circulation was CZK 469.5 billion on 31 December 2014, up by CZK 27.7 billion on a year earlier.

#### Currency in circulation – 1 Jan. 2009 to 31 Dec. 2014

(in CZK billions)

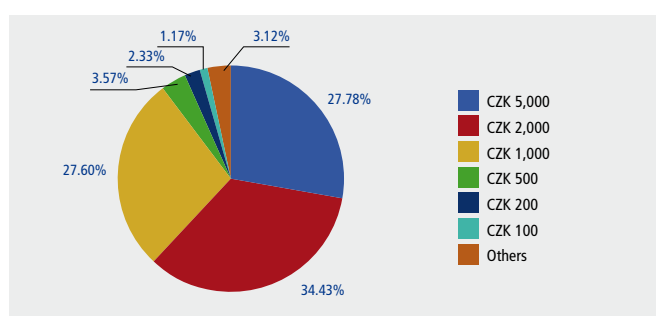


#### Number of banknotes and coins in circulation as of 31 December 2013 and 31 December 2014

	2013	2014	2013	2014
Denomination	CZK millions		millions of pieces	
CZK 5,000	126,758.8	130,432.1	25.4	26.1
CZK 2,000	145,092.1	161,622.1	72.5	80.8
CZK 1,000	124,544.7	129,596.6	124.5	129.6
CZK 500	15,571.2	16,738.3	31.1	33.5
CZK 200	10,550.2	10,919.8	52.8	54.6
CZK 100	5,260.1	5,491.7	52.6	54.9
CZK 50	588.2	585.2	11.8	11.7
CZK 20	103.9	0	5.2	0
<b>Banknotes, total</b>	<b>428,468.6</b>	<b>455,385.8</b>	<b>375.9</b>	<b>391.2</b>
CZK 50	4,295.5	4,687.1	85.9	93.7
CZK 20	3,198.2	3,362.4	159.9	168.1
CZK 10	1,852.4	1,941.0	185.2	194.1
CZK 5	1,080.4	1,131.5	216.1	226.3
CZK 2	770.3	808.6	385.2	404.3
CZK 1	471.7	494.1	471.6	494.1
CZK 0.50	183	0	366	0
<b>Coins in circulation, total</b>	<b>11,851.4</b>	<b>12,424.7</b>	<b>1,869.9</b>	<b>1,580.6</b>
Precious metal coins	1,526.7	1,665.0	2.2	2.3
<b>Total</b>	<b>441,846.7</b>	<b>469,475.5</b>	<b>2,248.0</b>	<b>1,974.1</b>

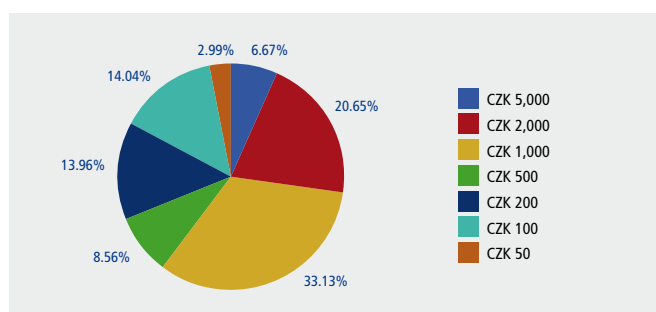
### Structure of currency in circulation

(in CZK)



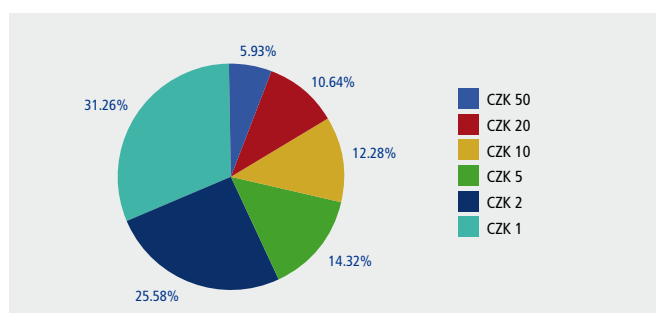
### Structure of banknotes in circulation

(in pieces)



### Structure of coins in circulation

(in pieces)



In all, 107.7 million banknotes, 40.6 million coins, 121,300 commemorative silver coins and 16,800 gold coins were produced in 2014. These banknotes and coins, including those intended for collectors, cost the CNB a total of CZK 361 million to produce.

Cash turnover at the CNB's branches amounted to CZK 1,397.3 billion, up by 0.4% year on year. The CNB's cash offices received 720.8 million banknotes and 394.2 million coins from circulation and issued 733.0 million banknotes and 458.2 million coins.

The CNB's branches processed 726.7 million banknotes and 381.6 million coins (compared to 720.0 million banknotes and 395.6 million coins in 2013). The CNB removed 12.7% of the total number of processed banknotes as unfit for further circulation.



In 2014, the CNB put into circulation five CZK 200 commemorative silver coins and one CZK 500 silver coin. CZK 5,000 gold coins continued to be issued in the fourth year of the Bridges in the Czech Republic cycle. The coins depicted the Jizerský bridge on the Tanvald-Harrachov railway line and the reinforced concrete bridge at Karviná-Darkov.

## → Non-cash payments

The CNB keeps the accounts of the state and operates systems for transferring interbank payments and settling short-term securities transactions. Non-cash payment transactions are executed through the Czech Express Real-Time Interbank Gross Settlement System (CERTIS), the Short-Term Bond System (SKD) and the Automated Banking Operations (ABO) System.

The CNB's clients are organisational units of the state, for which the CNB maintains a whole range of accounts. On state budget expenditure accounts and selected revenue accounts for payments debited to them, organisational units of the state reserve funds for planned expenditures in the Integrated Information System of the Treasury (IIST) operated by the Ministry of Finance. Organisational units of the state transmit payment orders together with information on the reservation of funds in the IIST to the CNB; the CNB verifies the reservation of funds in the IIST before executing the payment order.

Other clients include subsidised organisations established by state organisational units and state funds, which are gradually transferring all their accounts to the CNB (in accordance with transitory provisions of Act No. 501/2012, amending Act No. 218/2000 Coll., on Budgetary Rules).



The entities whose accounts for the receipt of subsidies from the state budget are held at the CNB include state organisations, the Railway Transport Route Administration, self-governing territorial divisions and voluntary municipal organisations, Regional Councils of cohesion regions, public research institutions and public universities, as well as other legal entities with the approval of the Ministry of Finance. The CNB offers a limited range of services to these clients as it is required to do under Article 33(8) of Act No. 501/2012 Coll.

To manage their accounts, clients use the ABO-K internet banking system or the services of the CNB's branches in Brno, Hradec Králové, Ostrava and Prague or its regional offices in České Budějovice, Plzeň and Ústí nad Labem.

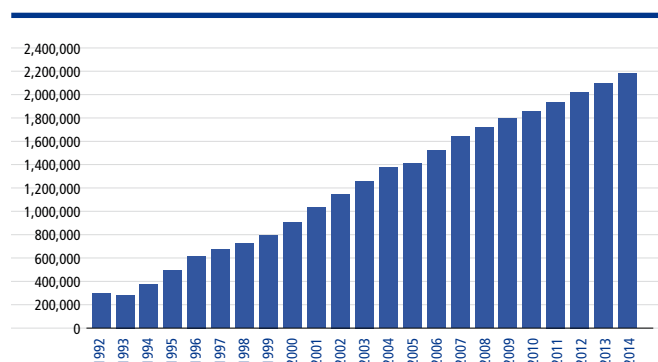
## CERTIS – INTERBANK PAYMENT SYSTEM

The CERTIS system processes interbank payments in the Czech Republic. Banks, credit unions and foreign bank branches are participants in this system. As of 1 December 2014, CERTIS comprised 45 direct participants (for which accounts are maintained in the system) and six third parties (for example, card payment clearing houses and securities clearing and settlement institutions).

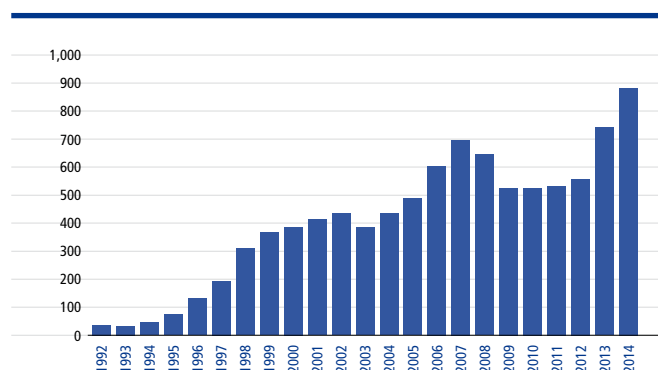
CERTIS processed 549 million transactions in 2014 (up by 4% year on year) with a total value of CZK 222,530 billion (up by 19.2%). The system processed a daily average of 2.2 million transactions. The average daily value of the transactions was CZK 883 billion.

The following charts show the number of transactions processed and the amount of funds transferred in CERTIS since 1992.

### Average daily number of transactions



### Average daily turnovers (in CZK billions)



## SKD – SHORT-TERM SECURITIES SETTLEMENT SYSTEM

The short-term securities settlement system operated by the CNB is a separate register of securities and a securities settlement system. Since 2011, certificates issued by accredited providers of certification services have been used for electronic signatures.

In 2014, all owner account contracts in the SKD system were replaced. Some inactive clients did not sign a new owner account contract and the numbers of clients and asset accounts in SKD thus decreased slightly. As of 31 December 2014, a total of 86 asset accounts – belonging to 54 clients (securities owners) – were registered in SKD. The system records bonds issued by the CNB and government bonds issued by the Ministry of Finance.

The securities recorded in SKD are used, among other things, as collateral for intraday credit, which the CNB extends to banks for smooth accounting purposes within CERTIS. They are also used for the CNB's repo operations and by the Ministry of Finance for daily liquidity management of the Single Treasury Account. On average, 40 transactions a day were processed in SKD in 2014. The average daily value of these transactions was CZK 149 billion.

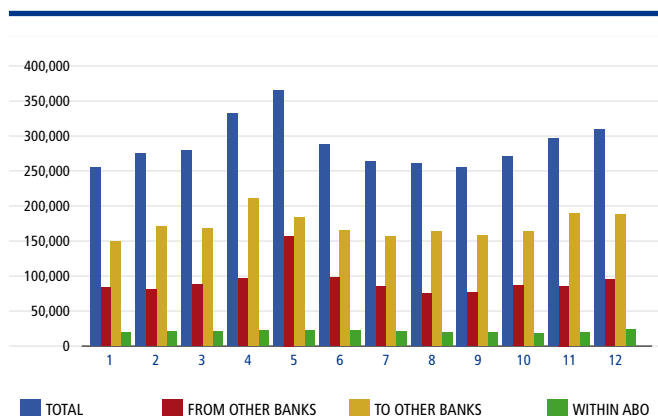
## ABO – THE CNB'S ACCOUNTING AND PAYMENT SYSTEM

The CNB keeps the accounts of its clients and the internal accounts of the central bank in the ABO system. At the end of 2014, the CNB maintained 22,150 ABO accounts, of which 3,839 were internal accounts, 3,674 were employee accounts and 14,637 were accounts of legal entities (14,178 of which were regulated Treasury accounts in the Czech currency and 128 were regulated Treasury accounts in the euro). Regulated Treasury accounts are subordinated to the Single Treasury Accounts, on which state budget revenues and expenditures and other financial operations of the state are realised.

Most clients use the ABO-K internet banking system to manage their accounts. In all, 9,829 users were registered in the system as of the end of 2014.

The following chart shows the average daily numbers of accounting transactions processed in 2014. The total number of transactions increased by 7.9% compared to 2013. The number of client orders rose by 10.4%.

### ABO – average daily number of transactions in 2014



## → FINANCIAL MARKET OPERATIONS

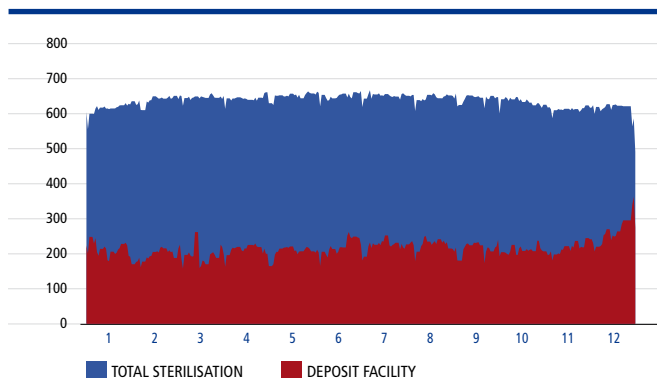
The CNB implements monetary policy by means of a system of monetary policy instruments. The main instruments include interest rate operations (repo operations and automatic facilities), foreign exchange interventions and reserve requirements. Interest rate operations play a pivotal role in steering short-term interest rates on the interbank market. The CNB Bank Board sets three interest rates: the two-week repo rate, the discount rate and the Lombard rate. The main monetary policy rate is the two-week repo rate. The discount and Lombard rates provide the floor and ceiling respectively for short-term interest rates on the money market. The CNB's key rates saw no changes during 2014. The discount and repo rates remained unchanged at the technical zero level of 0.05% and the Lombard rate at 0.25%.

The CNB continued to use the exchange rate as an additional instrument for easing monetary policy, with a commitment to intervene if needed to weaken the koruna against the euro so that the exchange rate of the koruna is kept close to CZK 27 to the euro. However, the exchange rate developments in 2014 did not generate any need to intervene and the amount of excess liquidity was thus not affected.

The CNB influences the liquidity of the banking sector through interest rate operations so as to maintain an optimum liquidity level for compliance with the reserve requirement. This ensures that short-term interest rates are stable at the desired level. The main instrument for managing short-term interest rates is the repo, announced three times a week with a maturity of 14 days. Repos are used for absorbing excess liquidity from the banking sector. The liquidity absorbed is remunerated at the two-week repo rate at most.

Excess liquidity in 2014

(in CZK billions)



The koruna-euro exchange rate in 2014



The CNB's monetary policy instruments also include two "automatic" facilities – the marginal lending facility and the deposit facility. Under the lending facility, the CNB lends overnight funds to banks in the form of a repo operation at the Lombard rate. The deposit facility gives banks the option of making overnight deposits with the CNB at the discount rate. The deposit facility was used a great deal during the year, as the discount rate was equal to the repo rate. Recourse to the lending facility was rare.

The total average amount of excess liquidity absorbed was CZK 637 billion. Of this, 34% was absorbed through the deposit facility and 66% through repo operations. The CNB also executed collateral exchanges. These were technical operations in which the CNB usually exchanged a security settled in the Central Securities Depository for a security settled in the Short-term Bond System (SKD). The aim of these operations was not to affect the banking sector's excess liquidity, but to provide liquid securities to banks, for instance for obtaining intraday credit.

The CNB also has liquidity-providing instruments (two-week liquidity-providing repos and foreign exchange swaps) in its monetary policy toolkit. These were launched in October 2008 as a result of the outbreak of the financial crisis and are important for the stability of the domestic financial market. Although they were not used actively by banks in 2014, the CNB considers it appropriate to keep them available indefinitely.

## → International reserves management

The CNB manages its international reserves, which are its foreign assets in convertible currencies. They are used mainly to support the CNB's independent monetary policy-making and as a source of foreign exchange liquidity for CNB clients. The size and structure of the reserves are published regularly in the *Financial markets* section of the CNB website. At the end of 2014, the international reserves totalled CZK 1,244 billion in koruna terms, equivalent to EUR 44.9 billion or USD 54.5 billion.

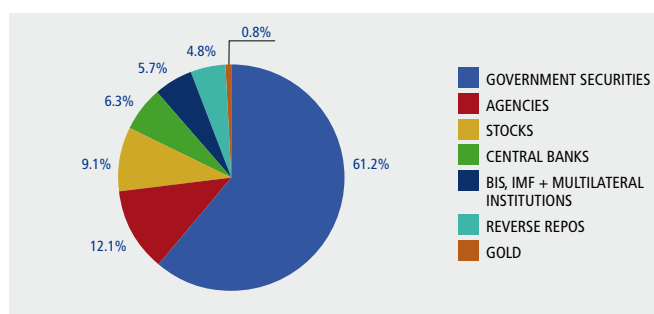
### Currency structure of international reserves assets as of 31 December 2014 (portfolio currency)

EURO	25,384 million
US DOLLAR	9,682 million
CANADIAN DOLLAR	7,398 million
AUSTRALIAN DOLLAR	4,260 million
SWEDISH KRONA	15,899 million
JAPANESE YEN	249,113 million
BRITISH POUND	619 million
SDR	1,195 million
GOLD	10.6 t

Note: The data in the table are not adjusted for liabilities; part of the USD assets are diversified into JPY and GBP through currency forwards.

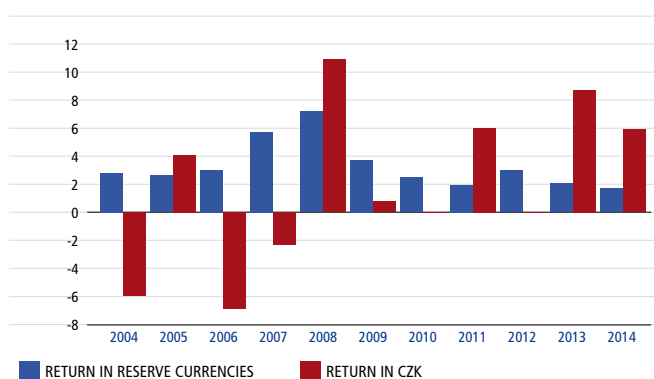
The CNB invests the international reserves in accordance with the principles of its reserve management policy and subject to investment opportunities and the situation on the relevant markets. The largest part of the reserve portfolio is invested in debt securities issued by selected governments of advanced countries, selected government-guaranteed bonds and bonds issued by top-rated multilateral institutions. Other instruments used for international reserves management include (in order of significance): shares, repos, specific covered bonds, deposits, futures, and interest rate, currency and equity swaps. All derivatives transactions are backed by financial collateral.

## Investment allocation as of 31 December 2014



The international reserves recorded a year-on-year rise in koruna terms due mainly to external flows into the portfolio (CZK +52.9 billion), positive valuation changes (CZK +45.3 billion) and portfolio returns (CZK +19.7 billion). A partial currency reallocation of flows into the international reserves portfolio was made in the course of the year, during which the relative representation of the euro was reduced in favour of the Canadian and Australian dollar and the Swedish krona.

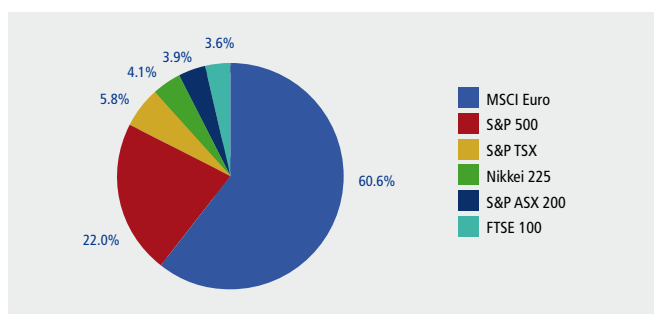
## Comparison of the total return on international reserves in 2014 with previous periods (in %)



The overwhelming majority of the international reserves are actively managed. The individual portfolios recorded the following returns in 2014: euro 1.09%, US dollar 0.91%, Canadian dollar 2.77%, Swedish krona 3.77% and Australian dollar 8.76%. The weighted average of the return on the portfolios in reserve currencies was 1.69%.

The equity portfolios are managed by BlackRock and State Street Global Advisors and are invested on the following markets using the relevant benchmark indices: European (MSCI Euro), US (S&P 500), UK (FTSE 100), Japanese (Nikkei 225), Canadian (S&P TSX) and Australian (S&P ASX 200).

## Structure of the equity portfolio as of 31 December 2014



### Note:

The size of the equity exposure is targeted at 10% of the size of the international reserves (adjusted for the SDR allocation). For this reason a 10% ratio does not need to be maintained between the size of each individual equity portfolio and its "counterpart" in the form of a fixed interest rate portfolio in the same currency.

The ability of the IMF to draw further tranches under the first bilateral loan agreement concluded in 2010 expired at the end of the first quarter of 2014. The second bilateral loan agreement of 2013 with a credit line of up to EUR 1.5 billion remained inactive throughout 2014. The IMF thus did not start drawing any new tranches in 2014. By contrast, several early repayments of loan tranches drawn in 2010 and 2011 were made. These totalled EUR 66.3 million. The total net nominal size of the credit line declined to EUR 76.3 million at the end of 2014.

## → The CNB as the bank of the state

The Czech National Bank provides banking services for the state and the public sector under the Act on the Czech National Bank and the Act on Budgetary Rules, i.e. it maintains accounts and provides payment services and services relating to liquidity management of the Single Treasury Accounts.

A major amendment to the Act on Budgetary Rules entered into force on 1 January 2013. Among other things, this amendment greatly expanded the set of entities subordinated to the Treasury, leading to an increase in the number of CNB clients. The situation in the area of provision of services to the state and other entities connected to the Treasury stabilised in 2014. These clients now almost exclusively use internet banking. Only 0.3% of orders are in paper form. As of 31 December 2014, the CNB maintained 14,000 accounts under the Act on Budgetary Rules or other laws. A total of 260,000 transactions took place on the Treasury accounts on average per day.

The CNB is also involved in the Integrated Treasury Information System (the fund reservation system for the budget expenditure of state organisational units), specifically in the process of verification of fund reservation before the execution of payment orders. This means in practice that in the event of a payment (expenditure) from the state budget account, the relevant state organisational unit reserves in the Treasury system the corresponding amount from the budget assigned to it for the given fiscal year, and then sends the payment order to the CNB for execution. Thanks to the fact that the payment system and the Treasury system are interconnected, the CNB verifies whether funds have been reserved for the said payment in the Treasury system and only later accepts the payment order for execution.

## SUPPORT FOR TREASURY LIQUIDITY MANAGEMENT

The CNB is responsible for the daily consolidation of individual accounts subordinated to the Treasury under the koruna-denominated and euro-denominated Single Treasury Accounts and works closely with the Ministry of Finance to manage liquidity on these accounts. This

daily cooperation consists primarily in managing the liquidity of the koruna-denominated Single Treasury Account. This account includes, for example, the balances on state budget revenue and expenditure accounts, state financial assets accounts (e.g. yields on government bond issues), revenue and customs offices' accounts, state funds accounts and so on. Consolidation of all these funds on a single account enables the authorities to manage Treasury liquidity effectively and to finance the state budget balance. Every morning, CNB and Ministry of Finance staff compile a daily estimate of Single Treasury Account revenues and expenditures. During the day, this estimate is compared with the actual flows of funds on accounts subordinated to the Single Treasury Accounts. This enables us to respond flexibly to short-term fluctuations in state budget revenues and expenditures. If revenues are higher than expenditures, the free liquidity is invested on the money market. If the opposite situation occurs, the higher expenditure needs are covered from Treasury funds and, if they are insufficient, the Ministry of Finance raises funds on the money market by selling T-bills. Thanks to the system of single accounts and the CNB's ability to monitor financial flows from/to the individual accounts under the Treasury throughout the business day, the balance on the Single Treasury Accounts is maintained at just a few millions even though transactions worth billions of korunas are settled every day.

## SUPPORT FOR STATE DEBT FINANCING

In the area of state debt management, the CNB carries out primary sales of both short-term and long-term government bonds for the Ministry of Finance and acts as administrator of the issues. In 2014, the CNB organised 17 auctions of T-bills, with maturities of 9 and 12 months and sales totalling almost CZK 115 billion. The CNB also executed 26 auctions of government bonds, with sales exceeding CZK 150 billion. As administrator, the CNB made coupon payments for 21 government bond issues and a payment of principal on one maturing issue. It also organised coupon payments and repayments of principal for issues of government saving bonds.

## → ECONOMIC RESEARCH

Economic research at the CNB creates an analytical and knowledge base for monetary policy-making, financial market supervision and maintaining financial stability, and furthers the development of the central bank's human capital. Economic research also helps to develop the CNB's position within the ESCB and vis-à-vis the domestic and international academic community. Details on research activities can be found in the *Economic research* section of the CNB website.

In 2014, 20 internationally reviewed articles were published in the CNB Working Paper Series and the CNB Research and Policy Notes Series and in two issues of the Economic Research Bulletin. Prestigious journals such as the *Journal of Financial Stability*, the *International Journal of Central Banking* and the *Journal of International Money and Finance* published 13 research papers by CNB economists. Experts from foreign central banks, multilateral organisations and major universities collaborate with CNB economists on research projects. The relevance and quality of research outputs were assessed and internationally compared in the report *CNB Economic Research in 2014*.

Research project coordinators assist in the monetary policy-making process by preparing opinions on economic situation reports and the minutes and transcripts of monetary policy meetings. Topics raised during monetary policy discussions are taken into account when setting research priorities. Research project outputs are regularly used in CNB documents.

In 2014 the CNB held its tenth Research Open Day, at which the results of CNB economic research were presented to a broader professional audience. The Economic Research Department Award for the best research publication is regularly presented at this event.



The CNB was actively involved in the ESCB Macro-prudential Research Network (MaRs), which was concluded by a final conference. CNB experts were also involved in the Competitiveness Research Network (CompNet), the objective of which is to develop a consistent analytical framework for assessing the competitiveness of individual European countries. The CNB also contributed to the activities of the renewed ESCB Wage Dynamic Network (WDN), within which a survey of firms was conducted in 2014 regarding the impacts of the 2008–2009 crisis on employment, remuneration and pricing.

The Research Advisory Committee is an advisory body to the CNB Bank Board in the area of research. The Committee's main role is to draw up recommendations for the Bank Board's decisions on research projects. The members of the Committee include foreign experts. In 2014, the President of the Committee was again CNB Governor Miroslav Singer and its Chairman was CNB Board Member Kamil Janáček.

## → EUROPEAN AND INTERNATIONAL RELATIONS

### EUROPEAN CENTRAL BANK, EUROPEAN SYSTEM OF CENTRAL BANKS AND EUROPEAN SYSTEMIC RISK BOARD

CNB Governor Miroslav Singer and CNB Vice-Governor Vladimír Tomšík attended the meetings of the General Council of the European Central Bank (ECB), where the governors of all the central banks of the EU countries are represented. Documents on macroeconomic, monetary and financial developments around the world and in the EU and on fiscal developments in EU countries were discussed in 2014. The meetings also dealt with the regular ECB Convergence Report, the representation of Europe in the IMF and the economic impacts of the Russia-Ukraine crisis. Monetary policy measures of central banks of non-euro area EU member countries were also debated.

CNB representatives were involved in the work of the 13 committees of the European System of Central Banks (ESCB) and numerous sub-committees and working groups. The CNB processed about 140 documents in the written consultations of the ECB General Council



on European legislation, national legislation and ECB documents. In seven cases the CNB responded in the form of a Governor's letter to the President of the ECB. It commented, for example, on the draft ECB Convergence Report, on numerous EU legislative proposals (the directive on transparency of securities financing transactions, the directive concerning measures to ensure a high common level of network and information security across the Union, and the regulation on reforming the structure of the EU banking sector) and on ECB opinions on the draft Hungarian act transposing the Bank Recovery and Resolution Directive and on the National Bank of Slovakia's role in resolution on the financial market.

The CNB Governor and a Vice-Governor also regularly attended the meetings of the General Board of the European Systemic Risk Board (ESRB), which dealt with systemic risks in the EU financial market and the development of a macroprudential policy framework. In June, the ESRB published a recommendation on guidance for setting countercyclical buffer rates. The CNB fulfilled the reporting duty arising from the recommendation on funding of credit institutions (regarding covered bonds and other instruments that generate encumbrance and regarding risk management of asset encumbrance) and from the recommendation on intermediate objectives and instruments of macroprudential policy. Work also continued on preparing the planned revision of the ESRB regulation. The European Commission is expected to finalise its proposal in 2015.

## RELATIONS WITH EU COUNCIL, EU COMMITTEE

Although the CNB has no direct representation in the EU Council, except in some of its advisory bodies, such as the Economic and Financial Committee (EFC), it works with the government and the relevant government departments and contributes to the coordination of European issues through the EU Committee at both the government level and the working level. The CNB actively commented on topics of relevance, especially in the areas of the financial markets and economic and monetary union. Attention was focused on the continuing work on the banking union project, among other things bridge financing in the transitional period of the Single Resolution Fund within the Single Resolution Mechanism, including the issue of equal treatment of members and non-members of the Single Supervisory Mechanism. Key issues also included a comprehensive assessment (stress tests) of the EU banking system, backstops in the Single Resolution Mechanism and structural reform of the EU banking sector.

## INTERNATIONAL MONETARY FUND

The IMF focused on completing the reviews of some of its policies (the Triennial Surveillance Review, the review of the Financial Sector Assessment Program and the review of IMF credit facilities). Work continued on a new credit framework relating to debt vulnerability. There was also discussion of experience gained during the crisis (with the aim of reducing the probability of serious future crises) and of steps to bridge the period until the 2010 quota and governance reforms are ratified.

An IMF Article IV mission to the Czech Republic took place in May. From the CNB's perspective, the dominant issue was the discussion about the use of the exchange rate as a monetary policy instrument at the zero lower bound. As usual, the IMF's report summarised developments in the Czech economy and commented on economic policy. Among other things, the IMF supported keeping the foreign exchange intervention policy in place until the end of 2015, which it regarded as an appropriate timescale in terms of market expectations.

A specific event in which the CNB was involved was the New Member States Forum organised by the European Department. Representatives of the central banks and finance ministries of six new non-euro-area EU Member States (the Czech Republic, Bulgaria, Romania, Croatia, Hungary and Poland) attended the Forum, which was held in Warsaw on 12 December 2014 and focused mainly on discussing the pros and cons of euro adoption, accession to the banking union and the Single Supervisory Mechanism before adopting the euro, and structural reforms, fiscal framework reforms and pension system reforms.

In 2014 the CNB continued to be involved as a creditor in IMF assistance provided under the financial transactions plan to other member countries experiencing balance of payments difficulties. In addition, the CNB and the IMF have signed two bilateral loan agreements to enhance the IMF's resources.

### CNB ACTIVITIES IN OTHER INTERNATIONAL ORGANISATIONS

The CNB Governor attended the regular meetings of central bank governors of the member countries of the Bank for International Settlements (BIS). The CNB was also represented at the regular meeting of vice-governors and at selected meetings of the Central Bank Governance Group and the Basel Consultative Group, which is part of the Basel Committee on Banking Supervision. The CNB also regularly participates in the meetings of a number of OECD working bodies, particularly the Economic Policy Committee and the Committee on Financial Markets. An economic review of the Czech Republic, to which the CNB contributed, was published in March 2014. CNB representatives also attended the annual meeting of the European Bank for Reconstruction and Development (EBRD).



## → Foreign technical assistance

The CNB organised 27 events in 2014 to provide technical assistance to its foreign partners. Eight seminars were attended by 150 experts from 29 central banks, and 13 consultations took place for 68 participants from 10 central banks and supervisory authorities, mainly from Albania, Azerbaijan, Belarus, Bosnia and Herzegovina, China, Kosovo, Montenegro and Sudan. The CNB also provided expert assistance in the form of consultations and lectures abroad. Within the ESCB, it participated in two projects to analyse the readiness of Albania's central bank for future ESCB membership in the monetary policy area. CNB experts took part in two projects funded by the European Commission agency TAIEX in the area of statistics for the central bank of Macedonia. CNB experts also provided technical assistance in Armenia, Macedonia, Uganda and Zimbabwe in partnership with the IMF as part of its missions and educational programmes.



# **ONE THOUSAND THREE HUNDRED AND TWENTY-ONE**

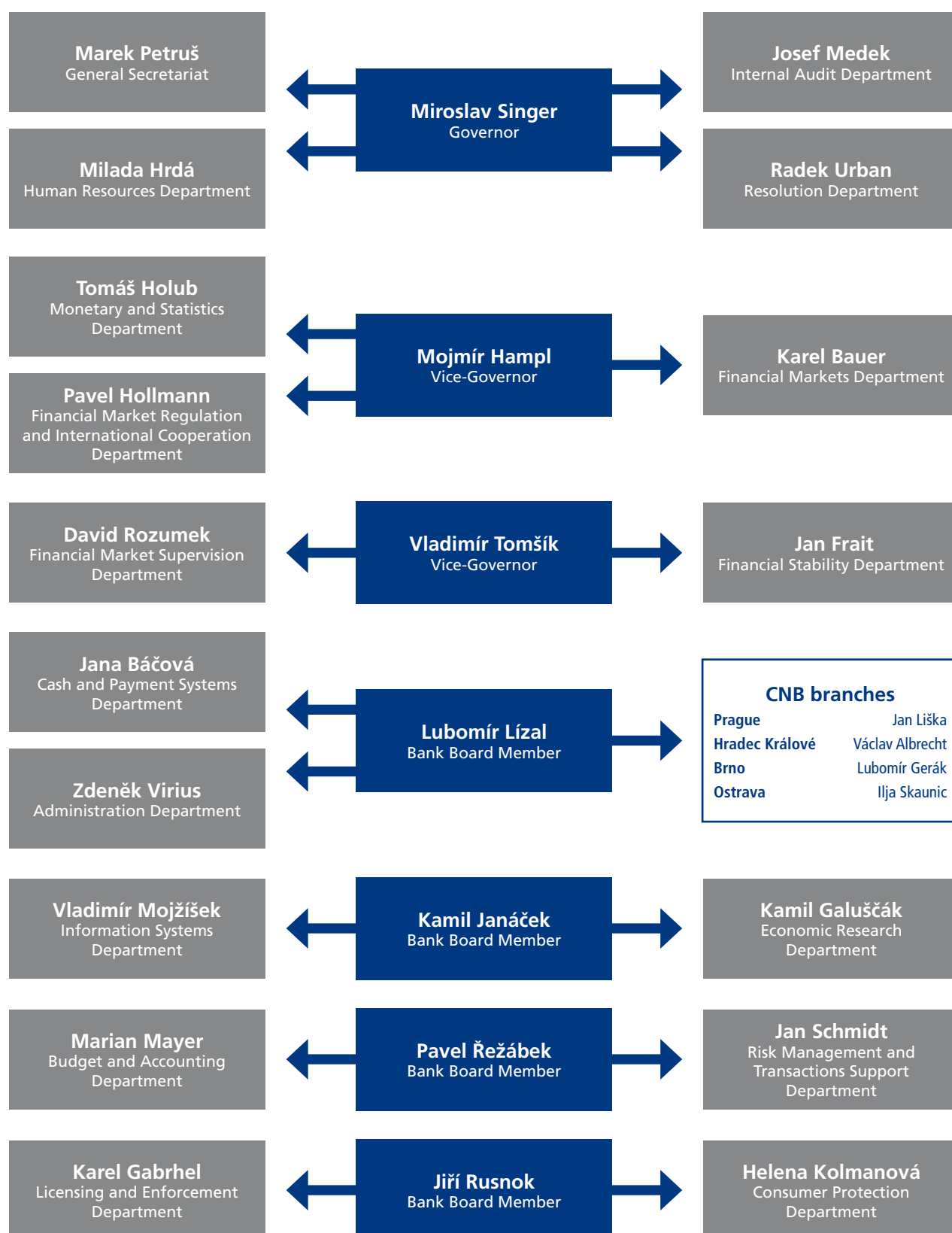
This is the number of employees  
working to ensure  
that the Czech National Bank  
fulfils its objectives.



# MANAGEMENT AND ORGANISATION

# MANAGEMENT AND ORGANISATION

## → ORGANISATIONAL CHART AS OF 31 DECEMBER 2014





The CNB's organisational structure consists of a headquarters in Prague and four branches in Prague, Hradec Králové, Brno and Ostrava. In addition, the CNB is represented in České Budějovice, Plzeň and Ústí nad Labem by regional offices of its headquarters, where selected units of the Cash and Payment Systems Department, the Financial Market Supervision Department and the Licensing and Enforcement Department are located (see the CNB website: *About the CNB > CNB offices in the Czech Republic*).

The CNB has a two-tier management system. Fundamental decisions relating to the fulfilment of the CNB's primary objective, namely to maintain price stability, and other tasks corresponding to the CNB's responsibilities are taken by the Bank Board. Responsibility for implementing the Bank Board's decisions and the day-to-day running of the bank is delegated to the executive directors of departments and branches.

## BANK BOARD

The Bank Board is the supreme governing body of the CNB and takes decisions as a collective body by a simple majority of the votes cast. In the event of a tie, the chairperson has the casting vote. The members of the Bank Board, in addition to collectively managing and deciding, oversee the activities performed by the CNB's organisational units according to a scheme defined by the Bank Board (see the organisational chart of the CNB as of 31 December 2014).

The President of the Czech Republic appointed Jiří Rusnok as a member of the CNB Bank Board with effect from 1 March 2014. Mr Rusnok replaced Eva Zamrazilová, whose mandate expired on 28 February 2014.



## EXECUTIVE DIRECTORS OF DEPARTMENTS AND BRANCHES

These senior officers of the CNB carry out the decisions taken by the Bank Board and are responsible – subject to the CNB's development strategy and plans for the individual areas of competence of the CNB – for the performance of the activities of the units they manage as defined in the Organisational Statute. The executive directors set targets and tasks for the staff under them and perform the employer's rights and duties under labour law in respect of those employees. Their powers and responsibilities relate not only to direct management activities, but also to methodological management activities in their competence, cooperation with other organisational units of the bank and with external partners in the Czech Republic and abroad, and to the submission of proposed solutions to issues of fundamental significance to the Bank Board.

## HEADQUARTERS

The organisational units of CNB headquarters are departments (subdivided into divisions). In their areas of competence defined in the CNB Organisational Statute, they are responsible for the implementation of the bank's main and ancillary activities and for methodological management within the headquarters and in respect of branches. Coordination and advisory bodies – committees, commissions and project teams – are used to implement Bank Board decisions and perform activities that cover the areas of competence of more than one organisational unit and that depend on close and efficient cooperation between them.

The competences of the CNB and its organisational units were extended and amended in 2014 on the basis of new legal regulations and Bank Board decisions on the implementation of systemic changes.

Act No. 89/2012 Coll., the Civil Code, was fully implemented into the CNB's internal regulations and working procedures with effect from 1 January 2014. Act No. 135/2014 Coll., amending certain laws in connection with the stipulation of access to the activities of banks, credit unions and investment firms and the supervision thereof, was implemented (transposing CRD IV). This law extended the CNB's responsibilities to include new activities, and its implementation as of 1 July 2014 involved:

- providing for activities relating to the establishment of the CNB as an authority responsible for performing activities connected with the resolution of credit institutions and investment firms (a Resolution Division was set up in the General Secretariat as a temporary organisational solution; a Resolution Department was established on 1 November 2014);
- introducing a mechanism for receiving and evaluating reports on failure or imminent failure to comply with sectoral laws and related legal rules, i.e. whistleblowing (responsible unit: Financial Market Supervision Department);
- issuing provisions of a general nature concerning the countercyclical capital buffer and the systemic risk buffer and evaluating compliance with these provisions (responsible unit: Financial Stability Department);
- establishing a new method for publishing final administrative decisions (responsible unit: Licensing and Enforcement Department);
- extending the CNB's information duty to the European Commission, the ESRB, European supervisory authorities and relevant foreign authorities – responsible units: Financial Market Supervision Department (supervision of financial market entities) and Financial Stability Department (capital buffers).



A project was completed to systematically reorganise the CNB's branch network by reducing the number of branches from seven to four – two in Bohemia (Prague and Hradec Králové) and two in Moravia (Brno and Ostrava) – and integrating activities currently performed by branches into CNB headquarters. The following branches closed down: Ústí nad Labem (on 30 April 2014), Plzeň (on 31 May 2014) and České Budějovice (on 30 June 2014). Their main activities in the area of money reserves management and payments were transferred to the Cash and Payment Systems Department and its newly created operational services divisions in Ústí nad Labem, Plzeň and České Budějovice. However, the regional offices continue to provide all the services previously provided to the public and non-bank clients, and the CNB thus remains present in all seven regions.

On 1 December 2014, the Communications Department was abolished and its activities were transferred to a new Communications Division in the General Secretariat, with the exception of activities under Act No. 106/1999 Coll., on Freedom of Information, which were transferred to the Licensing and Enforcement Department. This led to a streamlining of the organisational structure of the CNB's headquarters and to centralisation into the General Secretariat of activities consisting in the provision of administrative support to the Bank Board and the planning and organisation of the CNB's professional and social events.



## BRANCHES

The CNB's branches are divided into divisions. They represent the bank in their regions of jurisdiction and are contact points for the CNB's relations with state and local authorities and legal and natural persons that have registered offices or residence addresses in the relevant region when dealing with the CNB under the relevant legal rules. This does not affect the right of the said entities to deal with the CNB's headquarters in Prague. The main tasks of the CNB's branches include managing money reserves, maintaining accounts under the Act on Budgetary Rules and accounts of other CNB clients falling within their fields of competence, and making payments for their clients.

The activities of the CNB's branches were affected in 2014 by the above-mentioned restructuring of the CNB branch network and related other measures (the transfer of activities in the areas of financial market supervision and accounting to CNB headquarters), which resulted in a reduction of the number of divisions in the remaining branches from three to two.

## → HUMAN RESOURCES

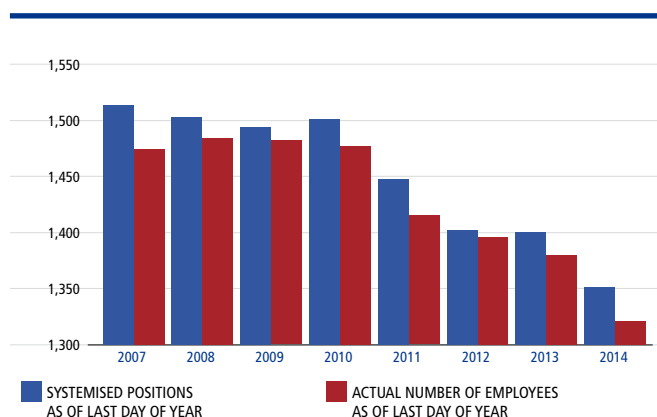
The CNB systematically seeks high-quality employees, supports them in furthering their education and works to motivate them. In 2014 it came second in the "Business" category in the Czech Republic in the "Top 100 IDEAL Employers" ranking organised by Universum.

### NUMBER OF POSITIONS AND EMPLOYEES

The CNB continued to streamline its branch network (a process it had launched in 2013). This had a significant impact on the number and structure of job positions in 2014. The number of positions fell again and stood at 1,351 on 31 December 2014, the lowest figure since the CNB was established in 1993. The change in the number of positions reflected, on the one hand, a reduction connected with the streamlining of the branch network and, on the other hand, an increase owing to the creation of a resolution unit and an expansion of financial market prudential inspection capacity.

As of 31 December 2014, the CNB had 1,321 employees, down by 59 from the end of 2013. A total of 92 new employees were taken on. In all, 170 persons terminated their employment (87 of which due to organisational changes), 29 persons retired and 18 persons saw their fixed-term contracts expire. The total staff turnover rate in 2014 was 12.6%, comparable with that recorded in 2011, when a number of organisational changes were also made. As of 31 December 2014, the average length of employment was 14.1 years, almost the same as in 2013 (14.2 years).

### Number of employees and number of positions



### RECRUITMENT AND SELECTION

The number of filled vacancies increased last year. This is also partly illustrated by a marked year-on-year rise in the number of new employees. The increase in the number of filled vacancies at the CNB's headquarters is mainly due to the streamlining of the branch network and a substantial expansion of activities in the area of financial market supervision. In addition to numerous expert positions, a number of selection procedures were opened for senior management positions. To fill these positions, the CNB made use of both internal sources of high-quality candidates and external selection procedures, which applicants from abroad also took part in.

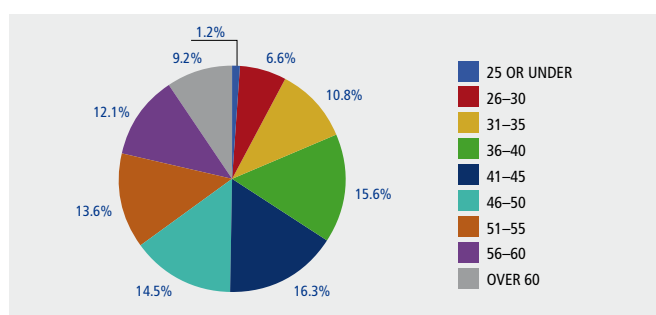
## EDUCATION, AGE AND GENDER STRUCTURE

The CNB has long had a balanced age, gender and skills structure. This reflects its equal opportunities policy for all job applicants and employees.

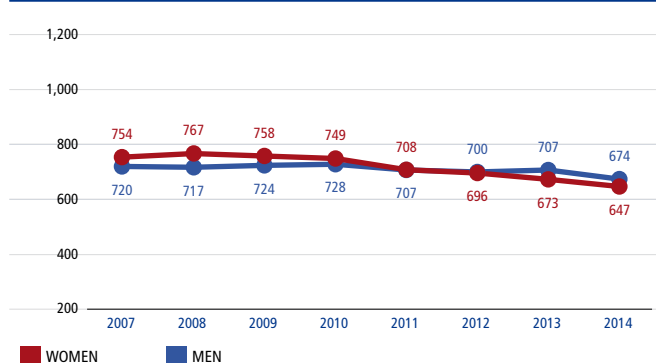
The education structure of employees remained unchanged. University graduates made up 59% of the total workforce, while employees with higher vocational training or secondary school education ending with a school leaving exam (including vocational training ending with a school leaving exam) accounted for 31% and employees with vocational training without a school leaving exam or with basic education recorded a 10% share.

As in previous years, the age structure of employees did not show any major year-on-year change. All age groups are evenly represented. Employees aged 41–45 account for the largest share (16.3%). The diverse age composition of working teams ensures that those teams function properly and smoothly absorb changes stemming from generational turnover. The average age of employees decreased by around seven months to 45 years in 2014 compared to 2013.

### Age structure of employees as of 31 December 2014



### Representation of men and women



As in previous years, the shares of men and women in the CNB workforce remained balanced in 2014.

## INCENTIVE SYSTEM

The wage system is one of the CNB's key tools for recruiting, motivating and developing staff. The CNB constantly optimises both its remuneration system and performance appraisal system.

Personnel expenses, which comprise wage costs, including temporary sick leave payments, obligatory insurance contributions and other social expenses (pension insurance, health care and food allowances), training expenses and employee benefits, amounted to CZK 1,302 million in 2014, up by 4.7% on a year earlier. This increase was due to a higher wage bill based on wages, bonuses, holiday pay and extra remuneration which the bank committed itself to during collective bargaining with the trade union organisation for 2014, and also to an increase in funds for severance pay paid due to the abolition of job positions as part of the streamlining of the branch network.

### In 2014, the salaries of Bank Board members were as follows:

	Gross salary in CZK <sup>1)</sup>	Net salary in CZK <sup>2)</sup>
Miroslav Singer	5,022,528	3,634,932
Mojmír Hampl	4,031,319	2,919,775
Vladimír Tomšík	4,014,834	2,856,233
Lubomír Lízal	3,490,930	2,503,076
Kamil Janáček	3,390,136	2,405,514
Pavel Řežábek	3,387,557	2,428,493
Eva Zamrazilová <sup>3)</sup>	512,826	364,179
Jiří Rusnok <sup>4)</sup>	2,763,088	1,982,734

1) The gross salary comprises the basic wage, holiday pay, performance-related bonuses and bonuses for working on non-working days.

2) The net salary is the gross salary net of state health insurance contributions, social security contributions, state employment policy contributions, income tax and solidarity tax and tax discounts for the taxpayer and tax discounts for dependent children for those Bank Board members who applied for the discount.

3) The term of office of Eva Zamrazilová expired on 28 February 2014 and she terminated her employment at the CNB as of the same date.

4) Jiří Rusnok was appointed a member of the Bank Board with effect from 1 March 2014.

## PROFESSIONAL DEVELOPMENT

The CNB regards staff education as a key part of human resource management. Employees can deepen and extend their knowledge and skills during internal training provided by domestic external organisations, and also by attending seminars abroad. Spending on employee training totalled CZK 25.5 million in 2014.

Internal training events are used primarily to train new employees. In addition to courses familiarising them with the central bank's main functions, they also take an e-learning induction course. Specialised courses are aimed at enhancing skills, particularly for supervisory departments. They feature lecturers from major audit firms (Ernst & Young, KPMG). Courses focusing on employees' personal development are also an integral part of training. A number of training events were held for regional office staff who are going to be involved in financial market supervision following the completion of the systemic reorganisation of the CNB branch network.

Language training at the CNB mainly took the form of regular language training, intensive language courses and e-learning. The main goal was to enhance knowledge of specialised terminology and communication skills.

The CNB's manager programme, which is updated every year, included lectures and training sessions tailored to the needs of managerial positions. Participation in international seminars and workshops made it possible for employees to share information and knowledge with colleagues from partner central banks. Important training events included training in the fields of financial stability, economic modelling and the financial markets. Staff also had the opportunity to attend training events organised by the IMF, the Joint Vienna Institute and the Financial Stability Institute. Supervisors took advantage of seminars organised by the authorities responsible for supervising the individual sectors of the financial market in the EU (EBA, ESMA and EIOPA).



The CNB has become a sought-after central bank organising seminars within the European System of Central Banks. In all, 13 training events for 150 experts from other EU central banks took place at the CNB.

## **TWENTY-SEVEN**

In 2014, the exchange rate of the koruna became a monetary policy instrument used instead of interest rates to fulfil the inflation target. The CNB stated repeatedly that it would, if necessary, maintain the exchange rate of the koruna close to CZK 27 to the euro.



# PUBLIC RELATIONS



# PUBLIC RELATIONS

## → EXTERNAL COMMUNICATIONS

Communication with the public in 2014 focused mainly on monetary policy. Criticism of the use of the exchange rate as an instrument for easing the monetary conditions from some sections of the Czech public led to more frequent and more refined communication of the benefits of the weakened koruna for the economy, the necessity of price stability and the principles of the exchange rate commitment. The CNB further developed its communication procedures with the aim of getting across the decisions of the Bank Board and the conclusions of economic analyses in the monetary policy area to the public directly and as soon as possible. For its openness and use of new communication tools, the CNB received the prestigious Central Banking Transparency Award from Central Banking Publications in January 2015.



A website section called cnBlog was created for blog posts by the Governor, members of the Bank Board and experts. Its pages, containing more than 50 opinion pieces, were viewed more than 30,000 times in 2014. Press conferences and meetings with analysts following the Bank Board's monetary policy meetings now take place earlier and are streamed online on the CNB website. The public can also watch live streams from roundtable meetings between central bank representatives and prominent businesspeople in the regions of the Czech Republic. These roundtables widened the range of discussion meetings held between the CNB and the professional public last year.

Another new communication channel is the CNB Newsletter, which provides e-mail subscribers with a regular overview of the past week's most important news. The CNB continued to use its profiles on Twitter, Facebook, YouTube and LinkedIn. The LinkedIn profile was set up to address specific target groups among the professional public more effectively (journalists, analysts, private sector workers).

In 2014, the CNB also offered the public additional options for using its "Czech Money" mobile app. The app enables users to view Czech banknotes and coins and their protective elements in detail on iOS and Android mobile devices. An extended version of the app containing the exchange rates declared by the CNB and a calculator is available to users of Windows 8 tablets and now also iOS mobile devices.

The CNB also focused on its main communication topic – the weakening of the koruna – in the area of financial education. On the home page of the CNB website the public can follow an inflation barometer showing current inflation in comparison with the inflation target which the central bank aims to hit. For the general public, the CNB created an animated



infographic “Helping the Czech economy – support 2% inflation with us”, which aims to explain as clearly as possible the reasons for this step and its effects on the Czech economy. It is available on the website, on the CNB’s YouTube channel and at the People and Money exhibition. This infographic is also available as a pop-up picture book. In 2014 the CNB continued the previously launched financial education activities organised by CNB branches in their regions. These activities include collaborations with the Silesian

University in Opava, the School of Business Administration in Karviná and the Faculty of Economics and Administration at Masaryk University in Brno.

The main topics of day-to-day public interest were the exchange rate commitment and the benefits of the weaker koruna for the Czech economy, financial market companies and intermediaries, and banknotes and coins. Last year the CNB responded to 1,466 phone queries, 4,283 electronic submissions and 964 written submissions.

## → EXHIBITION

The CNB Exhibition, located in a former strong-room, celebrated its 13th birthday in 2014. Almost 200,000 registered visitors, mostly school pupils and students, have visited the permanent exhibition *People and Money* since it opened. The exhibition is designed as a guide through the history of monetary relations and monetary developments. Modern audiovisual technology and 65 showcases provide a unique set of information about the history of money and monetary policy in the Czech Republic for experts and the general public alike. The CNB Exhibition is used not only for reservation-based “standard tours” throughout the year, but also for one-off tours for groups and schools. Its unique character also makes it an interesting venue for meetings with official domestic and foreign visitors and for shooting various TV programmes. More information is available in the *People and Money* section of the CNB website.



## → SPECIAL LIBRARY

The primary mission of the CNB's special library is to provide staff and outside specialists with information. To this end, it offers lending, advisory, reference and bibliographic information and research services (searches for information from all available information sources). Its highly specialised collection and access to numerous electronic sources allow users to obtain information in the fields of banking and economics in general, law and computer technology and to some extent in other areas as well. The library maintains and provides access to more than 76,000 publications and 700 periodicals, a large number of research reports and annual reports, and other publications (bank documents, brochures, etc.). The electronic catalogue is being systematically built up as part of the T Series library information system and is integrated into the Single Information Gateway operated by the National Library of the Czech Republic. Electronic records are regularly sent to the Union Catalogue of the Czech Republic. Internet access via both a wired connection and a secure wireless network is available to library users. All information about the library, including the electronic catalogue and contacts, is available in the *CNB special library* section of the CNB website.

## → ARCHIVE

The CNB Archive cares for the archive documents produced by the CNB and its legal predecessors. At the end of 2014, it contained 63 archive collections offering a unique view of the political, economic, social and cultural history of the Czech lands and Central Europe. The CNB Archive's research room is open all year round subject to prior consultation. Anyone interested in obtaining information from, or studying in, the CNB Archive should visit the CNB website (*About the CNB > Archive of the CNB*) or e-mail [archiv@cnb.cz](mailto:archiv@cnb.cz).

The operation of the CNB Archive was significantly affected by work relating to the implementation of Act No. 428/2012 Coll., on Property Settlement with Churches and Religious Societies and on the Amendment of Some Other Acts. More than 400 enquiries were dealt with in this context. The CNB Archive was also involved in several important projects, such as a presentation of its archive documents to secondary school and university teachers and students at the conference *Archives to Schools, Archivists to Teachers* and the National Museum exhibition *Money*.

## → CONGRESS CENTRE

The CNB Congress Centre, located in the listed building of the former Commodity Exchange, is a venue for meetings between the CNB's top management and representatives of other central banks, financial market and trade union representatives, analysts and journalists. The CNB's specialised units hold conferences, lectures, presentations, seminars, ECB committee and working group meetings, quarterly insurance intermediaries' examinations and various training sessions there. Thanks to its flexible spaces and modern technology, the Congress Centre is one of Prague's most popular venues. External partners organise about 40 professional and social events there a year. Clients include public and private institutions, both domestic and foreign, from various fields of activity. The key events in 2014 included a meeting of an ESCB committee and meetings of the EIOPA and the EBA. A further edition of the international seminar *Basics of working in the ESCB* also took place. More information is available in the *Congress Centre* section of the CNB website.



## **ONE KORUNA**

The Czech koruna is the monetary unit of the Czech Republic. The one-koruna coin was designed by the sculptor Jarmila Truhlíková-Spěváková.



# FINANCIAL REPORT



# FINANCIAL REPORT



## INDEPENDENT AUDITOR'S REPORT To the Bank Board of the Czech National Bank

Having its registered office at: Na Příkopě 28, 115 03 Prague 1  
Identification number: 481 36 450

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Registered at the Municipal Court in  
Prague, Section C, File 24349  
Id. Nr.: 49620592  
Tax Id. Nr.: CZ49620592

### Report on the Financial Statements

Based upon our audit, we issued the following audit report dated 18 March 2015 on the financial statements which are included in this annual report on the attached CD-ROM:

"We have audited the accompanying financial statements of the Czech National Bank, which comprise the balance sheet as of 31 December 2014, and the income statement and the statement of changes in equity for the year then ended, and a summary of significant accounting policies and other explanatory notes.

### Management's Responsibility for the Financial Statements

The management of the Czech National Bank is responsible for the preparation and fair presentation of these financial statements in accordance with accounting regulations applicable in the Czech Republic, 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.

### Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with the Act on Auditors and International Standards on Auditing and the related application guidelines issued by the Chamber of Auditors of the Czech Republic. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements 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 entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### Opinion

In our opinion, the financial statements give a true and fair view of the financial position of the Czech National Bank as of 31 December 2014, and of its financial performance for the year then ended in accordance with accounting regulations applicable in the Czech Republic.

### Other Matters

The financial statements of the Czech National Bank for the year ended 31 December 2013 were audited by another auditor who issued an unqualified opinion on those financial statements on 19 March 2014."

### Report on the Annual Report

We have also audited the annual report of the Czech National Bank as of 31 December 2014 for consistency with the financial statements referred to above. This annual report is the responsibility of the Czech National Bank's management. Our responsibility is to express an opinion on the consistency of the annual report and the financial statements based on our audit.

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee, and its network of member firms, each of which is a legally separate and independent entity. Please see [www.deloitte.com/cz/about](http://www.deloitte.com/cz/about) for a detailed description of the legal structure of Deloitte Touche Tohmatsu Limited and its member firms.



We conducted our audit in accordance with International Standards on Auditing and the related application guidelines issued by the Chamber of Auditors of the Czech Republic. Those standards require that the auditor plan and perform the audit to obtain reasonable assurance about whether the information included in the annual report describing matters that are also presented in the financial statements is, in all material respects, consistent with the relevant financial statements. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the information included in the annual report of the Czech National Bank is consistent, in all material respects, with the financial statements referred to above.

In Prague on 21 April 2015

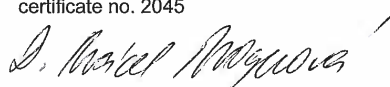
Audit firm:

Deloitte Audit s.r.o.  
certificate no. 79



Statutory auditor:

Diana Rádľ Rogerová  
certificate no. 2045



## Financial statements

<i>ASSETS</i>		<i>31 December 2014 in CZK millions</i>	<i>31 December 2013 in CZK millions</i>
1.	Gold	648	664
2.	Receivables from the International Monetary Fund	59,979	57,950
3.	Receivables from abroad, including securities	1,197,432	1,072,748
3.1.	Deposits at foreign banks and financial institutions	83,361	5,623
3.2.	Securities	1,053,385	956,273
3.3.	Other receivables from abroad	60,686	110,852
4.	Receivables from domestic banks	0	0
5.	Fixed assets	3,776	3,962
5.1.	Tangible fixed assets	3,753	3,934
5.2.	Intangible assets	23	28
6.	Other assets	5,300	6,297
6.1.	Other financial assets	4,378	4,325
6.2.	Other	922	1,972
<b>TOTAL ASSETS</b>		<b>1,267,135</b>	<b>1,141,621</b>

<i>LIABILITIES AND EQUITY</i>		<i>31 December 2014 in CZK millions</i>	<i>31 December 2013 in CZK millions</i>
1.	Notes and coins in circulation	469,476	441,847
2.	Liabilities to the International Monetary Fund	46,076	43,782
3.	Liabilities abroad	22,724	604
3.1.	Loans from foreign banks	5,084	0
3.2.	Other liabilities abroad	17,640	604
4.	Liabilities to domestic banks	690,435	664,077
4.1.	Loans received	216,601	380,303
4.2.	Bank monetary reserves	199,193	59,638
4.3.	Other liabilities to banks	274,641	224,136
5.	Liabilities to the state and other public institutions	3,798	25,510
6.	Provisions	262	228
7.	Share capital	1,400	1,400
8.	Funds	8,050	8,050
9.	Revaluation reserve	10,826	2,382
10.	Accumulated losses from previous periods	-50,449	-123,565
11.	Net profit for the period	56,560	73,116
12.	Other liabilities	7,977	4,190
<b>TOTAL LIABILITIES AND EQUITY</b>		<b>1,267,135</b>	<b>1,141,621</b>

<i>OFF-BALANCE SHEET</i>		<i>31 December 2014 in CZK millions</i>	<i>31 December 2013 in CZK millions</i>
1.	Guarantees issued	157,954	158,074
2.	Issued loan commitments	41,588	65,004
3.	Receivables from spot, term and futures transactions	187,810	79,797
4.	Liabilities from spot, term and futures transactions	187,783	78,939
5.	Guarantees received	226,964	226,335
6.	Collateral received	79,145	127,317

<i>INCOME STATEMENT</i>		<i>31 December 2014 in CZK millions</i>	<i>31 December 2013 in CZK millions</i>
1.	Interest income and similar income	6,676	5,075
1.1.	Interest from fixed income securities	6,380	4,819
1.2.	Other	296	256
2.	Interest expense and similar expense	-390	-310
3.	Income from shares and other interests	2,840	2,562
4.	Fee and commission income	353	309
5.	Fee and commission expense	-106	-88
6.	Gains less losses from financial operations	48,874	67,179
6.1.	Net foreign exchange gains / losses and foreign exchange spread	43,625	47,373
6.2.	Other	5,249	19,806
7.	Other operating income	732	737
7.1.	Income from money issue	535	464
7.2.	Other	197	273
8.	Other operating expense	-553	-495
8.1.	Expenses for production of notes and coins	-363	-415
8.2.	Other	-190	-80
9.	Administration expense	-1,609	-1,572
9.1.	Personnel expenses	-1,302	-1,243
9.1.1.	Wages and salaries	-921	-875
9.1.2.	Social and health security	-299	-291
9.1.3.	Training and employee benefits	-82	-77
9.2.	Other administration expenses	-307	-329
10.	Depreciation and amortisation of fixed assets	-257	-279
11.	Reversal of provisions for receivables and guarantees, income from receivables already written off	7	460
12.	Write offs, additions and utilisation of provisions for receivables and guarantees	-7	-462
13.	Net profit for the period	56,560	73,116

The full version of the financial statements of the Czech National Bank as of 31 December 2014, including the notes thereto, is available on the CNB website (*About the CNB > Performance > Financial statements*) and on CD-ROM.

The income and expense structure used in the following text provides information according to the purpose of the bank's expenditure, while the attached standard financial statements give an overview of income and expenses with regard to type.

### The CNB's income and expenses in 2014

(in CZK millions)

	<i>Expenses</i>	<i>Income</i>	<i>Net</i>	<i>y-o-y change</i>
Monetary area	21,119	79,232	58,113	-16,607
monetary policy-making	354	0	-354	-114
international reserves management	16,996	31,688	14,692	-12,663
valuation changes	3,626	46,441	42,815	-3,811
client operations	13	1,096	1,083	110
other operations	130	7	-123	-129
Currency issuance and management	363	551	188	120
Operations	1,928	187	-1,741	-69
<b>Total</b>	<b>23,410</b>	<b>79,970</b>	<b>56,560</b>	<b>-16,556</b>

Note: Operations include all personnel expenses, depreciation and amortisation, purchased services, energy consumption, etc.

The CNB recorded a profit of CZK 56,560 million in 2014, owing mainly to unrealised foreign exchange gains and income on international reserves management. In the period under review, the koruna weakened against all reserve currencies except the Swedish krona. The largest foreign exchange gains and losses were recorded for the US and Canadian dollar-denominated portfolios. The income on international reserves management was due in roughly equal measure to the bond and equity portfolios. Financial market interest rates continued to decline from their already very low levels in 2014. This led to lower interest income. The market value of bonds, on which the CNB recorded capital gains, simultaneously increased. However, these were mostly unrealised capital gains, which are recorded on the balance sheet as valuation changes due to the revaluation of securities to market value. The second-largest component of income on international reserves management was due to growth in foreign stock markets coupled with dividend income.

The bank's profit was also favourably affected by the still low sterilisation costs, which depend on monetary policy interest rates and the amount of sterilisation liabilities. The interest rates on the central bank's monetary policy operations were at "technical zero" throughout 2014. As a result, even the marked year-on-year increase in sterilisation liabilities that occurred after the CNB further eased monetary policy in late 2013 did not have a significant effect on the CNB's financial performance.

The result in the area of currency issuance was affected mainly by lower purchases of banknotes and coins, which fell by 14% year on year due to reduced money circulation needs, and by one-off income on invalid banknotes and coins. The possibility to exchange invalid CZK 20 banknotes and 50-heller coins expired on 31 August 2014. The total nominal value of the unreturned banknotes and coins of CZK 286 million was then recorded as CNB income.

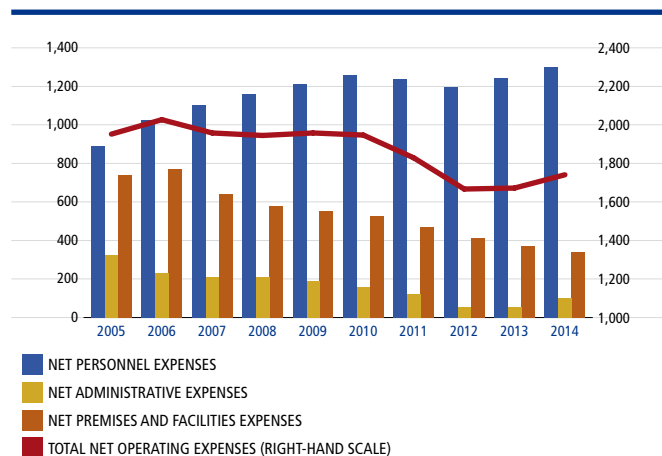
The bank's net operating expenses rose by 4% year on year. This result was due to several factors. The important ones included a rise in the central bank's total wage bill and an increase in payments to the European supervisory authorities coupled with a decrease in administrative fees charged in the course of the CNB's supervisory work.

The CNB constantly strives to increase the efficiency of all its activities. For example, 2014 saw the completion of the branch reorganisation project, which aimed to create a more efficient branch network with fewer employees and lower operating expenses. The project took about a year to implement and the required financial effect is not expected to be felt until 2015, as the project was completed halfway through the year. Overall, the project resulted in a reduction of 112 job positions. The fall in the number of employees was partly offset by the need to recruit additional financial market supervisory staff for the areas of enforcement proceedings and supervision of compliance with the Act on the Circulation of Banknotes and Coins. In connection with its new duties arising from EU law, the CNB established a new Resolution Department to deal with crisis situations in financial market entities.

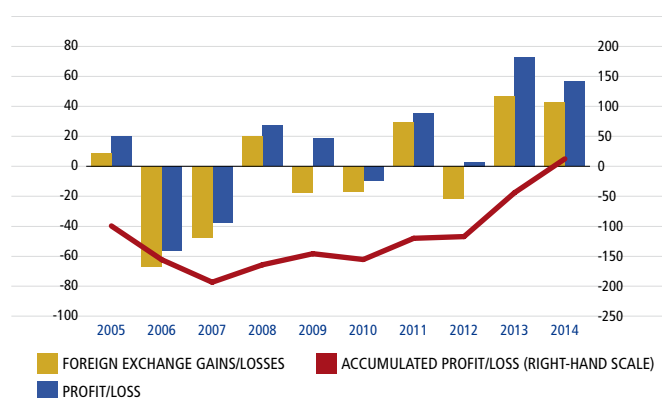
The CNB's profit for 2014 enabled it to fully cover the remainder of its unpaid book loss of previous years, which had been on the central bank's balance sheet since 1998. The assumption that the accumulated loss would be covered using future profits was thus fulfilled. In line with financial management principles, the rest of the profit was allocated to the CNB reserve fund. The CNB's capital increased year on year to a positive value of CZK 26,387 million.

More comprehensive information about the CNB's performance in 2014 is available on the CNB website (*About the CNB > Performance > Financial Reports*).

#### The CNB's net operating expenses 2005–2014 (in CZK millions)



#### The CNB's performance 2005–2014 (in CZK billions)



## **ONE HUNDRED AND SIX**

Under Act No. 106/1999 Coll.,  
on Freedom of Information,  
the CNB provides information  
relating to its responsibilities  
within the meaning  
of Article 2(1) of this Act.



# **PROVISION OF INFORMATION UNDER ACT NO. 106/1999 COLL., ON FREEDOM OF INFORMATION**

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## PROVISION OF INFORMATION UNDER ACT NO. 106/1999 COLL., ON FREEDOM OF INFORMATION

The CNB provides information pursuant to Act No. 106/1999 Coll., on Freedom of Information, as amended (hereinafter the "Act") by way of disclosure on the internet, primarily at [www.cnb.cz](http://www.cnb.cz), or to applicants on the basis of applications.

### A) INFORMATION PROVIDED IN 2014 ON THE BASIS OF APPLICATIONS:

1. Number of applications for information under the Act: 59
2. Number of decisions refusing an application: 24
3. Number of appeals submitted against decisions: 11
4. Transcript of the relevant parts of each court judgement concerning the examination of the legality of an obliged entity's decision refusing an application for information and an overview of all expenses incurred by the obliged entity in connection with court proceedings on rights and obligations under this Act, including its own staff expenses and legal representation costs:  
The CNB's actions in dealing with applications under Act No. 106/1999 Coll. were not subject to judicial review in 2014, so the CNB incurred no related costs.
5. Number of exclusive licences granted, including justification of the need to grant exclusive licences: 0
6. Number of complaints submitted under Article 16a of the Act, reasons for their submission and a brief description of the manner in which they were dealt with: 3
  - (i) A complaint about the CNB's action in dealing with the complainant's application for the provision of a specific internal regulation. The complaint contested the action of the obliged entity in dealing with the application because the obliged entity had not provided the complainant with the requested internal regulation, but had referred her to the CNB website containing the relevant information. The complaint was dealt with under the procedure laid down in Article 16a(5) of the Act, and a decision refusing the application was issued.
  - (ii) A complaint about the CNB's action in dealing with the complainant's application for the provision of specific internal regulations and information relating to several dozen questions asked by the complainant. The complainant disagreed with the obliged entity's call upon him to clarify his application as the obliged entity had regarded the requested information as too general. The complaint was dealt with under the procedure laid down in Article 16a(5) of the Act, and a decision refusing the application was issued.
  - (iii) A complaint about the CNB's action in dealing with the complainant's application for the provision of specific internal regulations and information relating to around ten questions. In the complainant's opinion, the obliged entity had provided incomplete information in response to her questions; furthermore, the complainant disagreed with the fact that part of her application had been dealt with by reference to already published information and requested either direct provision of the information and provision of the relevant internal regulations, or the issuance of a decision refusing the application. The complaint was dealt with under the procedure laid down in Article 16a(5) of the Act, and a decision partly refusing the application was issued.

7. Other information relating to application of the Act:

It is apparent from the above summary of the number of applications received in 2014 that this number is comparable with the previous year. The public's interest in information concerning the CNB's areas of responsibility remains virtually the same. The applications pertain to a broad and diverse range of information which cannot be narrowed down to typical groups. For example, more than one application contained queries from the public regarding specialised issues in the areas of statistics, the balance of payments and circulation of banknotes and coins. Other subjects of applications included queries regarding procurement, enforcement proceedings and the CNB's internal regulations.

**B) INFORMATION PROVIDED BY WAY OF PUBLIC DISCLOSURE:**

The CNB also publishes information in a manner allowing remote access pursuant to Article 3(2) of the Act and provides information pursuant to Article 5(1), (2) and (3) of the Act. The information is available on the CNB website [www.cnb.cz](http://www.cnb.cz) and on notice boards at CNB headquarters and branches, in locations accessible to the public. Other information on the activities and responsibilities of the CNB is also published on the state administration web portal.

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