Bank of Finland Annual Report 2011

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Bank of Finland
Annual Report
2011

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Foreword

The economic developments of 2011 were marked by an exceptionally high level of economic uncertainty. This had a negative effect on growth prospects and, at the same time, disturbed the European financial markets' recovery from the confidence crisis that has bothered them for the last few years.

There are several reasons worth mentioning behind the heightened level of uncertainty. The social unrest that erupted in many Arab nations in the early part of the year and the nuclear catastrophe at Fukushima that followed the Japanese tsunami caused new disturbances to the recovering world economy, adding to the uncertainty. In the summer, economic prospects were overshadowed by a political dispute in the United States regarding federal debt ceilings. Towards the end of the year, the debt problems of a number of southern European countries reached new crisis levels, which threatened the financial stability of the entire euro area. All of these factors had a detrimental effect on the euro area's economic performance and already the latter part of the year was clearly disappointing. The fragile recovery that had been witnessed over a couple of years came to a halt, with the year ending on signs of a recession.

The weakening of the economic situation over the year also had an impact on monetary policy. In the early part of the year, crude oil and other commodity prices rose to high levels and the rate of euro area inflation accelerated. Against this background, the European Central Bank increased its policy rates twice. However, the rapid weakening of the economic outlook in the summer and the spread of the sovereign debt crisis in the euro area demanded new and determined measures of the monetary policy. In the summer the ECB activated its Securities Markets Programme and towards the end of the year implemented two policy rate cuts. On top of which, bank liquidity was supported by extensive new credit operations with a three-year maturity.

When, in order to manage the exceptional conditions, the Eurosystem has had to notably increase the volume of its monetary policy operations, the risk borne by central banks has also increased. For this reason, over the last few years, risk management has been significantly intensified at the Bank of Finland and also at the Eurosystem level. At the same time, the Bank of Finland has augmented the risk buffers of its balance sheet to secure its capital resources and to ensure its ability to distribute a share of the Bank's profits for the needs of the State in the future, too.

Along with the crisis management measures, economic and monetary policies must pay increasing attention to building stable foundations for economic growth over the longer term. This is an area where the euro area countries share a special common interest. The increase in government indebtedness has to be halted and mechanisms created that will ensure confidence in the sustainability of the euro countries' public finances. At the same time the foundations to growth need to be reinforced through structural reform which will increase the member countries' economic flexibility, competitiveness and employment.

A key lesson that has come out of the trials of the last few years of the financial crisis has been that supervision of the individual financial institutions alone is not enough to ensure stability, rather that risks arising in the financial sector need to be monitored and managed as a whole. The European Systemic Risk Board (ESRB) was set up in order to undertake this so-called macro-prudential supervision, and began operations at the beginning of the 2011. It is mandated to coordinate and guide the actions of the respective national authorities. Ensuring stability also requires the development of new instruments with which the authorities responsible for the financial markets can intervene, increasingly effectively, in developments that threaten the stability of the markets. Central banks, being constantly in touch with the workings of the money markets and, in times of crisis, having to make practical decisions on securing banks' liquidity, will hold a key position in the European supervisory architecture that is currently in the process of being established.

For the present, the Finnish banking sector appears to have weathered the crisis relatively intact. Despite that, ensuring financial stability more effectively under all conditions is a task which we must also take on. According to the programme of the new government, formed after the spring general election, the Financial Supervisory Authority will be provided with powers to use macro-prudential policy instruments, for example in limiting companies' and households' excessive indebtedness. Work on these powers and the development of the respective instruments is currently underway. It is essential that, in this respect, Finland meets the highest international and European requirements in the future, too.

Finland's general government deficit is also too large and limiting the increase in the nation's indebtedness is a vital objective. A new and worrying feature started to mar Finland's economic picture, when the current account balance of the country started to show a deficit in 2011. The disadvantageous developments in foreign trade tell both of Finland's competitiveness and the weakening structure of industry in relation to market requirements as well as of the public sector deficit that unsettles the national economy's financial balance. An extended period of current account deficit would mean an increase in the national economy's foreign debt. That would sit badly with an ageing society such as Finland's which ought rather to be gathering its resources for future use than using them up ahead of time. It is now essential that economic policy should strengthen Finland's long term prospects for economic growth. Continuous attention must be paid to balancing government finances, dampening the rise in domestic costs and to increasing the supply of labour.

The Bank of Finland celebrated its 200th anniversary in 2011. This gave the Bank ample opportunity to make its work and role better known. The Bank's two-part history was completed, the first part of which, Imperial Cashier to Central Bank, was published in April 2011 while part two, Parliament's Bank, will be published in March 2012. Over the anniversary year the Bank organised a number of events with the aim of making both the Bank of Finland's history and present activities better known. Of these events, guided art tours, where the doors of the Bank's head office were thrown open to the public, drew a satisfyingly large crowd. Along with the cultural experience the Bank offered to over 13,000 visitors it also wanted to underline that, as the Parliament's bank, it really does belong to the people of Finland.

However, the Bank of Finland always directs its activities in the direction of the future. Over the course of the year, in line with its revised Vision Statement, the Bank wanted make itself known as a forward-looking and effective central bank as well as a constructive and influential member of the Eurosystem. The prerequisites for this being achieved are established through the dedicated work of the Bank's staff and through sound external cooperation. I would like to extend my thanks to the staff of the Bank at the end of a challenging but successful year.

Erkki Liikanen
6 March 2012

The May meeting of the ECB Governing Coucil was held in Helsinki in 2011.

Photo: Lehtikuva.

Bank of Finland

The Bank of Finland is Finland's national central bank and a member of the European System of Central Banks (ESCB). The Bank of Finland is an institution governed by public law operating under the guarantee and care of the Parliament. The superintendence of the Bank's activities is undertaken by the nine-member Parliamentary Supervisory Council, appointed by the Finnish Parliament. The Bank's status is defined in the Finnish constitution, and its activities are regulated by the Statute of the European System of Central Banks and the Act on the Bank of Finland.

Established in 1811, the Bank of Finland is the fourth oldest central bank in the world. Initially it operated as an exchange bureau for banknotes, loan office and state cashier. Gradually it assumed the role of central bank as Finland's monetary and banking systems developed. The Bank of Finland's present position dates from 1868, when the Bank became subject to the Parliament. The Bank became part of the European

The Board of the Bank of Finland.
From the left: Pentti Hakkarainen, deputy Governor, Erkki Liikanen, Governor and Seppo Honkapohja, Member of the Board.
They are standing in front of a new addition to the Bank's art collection, "Untitled" by Marianna Uutinen, acquired in 2011.

Photo: Peter Mickelsson.

System of Central Banks in 1998, and the transition to the single currency of the euro area was made from the beginning of 1999.

In addition to monetary policy preparation and monitoring of financial market stability, the core functions of the Bank of Finland include operational central bank tasks in connection with interbank payments, the implementation of monetary policy and the secure and efficient maintenance of currency supply in Finland.

Although the monetary policy decisions of the Eurosystem are centralised in the Governing Council of the European Central Bank, responsibility for their implementation remains at national central bank level. The Governor of the Bank of Finland is a member of the ECB's Governing Council and thereby participates in the decision-making process affecting the entire Eurosystem, as an independent and impartial decision-maker. Experts from the Bank of Finland monitor and assess developments in the financial and real economy supporting the Governor's decision-making.

In its function of oversight of the financial markets, the Bank of Finland is responsible for the macroeconomic perspective while supervision of individual market operators is undertaken by the Financial Supervisory Authority, functioning as an independent authority in connection with the Bank of Finland. Both the Governor of the Bank of Finland and the Director General of the Financial Supervisory Authority belong to the European Systemic Risk Board (ESRB), operating in conjunction with the European Central Bank, in which Governor Liikanen is a voting member of the General Board.

In 2011, the Board of the Bank of Finland was composed of the Governor Erkki Liikanen, Deputy Governor Pentti Hakkarainen and Member of the Board Seppo Honkapohja. During the review year, a total of about 421 staff were employed in the 6 departments of the Bank's head office and the 4 regional offices. The Financial Supervisory Authority has its own Board, chaired by the Deputy Governor of the Bank of Finland, Pentti Hakkarainen. At the end of 2011 the FIN-FSA employed a total of 208 staff. The FIN-FSA produces its own annual report on its activities.

Box 1.

The Bank of Finland celebrates its 200th anniversary

December 2011 saw 200 years since Emperor Alexander I of Russia ratified a proclamation enabling the establishment and operations of an Office for Exchange, Lending and Deposits for the Grand Duchy of Finland.

The various phases that the Bank of Finland has lived through over the 200 years that followed the proclamation have been laid out in a two-volume history published by the Bank. The first volume of the work, written by Dr Antti Kuusterä, Senior Lecturer, and Juha Tarkka, (Dr. Pol.Sc.), *Imperial Cashier to Central Bank*, was published in April 2011. It covers the period from the establishment of the Bank to the outbreak of the Finnish Winter War in late autumn 1939. The second volume *Parliament's Bank*, by the same writers, will be published in March 2012. The second volume of The Bank of Finland 200 Years goes into the Bank's operations during the war years and the decades following the Second World War up to the 1990s.

Details from the Bank of Finland's history were also presented in a documentary produced by Frank Media *Building Finland – The Bank of Finland 200 years*. The documentary was aired on Finland's MTV3 television channel in May and December.

The Bank launched its anniversary celebrations in January 2011 by arranging an exhibition, presenting the key works of the Bank of Finland's art collection. Members of the Bank of Finland staff, who were interested in art and had prepared themselves by studying the Bank's art and the artists behind the works, acted as guides to the viewing public. The event exceeded all expectations and over the five days of the exhibition, more than 7,000 members of the public came to see the Bank's art.

Based on the enormous success of this exhibition it was decided to hold a smaller scale exhibition in August. The four evenings and the weekend of this second exhibition were attended by more than 4,300 visitors. In the spring and autumn the Bank organised a large number of group visits where the visitors were first taken round the Bank of Finland Museum and introduced to the Bank's activities and then given a guided tour of some of the art on display in the Bank's head office. Including these group guided tours, more than 13,000 people viewed the Bank's art collection over the course of the anniversary year. It is also possible to take virtual tours of both the architecture of the head office building as well as some of the highlights of the Bank's art collection via the Bank of Finland website.

The Governing Council of the European Central Bank convened outside Frankfurt twice in 2011. In May 2011 it was the turn of the Bank of Finland to host the meeting. The meeting brought to Helsinki a large number of representatives from international economic press. Immediately following the meeting, the Bank of Finland arranged a two-day international conference on the theme of *Monetary Policy under Resource Mobility*. In addition to the members of the ECB Governing Council, the conference was attended by a large number of heads and experts from other central banks, well-known economists and economic correspondents from around the world.

In August the Bank organised a one day symposium on the subject of the economic history of the Baltic region in the city of Turku, the Bank of Finland's original home town. As well as presentations from Finnish speakers the symposium included presentations on the history of central banks from Sweden and Russia.

In April 2011, the staff of the Bank of Finland the Financial

Supervisory Authority and their families were invited to get to know the Bank's facilities and art collection. On December 10 existing staff and member's of the Bank's pensioners club were invited to an event at the Helsinki Music Centre. The invitation included a concert by the UMO Jazz Orchestra, with soloists Jukka Perko on saxaphone and vocalist Anna-Mari Kähärä.

The Bank's anniversary year came to a climax with an evening laid on for invited guests, also arranged in the Helsinki Music Centre, on 13 December. The evening's entertainment included a showing of Peter von Bagh's film essay *Finns and money – A love story*. The film was followed by a conversation in which the reporter Seppo Toivonen interviewed Sirkka Hämäläinen, the former Governor of the Bank of Finland and Erkki Liikanen, the present Governor of the Bank. After the interval the Helsinki City Orchestra, conducted by Jukka-Pekka Saraste, played a selection of pieces by Lindberg, Sibelius and Fauré, and the soloist was the violin virtuoso Elina Vähälä.

Media correspondent Seppo Toivonen interviews the former Governor of the Bank of Finland Sirkka Hämäläinen and the current Governor Erkki Liikanen in the Music Centre, at an event arranged to celebrate the Bank's 200th anniversary.

Photo: Peter Mickelsson.

Bank of Finland's strategic implementation in 2011

Bank of Finland – builder of economic stability. Price stability, secure payment systems and reliable financial systems promote robust economic growth, employment and the well-being of Finnish society.

The Bank of Finland's values as well as mission and vision statements were renewed over the course of 2011. The process of incorporating the mission statement, vision and values into the Bank staff's daily thinking will continue throughout 2012. (See Box 2).

The Bank's currency supply strategy was accomplished by continuing the process of reducing the number of regional offices from four to two, over a couple of years, ending in 2012.

The Bank of Finland as part of Finnish society

The Bank of Finland is an influential member of the Eurosystem and the domestic economic policy debate.

The intensification of the financial and sovereign debt crisis and their expansion into the larger euro countries have had an impact on the Bank's strategy work. The Bank of Finland has made its contributions to domestic economic policy discussions, particularly in areas concerning indebtedness, growth and financial market stability. The bank's experts have underlined the importance of price stability in securing the euro area's common monetary policy, and tight fiscal policy as the best way to ensure stability and employment.

Together with the Financial Supervisory Authority, the Bank of Finland participates in the work of various working groups set up to meet the requirements of the Government's programme relating to macroprudential systems. The Bank's objective is to secure the stability and efficiency of the financial markets through timely stability analysis and maintaining appropriate crisis management.

The Bank of Finland and the Eurosystem

As a member of the Governing Council of the ECB, the Governor of the Bank of Finland participates in decision-making regarding the monetary policy of the euro area. The meetings of the ECB are held to analyse monetary and economic developments, the operational framework of the monetary policy, payment systems and other central banking functions and related decision-making. The Bank's experts are extensively involved in the preparation of all these matters.

The Bank's strategic objective is to increase international cooperation in the field of financial market supervision and to step up cooperation between the competent authorities in Finland.

The Bank of Finland took an active part in the work of the European Systemic Risk Board (ESRB). The Board commenced its activities at the beginning of 2011. Cooperation between the Bank and the FIN-FSA in financial stability issues and in the European Systemic Risk Board has become closer, while the division of labour has been made clearer. In this context, a key role is played by prevention and mitigation of systemic risks as well as monitoring threats to the stability of the financial system.

Strategic focal points in 2011 included evaluating the risks to the Bank of Finland's balance sheet and minimizing those risks by ensuring the strength of the balance sheet. The Bank of Finland participates in liquidity management in the euro area's banking system in the preparation of monetary policy and via conduct of market operations. Risks arising from market operations form part of the Bank's overall risks.

In accordance with its strategies, the Bank of Finland is involved in development of the payment system and oversight in cooperation with both national and international authorities. The process of implementing the simulator developed by the Bank of Finland as an oversight tool for the Eurosystem's payment systems continues.

The Bank of Finland's strategy and evaluation tools were renewed based on the mission statement and values revision in 2012. The Bank's strategic objective is to be one of the most efficient EU central banks.

The Bank of Finland organised a guided art exhibition for members of the public in the head office, in honour of its anniversary.

Photo: Peter Mickelsson.

Box 2

Bank of Finland's mission, vision and values

The Bank of Finland's mission, vision and values statement underwent a thorough revision in 2011. Over the course of the year, the Bank's entire organisation was involved in commenting on the mission statement and working on the vision and common set of values.

Mission

Bank of Finland – builder of economic stability, secure payment systems and reliable financial systems promote robust economic growth, employment and the well-being of Finnish society.

The mission statement is an expression of the nature and direction of the Bank's organisation functions and is used to describe what the organisation does and why.

Vision

The Bank of Finland is known as a visionary and effective central bank as well as a constructive and influential member of the Eurosystem.

The values statement underlines the Bank of Finland's objective of being a forward-looking authority, whose activities and statements are constructive in promoting the long term robustness and stability of Finland's economy. References to efficiency show that the Bank itself aims to operate in the spirit of its own statements.

A constructive role within the Eurosystem requires the Bank of Finland to be actively involved in developing solutions to the Eurosystem members' common problems. While being influential imposes high expectations on the competencies and communication skills of the Bank's personnel.

Values

Competent – Constructive – Accountable

The values reflect attitudes to work, colleagues and the rest of society. The values drive the Bank of Finland staff's day-to-day activities and underpin the organisation's working culture. The entire organisation of the Bank was involved in the preparation of the values statement.

Competent

Extensive competence and high professional ethical standards are the foundations of our work. We constantly update our skills and working practices.

Constructive

We work together with mutual respect and towards common objectives. We encourage frank discussions and air our ideas openly.

Accountable

We act responsibly and independently. We are reliable cooperative partners.

Bank of Finland activities 2011

Monetary Policy

The ECB's monetary policy and its preparation

Bank of Finland – contribution to preparation of monetary policy

As a member of the Governing Council of the ECB, the Governor of the Bank of Finland participates in monetary policy decision-making. In addition, experts from the Bank of Finland contribute to the preparation of monetary policy decisions and other background work. They contribute to the preparation of Governing Council's meetings in the context of the Eurosystem's Monetary Policy Committee and the Market Operations Committee. The Bank of Finland's influence in the Eurosystem draws on preparation work in a number of the Bank's departments. In 2011 the emphasis of monetary policy preparation was on non-standard monetary policy measures to address debt market disruptions.

Eurosystem's key interest rates remained exceptionally low in 2011

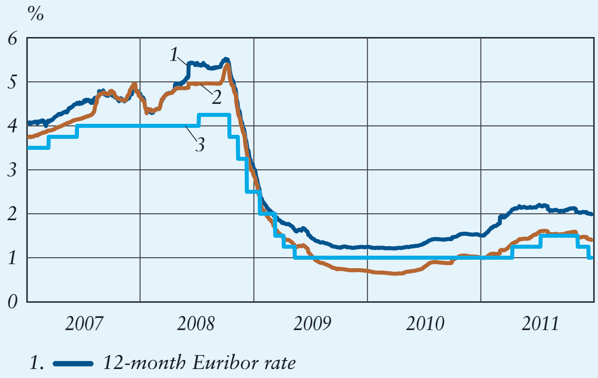
Through its monetary policy, the ECB primarily aims to keep the inflation rate in the euro area, as measured by the Harmonised Index of Consumer Prices (HICP) below, but close to, 2% over the medium term. The Governing Council of the ECB monitors and analyses the economic outlook for the euro area and sets its key interest rates at a level that best supports price stability over the medium term.

In 2011 the Eurosystem's key interest rates remained exceptionally low (Chart 1). In the latter half of the year sovereign debt problems escalated in certain euro area countries, resulting in severe tensions in financial markets. The macroeconomic environment was challenging, as Greece's problems in particular heightened and Italy's general government outlook gave markets cause for concern. Problems arising from financial market disruptions on monetary policy transmission played a central role in the decisions of the ECB Governing Council in the latter part of 2011. The Governing Council repeatedly emphasised during the year that all the non-standard measures taken during the period of acute financial market tensions were, by construction, temporary in nature. The non-standard measures are discussed in greater detail in the next section (Implementation of monetary policy in the euro area and in Finland).

Actual inflation in the euro area was relatively brisk in 2011, 2.7% as measured by the HICP. In 2010 the inflation rate had been 1.6%. In the early part of 2011, strong growth of emerging economies fuelled the rise in energy and commodity prices in particular. Energy prices remained high throughout the year also on account of political tensions in North Africa and the Middle East. In March-June the HICP inflation was about 2.7%. Inflation remained high also in the latter part of the year, accelerating to 3% in September-November. In addition to continued high energy and commodity prices, the rise in inflation in the latter part of the year was also attributable to increases in indirect taxes and administered prices in a number of countries.

At the beginning of 2011 the interest rate on the ECB's main refinancing operations (MROs) was 1%, the level maintained since May 2009. Based on the assessment of risks to inflation, the ECB Governing Council increased the key interest rates by 0.25 percentage point in April and July, after which the interest rate on the MROs was 1.5% (Chart 1). The underlying momentum of economic activity in the euro area was positive, despite uncertainty remaining elevated. The monetary policy stance remained accommodative even after these interest rate rises, lending considerable support to economic activity and job creation. However, the economic analysis indicated in April that risks to the outlook for price developments were on the upside. Monetary liquidity remained ample with the potential to accommodate price pressures. Anchoring of inflation expectations is a prerequisite for monetary policy to contribute to economic growth in the euro area. The further adjustment of the accommodative monetary policy stance in July was warranted in the light of upside risks to price stability.

Chart 1.
Monetary policy transmission mechanism



Source: European Central Bank.

In autumn 2011 the euro area economic outlook weakened substantially. Ongoing tensions in financial markets had an unfavourable effect on financing conditions and confidence. These tensions were assessed as continuing to dampen economic activity in the euro area. Uncertainty relating to the economic outlook and intensified downside risks to growth were expected to dampen price, cost and wage pressures in the euro area, and these pressures were expected to remain modest over the policy-relevant horizon. Inflation had remained high and it was likely to stay above 2% for several months to come, before declining to below 2%. On the basis of these exceptionally rapidly changing factors, the ECB Governing Council reduced the key interest rates by 0.25 percentage point twice at the end of the year, first in November and then in December. In December the interest rate on the MROs had been lowered back to 1%.

Inflation risks increased in the first half of the year

Economic growth recovered in the first half of the year, and inflation risks began to increase in response to higher energy and commodity prices (Chart 2). In March the ECB Governing Council revised its assessment of inflation and economic growth for 2011 and 2012 upwards. It also assessed risks to the outlook for price developments as being on the upside. The Governing Council expressed its concern over the fact that price and wage setters' behaviour should not lead to broadly based second-round effects stemming from higher commodity prices. On the basis of upward risks to inflation, the Governing Council decided in April to raise the key interest rates by 0.25 percentage point. The interest rate on the MROs increased to 1.25%. Prior to this interest rate increase, the key interest rates had been unchanged since May 2009, ie for almost two years. The Governing Council stated that the stance of monetary policy remained accommodative after the interest rate rise and that it continued to lend considerable support to economic activity and job creation.

Sovereign debt problems in the euro area were reflected in the first half of the year in a rise in interest rates on bonds of some small euro area countries. In April the ECB Governing Council assessed that the ongoing tensions in some segments of the financial markets that may potentially spill over to the euro area real economy posed downside risks to economic growth. However, in March-August the risks to economic growth were regarded as being broadly balanced.

Owing to the natural and nuclear disasters in Japan, the ECB participated in an exchange rate intervention to dampen fluctuations of the Japanese yen. Besides the Bank of Japan, other banks participating in the intervention were the Federal Reserve (Fed), the Bank of England and the Bank of Canada. Still in May, the Governing Council assessed that there were potential risks stemming from the economic impact on the euro area and elsewhere of the natural and nuclear disaster in Japan.

The Portuguese sovereign debt markets deteriorated in the first half of 2011, and in April Portugal, in addition to Greece and Ireland, became the third euro area country to sign a joint adjustment programme designed by the EU and the International Monetary Fund (IMF) and became dependent on external financing. In May the Governing Council welcomed the EU/IMF economic and financial adjustment programme agreed by the Portuguese government, which was assessed as containing the necessary elements to bring about a sustainable stabilisation of the Portuguese economy. In Greece and Ireland, government debt problems had already escalated in 2010 when the Eurosystem actively participated in the preparation of financial assistance packages also to these countries, together with the European Commission and the

Chart 2.
Harmonised Index of Consumer Prices for the euro area

Change from year earlier, %

Source: Eurostat.

IMF. During the year the Governing Council repeatedly emphasised that strengthening financial market confidence and reducing sovereign risk premia required immediate and credible multi-year fiscal consolidation.

Aggravating debt problems and higher interest rates on sovereign bonds increased tensions in interbank money markets already in the first half of 2011. Starting from January the ECB Governing Council repeatedly stressed that banks should, where necessary, expand the availability of credit by retaining earnings, turning to the market to strengthen their capital bases or taking full advantage of government support measures for recapitalisation. The Governing Council supported bank liquidity throughout the year for instance by continuing its fixed-rate full-allotment approach applied in bank refinancing operations since October 2008. This means a commitment to accommodating banks' liquidity needs in full at a predetermined interest rate, as long as banks provide adequate collateral. The Governing Council also emphasised repeatedly that it would ensure that liquidity constraints would not hamper solvent banks' operations. However, the Eurosystem's balance sheet relative to GDP remained almost unchanged in the first half of 2011.

In March-May the Governing Council's view was that risks to the medium-term outlook for price developments remained on the upside. In assessing inflation risks, the Governing Council stated in spring and early summer the following: Upside risks relate, in particular, to higher-than-assumed increases in energy prices, not least on account of the ongoing political tensions in North Africa and the Middle East. More generally, strong economic growth in emerging markets, supported by ample liquidity at the global level, may further fuel commodity price rises. Moreover, increases in indirect taxes and administered prices may be greater than currently assumed, owing to the need for fiscal consolidation in the coming years. In addition, the Governing Council stated that risks also related to stronger than expected domestic price pressures in the context of the ongoing recovery in activity. At its meeting in May, which was held in Helsinki, the Governing Council emphasised that, besides upside risks to inflation, the economic environment was subject to elevated uncertainty.

Interest rate increases in the first half of 2011 restrained risks to inflation

In June the ECB Governing Council revised its assessment of inflation and economic growth for 2011 upwards. In July the Governing Council increased the key interest rates by 0.25 percentage point, already for the second time in 2011, on account of risks to price stability. The interest rate on the MROs increased to 1.5%, and according to the Governing Council the monetary policy stance remained accommodative. The Governing Council emphasised that, all in all, it was essential that the price developments in the first part of 2011 would not give rise to broad-based inflationary pressures over the medium term. It stressed that the decision contributed to keeping inflation expectations in the euro area firmly anchored in line with the aim of maintaining inflation rates below, but close to, 2% over the medium term.

In July the underlying momentum of economic activity in the euro area was still positive. However, the situation in Greece had turned more difficult than anticipated, and in July 2011 the EU heads of state or government agreed on the principles of a new support package for Greece. According to EU and IMF assessments, the economic situation in Ireland and Portugal remained roughly in line with the EU/IMF adjustment programme in 2011. The Irish economy in particular improved in the latter part of the year, and the interest rates on Irish government bonds clearly diverged from the corresponding rates in Greece and Portugal. In the latter two countries, the spread on government bonds relative to the corresponding rates in Germany widened throughout the year.

The Governing Council has repeatedly urged euro area governments to take fiscal policy action and

The governors of the euro area central banks participated in the ECB's Governing Council meeting in Helsinki in May 2011.

Photo: Lehtikuva.

implement structural reforms. In March the Governing Council stressed that the sovereign debt crisis in the euro area had reinforced the need for an ambitious reform of the euro area economic governance framework. In April the Governing Council was of the view that the package of six legislative proposals on economic governance, adopted by the European Council at its summit on 24–25 March 2011, went some way to improving economic and budgetary surveillance in the euro area. However, the Governing Council urged on more stringent requirements, more automaticity in the procedures and a clearer focus on the most vulnerable countries with losses in competitiveness. In June the Governing Council emphasised that the implementation of credible fiscal adjustment strategies was crucial in view of ongoing financial market pressures. In July the Governing Council welcomed the introduction of the European Semester, including the then-recent submission of countries' National Reform Programmes that incorporated commitments made under the Euro Plus Pact.

The ECB Governing Council increased non-standard monetary policy measures in the second half of the year

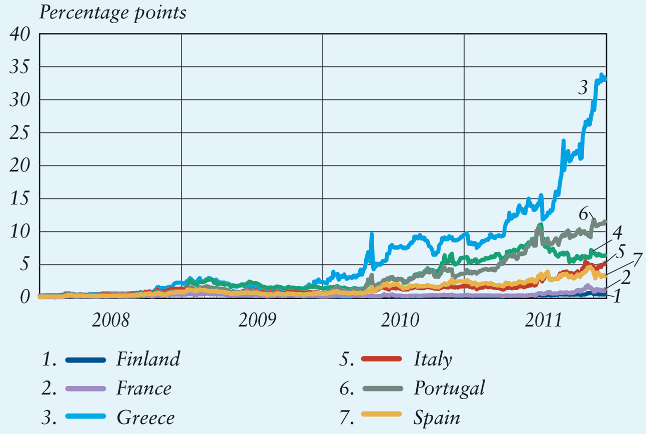
In August the Governing Council considered inflation risks to still be on the upside, while growth risks were broadly balanced. However, the Governing Council stressed that the operational environment was subject to particularly high uncertainty. In summer the economic outlook had begun to deteriorate for both Europe and the United States. At the same time, market uncertainty about political decision-making heightened in response to European crisis management problems and difficulties relating to debt ceiling negotiations in the USA. As a result of the worsened economic situation, the Governing Council revised its assessment of inflation and economic growth for 2011 and 2012 downwards in September. It also assessed risks to economic growth as being tilted on the downside, in an environment of particularly high uncertainty and tensions in financial markets. Inflation risks were no longer assessed to be on the upside, but on balance instead. Financial conditions were also assessed to have tightened.

In the latter half of 2011 sovereign debt problems escalated in certain euro area countries, resulting in severe tensions in financial markets. The ECB Governing Council had to address the exceptionally high level of uncertainty with non-standard monetary policy measures. Euro area sovereign bond markets deteriorated rapidly starting from the end of July, creating agitation in euro area financial markets. The fragile economic outlook intensified market concerns about the sustainability of public finances in Italy and Spain in particular. This was evidenced in July-August in interest rates on government bonds, which began to climb up in these two countries (Chart 3).

Financial market tensions were reflected in the financial sector, and in autumn problems began to emerge in banks' ability access financing. In the latter part of the year the Eurosystem addressed elevated market uncertainty for example by extending maturities of loans to banks. Already in August the ECB Governing Council decided to conduct a liquidity-providing supplementary longer-term refinancing operation (LTRO) with a maturity of approximately 6 months. The Governing Council also expanded the Securities Markets Programme (SMP) initiated in May 2010. Under the SMP, the Governing Council can purchase private and public debt securities in market segments that are dysfunctional and pivotal to the monetary policy transmission mechanism. In August–December the Eurosystem conducted outright purchases of securities within the context of SMP in an amount of approximately EUR 138 billion. The liquidity impact of SMP purchases was sterilised with liquidity-absorbing operations. The Governing Council has emphasised repeatedly that all the non-standard measures taken during the period of acute financial market tensions are, by construction, temporary in nature.

In October the Governing Council assessed that downside risks to growth had intensified and stressed that the risks to the economic outlook were subject to particularly high uncertainty. The Governing Council's view was that ongoing tensions in financial markets and unfavourable effects on financing conditions were dampening the pace of economic growth in the euro area in the

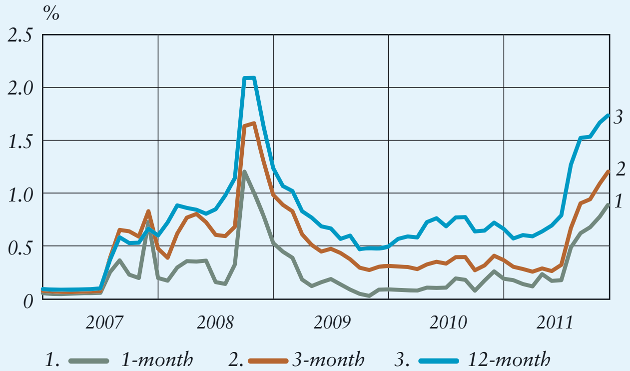
Chart 3.
Spread between government bond yields in selected countries and the corresponding German government bond yield



Bond maturity about 10 years.
Source: Bloomberg.

second half of 2011. It also stressed that the situation of the banking sector called for particular attention. Banking sector problems were reflected in interbank money markets, for example in the widening spread between secured and unsecured interest rates in the latter half of 2011 (Chart 4). To support the financial sector, the Governing Council announced that it would continue to conduct fixed rate tender procedures with full allotment in all operations for as long as necessary, and at least until mid-2012. It also decided to conduct two new additional LTROs with a maturity of approximately one year. Furthermore, the Governing Council announced that it would launch a new covered bond purchase programme (CBPP2) with a targeted nominal amount of EUR 40 billion. The previous CBPP had been

Chart 4.
Spread between secured and unsecured interest rates in the euro area



Spread between Euribor and EUREPO rates.
Source: Reuters.

launched in summer 2009. Through this programme the Eurosystem can conduct monetary policy through the banking sector, as covered bonds are instruments issued by banks.

Weakening of economic outlook at the end of the year led to interest rate decreases

In November the ECB Governing Council lowered the interest rate on the MROs by 0.25 percentage point. The Governing Council was headed by Mario Draghi, President of the ECB, as Jean-Claude Trichet's term in office as President ended at the end of October. The Governing Council assessed that, owing to their unfavourable effects on financing conditions and confidence, the ongoing tensions in financial markets were likely to dampen the pace of economic growth in the euro area in the second half of 2011 and beyond. In its decision the Governing Council took account of the fact that, in such an environment, price, cost and wage pressures in the euro area were also expected to moderate. In November the Governing Council continued to view the risks to the medium-term outlook for price developments as broadly balanced. It also stated that the economic outlook continued to be subject to particularly high uncertainty and intensified downside risks.

At the same meeting in early November, the Governing Council stressed that it was absolutely imperative that euro area national authorities rapidly adopt and implement the measures announced and recommended in the Euro Summit statement of 26 October 2011. The Euro Summit held at the end of October aimed at designing a plan to stop euro area sovereign debt problems from spreading further and stabilise the situation. The summit was held against the background of increased concerns over the banking sector and financing conditions in Europe as well as the effects of rises in interest rates on Italian government bonds in particular. The key decisions taken in the summit concerned solving the increasingly difficult situation in Greece, attempts to increase the capacity of the European Financial Stability Facility (EFSF), and bank recapitalisation. The Governing Council welcomed the agreement of the European Council to increase the capital position of banks to 9% of core Tier 1 by the end of June 2012. It also fully supported the call to national supervisors to ensure that banks' recapitalisation plans would not lead to excessive deleveraging. At its meeting in early November the Governing Council emphasised that governments of countries under joint EU/IMF support programmes (Greece, Ireland and Portugal) and those of countries that are particularly vulnerable must stand ready to take any additional measures that become necessary.

In November financial market disruptions were also fuelled by the political crisis in Greece and Italy, which resulted in the election of a new prime minister and government in both counties. In addition, uncertainty in November about the prospects for solving the euro area debt crisis led to increases in the interest rates on French and Belgian government bonds. In December the situation in the euro area sovereign bond markets remained challenging but eased slightly compared with November. The interest rates on Spanish government bonds in particular decreased relative to corresponding rates in other debt crisis countries.

As the economic situation deteriorated further, the ECB Governing Council continued to reduce the key interest rates in December and lowered the interest rate on the MROs by 0.25 percentage point to 1%. The Governing Council revised its assessment of economic growth for 2012 markedly downwards and stated that the economic outlook for the euro area was subject to substantial downside risks in an environment of high uncertainty. In its decision the Governing Council took into account the fact that in such an environment, cost, wage and price pressures in the euro area were expected to remain modest over the policy-relevant horizon.

The ECB Governing Council supported the functioning of the financial sector

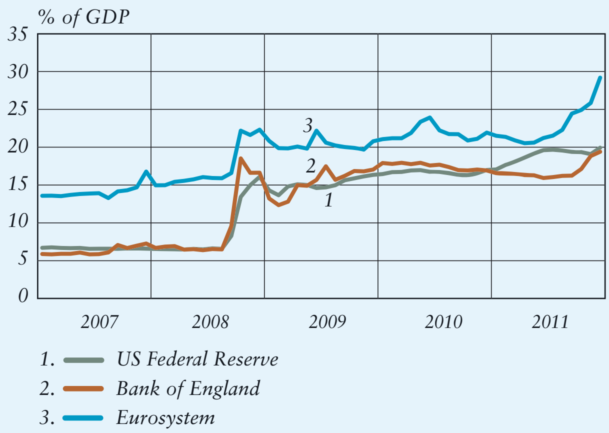
In November-December the Governing Council also made a number of decisions to ensure bank liquidity and to facilitate the functioning of the euro area money markets. These measures were expected to support the provision of credit to households and non-financial corporations. On 30 November 2011 the world's leading central banks announced new coordinated action to provide liquidity to the global financial system by lowering the pricing on US dollar liquidity swap arrangements by 0.50 basis points. They also agreed to establish bilateral liquidity swap arrangements so that liquidity could also be provided in other main currencies. In addition to the ECB, banks participating in these actions were the Federal Reserve, the Bank of England, the Bank of Japan, the Bank of Canada and the Swiss National Bank. At its meeting in early December the Governing Council also adopted new significant non-standard measures to support the liquidity situation and functioning of the banking sector. It decided to conduct two exceptionally long LTROs with a maturity of three years. It also decided to reduce the reserve ratio applicable to minimum reserves from 2% to 1% and ease collateral requirements by expanding the scope of eligible collateral and their rating thresholds.

In this context the Governing Council reiterated that all euro area governments urgently needed to do their utmost to support fiscal sustainability in the euro area as a whole. In addition, commitment to long-term structural reforms was also necessary to support economic growth and the functioning of the euro area. In December the Governing Council stated that a new fiscal compact, comprising a fundamental restatement of the fiscal rules together with the fiscal commitments that euro area governments have made, was the most important pre-condition for restoring the normal functioning of financial markets.

The non-standard measures to support the functioning of the financial sector in the latter part of 2011 in particular, together with certain other factors, increased the size of the Eurosystem's balance sheet relative to GDP (Chart 5). The Eurosystem's balance sheet relative to GDP expanded from about 21% in early 2011 to almost 30% in December 2011. The Eurosystem conducted outright purchases under SMP by about EUR 138 billion in 2011, and at the end of the year the Eurosystem's SMP holdings totalled approximately EUR 212 billion. Purchases conducted under the new Covered Bond Purchase Programme totalled approximately EUR 3 billion in 2011. Purchases under the original CBPP amounted to about EUR 59 billion at the end of 2011. The Eurosystem's balance sheet total increased also on account of longer-term refinancing operations. The additional liquidity borrowed by banks under these operations flowed back to central bank mainly through banks' short-term deposits.

Besides the combined balance sheet total of the Eurosystem central banks, there was also an exceptional increase in balance sheets of a number of the national central banks due to growth in items between Eurosystem central banks. This was particularly affected by capital outflows from countries with financial problems. Funds flowed to resilient countries' money markets and further to their central banks. As a result of these financial flows, claims of the resilient countries' central banks on problem countries' central banks grew significantly in Eurosystem interbank payment accounts. This also led to an exceptional expansion of the balance sheet of the Bank of Finland.

Chart 5.
Central bank balance sheet



Sources: National statistical offices, Eurostat and Bloomberg.

Implementation of monetary policy in the euro area and in Finland

Eurosystem ensured access to central bank refinancing

The implementation of monetary policy ensures the pass-through of the decisions taken by the Governing Council of the ECB to market rates and further to the activities of households and non-financial corporations, and thereby to price developments. The most important monetary policy instruments are central bank refinancing operations for which the price, volume, maturity and timing can be changed and, in so doing, steering interbank money market rates. Having kept the key ECB interest rates unchanged for almost two years, the Governing Council of the ECB in April raised the interest rate on the main refinancing operations (MROs) by 0.25 percentage points to 1.25% on account of upside risks to price stability. Other terms and conditions of refinancing were largely kept unchanged in the first half of the year. The interest rate was raised further to 1.5% in July.

In July–August, tensions in euro area government bond markets started to intensify, which led to new purchases in the Eurosystem's Securities Markets Programme (SMP), launched in May 2010. The MRO rate was lowered by a quarter of a percentage point in both November and December in response to the changed inflation outlook, and it stood at 1% at the end of the year. The interest rate on the deposit facility was kept 0.75 percentage point lower than the policy rate throughout the year and, correspondingly, the interest rate on the marginal lending facility was kept 0.75 percentage point higher than the policy rate. In the second half of the year, banks were also offered refinancing with exceptionally long maturities, and in December the Governing Council of the ECB announced a number of non-standard measures to strengthen the transmission of monetary policy. One of these was the conduct of two longer-term refinancing operations (LTROs) with a maturity of 36 months.

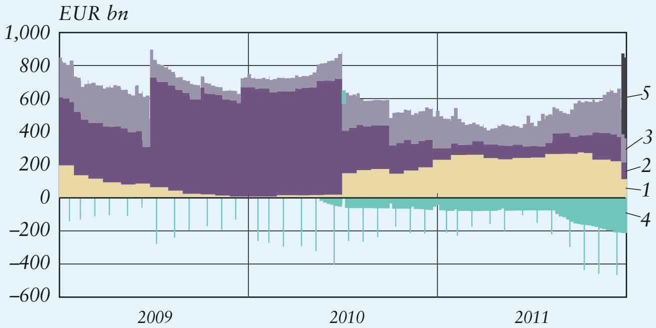
Banks need central bank refinancing to meet various liquidity requirements, for example, in order to fulfil their minimum reserve requirements and to cover the public's demand for banknotes. The banks purchase the banknotes from the central bank. Since the onset of the financial crisis, the importance of liquidity has been highlighted and, simultaneously, growing lack of confidence between banks and deterioration of banks' credit ratings have divided the money market into two parts: some banks obtain central bank credit in order to safeguard their liquidity, while others deposit their excess funds with the central bank, instead of other banks.

Monetary policy counterparties are provided access to central bank refinancing, against eligible collateral, by participating in refinancing operations carried out on a decentralised basis.[1] The Governing Council of the ECB continued

[1] Monetary policy counterparties operating in Finland participate in the refinancing operations at the Bank of Finland, where the Market Operations division of the Banking Operations department is responsible for their implementation.

to apply the fixed rate full-allotment policy in all refinancing operations, introduced in autumn 2008, throughout the year, which significantly reduced market uncertainty related to the liquidity situation. Banks had the opportunity of obtaining liquidity in amounts they needed at a fixed interest rate in all types of operations against collateral accepted by the Eurosystem. In the euro area, the average maturity of central bank refinancing remained longer than prior to the financial crisis, with approximately 70% of maturities being longer than one week. In the first half of 2010, longer-term refinancing operations (LTROs) accounted for an average of as much as 90% of liquidity allotted to banks, whereas before the money market tensions that commenced in 2007 the bulk, or 60–70%, of refinancing was allocated to banks in the main refinancing operations (MROs) with a one-week maturity. The volume of liquidity allotted in the most important policy operation under normal circumstances, the MRO, was on average EUR 130 billion in the first half of 2011, increasing to about EUR 180 billion in the latter half. The MROs were conducted once a week as fixed-rate tenders. In the three-month LTROs conducted regularly once a month, the interest rate has since October 2010 been fixed at the average interest rate of the MROs over the life of the respective operation. The outstanding volume of three-month liquidity allotted in the euro area during the year averaged EUR 245 billion.

Chart 6.
Eurosystem open market operations



1. Longer-term refinancing operations (3 months)
2. Supplementary longer-term refinancing operations (1–12 months)
3. Main refinancing operations (1 week)
4. Fine-tuning operations (1–7 days)
5. Supplementary longer-term refinancing operations (36 months)

Source: Bank of Finland.

Excess liquidity declined in the first half of the year

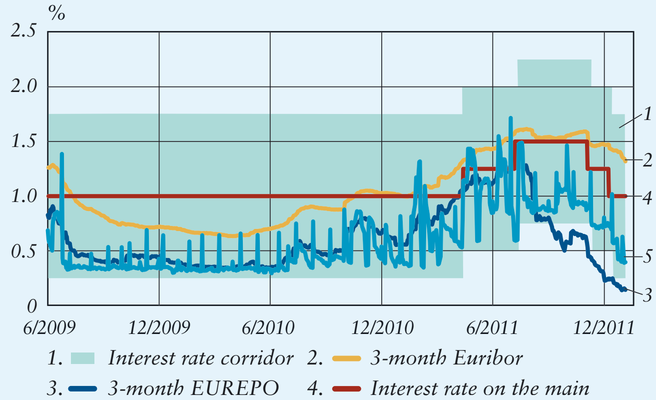
Banks fulfil their minimum reserve requirements by depositing an amount of money equivalent to the reserve requirement on their current accounts with the central bank over a maintenance period of about one month. Roughly speaking, the banking system has excess liquidity when banks' current accounts are larger than the minimum reserve requirements imposed on them. When the money market has become dysfunctional and Eurosystem operations enable unlimited access to refinancing, banks' demand for central bank refinancing exceeds their minimum liquidity needs and the use of overnight deposits with the central bank increases.

Banks' deposits with the central bank are remunerated at the MRO rate when these deposits serve to fulfil reserve requirements. As soon as the reserve requirements are fulfilled, no interest is paid on excess amounts, and it is worthwhile for banks to place them as overnight deposits. However, depositing this excess liquidity back with the central bank is expensive for the banking system, because the interest rate on the deposit facility is 0.75 percentage point lower than the interest rate on the MROs. Consequently, the impaired functioning of the money market was key to explaining growth in the volume of excess liquidity.

In early 2011, the amount of liquidity allotted to banks continued to contract compared with the situation in 2010, remaining at EUR 400–500 billion in the euro area (Chart 6). Meanwhile, the amount of excess liquidity declined to an average of EUR 25 billion in the January–June maintenance periods. Following the expiry at the end of 2010 of the last outstanding 12-month LTRO, the stock of refinancing operations with exceptionally long maturities fell notably. In the first half of the year, of non-standard euro-denominated operations, only operations with a maturity of one maintenance period, ie about one month, were in use and were carried out once a month. Normalisation in the interbank money market continued in the early part of the year, as the smaller volume of excess liquidity made it increasingly necessary for banks to operate in the markets. The trading volume of the EONIA overnight interest rate remained at the same level as at the end of 2010, about EUR 40 billion. Money market risk premia also remained at the same level as at the beginning of 2010.

In general, the aim of the operational framework for monetary policy is to stabilise the shortest money market interest rates to a level close to the policy rate. As the volume of excess liquidity increases, banks are more likely to make overnight deposits with the central bank and, correspondingly, recourse to the marginal lending facility declines. Hence, the shortest money market interest rates fall towards the interest rate on the deposit facility, as it is not financially reasonable for banks with surplus liquidity to pay higher interest rates in the interbank market than does the central bank. Once the volume of excess liquidity has become considerable, the shortest money market interest rates no longer respond to changes in the volume of excess liquidity. Following the expiry of 12-month operations in 2010, volatility in

Chart 7.
Developments in policy rates and interbank money market interest rates



Source: Bloomberg.

the EONIA increased appreciably. The structural liquidity deficit of the banking system could no longer be fulfilled via longer-term refinancing operations (LTROs), and it was necessary for banks to also borrow in the main refinancing operations (MROs).

In the first half of 2011, the EONIA continued to fluctuate. It was on average higher than in 2010, reflecting the reduced amount of excess liquidity. In addition, volatility within each maintenance period was driven by banks' front-loaded fulfilment of reserve requirements, which reduced the volume of excess liquidity at the beginning of each maintenance period, thereby contributing to an upward movement of the EONIA. The amount of excess liquidity was at its lowest level in the May maintenance period. Money market interest rates rose from March to June (Chart 7).

Deepening sovereign debt crisis increased money market disruptions

The situation in the money market deteriorated again in July–August, when the sovereign debt crisis caused uncertainty and the economic outlook changed worldwide. In the course of the autumn, estimates pointed to a slowdown in European economic growth and risks of faster-than-expected inflation waned. Attention was also focused on US public finances: the credit rating agency Standard & Poor's, for example, downgraded the US credit rating to AA+. The worsening of the situation was reflected in euro area government bonds in particular as higher Spanish and Italian government bond yields. Uncertainty about the timing and form of additional Greek financing heightened, especially after Greece's announcement at the end of October of its intention to call a referendum on new adjustment measures. In November, bond yields of AAA-rated governments, such as France, the Netherlands and Finland, also increased. Credit ratings of many euro area countries were lowered, and in December Standard & Poor's evaluated that the ratings of 15 euro area governments had weakened against the backdrop of systemic risks.

These tensions were reflected in the money market as a rise in risk premia to their highest levels observed since the Lehman Brothers collapse at the end of 2008. Expectations of lower interest rates, priced in by the markets, pushed down secured money market interest rates more than unsecured rates, which increased a rise in risk premia. Interest rates secured by the highest-rated German government bonds (repo rate), fell significantly, even dropped below the interest rate on the Eurosystem's overnight deposit facility. In order to reduce uncertainty over liquidity, the Governing Council of the ECB decided on carrying out new refinancing operations with very long maturities: about EUR 50 billion worth of six-month liquidity was provided to banks in August and about EUR 57 billion worth of 12-month liquidity in October. Recourse to the marginal lending facility also increased from September onwards, with a daily average of more than EUR 4 billion in the

November maintenance period, despite an abundance of excess liquidity in the banking system. Overnight deposits in the November maintenance period already averaged some EUR 250 billion.

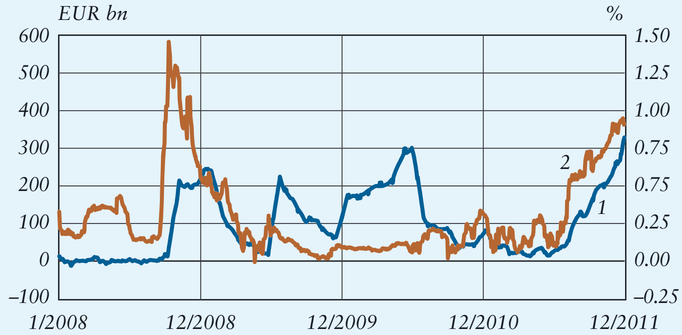
ECB conducted an historically large market operation

In December, the functioning of euro area financial markets was considerably impaired. The Governing Council of the ECB decided on longer-term refinancing operations (LTROs), to be conducted in December and February, with particularly long, ie three-year (about 36-month) maturities, aimed at ensuring the transmission of monetary policy and easing banks' longer-term funding. The interest rate used in the LTROs is fixed at the average interest rate of the main refinancing operations (MROs) over the life of the respective operation. Exceptionally, banks were granted the option of early repayment in part or in full one year after the inception of the operation in question. Moreover, banks that had obtained liquidity in the 12-month LTRO in October were allowed to move their outstanding amounts to the December 36-month LTRO, effectively switching these amounts to this new operation.

In order to facilitate the functioning of the money market, the Governing Council of the ECB also lowered the reserve ratio used to calculate banks' reserve requirements by one percentage point to 1%, which reduces the structural liquidity deficit of the banking system and thereby the banking system's collateral needs. Owing to the full-allotment policy and the large volume of outstanding refinancing, the minimum reserve system is not needed to the same extent as before to stabilise the shortest market interest rates. For the same reason, fine-tuning operations conducted on the last day of the maintenance period were also discontinued.

The 36-month LTRO conducted in December was, in value terms, the largest market operation ever carried out in the euro area: 523 banks participated for a total amount of EUR 489 billion. This included EUR 46 billion moved from the 12-month LTRO allotted earlier. The volume of excess liquidity rose after the operation, reaching a record high of almost EUR 480 billion. This was about EUR 130 billion more than just before the expiry in June 2010 of the first 12-month LTRO (Chart 8). Correspondingly, in the

Chart 8.
Excess liquidity in the euro area banking system, spread between unsecured and secured interest rates



1. Excess liquidity in the euro area banking system (left-hand scale)*
2. 1-month Euribor – 1-month EUREPO (right-hand scale)

* Current account holdings with central banks – minimum reserve requirements + overnight deposits – marginal lending facilities. 30-day moving average.

Source: Bank of Finland.

latter half of December, overnight deposits were made for an average amount of EUR 330 billion. At the end of the year, banks' borrowing from Eurosystem monetary policy operations amounted to about EUR 850 billion, with considerably longer maturities than at the beginning of the year.

Even so, the shortest money market interest rates did not decrease as close to the interest rate on the deposit facility as in the first half of 2010, the last time when equally large amounts of excess liquidity had prevailed. On the contrary, the EONIA remained about 0.20 percentage points higher than the interest rate on the deposit facility, as more credit risk premia had been priced into interbank deposits. Partly for the same reason, unsecured EURIBOR rates declined only moderately at the end of the year. The approaching turn of the year also dampened the fall in interest rates, as banks' activity usually slows towards the end of the financial year.

Debt crisis reflected in Eurosystem's collateral framework

The Eurosystem provides central bank refinancing to credit institutions only against submission of adequate collateral. Debt instruments fulfilling certain eligibility criteria are accepted as collateral. A list of eligible marketable assets is published on the ECB's website. In order to determine the collateral value of underlying assets, they are priced daily and are subject to valuation haircuts according to Eurosystem definitions. Moreover, the total value of collateral submitted by the borrower of central bank funds may include only a limited amount of uncovered bonds issued by groups of credit institutions.

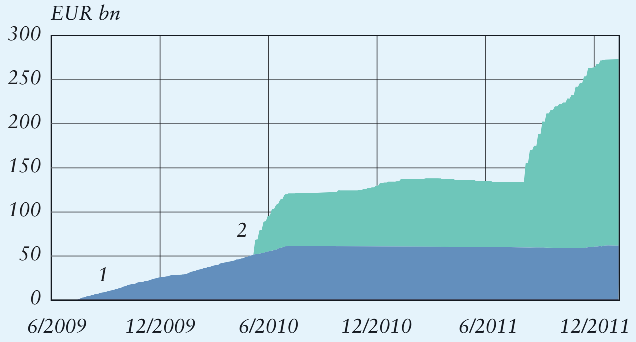
Euro area sovereign debt problems and financial market disruptions had an impact on the Eurosystem's eligibility criteria in 2011. In March, the ECB announced collateral eligibility in Eurosystem credit operations for bonds issued or guaranteed by the Irish government, despite their credit rating falling below the normal minimum credit rating threshold, the BBB level. A similar announcement was published in July for the collateral eligibility of Portuguese government bonds. The decisions were based on these governments' commitments to their relevant EU/IMF support programmes. A corresponding lowering in the credit rating threshold for Greek government bonds had already taken place in 2010. At the end of 2011, some credit rating agencies still kept Irish and Portuguese ratings at the level of BBB. All rating agencies used by the Eurosystem had downgraded the Greek rating below the BBB level by early 2011.

Updated haircuts were introduced in the Eurosystem's risk control measures. Furthermore, the requirement to have a rating from at least two eligible rating agencies, earlier imposed on asset-backed securities (ABSs), was extended to be valid for all assets of this class, irrespective of the time of issuance. In September, the ECB announced collateral eligibility, from the beginning of 2012, for bonds issued by credit institutions that are traded on non-regulated markets accepted by the

ECB (and fulfil other eligibility criteria). Previously, only listed bonds had been accepted as collateral. Moreover, the 10% limit for the collateral use of uncovered bonds issued by groups of credit institutions was reduced to 5% of the total value of collateral submitted by the borrower of central bank funds.

In the latter half of 2011, the ECB announced Eurosystem measures to support bank lending and money market activity. These measures also included an increase in collateral availability. Collateral assets were increased by reducing the rating threshold for certain types of ABSs to a single A rating and by allowing national central banks to accept as collateral, as a temporary solution, credit claims that satisfy specific eligibility criteria.

Chart 9.
Changes in Eurosystem securities purchase programmes



1. Covered Bond Purchase Programme (CBPP1 and CBPP2)
2. Securities Market Programme (SMP)

Source: European Central Bank.

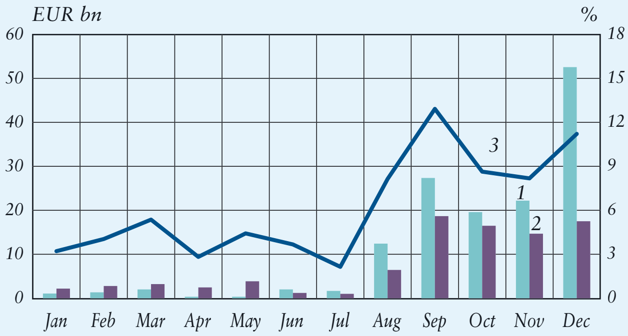
Securities Markets Programme reactivated in August

The Eurosystem launched the Securities Markets Programme (SMP) in May 2010, as the monetary policy transmission mechanism had been disrupted in certain market segments as a consequence of the financial crisis. The programme is a non-standard monetary policy measure, which will be continued for as long as the purchases are deemed necessary. The programme allows purchases of both private and public debt securities in the secondary market, and the liquidity effect of the purchases is sterilised via weekly collections of fixed-term deposits. Accordingly, the purchases have no impact on the stance of monetary policy. At the Bank of Finland, the Investments division of the Banking Operations department is responsible for carrying out Eurosystem monetary policy purchase programmes. The purchases are executed with counterparties to Eurosystem monetary policy and investment operations.

The SMP was not used in practice in the first half of 2011, at the end of which the size of the programme was almost the same as at the beginning of 2011, ie EUR 74 billion. As the situation in the financial markets deteriorated in July–August and monetary policy transmission was markedly hampered, the programme was reactivated in an effort to stabilise euro area sovereign debt markets. On 7 August, the President of the ECB announced the Eurosystem's active implementation of the programme for purchases, and by 2 September the size of the programme had increased in net terms by EUR 55 billion, to EUR 129 billion. Subsequently purchased net amounts declined slightly, to EUR 32 billion in September and to about EUR 20 billion in both October and November. At the end of the year, the value of debt securities purchased under the programme amounted to EUR 211.5 billion (Chart 9).

Banks play an important role in financial intermediation in Europe, and covered bonds are a key source of longer-term funding for banks. In October, the Governing Council of the ECB decided to launch a second Covered Bond Purchase Programme, in which the Eurosystem buys euro-denominated covered bonds issued in euro area primary and secondary markets. The first programme of this type had ended in June 2010, with the completion of the targeted amount of purchases of EUR 60 billion. Purchases of EUR 40 billion under the new programme were commenced in November and are scheduled to be completed by October 2012. By the end of 2011, about EUR 3 billion worth of covered bonds had been purchased under the programme. The programme improved bank funding conditions by reducing risk premia on covered bonds and increasing primary market issuance especially at the early stage of the programme. The Bank of Finland participates in the programmes with a share corresponding to its capital key, and purchased bonds are included in the Bank's balance sheet.

Chart 10.
Finnish counterparties' contribution to Eurosystem monetary policy deposits, 2011



1. Overnight deposits with the Bank of Finland
2. Fixed-term deposits with the Bank of Finland
3. Share of Eurosystem deposits (right-hand scale)*

* Includes both overnight and fixed-term deposits.
Sources: European Central Bank and Bank of Finland.

Eurosystem also safeguarded banks' access to dollar funding

The ECB's swap line with the US Federal Reserve enabled the provision of US dollar funding to euro area banks throughout the year against delivery of collateral eligible for the Eurosystem. It was decided in June to extend the validity of the liquidity swap arrangement between the ECB and the US Federal Reserve until August 2012 and in the latter half of the year still until February 2013. US dollar financing at terms of 7 days was offered throughout the year in compliance with the full-allotment policy, but banks did not take up this option until September. In September, the Governing Council of the ECB exceptionally decided on the conduct of three US dollar liquidity-providing operations with a maturity of three months.

At the end of November, it was further decided, in cooperation with the US, Japanese, UK, Swiss and Canadian central banks, to authorise the use of reciprocal swap lines until 1 February 2013. This enabled euro area banks' access, whenever necessary, to liquidity in foreign currencies other than the US dollar. It was also agreed to lower the pricing on the US dollar liquidity swap arrangement by 0.5 percentage point to 0.5%, plus the US dollar Overnight Index Swap (OIS) rate. At the same time, the Governing Council of the ECB decided to reduce the initial margin for collateral in US dollar operations and to introduce weekly updates of the EUR/US exchange rate to carry out margin calls. In December, banks obtained more than USD 50 billion in three-month liquidity at the new lower interest rate. In the year's last two-week operation extending over the turn of the year, 34 euro area banks participated for an amount of USD 33 billion. Total outstanding US dollar liquidity at year-end was about USD 85 billion.

Banks operating in Finland increased their deposits related to monetary policy operations and overnight deposits

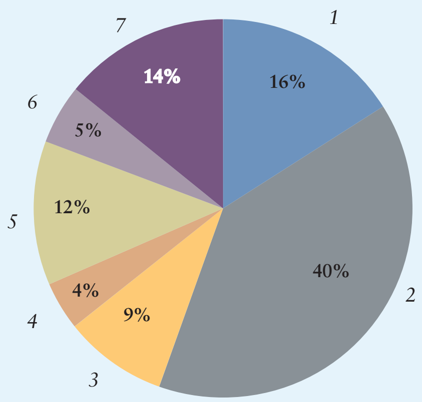
Banks operating in Finland placed an abundance of fixed-term deposits related to monetary policy operations and overnight deposits under the Eurosystem's deposit facility, which is one indication of banks' good liquidity. In 2011, the ECB carried out 80 refinancing operations, but banks operating in Finland participated only in 10 operations for obtaining liquidity. In December, liquidity provided to Bank of Finland counterparties in the main refinancing operations (MROs) amounted to EUR 0.01 billion and in the longer-term refinancing operations (LTROs) to about EUR 2.3 billion. In total, this accounted for only 0.3% of all outstanding Eurosystem credit operations. It was possible to make fixed-term deposits in liquidity-absorbing operations under the Securities Markets Programme and in operations conducted on the last day of the maintenance period, of which there were a total of 64 operations. From 16 Bank of Finland counterparties, 4 on average participated in these operations.

The volume of fixed-term deposits placed by banks operating in Finland increased considerably in the second half of the year, ie from EUR 1.2 billion in June to EUR 17.5 billion at the end of December (Chart 10). The relative share of these deposits of all Eurosystem deposits also grew. When 2–5% of the deposits were made in Finland in the first half of the year, the share rose to 12% in September, to stand at 8% at the end of December, ie manifold compared with the Bank of Finland's capital key. In addition to fixed-term deposits, the volume of overnight deposits increased in Finland in the latter half of the year, from EUR 2 billion at the end of June to about EUR 52.5 billion in December, which was 13% of all overnight deposits and 4 percentage points more than at the beginning of the year. The increase in the volume of deposits related to monetary policy operations and overnight deposits almost exclusively explained the Bank of Finland's balance sheet growth from EUR 32 billion in June to almost EUR 98 billion in December.

Bank of Finland counterparties face no shortage of collateral

Bank of Finland counterparties need adequate collateral both for covering

Chart 11.
Use of collateral by Bank of Finland counterparties, by asset type (averages in 2011)



1. Central and general government securities
2. Covered bank bonds
3. Uncovered bank bonds
4. Corporate and other similar bonds
5. Asset-backed securities
6. Credit claims
7. Fixed-term deposits

Source: Bank of Finland.

credit obtained in monetary policy operations and for handling payment transactions. As banks' participation in Eurosystem refinancing operations in 2011 was very modest, the bulk of their collateral needs stemmed from intra-day credit within the TARGET2 system. In addition, the surplus of collateral put forward by counterparties with the central bank was sizeable. On average, the total amount of collateral remained broadly unchanged at about EUR 23 billion compared with the previous year. Of this amount, about half were surplus collateral reserves.

Viewed by type of collateral, counterparties mostly used covered bank bonds throughout the year, which accounted for 40%, on average, of total collateral assets (Chart 11). Debt securities issued by central government and public sector entities constituted the second largest component (16%). This was followed by asset-backed securities (ABSs) and fixed-term deposits placed via liquidity-absorbing fine-tuning operations, which both accounted for more than 10%, on average, of the total collateral volume. Of these, the former type of collateral contracted markedly during the year, whereas the latter increased. Collateral use of credit claims as well as that of corporate bonds and other marketable assets was modest, as was that of uncovered bank bonds, in respect of which collateral use is restricted by issuer-specific limits.

As in previous years, Bank of Finland counterparties preferred cross-border collateral as more than three quarters of all, and almost 95% of marketable collateral assets had been delivered for collateral purposes using the correspondent central banking model (CCBM). Under this arrangement, Eurosystem central banks act as custodians for one another in order to enable transfers of securities issued abroad. Of domestic securities, banks only submitted government debt securities as collateral.

Similarly, the Bank of Finland held collateral assets via the CCBM for the account of other central banks to an average value of just under EUR 600 million in 2011.

The Bank of Finland and economic policy in Finland

Finland's total output increased in 2011, as the economy continued to improve from the recession of 2008 and 2009. However, growth remained weaker than in 2010, and in the course of 2011 the outlook became more uncertain. As a result, the Bank of Finland revised its forecast for economic growth for 2011 and 2012 downwards in December 2011 compared with the earlier forecasts.

After a favourable period that continued until early 2011, weaker developments in the global economy and international trade, economic difficulties in Europe and problems in the electrical and electronics industry began to hamper Finnish exports. Until then, Finnish exports had not reached the levels observed prior to the recession of 2008 and 2009, since the demand for capital goods in developed economies – an important source of demand for Finnish exports – had not shown marked recovery. As a result of subdued exports, the share of industry in total output remained significantly smaller in 2011 than in the pre-recession years.

Domestic investment and consumption demand developed more favourably than exports in 2011. Non-residential fixed investment recorded growth in both non-residential construction investment and investment in machinery and equipment, compared to a reduction in the previous year. Low interest rates and improved employment levels supported household demand. Private consumption continued to grow steadily. Residential investment grew too, although growth moderated from the exceptionally brisk pace recorded in 2010.

Weaker export developments and the protracted fall in export prices relative to import prices led to the erosion of Finland's current account surplus. The current account was in deficit in 2011, after having been in surplus since the mid-1990s.

In the latter part of 2011 the outlook for exports and investment deteriorated in particular, amid increasing uncertainties related to international economic developments and the stability of the European financial system. The outlook for private consumption remained more solid according to the Bank of Finland December 2011 forecast.

Unemployment clearly fell in 2011. The employment situation had begun to improve already in the previous year, after having deteriorated markedly during the recession in 2009. Nevertheless, the unemployment rate remained clearly above the pre-recession levels. Industrial employment, which had declined most strongly during the recession, scarcely picked up at all in 2010 and 2011. In 2011 employment increased most in services, especially in educational, social and health care services.

As the economic outlook deteriorated, a renewed risk of rising unemployment emerged. The Bank of Finland emphasised that this would have long-lasting effects, with the skills of the unemployed deteriorating and more people becoming excluded from working life. The increase in youth unemployment and the number of long-term unemployed would pose particularly worrying problems. The Bank of Finland assessed that such a scenario could be countered by both ensuring there is a financial incentive to work and providing public measures that help support the maintenance of working capacity.

Many enterprises in industry in particular had not fully recovered from the recession of 2008 and 2009, and the deterioration of the economic outlook in the latter half of 2011 posed a threat to their operating conditions. The structural changes in the Finnish economy relating to changes in global demand and production structures seemed to continue at a rapid pace. The Bank of Finland stressed that the actualisation of structural changes with as little damage as possible would require adaptability in the economy. In the process of adapting, there would be an important role for an efficient financial system, and also for flexibility in wage formation at enterprise and industry levels.

Inflation picked up in Finland in 2011. Measured by the Harmonised Index of Consumer Prices (HICP), prices rose by 3.3% from the previous year. The rise in consumer prices was particularly fuelled by higher energy and other commodity prices in global markets and changes in indirect taxes. Reviewed by annual averages of changes in the HICP, inflation had remained higher in Finland than in the euro area on average already for four consecutive years.

Finland's central government deficit remained substantial in 2011, and general government on the whole continued to post a deficit. However, deficits contracted from the previous year owing to the economic recovery and tighter fiscal policy. In the second half of 2011, weaker economic outlook and sovereign debt problems placed the outlook for public finances in a new light again, also in Finland.

The Bank of Finland emphasised the need for measures to substantially improve the sustainability of public finances so as to bring the outlook for Finland's public finances onto a sustainable footing despite an ageing population. This would be possible particularly through action to prolong working careers and reforms to boost labour productivity in basic public services. The Bank of Finland stressed that these measures needed to be implemented in time. Otherwise there was a risk of a situation where the general government deficit should be reduced rapidly at a time when economic developments were already weakening.

In 2011 the Bank of Finland published three forecasts for Finnish macroeconomic developments: the first in March, the second in June and the third in December. The Bank of Finland participated in a variety of ways in analysis and economic policy discussions relating to global and domestic economic development. On several occasions the Governor and experts of the Bank of Finland were consulted by the Parliament and other domestic institutions.

Box 3.

Housing prices and household indebtedness in the Nordic countries

Compared with the preceding years, there was an exceptional increase in housing prices in the Nordic countries during the ten years prior to the financial crisis. At the same time, household indebtedness rose markedly. Housing price increases were largely attributable to favourable economic developments, low real interest rates, possibilities of raising even larges loans on more flexible terms as well as the growth in household incomes. These developments have resulted in an increase in household debt and the related risks. There are, however, important country-specific differences, and in Finland housing prices and household indebtedness have developed more moderately than on average in the other Nordic countries.

Over the past three decades, housing prices have risen in almost all developed countries in real terms (ie in relation to average growth in consumer prices). In 1978–2008 housing prices grew annually by an average of 1.7% in Denmark, 2.1% in Finland, 2.5% in Norway and 1.2% in Sweden. The corresponding figures for the United States and United Kingdom were 1.1% and 4.1% respectively. Long-term growth in housing prices is largely attributable to lower real interest rates, stabilisation of macroeconomic developments, urbanisation, population growth and higher income. On average, housing prices have risen the most in areas where population density is high and land suitable for construction is scarce.

In the decade preceding the financial crisis, growth in housing prices picked up in the Nordic countries, as in a number of other countries. In 1997–2007 real housing prices rose the most in Sweden (113%), Norway (105%) and Denmark (86%) and the least of all in Finland (58%). Compared with previous years, the rise was exceptionally sharp in all countries.

A common feature in housing price developments in Sweden, Norway and Finland is that the impact of the financial crisis on housing prices has, at least so far, remained small. Housing prices picked up sharply after a short period marked by a slight fall. On the other hand, housing prices in Denmark have already fallen by 24% from their record levels.

The relatively strong growth in housing prices in Finland, Sweden and Norway over the past years is at least partly explained by low interest rates and the fact that the employment situation has not weakened markedly. Households' purchasing power has remained good, and housing price increases have not been linked to excessive construction. Particularly in Sweden, but to some extent also in Finland, housing supply has not been able to meet the growth in demand even though housing construction in Finland was exceptionally buoyant during the economic upturn.

The sharp rise in housing prices has been reflected in increased household indebtedness. Prior to the financial crisis, the trend growth of indebtedness followed very similar patterns in all Nordic countries, even though each country's starting point differed. In Denmark household indebtedness is very high by international standards, whereas in Finland it has been lower than in the other Nordic countries and close to the euro area average.

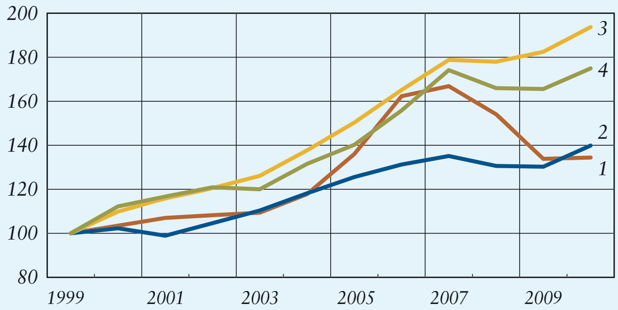
In addition to lower real interest rates, changes in housing finance have also been among the key factors behind the rapid growth of household indebtedness. Housing loan maturities have lengthened and at the same time loan amounts have increased relative to income and collateral in all Nordic countries. In Finland, however, housing loans are generally smaller and have shorter maturities than loans in Sweden and Denmark. In Finland, a housing loan typically has a maturity of 20–25 years, compared to 30 years in Denmark and 30–50 years in Sweden. Very high loans with long maturities of up to 60 years have also been taken out in Finland, but their popularity has remained low. The Financial Supervisory Authority has recommended that the maximum maturity of a loan should not exceed 25 years.

Loans with no payment of the principal (interest only home loans) have become a very popular housing loan type in the Nordic countries. According to the European Commission and the Norwegian and Swedish supervisory authorities, such loans account for over half of the loans in Denmark, about 1/6 in Norway and 1/5 in Sweden; in large towns as much as 1/3. This type of loan increases households' financial risks which may materialise particularly in the case of falling housing prices and increasing unemployment. Interest only home loans have not, at least yet, become popular in Finland.

Even though the current estimation is that at least the majority of Nordic households appear to be able to service their debt without material problems, household risks have increased considerably along with indebtedness. Higher loan burdens have made households' financial situation more vulnerable, and at the same time this has signified increased vulnerability to disruptions at the level of the economy as a whole. Developments in housing prices and household indebtedness appear to be more worrying in other Nordic countries than in Finland. Nevertheless, it is clear that households' risks have increased even in Finland.

Chart A.
Real housing prices

Index, 1999/I = 100

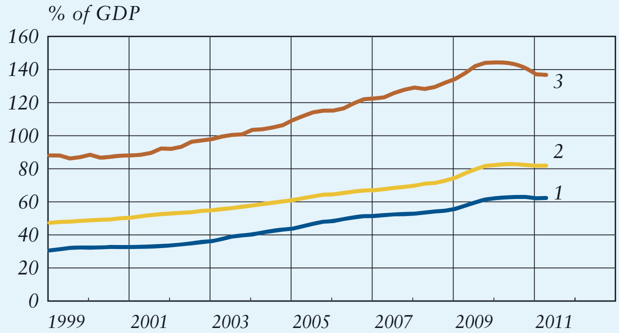


1. Denmark
2. Finland
3. Sweden
4. Norway

Deflated nominal housing prices.
Sources: National statistical authorities and Bank of Finland.

Chart B.
Household debt relative to GDP

% of GDP



1. Finland
2. Sweden
3. Denmark

Source: Eurostat.

Financial system

Financial stability

The sovereign debt crisis escalated, and banks' funding became difficult – Europe on the verge of a systemic crisis

As the sovereign debt crisis escalated and spread to the large euro area countries, the negative features of the shared destiny of banks and governments became increasingly evident. The sovereign debt crisis primarily affected banks in countries suffering from the crisis and those with major investments in bonds issued by governments suffering from the sovereign debt crisis. Market confidence in these banks eroded as the sovereign risk increased thus hampering their funding.

In early 2011, particularly banks in crisis economies faced difficulties in obtaining long-term funding at reasonable interest rates. Many euro area banks had to rely on refinancing acquired via the ECB's monetary policy operations. In late 2011, growing uncertainty amidst the debt crisis resulted in a significant decrease in the markets' risk appetite, and investors took a sceptical attitude towards almost the entire banking industry. European banks' funding difficulties became more extensive: long-term unsecured funding from the financial markets was near a standstill in late summer 2011, and the drying up of interbank lending was broad-based.

In order to restore confidence, it became increasingly necessary to bolster banks' capital positions. Strengthening the capital adequacy of a weak bank via private funding is however challenging in the current market situation. At the same time, many European governments suffering from the debt crisis have only limited possibilities of supporting the distressed banks via capital injections or guarantees. In the early stage of the financial crisis, governments used large amounts of funds to support the financial system. This weakened the fiscal position of the governments. At the same time, government finances were burdened by fiscal stimulus measures and lower tax receipts as a result of the sluggish economy.

The vicious cycle of the debt crisis and the ensuing drying up of funding resulted in severe disruptions in the financial markets.

The Finnish financial system remained stable

Twice a year, the Bank of Finland publishes its evaluation regarding the stability of the domestic and international financial systems. This evaluation is targeted at all parties active in the financial sector, other authorities and general public, not only to inform them but to facilitate discussion about risks to financial stability. According to the Bank of Finland's stability assessments published in May and December 2011, the most significant threats to the stability of the Finnish financial system still derive from outside our country's borders. Finnish banks' funding deficit, ie the difference between loans to the non-financial sector and deposits by the sector, is large compared to the other European countries. Banks cover this funding gap mainly via foreign market funding. In a crisis, investors typically withdraw from peripheral countries, such as Finland, and thus international market disturbances could suddenly weaken the availability of funding in Finland.

Considering the severity of the debt crisis, Finland's financial system has operated well. Finnish banks do not seem to have tightened the provision of credit to Finnish non-financial corporations, and in contrast to some other euro area countries, there have been no indications of a credit crunch in Finland. The stability of the financial system is mainly due to the fact Finnish banks' capital adequacy has remained very strong. The banking sector's ratio of common equity (Core Tier 1) and risk-weighted assets was 12.8% at the end of September 2011. This is well above the current minimum requirement and the temporary minimum ratio of 9% that the European Banking Authority (EBA) requires major European banks to reach by the end of June 2012. The results of the stress tests conducted by the Financial Supervisory Authority in spring 2011 show that the Finnish banking sector's capital adequacy would withstand a scenario of negative GDP in 2011–2012 and a decline in asset prices accompanied by a fall in short-term interest rates to very low levels.

The strong capital positions have facilitated funding for Finnish banks. Finnish banks covered the majority of their funding needs for 2011 already prior to the escalation of the debt crisis. Banks have prepared for the increase in uncertainty by bolstering their liquidity buffers and lengthening the average funding maturities. Finnish banks have also increasingly resorted to covered bonds in their long-term market funding. The heightened financial market tensions in autumn 2011 however also hampered the funding of Finnish banks on international financial markets.

Finnish banks have prepared for possible financial market disruptions by reducing their indebtedness, extending the maturity of their loan programmes, and reinforcing their cash reserves. The aggregate debt of Finnish non-financial corporations relative to GDP was already before the crisis smaller than in several other European countries. On the other hand, the household sector's indebtedness continues to increase, which weakens the ability of households and the economy to adjust to economic disturbances. The exceptionally low levels of interest rates and moderate employment developments have sustained particularly the demand for housing loans. In the May 2011 evaluation, the Bank of Finland expressed its concerns about the level of household debt and recommended that household measure the size of their loans with their repayment capacity, and that banks would not grant households loans that are too large relative to their collateral and debt servicing ability.

European banks were required to bolster their balance sheets to restore the stability of the financial system

In early 2011, the new European Banking Authority (EBA) was mandated to coordinate EU-wide stress tests to assess the resilience of 90 European banks. The main purpose of the stress tests was to increase the transparency of the evaluation of banks' financial position and to provide authorities information on banks' recapitalisation needs. Eight banks fell below the capital threshold. The Bank of Finland and the Financial Supervisory Authority participated in preparations for the stress tests on the Finnish banking sector.

As the crisis escalated, it became necessary to raise European banks' capital ratios above the level defined in the stress tests in order to safeguard banks' access to lending and lending capacity. Due to major uncertainties concerning banks' real exposures, market participants' capital requirement for banks was significantly tighter than the statutory requirement. The EU summit in October 2011 agreed that large European banks have to raise their common equity Core Tier 1 capital ratio to at least 9% by the end of June 2012. Calculations that the European Banking Authority and national supervisors required banks to submit show that 31 large European banks have to bolster their capital position to reach the target. The banks' aggregate capital deficit was – including the EUR 30 billion support granted to the Greek banking sector by the IMF and EU – approximately EUR 115 billion.

In strengthening their lending capacity, it is essential that banks tap primarily private sources for new capital, build up their capital base by retaining earnings or reducing profit distribution. In the May 2011 evaluation, the Bank of Finland thus recommended eg that banks in the EU should reinforce their balance sheets to enable them to support a recovery in economic growth. Based on the outcome of the stress tests, the authorities thus recommended decisive action to improve the capital positions of weak but viable banks primarily via private sector sources.

Reform of financial market regulation continued in 2011

While the acute crisis demanded increasing attention, work continued on the development of long-term financial regulation and supervision. The purpose of the reform is to ensure that new financial crises emerge as rarely as possible and to minimise the impact of possible crises on the operations of the financial markets and the real economy. Of the reform projects, the most significant are the Basel III reform, the tighter regulatory and supervisory framework for systematically important financial institutions (SIFIs) and the EU-level crisis management framework (EU regulatory initiatives and their implementation in Finland, see Appendix Key measures affecting the financial markets in 2011).

The implementation of the Basel III reform into EU legislation made rapid progress over the course of the year. In July 2011 the European Commission published a proposal for a capital requirements directive and regulation (CRD VI) for banks. The Commission's proposal deviates from the Basel III regime in some respect. The Basel Committee's recommendations define international minimum requirements for banks capital adequacy, liquidity and leverage. In contrast, according to the Commission's proposal, the EU member states could not deviate downwards or upwards in most of the requirements. Discussions on the new capital requirements directive and regulation should be finalised in 2012. The Bank of Finland took part in the development of financial regulation within the EU via participation in ECOFIN and the European System of Central Banks as well as in preparations supporting national implementation, in cooperation with the Ministry of Finance and the Financial Supervisory Authority.

As part of the global reform of financial regulation, authorities will impose on systemically important banks tighter capital requirements than on others. A list of globally systemically important banks (G-SIBs) was published in autumn 2011. In addition to the tighter capital requirements, authorities' responsibilities, powers and cooperation arrangements were defined as to facilitate the reorganisation of a bank's business in a crisis situation without costs for taxpayers. Moreover, the supervision of these banks will be intensified. Some countries, for example the United Kingdom, Switzerland and Sweden, have announced plans to impose on systemically important banks even tighter capital requirements as these countries have a highly concentrated and large banking sector relative to the size of their economies.

Insolvency regulation on conventional non-financial corporations is not highly effective in the insolvency of a financial institution. The legislation on the resolution of financial institutions will therefore be reformed and harmonised. The European Commission prepared in 2011 its proposal for a directive on a crisis management framework for banks. In spring, the Commission launched a public consultation on the proposed reform. Also the Bank of Finland issued an opinion on the proposal, and the Commission is expected to issue a proposal for a directive in spring 2012. The proposal for an EU framework for crisis management includes new ideas particularly on preventive measures by authorities and early intervention. In the May 2011 evaluation, the Bank of Finland noted that Finnish authorities should also be equipped with strong enough powers to intervene at a sufficiently early stage in the activities of financial institutions that are experiencing difficulties and, where necessary, restructure or terminate their operations. Under the Commission's proposal, the crisis management measures will be financed via national stability funds. The funds would be financed by charging financial institutions a stability fee, which is a type of bank tax.

Financial market infrastructure

The financial market infrastructure comprises payment systems and securities trading, clearing and settlement systems. Their reliable and efficient functioning is crucial for both the financial markets and the economy overall, as possible disruptions or problems in this fundamental infrastructure of the economy may, in the worst case, paralyse the entire economy.

In the conduct of its statutory oversight activities, the Bank of Finland seeks to ensure the smooth functioning of the financial market infrastructure. The Bank of Finland's oversight duties involve the monitoring and assessment of the operation of the systems and risks and, when necessary, inducing change. Cooperation with domestic and international authorities and market participants is part of this work.

During the financial crisis, the financial market infrastructure has functioned reliably, supporting the smooth operation of the financial markets. The TARGET2 system, which is maintained by the EU central banks has on the whole, functioned reliably. In retail payments, migration to the Single Euro Payments Area (SEPA) is a major project in which Finland is a forerunner. In the year under review, SEPA credit transfer replaced the domestic credit transfer. Migration to SEPA credit transfers meant a change from the domestic interbank payment system to STEP2, a pan-European system managed by EBA CLEARING. Due to various reasons stemming from the change, there were relatively many payment delays in 2011. The Bank of Finland has required banks to take measures to ensure the smooth processing of payments and under the auspices of the Federation of Finnish Financial Services, work to remedy the situation has been started.

The service providers of the Finnish securities markets – the stock exchange, central counterparty and central securities depository – have operated reliably. Changes in market structure and the harmonisation of regulation and supervision are deepening the integration of European securities markets. TARGET2-Securities (T2S) is the Eurosystem's securities settlement platform with a centralised structure. T2S is currently in the development phase, and it is due to go live in 2015. In 2011, the Bank of Finland continued to actively participate in the TARGET2-Securities initiative: in its catalyst role, the Bank has coordinated national preparations and policy views, introduced the views of the Finnish markets on the European level, and kept Finnish stakeholders informed about the progress of the T2S project.

A major domestic regulatory initiative is the overall reform of securities markets legislation, on which a working group submitted a report in February 2011. The Bank of Finland participated in the workgroup and its sub-working groups. The objective was to eg improve the clarity and intelligibility of securities markets legislation and to harmonise it with EU regulation. The overall reform is important for the functioning and competitiveness of the Finnish securities markets, and the related legislative proposals are scheduled for introduction to the parliament in 2012.

In its role as a catalyst for the development of financial market infrastructure, the Bank of Finland organised in May 2011, for the fifth time, a payment forum addressing the future of payments. This time, the forum discussed

Box 4.

Macroprudential supervision

The outbreak and development of the global financial crisis showed that systemic risks threatening the functioning of the financial system as a whole had not been sufficiently considered in supervision and regulation. When realised, systemic risk disrupts the normal functioning of the financial system and causes losses in the real economy, even if single elements of the system (banks, insurance companies etc.) are sound.

Authorities responsible for macroprudential supervision should identify systemic risks well in advance and, in the case of a threat of those risks realising, decide on measures to mitigate the probability of risk realisation and restrain the impact of the risks on both the financial system and real economy. Successful macroprudential policy reduces the probability of financial crises and smoothens the changes in credit provisioning (so-called credit cycles), and thereby promotes long-term economic growth.

Traditional institution-level supervision – so-called microprudential supervision – differs from macroprudential supervision in that it focuses on the risks to single agents operating in the financial system. Close cooperation between these supervisory segments is warranted to ensure information exchange and the compatibility of measures taken. The connection between macroprudential supervision and monetary policy aiming at price stability should also be considered. Monetary policy alone is insufficient to ensure financial stability. Macroprudential supervision can facilitate promotion of successful monetary policy.

There are new policy tools being developed for the use of authorities responsible for macroprudential supervision. Measures to restrain procyclicality of the financial system include the obligation for financial institutions to increase their capital buffers in times of prosperity and reduce them when the situation is more strained. This sustains financial institutions' lending capacity in cyclical downturns. Policy measures to address structural systemic risks (eg interinstitutional linkages and systemically important financial institutions, SIFIs) are taken in proportion to the respective level or significance of systemic risks of a specific institution or function.

Within the EU, the authority responsible for macroprudential oversight of the financial system is the European Systemic Risk Board (ESRB) which commenced operations at the beginning of 2011. The ESRB has been mandated to identify risks to the financial stability at the EU level, prevent and mitigate such risks and ensure the financial system's shock-absorbing capacity in the event of risk realisation. The ESRB may issue risk warnings and recommendations addressed to the EU as a whole, one member state or a group of member states, European Supervisory Authorities or national supervisory authorities. The Board issued its first public recommendation in October 2011. Those to whom this recommendation concerning risks to foreign currency lending is addressed must follow the recommendation, or provide adequate justification for non-compliance to the ESRB (the principle of comply or explain).

The ESRB's decision-making body, the General Board, convened four times in 2011. Matters discussed within the Board included commencement of the ESRB's activities, assessment of risks to the stability of the financial system and decisions on measures to ensure financial stability. The Advisory Technical Committee (ATC), which is part of the ESRB, monitors financial stability and identifies systemic risks as well as develops policy tools to be used in macroprudential supervision. The Advisory Scientific Committee (ASC) in turn provides advice and assistance in developing analysis methods and policy tools. The Secretariat of the ESRB, working in the ECB premises, is responsible for the day-to-day business of the ESRB, coordination of analysis work and maintenance of contacts with the European supervisory authorities and international stakeholders. The Steering Committee prepares the meetings of the General Board, advices the advisory committees and monitors the Secretariat's ongoing work.

As are the governors of other EU central banks, the Governor of the Bank of Finland is a Member with voting rights in the General Board. National supervisory authorities also participate in the General Board. The Bank of Finland and the Financial Supervisory Authority (FIN-FSA) are also represented on the Advisory Technical Committee. Participation in committee work has given the Bank of Finland's representatives the opportunity to influence for example the development of macroprudential tools and analysis of challenges facing the financial system.

Decision making in the ESRB is comparable to the monetary policy decision process. In Finland, the preparatory work is the task of the Bank of Finland's stability policy process. Experts from the Bank's Financial Stability and Statistics department as well as a number of other experts in the Bank and the FIN-FSA are involved. The preparatory process is an excellent example of close cooperation between the Bank of Finland and the FIN-FSA.

Implementation of the ESRB recommendations and national macroprudential policy is the responsibility of national authorities. A number of countries – including Finland – are yet to establish an authoritative or institutional body empowered to set requirements on financial institutions on the basis of financial stability arguments. However, national organisation of macroprudential supervision is enshrined in the Finnish government programme. The Bank of Finland considers the appointment of a working group important and will contribute to its work with its central bank competence.

the remaining challenges of electronic invoicing, as well as electronic authentication and mobile payments. The feedback received shows that the payment forum is perceived as having promoted the national payments strategy. In 2011, the Bank of Finland continued to develop analytical tools for payment and settlement systems. The TARGET2 Simulator, which is based on the Bank of Finland's BoF-PSS2 simulator, has been one of the key projects for developing quantitative oversight tools for the European System of Central Banks. The quantitative analysis of complex systems was also extensively discussed in the ninth international simulator seminar, which the Bank organised in August. The number of studies utilising the Bank of Finland's BoF-PSS2 simulator is expected to increase further in the near future as the new international oversight standards, which will be introduced in 2012, will require payment and settlement system operators to conduct stress and liquidity analyses.

Payment system services

TARGET2 (Trans-European Automated Real-time Gross Settlement Express Transfer system) is a payment system owned and operated by the Eurosystem for the processing of large payments in real time and on a gross basis. The TARGET2 system is also used for executing Eurosystem's monetary policy

The Bank's art exhibition tempted as many as 11 300 art enthusiasts to the head office in January and August 2011.

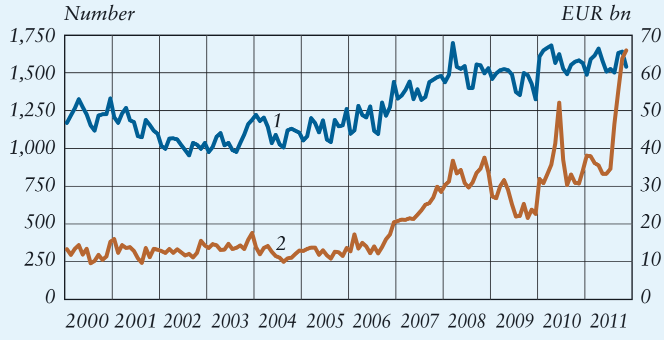
Photo: Peter Mickelsson.

operations, and all key payment and settlement systems use TARGET2 for settlement purposes.

In 2011 the TARGET2 system again functioned in line with the high availability requirements set for it. In the year as a whole, the TARGET2 system processed on average 348,505 payments per day, with an aggregate value of approximately EUR 2,385 billion. Of these, the TARGET2 component of the Bank of Finland, TARGET2-Suomen Pankki, executed on average 1,571 payments per day, with an aggregate value of about EUR 47.1 billion. The value and volume of payments processed in TARGET2 rose slightly at the level of the whole system. At the level of TARGET2-Suomen Pankki, the volume of payments decreased slightly but the value of payments increased considerably (Chart 12). In December 2011, TARGET2 had 987 direct participants connected to the system through 24 central banks' components. In the year under review, the Romanian Central Bank was the latest to join TARGET2 in July. At the end of 2011 the TARGET2-Suomen Pankki component had 23 participants, of which three were ancillary systems. In all, three new participants joined the TARGET2-Suomen Pankki in 2011.

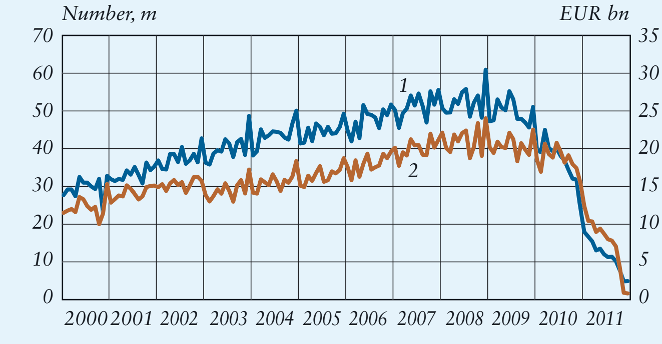
The interbank retail payment system (PMJ) transmitted wages and salaries, pension payments, credit transfers and card payments as batch transfers between 12 PMJ banks operating in Finland. The PMJ system functioned very smoothly throughout the year. Along with the introduction of SEPA credit transfers, the clearing of regular payments and credit transfers migrated at the end of the year to payment systems maintained by pan-European clearing houses. As a result, the volume of payment transfers processed in the PMJ system contracted substantially in 2011 (Chart 13).

Chart 12.
Daily average volume and turnover of TARGET payments processed for TARGET2-Suomen Pankki system participants



Source: European Central Bank.

Chart 13.
Volume and turnover of payments processed in the interbank payment system PMJ



Source: Bank of Finland.

Financial asset management

Table 1.
Bank of Finland's financial assets

	31 Dec 2011 EUR m	31 Dec 2010 EUR m
Foreign reserves	*4,428*	*4,135*
Gold	*1,918*	*1,664*
SDR	*555*	*439*
Euro-denominated financial assets	*11,682*	*11,296*
Total	***18,583***	***17,534***

Source: Bank of Finland.

Table 2.
Distribution of Bank of Finland's financial assets by currency*

Currency	*31 Dec 2011 %*	*31 Dec 2010 %*
US dollar (USD)	*16*	*16*
Pound sterling (GBP)	*4*	*4*
Japanese yen (JPY)	*3*	*3*
Gold (XAU)	*10*	*9*
SDR	*3*	*3*
Euro (EUR)	*64*	*65*
Total financial assets	***100***	***100***

** Impact of SDR hedging tranches taken into account.*
Source: Bank of Finland.

Table 3.
Return on bank of Finland's own financial assets in 2010 and 2011

	2011 %	2011 EUR m	2010 %	2010 EUR m
Interest rate return	*3.21*	*488.1*	*2.84*	*407.3*
Exchange rate return	*1.00*	*161.6*	*2.85*	*408.7*
Total return	*4.21*	*649.7*	*5.69*	*816.0*

Source: Bank of Finland.

Bank of Finland financial assets and financial asset management

The total value of financial assets in which the Bank of Finland invests is about EUR 20 billion. These assets are comprised of the Bank's own financial assets, the share of foreign reserve assets transferred to the ECB and the Bank of Finland's pension fund assets. At the end of 2011, the value of the Bank's own financial assets, the foreign reserve assets transferred to the ECB and the Bank's pension fund assets amounted to EUR 18.6 billion, EUR 903 million and EUR 544 million, respectively.

The Bank's own financial assets comprise foreign reserves and assets denominated in euro (Table 1). Foreign reserves, in turn, are composed of US dollars, pound sterling, Japanese yen, gold and items in Special Drawing Rights (SDR) (Table 2).

Objectives for the management of financial assets

From the viewpoint of the management of its financial assets, the Bank of Finland faces the challenge of aligning the partly conflicting security, liquidity and return requirements placed on the central bank. In managing its financial assets, the Bank of Finland secures the value of its financial assets and its ability to support the liquidity of the banking system and the economy, whenever necessary. Accordingly, when required, the Bank must always be able to provide liquidity for central banking needs; on the other hand, however, return on investment must be good relative to the level of risk involved, in order to safeguard continued favourable development of the balance sheet.

The partly conflicting needs of holding financial assets are met by dividing the financial asset management function into two separate entities: liquid assets and investment assets. The strategic target for the management of liquid assets is to ensure the Bank's ability to provide liquidity for acute policy needs under all circumstances. In the management of investment assets the aim is to safeguard the value of financial assets and the Bank of Finland's ongoing ability to meet with its central bank commitments. The strategic allocation set for investments and the strict restrictions established for credit risk ensure that the Bank of Finland's financial assets are managed prudently. Total return on financial assets in 2011 was 4.21%, about EUR 650 million (net of gold and Special Drawing Rights). Total return breaks down into interest rate return and exchange rate return (Table 3). The target set for return on the Bank's financial assets is the opportunity cost of holding the assets, which is the central bank interest rate for each investment currency. In 2011, the financial assets generated average return of 2.24% in excess of the central bank interest rate. The five-year moving average was 2.25% above the central bank interest rate.

A significant part of the Bank of Finland's financial assets is invested in government bonds, with the emphasis on issuers with the highest ratings. A marked fall in interest rates in the second half of the year led to an appreciation in the values of these investments, which is reflected in favourable interest rate return. A small amount of government bond investments were in bonds of euro area countries that have ended up in financial difficulties. These bond valuations have declined during the year. As these investments have been relatively small, they have not significantly eroded positive developments in total interest rate return. In the second half of the year, following euro depreciation, exchange rate changes affecting the Bank's foreign reserves were also positive. During the year, the value of the euro vis-à-vis the US dollar fluctuated within a range of 1.29–1.48, suggesting that the relatively low level of exchange rate return is due to the timing of review rather than a decline in exchange rate risk. When risks related to the Bank's financial assets are examined over a longer horizon, the impact of exchange rate risk on earnings is dominant over other sources of risk (Chart 14).

Chart 14.
Return of Bank of Finland's own financial assets

Source: Bank of Finland.

The interest rate return on financial assets is mainly affected by the strategic allocation of investments and duration. With strategic duration of about 2.5, the global decline in short-term interest rates had a positive impact on the Bank's investment returns. Relative to the size of the currency allocation, the highest interest rate returns were generated in the UK market for pound sterling-denominated securities (4.8%). Interest rate returns from markets for US dollar-denominated securities (3.1%) and euro-denominated securities (3.4%) were also good, especially with regard to expectations a year ago. Japanese yen-denominated returns remained at 0.6%, against the backdrop of Japan's long-sustained very low level of interest rates.

The Bank's Investment division is allowed to deviate from the strategic allocation within the established risk limits by making active investment decisions. Such decisions are made in respect of allocation weights, interest rate level and yield curve shape, as well as relative values of individual securities. Deviations enable more rapid responses than the strategic allocation to changing expectations of the future state of the economy. The aim of active investment decisions is to generate return in excess of the strategic benchmark. To this end, active investment decisions have been assigned a return target relative to the strategic benchmark, calculated in terms of a moving average from the last three years' returns. In the year under review, returns derived from active investment decisions were negative in the amount of EUR 8.9 million. Additional return according to the three-year moving average was 0.07%.

Table 4.
Strategic and year-end allocation of Bank of Finland's asset portfolio

Liquid assets	*Strategic allocation (%)*	*Allocation at year-end (%)*
Central government debt instruments	*100*	*100*
Investment assets	***Strategic allocation (%)***	***Allocation at year-end (%)***
Central government debt instruments	*70*	*61*
Agency debt instruments	*16*	*17*
Covered bonds	*5*	*7*
Corporate bonds	*5*	*11*
Cash holdings	*4*	*4*
Total	***100***	***100***

Source: Bank of Finland

Investments

The Bank of Finland's financial assets are invested in government and government related securities, covered bonds and corporate bonds in the chosen currencies. The investments of liquid assets are exclusively composed of US dollar-denominated government debt securities, which ensure the Bank of Finland's ability to provide promptly central bank refinancing in foreign currencies, if needed. The strategic allocation for investment assets (Table 4) includes assets from all permitted investment classes.

Investments are diversified to mitigate risks to individual investments, to generate additional return and to improve the investment return/risk ratio. In the management of credit risk, the key principles are the setting of a minimum credit rating threshold for issuers and an effective diversification of investments geographically, by sector and by rating category. The distribution of investments by credit rating and geographically is presented in the Notes on the balance sheet.

Main market developments

In 2011 and particularly in the latter half of the year, interest rate markets were dominated by one main theme: the debt crisis of euro area peripheral countries. The repercussions of the crisis were also reflected in US and UK government debt markets as a steep fall in interest rates in the second half of the year, whereas interest rate developments across euro area countries were mixed, with marked increases in risk premia for some countries. The first half of the year still witnessed reasonably calm market conditions, but over the summer market concerns began to increasingly focus, instead of on Greek, Irish and Portuguese debt problems, on the ability of Italy and Spain to cope with their debt burdens. In late summer, Italian and Spanish bond yields started to surge. In the course of the autumn, bond yields also began to rise for countries deemed as having strong economies, as investor concerns over higher debt burdens of even the strongest euro area countries and uncertainty about finding a solution for the debt crisis reduced the attractiveness of bonds. Overall, however, government bond yields for euro area countries considered the safest, such as Germany and Finland, declined during the year, but yields for euro area countries facing financial problems were pronouncedly higher at year-end than at the beginning of the year.

Developments in interest rate markets in 2011 were also influenced by the record low level of central bank policy rates and non-standard stimulus measures. In September, the US Federal Reserve (Fed) announced an Operation Twist, aimed at bringing down long-term interest rates and improving economic recovery and thus employment, via purchases by June 2012, of USD 400 billion worth of US long-term government bonds and sales of an equivalent amount of short-term government bonds. Expectations of this operation caused US government bond yields to decline as early as the first half of the year, with the fall steepening towards year-end, driven by the euro area debt crisis.

Reform of financial asset management and its implementation

In 2011, the Bank of Finland continued work on reforming its financial asset management, commenced in 2010. The main objective is to shift the focus of financial asset management towards a more overall approach and to act in accordance with market standards without abandoning a central bank perspective. A project for liquid assets separation was completed in 2011 as an important part of the reform work. The reform process advanced well, and was according to schedule in other respects, too.

In the course of 2011, the Investments division of the Banking Operations department was responsible for operating the Securities Markets Programme (SMP) and the second Covered Bond Purchase Programme

(CBPP2) launched in November, both related to the implementation of the ECB's monetary policy. In compliance with the Bank of Finland's insider rules, in conducting investment activities, the Bank refrains from operating in the same markets where monetary policy is implemented. Consequently, the existence of these programmes and their implementation by the Investments division have meant significantly more restricted own investment activities than normal.

Share of the ECB's foreign reserves managed by the Bank of Finland

Management of the foreign reserves of the European Central Bank has been distributed among the Eurosystem national central banks according to their respective capital keys. The foreign reserves managed on behalf of the ECB comprise assets denominated in US dollars and Japanese yen as well as gold and items in IMF SDRs. Foreign reserve management is based on the premise that each national central bank may as a rule manage only one portfolio. The Bank of Finland manages part of the ECB's reserves denominated in Japanese yen. Since the foreign reserve assets of the ECB are used for intervention purposes, security and liquidity objectives are pronounced in the investment of the foreign reserves.

The value of the net foreign reserve assets of the European Central Bank was approximately EUR 65.6 billion at the end of 2011. Since the beginning of 2011, the Bank of Finland has managed the yen-denominated share, amounting to about EUR 903 million at the end of 2011, as Finland's and Estonia's pooled portfolio of the ECB's foreign reserves. The ECB's Annual Report provides additional information on the management of its foreign reserves.

Bank of Finland's pension fund assets

The objective of the Bank of Finland's pension fund is to develop the management of assets held to cover the Bank's pension liability in accordance with the generally accepted principles for the management of pension assets. These may deviate from the principles applied to the management of the Bank's financial assets. The value of the pension fund's assets was EUR 544 million on 31 December 2011, with the Bank's pension liability also amounting to EUR 544 million. Total return on assets in 2011 amounted to 1%. More information on the pension fund's asset management is available from the fund's own annual report.

Investment risks and risk management

Investment risks

The risks to which the Bank of Finland's investment activities are exposed can be divided into market, credit, liquidity and operational risks.

Of market risks, the Bank of Finland is mainly exposed to exchange rate risk, interest rate risk and gold price risk. Market risk refers to risk of loss resulting from a decrease in the net value of the Bank of Finland's assets due to changes in either exchange rates, interest rates or the price of gold. The most important market risk affecting the Bank of Finland's activities is exchange rate risk, which arises from the need to hold foreign reserves.

Credit risk means a change in the creditworthiness of a counterparty to a financial transaction or of a securities issuer and, in an extreme case, a potential counterparty or issuer default. The bulk of the Bank of Finland's own financial assets are invested in interest-rate instruments issued by governments and other organisations, as well as bank deposits. If the creditworthiness of these issuers or counterparties changes or they default, the Bank of Finland may incur financial losses.

Liquidity risk refers to the risk that assets cannot be made available when the need arises or their conversion into cash causes additional costs. In central banking, all payment needs cannot be known for sure. In acting as the bank of banks, the central bank may have to face these needs quite unexpectedly.

Operational risks refer to risk of loss resulting from inadequate or failed internal processes, personnel, systems or external events. These may cause the Bank extra costs or losses.

Management of investment risks

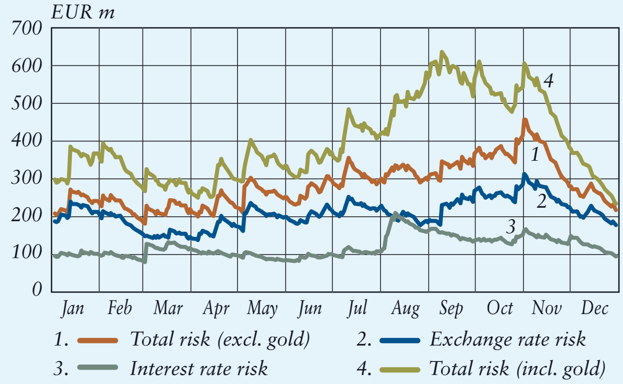
Risk management seeks to identify, measure and limit the risks related to activities. The Bank of Finland uses widely employed risk management methods, such as the Value-at-Risk or VaR method, as well as stress and scenario analyses. Another key element of the Bank of Finland's risk management is the development of risk management methods.

The Bank of Finland's financial assets are invested in order to meet the Bank's international commitments and crisis management needs. For these purposes, the Bank of Finland holds foreign reserve assets. The foreign reserve portfolio consists of foreign-currency-denominated investments and other claims, not separately hedged. Accordingly, the Bank of Finland's activities always involve exchange rate risk. Of key importance for the Bank's exposure to exchange rate risk are decisions on the size and currency distribution of its foreign reserve portfolio.

The targeted size and composition of the foreign reserve portfolio are generally assessed by the Bank of Finland at three-year intervals. The latest assessment was undertaken at the end of 2009, with the next assessment due in 2012 for the following three years. The Bank of Finland continued partial hedging against the SDR exchange rate risk in 2011 as in the previous year, by selling other SDR component currencies (US dollar, pound sterling and Japanese yen) against the euro.

In managing interest rate risk, the Bank of Finland mainly relies on 'modified duration', which is a measure of changes in the value of investments when the level of market interest rates changes. At the end of 2011, the average duration of the Bank's own financial assets was about 2.5. Interest rate risk related to financial assets is also managed by spreading both foreign-currency and euro-denominated investments among several debt instruments with different maturities.

Chart 15.
VaR figures for market risk in Bank of Finland's financial assets in 2011*



* One-month horizon, 95% confidence level.
Source: Bank of Finland.

The daily levels of total market risk, exchange rate risk and interest rate risk are measured in terms of the VaR figure (Chart 15). In addition, active investment is subject to a VaR limit for interest rate risk.

As one part of the revision of financial asset management, the Board of the Bank of Finland confirmed the credit risk management framework and credit risk limits in late 2011. These new decisions improved the efficiency of credit risk management mechanisms, with sovereign credit risk now taken better into account than previously. Towards the end of 2011, the Board also specified objectives, principles and limits for domestic investment activities.

Credit risk related to securities issuers and counterparties to deposits is gauged and limited daily in terms of a separate credit risk VaR method. VaR limits are established for three separate confidence levels (95%, 99% and 99.9%). The Bank of Finland requires sufficiently good creditworthiness from issuers in whose securities investments are made and from counterparties to trades. This is ensured by defining minimum permitted public credit rating thresholds. Within certain limits, investments can also be made in securities of domestic issuers without public ratings. These issuers are subject to separate scrutiny for establishing the relevant limits. Credit risk is also managed by an effective diversification of investments. Limits are established for all issuers, counterparties and debt instruments.

Liquidity risk is managed by holding a certain minimum amount of financial assets in investments that can be converted into cash without difficulty. For this reason, the Bank of Finland has defined its financial assets so as to include a component that must be highly liquid and saleable within a short period of time and at low cost. The Board of the Bank of Finland determines annually the amount of liquid assets. Although liquidity features are also taken into account in connection with other financial assets, the requirements are not as rigorous as for liquid assets. Limits are established for the maturity of investment instruments and for the Bank's share in individual bond issues or issuers' total debt. Moreover, securities lending and short selling are strictly regulated.

Operational risk is managed by means of sound and well-documented work flows. Ensuring staff adequacy and expertise is also important. Attention is focused on the reliability of information systems, for which sufficient backup arrangements are in place and tested regularly.

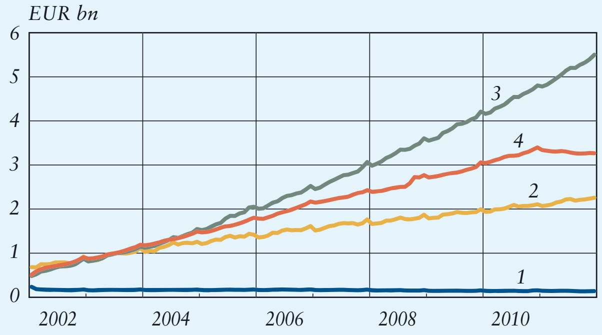
Banknotes and coins

The role of the Bank of Finland in currency supply is mainly limited to wholesale distribution of cash as well as to ensuring the quality and authenticity of coins and banknotes. As with other central banks in the Eurosystem, the Bank of Finland provides euro banknotes and coins in wholesale packages to the various professional cash handling firms, who then distribute them to the cash-paying public and as change to retailers and others, to meet their cash requirements. The individual members of the currency supply chain (banks, contracted cash handling companies and cash-in-transit companies) are responsible respectively for ensuring the supply of cash to account-holders and circulation of notes and coins through the return of cash for sorting and redistribution. Part of this money is returned to the central bank for authenticity and fitness testing.

Cash and cards provide the public with alternative means of accessing the purchasing power gathered in their bank account. As the use of cash in domestic retail transactions declines and various electronic means of payment increases, the Bank of Finland's role in planning and responsibility for monitoring has become more pronounced. The Bank of Finland is responsible for the wholesale services of the country's currency maintenance organisation as well as being the authority mandated with the powers to sustain the functionality, competitiveness and cost effectiveness of the nation's currency maintenance. In the last decade card payments have become the dominant form of payment instrument by consumers in retail transactions. In recent years, banks have actively taken steps to limit cash services, for instance the limiting distribution of cash through bank branches. Accessibility to cash distributed through ATMs and service levels have remained as before.

Last year the Bank of Finland concentrated on the planning of updated systems and implementation side of currency distribution. In the area of currency supply, the authorities made cooperative agreements with the private counterparties (Automatia and Rekla), in order that the availability and affordability of the means for cash payment by the public are ensured. Ultimately, the distribution of cash to bank branches and ATMs is part of the bank's own business functions, where the levels of service provided are demand led. Within Finland's currency distribution function, cooperation is facilitated by the exceptionally concentrated nature of the private currency distribution parties. In 2011, negotiations with the various private currency distribution participants, the Bank of Finland's most recent guideline decisions regarding changes in the central bank's currency distribution services and the timetable for their implementation were entered into in good time, ahead of their coming into force. By the end of 2012 the Bank of Finland will have closed down its Tampere and Kuopio regional offices. At the same time, the private members of the distribution organisation's possibilities for enlarged cash storage will be extended

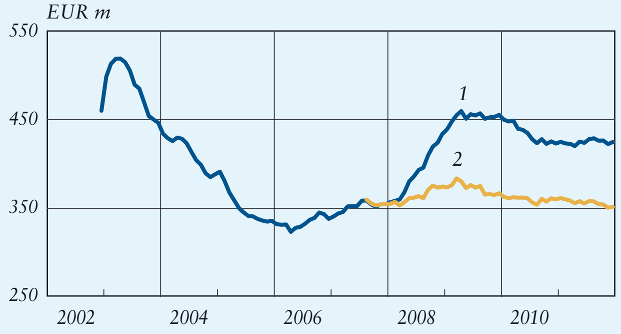
Chart 16.
Issuance of euro banknotes in Finland



1. Banknotes held for exchange (EUR 5 and EUR 10)
2. EUR 20
3. EUR 50
4. Large-value banknotes (EUR 100 – EUR 500)

Source: Bank of Finland.

Chart 17.
Moving annual total of banknotes sorted at the Bank of Finland



1. Banknotes sorted at the Bank of Finland
2. Banknotes sorted at the Bank of Finland, excl. bank packages (millions)

Source: Bank of Finland.

and the storage arrangements will be reorganised in line with other euro countries' arrangements, where the money deposited with the private service providers in their overnight safes are entered into the central bank's balance sheet.

Growth in issuance of euro banknotes slows with reduction in demand for EUR 500 banknotes

There continued to be growth in the issuance of euro banknotes in 2011 in terms of the banknotes distributed via ATMs, but from the beginning of the year a significant reduction in the demand for EUR 500 notes was seen (Chart 16). Estonia's joining the euro area had a key impact on this, as there is no longer the same volume of large denomination notes being taken over the border from Finland to Estonia. The net issuance of EUR 100 denomination banknotes into circulation, by the Bank of Finland has also dropped to the negative side over the reporting year, as more EUR 100-denomination notes arrive in Finland, brought by tourists, than the Finns themselves withdraw from banks. The EUR 50 banknote is the main note withdrawn by the Finnish public and is most extensively used by Finns travelling abroad. The need for small denominations, used as change, remained the same and therefore there are few changes in the use of cash as a means of payment. Distribution of euro banknotes from ATMs and bank branches in Finland fell only slightly, as it had in the previous year. On the other hand, banks reduced their cash services provision by closing down branch offices and offices offering cash services and in addition to cutting back on the opening hours of these cash service offices. The growth in the annual net issuance of euro-denominated banknotes slowed in 2011 to EUR 700 million.

The quantity of notes returned to the Bank of Finland and sorted by the Bank remained close to the volume seen at the end of 2010, despite an increase, in December 2010, in the banknote storage facilities offered by the Bank being increased from EUR 14 million to EUR 46 million (Chart 17). The cash-in-transit company Rekla began to take advantage of the storage opportunities in its own cash depots in 2011. Despite the increase and broadening of the storage facilities the volume of banknotes returned to the central bank was not reduced as was planned by the extension of the facilities.

Information released on renewal of currency distribution storage facilities and reduction of regional office network

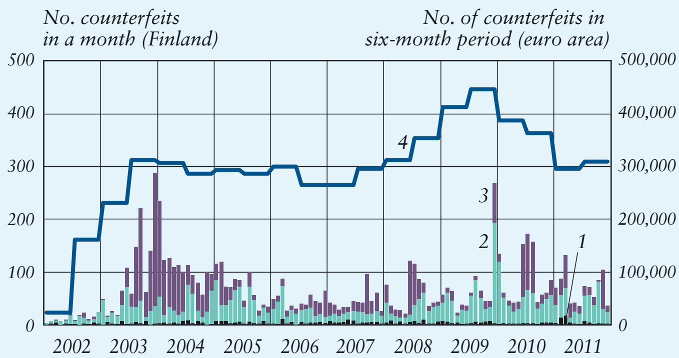
In June 2011 the Board of the Bank of Finland decided to change to the current credited interest-based arrangement, where the central bank's cash held by outside parties, to be brought in line with the storage systems used in other euro countries. Also in the new alternative currency maintenance solution, the counterparties are able to avoid overnight interest charges on the cash in storage. The purpose of the approach is to reduce logistically unnecessary returns to the central bank and thereby reduce the need for cash transit, increase local cash recycling and better cover the interest expenses of keeping the cash.

From here on the Bank of Finland will concentrate its currency maintenance activities in the Vantaa and Oulu offices and close down the Tampere and Kuopio regional offices by the end of 2012. The objective is to mould the Finnish currency supply in such a way that cash would increasingly circulate locally and that the Bank of Finland's own banknote sorting levels would be reduced. There is good reason to the reduction in the Bank of Finland's sorting, as the rejection level of notes meant for distribution through ATMs is clearly less than 10% which means, in practice, that it is mostly banknotes in good condition that are sent, unnecessarily, to the Bank for sorting (with the exception of authenticity checks). Also, the so-called rejection percentage of banknotes for change purposes processed through the central bank's sorting machines is only somewhat over 20%. From society's point of view, there are strong grounds for the elimination of overlapping work and increasing cost efficiency.

The terms of the currency distribution services provided by the Bank are due to be evaluated in 2012, which will cover such details as hours of business and the terms relating to banknotes returned to the Bank for sorting. The reasoning behind this is to reduce the quantity of notes that are handled unnecessarily and enhance banknote circulation. The private cash centres are already capable of sorting in line with the requirements of the Eurosystem's recycling framework regulations. Banknotes are generally already counted and sorted at the cash centres meaning that, from the point of view of quality control, the central bank's sorting becomes unnecessary and therefore does not provide adequate added value. In general only poor quality notes, in need of replacement, or notes suspected of being counterfeits should be returned to the central bank. Quality and authenticity checks are undertaken on all banknotes that are received by the central bank. This aspect of currency maintenance and distribution is provided free of charge and is both taken for granted and used extensively without due cause, which is why the new guidelines are seen as being necessary.

In association with the closing down of two of the Bank's regional offices, the Bank of Finland is in the process of moving and extensively broadening the possibilities for holding cash at the cash centres of the cash-in-transit companies. In this way, the various participants in the currency supply have the opportunity to better achieve cost efficiency. More extensive storage facilities mean a reduction in the so-called bulk cash transports, evening out the fluctuations in working day banknote sorting and more effective use of the human resources in the sorting centres. The credited interest on cash in storage will rise from the 1-month Euribor rate to banks' opportunity interest on holding cash, although technically it replaces direct income with nominal imputed income.

Chart 18.
Counterfeit euro banknotes in Finland and the euro area, by denomination



1. *Number of counterfeit banknotes held for exchange (5 and 10 euro notes) in Finland*
2. *Number of counterfeit banknotes in most common use (20 and 50 euro notes) in Finland*
3. *Number of counterfeit large-value banknotes (100, 200 and 500 euro notes) in Finland*
4. *Total number of counterfeit euro banknotes in the euro area over a six-month period*

Sources: European Central Bank and Finnish National Bureau of Investigation.

Return of markka gathered momentum towards the end of the year before end of the redemption period

The changeover to euro coins and banknotes a decade ago happened swiftly in Finland and a significant proportion of markka coins and banknotes were redeemed within a couple of weeks of the changeover. By the time the parallel use of markka and euro as a means of payment finished at the end of February 2002, almost 90% of redeemable markka banknotes had been removed from circulation. After this period, the annual markka redemption of banknotes through the Bank of Finland diminished by the year to less than FIM 10 million.

In good time. before the ten year redemption period was up, the Bank of

Finland launched a markka redemption information campaign which led to an upturn in returns from autumn 2011. The aim of the campaign was to ensure that the public would not neglect to return their markka coins and banknotes. From experience, the Bank had already observed that some of the members of the public still in possession of markka notes and coins would only redeem them at the very last minute. It would appear that a significant amount of markka notes and coins would remain unredeemed, as in approximately 8.5% of the value of the relative value of markka circulation at the end of the markka period remained in the possession of the public at the end of 2011. Based on a survey conducted, a majority of the public still in possession of markka coins and notes did not intend redeeming it at the central bank. In some cases the numismatic value of the markka can be greater than the nominal value.

The number of counterfeits dropped slightly over last year but levelled out towards the end of the year

From the peak of 2009, the number of counterfeit banknotes has steadily dropped throughout the euro area over the last couple of years, until by the end of 2011 when a slight upturn in numbers was detected (Chart 18). The reduction in counterfeits observed in the preceding years, was due to a reduction in the distribution of some key counterfeit series.

At the beginning of 2011, there were incidents of the distribution of some large-denomination euro counterfeits detected in Finland, which was repeated in November. The total value of counterfeits seized in Finland in 2011 anyway remained slightly below the previous year's level. A total of 827 counterfeit notes were removed from circulation in Finland, which was 225 fewer than in 2010.

Box 5.

Euro area deposit systems and storage arrangements for cash

The concept of the cash deposit system refers to the arrangements made between the central bank and the professional private parties involved in the nation's currency maintenance, whereby the parties have the right to place cash in safekeeping without interest being levied on the money concerned for its storage period. If the storage facilities offered by the central bank were not available, the cash would have to be returned to the central bank every evening in order to avoid safekeeping charges and imputed interest costs. However, smoothly operating currency maintenance requires the cash to available first thing in the morning, to be delivered to meet retail customers' needs such as in ATMs, bank branches or as change in shops.

The euro area has two types of deposit system in place. In Finland and other Nordic countries, the current arrangements are set up using cash depots, where cash issued for circulation is in the private counterparties' possession. The central bank then pays credited interest on the cash held. This cash can wait, without incurring costs, overnight in the private cash depot vaults as it waits for the following morning's transit to the end user. The money's associated liability for risk remains with the company in whose safekeeping the money is, and for which the cash-in-transit companies are insured. The banknotes in circulation are the central bank's zero-interest debt to the public and against which the central bank has capital interest earning assets. Monetary income (seigniorage) is usually received by the issuing central bank on banknotes put into circualtion, but under the Eurosystem, monetary income receiveable on banknotes is first calculated as a whole for the entire euro area and then divided between participating central banks according to the ECB's so-called capital key.

In many euro countries there is a different type of storage arrangement allowed by the respective central banks, the so-called NHTO inventories (Notes-Held-To -Order). Under this deposit system, the cash held is entered onto the central bank's balance sheet , even though it is being held at the cash-in-transit companies' depots. This is not banknotes put into circulation, and therefore does not generate monetary income, but on the other hand cash owned by the central bank does not put a strain on the private participating companies through interest burden. Central banks generally require that the security of the cash it possesses is ensured and insured against a broad range of risks or secured against liquid collateral. Finland is in the process of transferring over to an NHTO arrangement.

NHTO arrangements are already in place in several euro countries: Spain, the Netherlands, Ireland, Greece, Malta, Cyprus and Slovenia. The system in Greece was taken into use in the 1930s to avoid the complications of transportation of cash between the islands. While in Ireland, bank robberies led to the adoption of such deposit arrangements in the early 1970s. The adoption of this deposit system by the euro countries is justified by argument that through this system cash transportation can be reduced and deliveries based on regionally recycled of cash can be enhanced as well as being able to replace central banks' regional offices and thereby make currency supply more efficient. The total value of banknotes held in the euro area's banknote storage systems, at the end of 2009, was over EUR 3.5 billion which represents only 0.4% of the overall sum of banknotes put into circulation through the Eurosystem. A majority of banknotes in circulation are in the possession of the general public.

Other operations

Research

Economic research at the Bank of Finland supports the Bank's policy preparation, operational development and external influence. The aim of the Research unit is to produce internationally top-rank research in areas of key importance to the Bank's activities. This allows the Bank to make a strong contribution to the debate on monetary policy and financial market development, both in Finland and internationally.

The development of research activities at the Bank of Finland continued in 2011 with the formation of an updated organisational framework for research. During the year, the Research unit recruited several entrants to fixed-term, 3–5-year posts for doctorate-level research economists. In addition to domestic recruitment, the Bank also took part for the first time in the international recruitment event for young doctorate-level economists organised in Denver, Colorado in connection with the annual meeting of the American Economic Association (AEA). International recruitment will continue in the future.

Monetary research

Monetary research at the Bank of Finland is concentrated within the Research unit of the Monetary Policy and Research Department. In addition to the organisational changes carried out when the revamping of the Bank's research effort began in 2010, research priorities were also reviewed at that time. The new research policy and practice emphasises the stability of and interplay between the financial markets and the real economy. In 2011, the Research unit began steering research activities in accordance with the new priorities.

The sovereign debt crisis that followed on from the global financial crisis and international economic recession has brought new challenges for economic research. The international research community focused around issues of macroeconomic has relatively swiftly produced research results on the themes of general government sustainability, the limits to public debt, the macroeconomic effects of sovereign credit risk and the interplay between monetary and fiscal policy during economic crises and in the event of an unsustainable accumulation of public debt. In addition to these acute issues, criticism towards mainstream macroeconomic research continued – albeit in much more muted tones – as the international research community, instead of simply criticising, paid more attention than before to the development of alternative research approaches and analytical techniques. One clear conclusion to emerge from the debate is that, on the basis of the lessons from the crisis, research dealing with the behaviour and operational shortcomings of the financial markets should be more clearly integrated than before within mainstream macroeconomic analysis.

The priorities adopted by the international research community also fed through in 2011 into the research priorities at the Bank of Finland. During the year, the projects and publications of the Bank's Research unit focused on

1) the macroeconomic significance of financial factors, 2) the use of real-time data in analysing changes in euro area fiscal policies, 3) the mutual interdependencies between labour market search frictions, economic policy and cyclical dynamics, 4) the significance of company deaths and the birth of new companies for the cyclical dynamics of unemployment and 5) the significance of corporate control and management structures from the perspective of corporate risk-taking, innovations and growth. In 2011, such research projects gave rise to 24 discussion papers.

According to the results of these research projects, financial factors would appear to have a relatively undisputed importance in relation to macroeconomic cyclical dynamics, and, for example, they provide a good explanation for the investment and cyclical dynamics of the Finnish economy over the past 15 years. On the other hand, support for growth and economic activity have shaped the nature of discretionary fiscal policy in the euro area during the crisis. Moreover, research results suggest the different financing alternatives available within fiscal policy have key significance to recovery in an economy where search frictions affect the labour market's capacity for adjustment and the speed at which this can occur. Results also indicate that public expenditure growth has harmful long-term macroeconomic effects, albeit it is an effective tool for providing a short-term stimulus. According to research into the role of learning, the expectation formation mechanism crucially shapes the direct, short-term impacts of economic policy. In addition, clearly observable variations in key macroeconomic variables are characteristic features of learning-generated dynamics.

The minimum capital requirement is an addition to the Basel III regulations and provides a complement to risk-based capital requirements. The effects of the minimum requirement on the targeting of credit and, according to research into banking stability, the current minimum capital requirement of 3% could actually weaken banks' stability if a large model risk is incorporated into low-risk loans, as was done during the subprime crisis that spawned the recent general financial crisis. This is counter to the aims of the Basel Committee. The homogeneity of banks' loan portfolios caused by the minimum capital requirement could, thus, serve more as a channel for spreading instability and turbulence than as a means for the dispersal of risk. A minimum capital requirement well above the current level of 3% could increase banking stability even with the incorporation of a large model risk. On the other hand, research into the monetary policy significance of the stock market participation rate – a specific type of financial market imperfection – proposes that an optimal monetary policy strategy does not depend to any critical degree on the financial market participation rate. Moreover, according to estimates based on empirical studies carried out at the Bank, corporate indebtedness specifically hampers growth in those companies with problems in their management and control systems. Results indicate that the negative growth effects of indebtedness seem to disappear when the future value of senior managers' assets depends partly on the yield from a system of remuneration based on management stock options. This result can be considered significant, as it means that debt no longer serves as a constraint on corporate management when its incentives are shaped by a system of remuneration based on stock options.

Scientific meetings

In 2011, the Bank of Finland organised international scientific meetings on topics of relevance to its research activities. In May, as part of its 200th Anniversary celebrations, the Bank organised in Helsinki a high-level international conference entitled Monetary policy under resource mobility, to which were invited a number of internationally renowned academic economists and central bank governors. The conference was very well attended and received a great deal of coverage in the media.

The conference dealt with historical changes in global economic power relations, the monetary policy significance of the mobility or immobility of economic resources, financial market issues, and the connection between finance and economic growth.

Janet Yellen, Vice Chair of the Board of Governors of the US Federal Reserve

In May 2011, a number of well-renowned academic economists and central bank governors participated in the Bank of Finland's high-level conference "Monetary Policy under Resource Mobility".

Photo: Peter Mickelsson.

System, was invited to deliver the keynote address to the conference. The dinner speech was given by the President of the ECB, Jean-Claude Trichet, and the lunch speech by Mervyn King, Governor of the Bank of England.

The conference panels attracted renowned and respected professors from different parts of the world: Barry Eichengreen (University of California, Berkeley), Carl Walsh (University of California, Santa Cruz), Philippe Aghion (Harvard University), Martin Hellwig (Max Planck Institute for Research on Collective Goods) and Bengt Holmström (Massachusetts Institute of Technology, MIT). Central bank governors Jens Weidman (Germany) and Christian Noyer (France) chaired the sessions. Other participants on the panels were Masaaki Shirakawa (Japan), Sergey Ignatiev (Russia), Miguel Ordoñez (Spain), Mark Carney (Canada), Athanasios Orphanides (Cyprus), Agustin Carstens (Mexico), Nout Wellink (Netherlands), Yves Mersch (Luxembourg), Stefan Ingves (Sweden) and Stanley Fischer (Israel). The concluding panel of the conference was chaired by Steve Liesman, senior economics reporter for the US television channel CNBC.

In September 2011, the Research unit organised, in cooperation with the Centre for European Policy Research (CEPR) and the European Money and Finance Forum (SUERF), a conference for researchers to discuss the future of risk management and the latest research on this topic. The academic collaborator on the conference was the Journal of Financial Intermediation (JFI). JFI will publish the research papers presented at the conference and sent to the Journal, provided they meet the quality requirements set for its research publications. International researchers in the field were very active in sending their proposals to the conference. In the end, the conference's scientific committee selected 8 papers for presentation and comment at the conference from over 80 that were sent for consideration.

In October 2011, the Research unit organised, in cooperation with three external research bodies (TAMUCC, UEL and INFER), a research workshop on frequency domain research in macroeconomics and finance. International researchers sent in over 40 research papers, from which the scientific committee selected 18 for presentation at the workshop.

Bank of Finland Institute for Economies in Transition

The research efforts of the Bank of Finland Institute for Economies in Transition (BOFIT) mainly consist of applied macroeconomics with a focus on monetary and exchange rate policy issues. Research is also conducted on financial sectors. The primary target countries are Russia and China, although many research settings require the use of more extensive comparative data. Collaboration between research and monitoring forms the foundation for the work of BOFIT's experts. In 2011, BOFIT continued to publish (in both Finnish and English) its popular weekly digest of economic news items from Russia and China. Another aspect of BOFIT's work was the presentation of topical information releases on the Russian and Chinese economies. In addition to the needs of research and monitoring, the Institute's information service also caters to the needs of external customers.

Studies are published initially in BOFIT's own Discussion Papers series, of which 36 were published in 2011. In addition to the work of the in-house researchers, the series also includes articles by visiting scholars and studies presented at BOFIT's seminars and workshops.

2011 saw both the BOFIT 20th Anniversary Conference and an academic workshop on China's monetary and exchange rate policy. In addition, BOFIT assisted the Austrian central bank in organising the Conference on European Economic Integration (CEEI), which was held in Vienna in November. The main focus of the 2011 conference was on the impact on Europe of the economic rise of Russia and China, particularly the effects on the economies of Central, Eastern and Southeastern Europe (CESEE).

The Anniversary Conference also took a broad-ranging look at the challenges facing the Russian economy. The main speakers were Odd Per Brekk, head of the IMF's office in Moscow, Professor David Tarr from the New Economic School in Moscow and Evgeny Gavrilenkov, chief economist at the investment bank Troika Dialog. The dinner speaker was Professor Vladimir Mau, rector of the Russian Presidential Academy of National Economy and Public Administration. Topics covered included the adoption by Russia of an inflation-targeting approach to monetary policy and the potential of Moscow to operate as an international financial centre. Although the Central Bank of Russia has for several years had the objective of a more freely floating exchange rate and inflation targeting, introduction of the new approach will still require substantial changes in, among other things, monetary policy instruments and the functioning of the interbank money market. Other relevant factors include the need for a more predictable fiscal policy.

The Russian financial markets have in recent years being developing relatively rapidly, but most researchers and bankers are of the opinion that Moscow is not developing into an international financial centre, at least not very quickly. The idea is, however, a valuable one, if it can help foster further financial market development in Russia.

The May conference on China's monetary policy brought together a large group of top-class researchers from countries and territories such as China, Hong Kong and the United States. One of the main speakers was Robert N. McCauley from the Bank for International Settlements. Several presentations dealt with the efforts of the Chinese central bank to liberalise the financial markets and shift the basis of monetary policy more towards market mechanisms. Although the phased liberalization of capital movements has certainly continued, during the international financial crisis the banking system in

China was used very unambiguously as an instrument of economic policy. This perspective was highlighted by, for example, The Hong Kong Monetary Authority's Honglin Wang in his presentation. If more efficient financial intermediation is the objective, loan decisions, for example, should be based to an increasing degree on financial considerations.

In earlier years, BOFIT's financial systems research has focused mainly on Russia, but in 2011 the Chinese banking and financial system attracted greater interest than in the past. China's banking system is very large relative to the size of the country's economy, and it plays a very important role in financial intermediation. With China's extremely high savings ratio and continued controls on capital movements, the volume of deposits by households and businesses is very large. A significant proportion of these deposits is still being channelled into state-owned enterprises. In contrast, access to finance for small and medium-sized enterprises, in particular, is much harder. Although China's capital markets have developed strongly in recent years in response to the ongoing liberalization, their role in financial intermediation remains very small. Looking to the future, the liberalization of capital movements in China will also mean major changes in the financial markets, as Chinese businesses and households will enjoy a larger range of possible investments.

Statistics

The Bank of Finland is responsible for producing Finnish data for statistics on euro area monetary financial institutions (MFIs) and other financial and balance of payments statistics, together with corresponding national data. In the year under review, statutory European System of Central Banks' statistics were produced as required and issued according to schedule.

Demand for financial statistics increased in 2011. The debt crisis drove the need for more country- and sector-specific statistics on investment and debt, in particular. Regular publication of these figures was increased on the Bank's website, in addition to which there was more than the normal amount of ad hoc data requests, particularly on the detailed spread of securities investments. In the autumn, a new chart gallery section was opened on the website, which contains an up-to-date collection of charts depicting Finland's economy and financial markets. Users can download charts for their own presentations and reports, or preview the content of the gallery on screen.

The development focus in statistical output was on supporting analysis of financial market stability, and statistical cooperation within the European System of Central Banks (ESCB) was broadened to also support the data needs of the European Systemic Risk Board. Cooperation was also intensified between financial supervisors and central bank statistical units. The objective of cooperation is to avoid overlap in data collection and ensure the efficient exploitation of shared data. Work also continued on the harmonisation of concepts and methods in statistical and supervisory data collection.

Within the area of ESCB statistics, there are currently three major joint euro area projects under way. To serve the needs of statistics on securities holdings, a new reporting system on a security-by-security level is being developed and a common database is being constructed that will facilitate comprehensive analysis of sector-specific ownership of securities and changes therein. A new Statistics Regulation will be drafted during the course of 2012, and a new reporting regime launched in 2013.

Another large ESCB-level statistical project is the construction of a comprehensive register of financial sector institutions. This will extend the present register of credit institutions to also cover other financial sector institutions. Also planned is to increase the information content of the register, for example in respect of group structures.

For its part, work on the development of harmonised statistics on insurance companies progressed to the stage of cost-benefit analysis. A new Regulation on this is expected sometime in 2012.

The European Commission developed a scoreboard containing country-specific macroeconomic indicators for monitoring stability, the purpose of which is to provide clear data on developments in macroeconomic balance in Member States. The data for the Finnish indicators was provided in cooperation by the Bank of Finland and Statistics Finland.

The Bank of Finland launched implementation of the sixth edition of the IMF's Balance of Payments Manual. The data requirements update will necessitate a substantial overhaul of the balance of payments data collection and compilation system, and the project will continue through until the first half of 2013. In 2011, attention was also devoted to updating the infrastructure of statistical data systems and boosting the capacity of statistical output. The objective is efficient output of readily usable statistics.

International operations and activities

The Bank of Finland in the European System of Central Banks

The Governing Council of the European Central Bank (ECB) is the highest decision-making body in the Eurosystem. It is composed of members of the Executive Board of the ECB and the governors of the national central banks of countries that have adopted the euro. There were 17 of these in 2011, following Estonia's adoption of the currency at the turn of the year. Bank of Finland Governor Erkki Liikanen is a member of the Governing Council, and his personal alternate member is Deputy Governor Pentti Hakkarainen. The Governing Council generally convenes twice a month at the Eurotower in Frankfurt am Main. At the first meeting of the month it conducts a thorough evaluation of developments in the financial and real economy and takes its monthly monetary policy decision. In the second meeting of the month, discussion generally focuses on other tasks and responsibilities of the ECB and the Eurosystem. In 2011, two of the Governing Council's meetings were held outside Frankfurt: one organised by the Bank of Finland in Helsinki, and the other organised by the Bundesbank in Berlin. In addition, the Governing Council also held teleconferences and made decisions using a written decision-making procedure.

The Governor of the Bank of Finland is also a member of the ECB's General Council, which includes the governors of all the national central banks of EU Member States plus the President and Vice-President of the ECB. The General Council meets an average of four times a year.

In 2011, Board members and experts from the Bank of Finland participated in the work of the European System of Central Banks (ESCB) at all stages of preparation. The Bank of Finland had at least one representative on each of the ESCB committees as well as the Budget Committee, the Eurosystem IT Steering Committee and the Human Resources Conference. The bank was also represented in most of the working groups (altogether approximately 60). During the year, a total of 14 Bank of Finland employees were seconded to the ECB on fixed-term contracts of varying lengths.

The Eurosystem also has a number of temporary, high-level committees in such areas as IT and financial markets. Members of the Bank of Finland Board attended the meetings of these committees in accordance with their own areas of responsibility.

The ECB also has an Audit Committee, whose task is to improve ECB and Eurosystem administration and supervision. It is composed of three members of the Governing Council and is currently chaired by the Governor of the Bank of Finland, Erkki Liikanen.

The Bank of Finland and international economic policy

The Bank of Finland actively participates in international cooperation through a variety of organisations and cooperation bodies. Under Finnish law, the Bank of Finland is responsible for contacts between the Republic of Finland and the International Monetary Fund (IMF). The Bank of Finland also takes part as a shareholder in the activities of the Bank for International Settlements (BIS) and participates in six European Union committees and in the work of the Organisation for Economic Cooperation and Development (OECD).

International Monetary Fund

Finland's representative on the highest governing body of the IMF, the Board of Governors, was Bank of Finland Governor Erkki Liikanen, with Deputy Governor Pentti Hakkarainen as his alternate member. The IMF's Board of Governors held its annual meeting in Washington in September.

The IMF's advisory International Monetary and Financial Committee (IMFC) met in April and September. Following the resignation of the Committee's chairman, Egypt's Minister of Finance, Youssef Boutros-Ghali, Singapore's Minister of Finance Tharman Shanmugaratnam was appointed to chair the committee in March. The Nordic-

Baltic constituency was represented in the IMFC in April by Norway's Minister of Finance, Sigbjørn Johnsen, and in September by Nils Bernstein, Governor of central bank of Denmark. The IMF's Executive Board of 24 Directors and the Managing Director, who also serves as Chairman, are responsible for conducting the day-to-day operations of the IMF. Following the resignation of Managing Director Dominique Strauss-Kahn in May, French Finance Minister Christine Lagarde was appointed as his successor. She started in her new position in July.

Finland belongs to the Nordic-Baltic constituency within the IMF. In 2011, Benny Andersen from Denmark served as the constituency's common representative and member of the IMF Board. The Bank of Finland, together with Ministry of Finance, participated in the coordination of the constituency, led by Denmark. The purpose of the coordination is to form a common position on matters determined in the IMF Board.[1]

The Nordic-Baltic Monetary and Financial Committee (NBMFC) met before the IMFC meetings in April and September in order to prepare the constituency's policy positions. The Bank of Finland was represented on the NBMFC by Deputy Governor Pentti Hakkarainen. The alternate members of the NBMFC met twice in the year to prepare the NBMFC meetings. At the Alternates' meetings, the Bank of Finland was represented by Olli-Pekka Lehmussaari, Head of European and International Affairs.

The IMF has an important role in managing the still ongoing financial crisis that began in 2008, and this has been reflected in rapid growth in the volume of financial arrangements to member countries. At the end of 2011, the Fund had credit arrangements totalling SDR[2] 163.4 billion to support economic adjustment in 25 member countries caught up in or threatened by the financial crisis. The countries concerned included three members of the euro area: Greece, Ireland and Portugal. The arrangements for these three countries also involve participation by the European Union and by some individual EU Member States, with a total contribution twice that of the IMF's contribution.

The IMF's lending resources consist primarily of the member countries' quotas, which total SDR 238.4 billion, and if necessary, of borrowed resources from member countries. The Board of Governors approved a doubling of members' quotas to SDR 476.8 billion and a governance reform of the Executive Board in 2010. Ratification of these changes is currently ongoing in the member countries. In order to secure sufficient quota resources, the IMF Board hopes member countries will be able to complete ratification in time for the 2012 Annual Meeting. Finland ratified the

[1] The positions adopted by the Nordic-Baltic constituency can be seen in the bi-annual report Recent Policy Developments in the International Monetary Fund. The Nordic-Baltic Office, IMF (http://suomenpankki.fi/en/suomen_pankki/kv_yhteistyo/imf.htm).

[2] The Special Drawing Right (SDR) is an international reserve currency created by the IMF. It takes the form of a currency basket including the US dollar, the euro, sterling and the Japanese yen. At the end of the year under review, one SDR was equal to EUR 1.18654.

quota increase and governance reform in December 2011.

As increases to members' quotas are time-consuming processes, the IMF decided in 2009 to additionally reinforce its lending resources through direct loans agreed bilaterally with member countries. The Bank of Finland and the Fund signed such a bilateral loan in the amount of EUR 1.3 billion in 2010. In addition, in 2009, the IMF began work on reforming and expanding the New Arrangements to Borrow (NAB) in order to produce a more flexible and enlarged permanent additional credit line. When the reformed NAB came into force in March 2011, the Bank of Finland terminated the bilateral loan agreement entered into in 2010 and assumed responsibility for Finland's share in the reformed NAB, which involves a maximum commitment of SDR 2.23 billion.

By the end of 2011, 37 member countries participating in NAB had committed to providing the IMF with additional resources up to a maximum of SDR 366.1 billion. The use of NAB resources requires a formal activation decision. The NAB was activated twice in 2011, first at the beginning of April, and then at the beginning of October, for a fixed period of six months on both occasions.

Management of the international financial crisis generated pressures for changes in the IMF's lending toolkit. In addition to the traditional stand-by arrangement for countries with balance of payments difficulties, 2009 saw the introduction of the Flexible Credit Line (FCL). Its objective is to prevent the crisis from spreading to countries pursuing sound economic policies but subject to doubts in the markets largely because they border on crisis countries. Once a country has signed an FCL, it will be able to draw funds flexibly in case of a balance of payments crisis. To date, three countries (Mexico, Poland and Colombia) have signed an FCL with the IMF, but none of them has so far drawn any funds. Another facility also introduced in 2009 is the Precautionary Credit Line (PCL), which attaches conditions to the drawing of funds. It was redesigned at the end of 2011 and renamed the Precautionary and Liquidity Line (PLL). This facility was aimed at countries pursuing sound economic policies but with actual or potential balance of payments difficulties. The purpose of the PLL is to provide liquidity and bolster market confidence in a country's ability to weather the crisis due to its prudent economic policies.

The IMF has been strongly criticised for its inability to give timely warning of the impending threat of a global financial crisis despite the fact that surveillance over its member countries' economies, the global economy and the financial markets as well as risk assessment belong to its mandate. In the year under review, the Fund's Independent Evaluation Office (IEO) published an account of the surveillance activities conducted during the years preceding the financial crisis (2004–2007). The IEO concluded with recommendations that the IMF should communicate more clearly to authorities in member countries on shortcomings in their economic policies, and the IMF should be more open to critical points of view. According to the IEO, the analysis of the financial sector in particular should be more closely integrated into macroeconomic assessments. In addition, linkages, interdependencies and vulnerabilities between the financial sector and the macro economy should be more clearly identified. The IMF management agreed to take these recommendations into account in the future in order to enhance the effectiveness of surveillance. As in previous years, the IMF continued to cooperate closely with the G20 group. The IMF regularly prepared reports on the state of the global economy, the financial markets and on the countries in the G20 group for the group's meetings.

EU committees

The European Systemic Risk Board (ESRB), which began work at the beginning of 2011, is part of the European System of Financial Supervision. Its focus is on oversight of the financial markets at the macro level. Its role is to identify risks to the financial system as a whole and to prevent their development by issuing warnings and recommendations. The ESRB structure comprises a General Board, a Steering Committee, a Secretariat, an Advisory Scientific Committee and an Advisory Technical Committee. Decisions are taken by the General Board, on which Bank of Finland Governor Erkki Liikanen is a member with voting rights. Anneli Tuominen, Director General of the Financial Supervisory Authority, is a non-voting member. The Board convenes an average of four times per annum. The Bank of Finland also has a member on the Advisory Technical Committee.

In the year under review, the European Banking Authority (EBA) was established to replace the Committee of European Banking Supervisors (CEBS). The EBA's role is to ensure effective and uniform supervision and regulation of banks in the EU and strengthen international supervisory coordination by, for example, issuing regulatory and supervisory standards and conciliating and resolving differences of opinion between competent national authorities. In 2011, the EBA designed and implemented a stress test covering the major banks within the EU and defined temporary additional capital requirements for these banks. The membership of the EBA includes the banking supervisors of EU Member States and experts from the national central banks.

The European Union's Economic and Financial Committee (EFC) met 13 times during the year under review. The EFC's key responsibility is to prepare the meetings of the ECOFIN Council, which is comprised of economic and finance ministers of the EU Member States. In 2011, the work of the EFC focused particularly on management of the European debt crisis, close monitoring of the economic situation in EU countries and the increased need for coordinating economic policy.

Each EU Member State can appoint a maximum of two members to the Committee, one from their finance ministry and one from their national

Box 6.

Bank of Finland representatives at the ECB, EU and other international bodies in 2011

Bank of Finland representatives on the Governing Council of the ECB

Erkki Liikanen, member
Pentti Hakkarainen, alternate member
Maritta Nieminen, assistant
Antti Suvanto, assistant

Bank of Finland representatives on ESCB committees, the Budget Committee, the Eurosystem IT Steering Committee and at the Human Resources Conference

International Relations Committee
Pentti Hakkarainen
Olli-Pekka Lehmussaari (until 31 August 2011)
Janne Hukka (from 1 September 2011)

Accounting and Monetary Income Committee
Tuula Colliander

Committee on Cost Methodology
Annika Karjalainen
Hanna Järvinen

Legal Committee
Maritta Nieminen
Eija Brusila

Payment and Settlement Systems Committee
Marianne Palva
Kirsi Ripatti

Market Operations Committee
Harri Lahdenperä
Tuomas Välimäki

Monetary Policy Committee
Tuomas Saarenheimo
Jarmo Kontulainen

Financial Stability Committee
Kimmo Virolainen
Jouni Timonen (from 13 June 2011)

Risk Management Committee
Antti Nurminen
Kaarina Huumo

Banknote Committee
Mauri Lehtinen
Kari Takala

Internal Auditions Committee
Erkki Kurikka
Pertti Ukkonen

Information Technology Committee
Armi Westin (until 31 March 2011)
Petteri Vuolasto
Raimo Parviainen (from 1 April 2011)

Statistics Committee
Helka Jokinen (until 31 August 2011)
Laura Vajanne (from 15 October 2011)
Harri Kuussaari

External Communications Committee
Mika Pösö
Richard Brander

Budget Committee
Pirkko Pohjoisaho-Aarti

Eurosystem IT Steering Committee
Seppo Honkapohja

Human Resources Conference
Antti Vuorinen

Bank of Finland representatives on EU committees

European Systemic Risk Board, General Board
Erkki Liikanen

Economic and Financial Committee
Pentti Hakkarainen
Hannu Mäkeläinen, alternate member (until 15 March 2011)
Olli-Pekka Lehmussaari, alternate member (from 16 March 2011)

Economic Policy Committee
Veli-Matti Mattila (until 30 April 2011)
Lauri Kajanoja (from 9 September 2011)

European Banking Authority
Kimmo Virolainen

Committee on Monetary, Financial and Balance of Payment Statistics
Helka Jokinen (until 31 August 2011)
Laura Vajanne (from 15 October 2011)

Balance of Payments Committee
Harri Kuussaari

Bank of Finland representatives at the Bank for International Settlements (BIS), the IMF and the OECD

BIS meeting of central bank governors
Erkki Liikanen

IMF Board of Governors
Erkki Liikanen, member
Pentti Hakkarainen, deputy member

OECD Economic Policy Committee
Tuomas Saarenheimo
Samu Kurri

OECD Financial Markets Committee
Jyrki Haajanen

central bank. Each member has a personal alternate member. The meetings are also attended by representatives of the ECB and the European Commission. The EFC has convened in both restricted and extended composition. Representatives of the central banks participate in the latter.

The EFC has also met twice a year in the role of the Financial Stability Table. Representatives of EU supervisors have attended these meetings and reported on the condition of the Union's financial markets. During the year under review, meetings of the Financial Stability Table attached particular attention to financial market stability, banks' stress tests and banking capitalisation issues.

The work of the EU's Economic Policy Committee (EPC) is focused on preparation of the Union's economic policy guidelines and structural policy issues, including those based on the Lisbon Programme. The Committee comprises of Member States' finance ministries, some national central banks (eg the Bank of Finland is represented) as well as the European Commission and the ECB.

The Committee on Monetary, Financial and Balance of Payments Statistics (CMFB) has representatives from ,on one hand, national statistical authorities and Eurostat, and, on the other hand, the national central banks and the ECB. The Committee's remit is to foster better statistical cooperation between the ECB and Eurostat and to issue statements on statistical issues.

The Eurostat's Balance of Payments Committee members are the statistical authorities and central banks responsible for balance of payments statistics. The purpose of the Committee is to assist Eurostat in implementation of the Regulation of the European Parliament and the Council on Community balance of payments statistics.

Bank for International Settlements

The Bank for International Settlements (BIS) organises six regular meetings a year for central bank governors, in which the Governor of the Bank of Finland takes part. During the year under review, the meetings covered topical issues in the global economy and the financial markets, and particularly on the challenges posed by the crisis, such as the effects of the increased indebtedness.

The Governor of the Bank of Finland also took part in the Global Economy sessions of the Governors' meetings. In addition to the global economy, the discussions covered current challenges in the international financial system. As a shareholder in the BIS, the Bank of Finland was represented at its Annual General Meeting in June.

Other international activities

In 2011, the members of the Bank of Finland Board participated in numerous international meetings, seminars, conferences and other events.

Nordic cooperation continued in the customary manner, and this time the governors of the Nordic central banks, accompanied by experts from their banks, met in May on the Danish peninsula of Skagen. The main theme of this meeting was the Nordic housing market. Moreover, the governors of the Nordic central banks met each other on several occasions at Nordic meetings as well as in other international contexts.

Communications

The Bank of Finland's effective and specifically targeted communications are geared to keeping the general public well informed of the role and activities of the Bank itself and the Eurosystem as a whole. Monetary policy, financial markets and payment instruments are key areas of focus, with special interest paid to the activities of the Bank of Finland and the Eurosystem in these areas.

One important channel for external communications is the Bank's website. An updated website was launched in January 2011, with changes in layout, content and functionality. Among other advantages, it enables the pages to be used more easily with mobile devices. The Bank of Finland's web pages are viewed by close on 170,000 visitors every month. The aim of the web pages is to provide current information on the economy and financial markets as well as of the Bank of Finland and the overall operations of the Eurosystem.

The European debt crisis has also been reflected in the Bank's communications. In March, a blog was started up on the Bank of Finland's Internet site, where various experts have written on current economics topics from the central bank's perspective, in particular. The crisis has also featured as a theme in articles, speeches and interviews by the members of the Board and the Bank's experts.

The Bank of Finland's 200th anniversary showed itself in the Bank's communications, too. An art exhibition was arranged in the Bank's head office in January and August 2011, that brought in over 11,300 visitors and received extensive media coverage. In connection with the exhibition, virtual tours were launched on the Bank's Internet site showing more information on the Bank's art collection and another on the architecture of the head office building. In 2011 the first of two books recounting the history of the Bank of Finland was released. Additionally, in 2011, the Finnish television channel MTV3 broadcast a two-part documentary on the 200-year history of the Bank. The documentaries were aired twice over the course of the year. The actual 200th anniversary celebrations took place in December, in the newly-built Helsinki Music Centre, with separate events arranged for personnel and for Finnish invited guests.

In May 2011, The ECB's Governing Council's meeting was held in Helsinki and received extensive coverage in Finland and abroad. Generally, the ECB convenes the Governing Council outside Frankfurt twice a year. Through these euro area meetings, the ECB aims at emphasising its role as the central bank of the euro area as a whole. Following the Governing Council meeting, the Bank of Finland arranged a conference in celebration of its 200th anniversary, attended by key central bankers from around Europe and the rest of the world, as well leading academics from around the world. At the beginning of the autumn, an historical seminar was arranged in the city of Turku, looking at the Baltic's economic area from a variety of standpoints.

The most important publication of the Bank of Finland's external communications process is Euro & talous, which is translated into English as the Bank of Finland Bulletin and which, from the beginning of 2011, will be published five times a year. The press covered the Bank's June and December forecasts for the Finnish economy and in late spring the Bank published its issue of the Bulletin reviewing the stability of the financial market. In March and September issues of the Bulletin, the Bank presented its monetary policy and the Bank's international economic forecast. There were five press conferences arranged over the year in connection with the release of Euro & talous., The Bank of Finland publishes its BoF Online series via its Internet site. Over the reporting year, there were eight articles in this series.

The Bank of Finland's publications can be found under the link 'Publications'. A proportion of the Bank's publications are also available in printed format. For a summary of the key publications issued in 2011, see the Appendices (p. 139).

The Bank puts particular effort into the increased awareness of economic matters among the youth of the country. In 2011, the Bank was involved in the launch of a two-year research programme 'TOKATA' (derived from the Finnish for Participants, Means and Practices), aimed at enhancing young peoples' economic know-how. The research programme is the responsibility of Finland's National Consumer Research Centre and the University of Jyväskylä. The first interim report on the progress of the research was published in October.

The Bank of Finland has also set up an interactive website (www.euro.fi) 'More about the euro' aimed at teachers and pupils. The site provides background teaching material for economics studies and includes various games and tasks that teachers can use in the classroom. Over the reporting year, the Bank was involved in arranging educational tours for teacher, entitled Talous tutuksi (Getting to Know Economics) attended by about 240 teachers in all.

The Bank of Finland arranged the 14th Economic Guru competition for senior high school pupils, in association with the Finnish Federation of Financial Services and the Association for Teachers of History and Social Studies in Finland. The final competition was held in March 2011. The competition was won by Juhana Tikkanen from Ressun Lukio, Helsinki. The top three placed in the Economic Guru 2011 competition were also involved in the SuomiAreena public discussion forum, arranged in Pori by the Bank of Finland and the Union of Finnish Upper Secondary School Students, aimed at enhancing young peoples' economic know-how.

The Bank of Finland Museum acts as the main reception facilities for guests to the Bank as well as presenting the history of money and the Bank's activities within the European System of Central Banks. During the reporting year, the Museum received approximately 13,000 visitors. In January 2011, the Museum opened a seasonal exhibition entitled "Three currencies, two centuries, one Bank of Finland". The exhibition was a celebration of the Bank's 200-year history and told of the effects of monetary reform on life in Finland.

The Museum also arranged twelve events in its Studia Monetaria lecture series on macroeconomics and economic history, attracting more than 700 participants over the course of the year. In 2010 the Bank launched a series of open discussion forum sessions on the theme 'Economic Books' Talouskirja Nyt on recently published books in economics, and over the year two sessions in this series were arranged at the Museum. In May the discussion was based on the first part of the Bank of Finland's historical account by Antti Kuusterä and Juha Tarkka Imperial Cashier to Central Bank. The October session's theme was an anthology of the works of the 18th century thinker Anders Chydenius 'Anticipating The Wealth of Nations, The Selected Works of Anders Chydenius (1729–1803)'.

In April 2011, the first of the two-part history of the Bank of Finland, "Imperial Cashier to Central Bank" was published.

Photo: Peter Mickelsson.

Management and personnel

Management system

The key elements of the Bank of Finland's management system, in addition to the Bank's strategy, are the objectives and results framework, the action planning framework, staffing and budgetary ceilings and overall risk assessment. Overall risk assessment and analysis is integrated with action planning at department, unit and process levels. Performance appraisal and pay discussions with staff are another part of the Bank's management system.

Action planning

Action planning at department and process level is conducted with a three year timeline. The objectives of the action plan are written up in the form of the Bank's objectives and results framework, which is reviewed and undersigned by all the department heads, every year. The framework outlines what are the relevant indicators and major projects for the individual departments.

Objectives and results framework

The objectives and results framework embodies the Bank's agreed strategic objectives and the indicators against which achievement of the objectives is measured. Similarly, each department and process is led by the relevant section of the strategy framework. On an indicator scale of 1–5, achievement of the strategic objectives for 2011 was successful.

The Bank's heads of department are responsible for management and administration of their respective departments, ie for achievement of the set objectives and for personnel and budgetary issues. The aim has been to increasingly delegate decision-making power to division and unit heads.

Service competence and exercise of influence

The Bank of Finland is an influential member of the Eurosystem and the domestic economic policy debate. Service competence and exercise of influence is measured by customer surveys addressed to the Bank's senior management and staff, as well as customers and stakeholders. The Bank's influence in domestic economic policy making is assessed against the indicator of media coverage in the objectives and results framework.

Efficient use of resources

In the investment of the Bank's financial assets, the objective is to ensure capital adequacy and provide for stable profit distribution to the state. The yield of the Bank's financial assets is monitored on a quarterly basis by means of yield reports and forecasts.

The Bank has set specific objectives for the development of staff and budgetary resources. Staff and budgetary developments are monitored by the Board on a quarterly basis. The development of resources is benchmarked against other central banks.

Efficiency of internal processes

Process management has been introduced for the Bank's four core processes. This approach has been established and there is smooth interaction between the processes. The Bank of Finland and FIN-FSA, which operates in conjunction with the Bank, signed a Memorandum of Understanding

(MoU) on the division of responsibilities and exchange of information. Compliance with the spirit of the MoU is followed through the reporting of the Financial Markets and Statistics department of the Bank. Scope for remote working at the Bank has been expanded by means of information technology solutions.

Competence and wellness at work

A new management support tool, the management index, has been developed in the Bank and was introduced at the beginning of 2011.

Risk management within corporate governance

In line with the principles adopted by the Board, risk management is an integral element of the Bank of Finland's governance framework. Annual reporting on objectives and results incorporates an evaluation of the likelihood of the risks being realised over the period under review. The Bank's risks are divided into strategic risks, financial risks and operational risks. Overall responsibility for the provision and governance of risk management and the definition of the level of risk exposure rests with the Bank's Board, but each employee is responsible for the management of risks falling within his or her own job description and tasks.

Strategic risks

The Bank of Finland's strategic risks are related to strategic choices and the underlying assumptions regarding changes in the domestic and international operating environment. This approach to strategic risk assessment was applied for the first time in the 2011 strategy seminar.

Total financial risks

In the Bank's organisation, the monitoring and reporting of total financial risks in the balance sheet has been entrusted to the risk control division of the Administration department, which is responsible for assessment, analysis and management of portfolio risks. For a more detailed discussion of the total financial risks in the balance sheet, see page 87–88.

Operational risks

The risks of the Bank's core operative functions have mainly been assessed against set objectives and their achievement. However, the damage, loss and reputational aspects could be applied in the assessment of the risks related to systems and security.

The assessment highlighted the risks, recognised in the Bank's processes and practices, as well as the key person and key competency risks. In 2011, several of the Bank's departments and core processes reported that Europe's sovereign debt crisis makes banks susceptible to new risk. At worst, the risks could compromise the banks' credibility and independence.

The mandate of the risk committee was extended to cover monitoring of the scope and nature of the management of operational risk. The task of the committee is to evaluate the Bank's level of operative risk management and make recommendations on development of risk management procedures.

Personnel

The Bank of Finland's human resources management focuses on good management, competence utilisation across departments, competence augmentation through job rotation, on generating a motivating and creative working environment and measuring performance according to set objectives.

The Bank of Finland performs its employer role in an ethically sustainable, egalitarian and equitable manner, maintaining the conditions for a modern and wise learning organisation. The Board of the Bank of Finland accepted the Bank's and FIN-FSA's joint Equality Working Group's proposals for the revised Equality Plan, in which special consideration is paid to the harmonisation of working life and family life and gender proportionality in recruitment and managerial appointments.

An employee satisfaction survey is conducted every other year to monitor job satisfaction in the Bank. In the 2011 the job satisfaction index (JSI) matched the benchmark of expert organisations. The points perceived as improving job satisfaction included clarity of the strategic objectives, equality and egalitarian treatment of various personnel groups as well as information flow and the functionality of the organisation. The leadership index, measured annually, met its target levels better this year than that of expert organisations, on average.

At the end of 2011, the Bank of Finland had 420 employees. Of the total staff, 57% held expert positions. The number of staff in attendance declined over the year by 4.8%. Since joining the EMU, the Bank's headcount has been reduced by 44% (Chart 19), reflecting retirements and a tight recruitment policy. The Bank of Finland's strategic objective is to be one of the most efficient EU central banks.

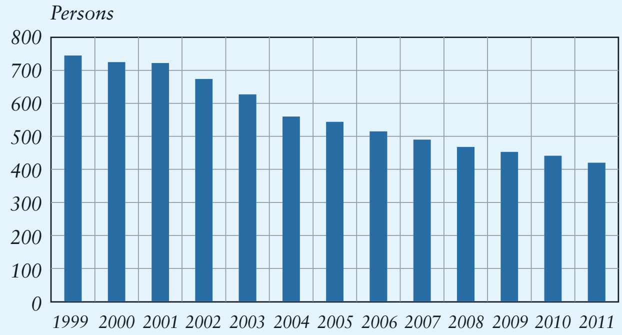
In 2011, 10 persons retired from the Bank, 17 left on expiry of their fixed-term contract and 14 left to take up employment with other organisations. There were 18 external appointments in all in 2011. The main emphasis, when filling vacancies that have come up in the Bank has been on internal recruitment.

The FIN-FSA's headcount at the end of the year amounted to 208 staff, with 75% in expert positions.

Labour market issues

The Bank's collective civil service agreement concluded in 2010 is valid from 1 October 2010 to 29 February 2012. In 2011 the general pay rise was 1.2%. Fixed performance-related pay

Chart 19.
Changes in headcount, 1999–2011



Source: Bank of Finland.

Table 5.
Human resource management highlights[1]

	2010	2011
Staff size		
Head count, Bank of Finland	441	420
Head count, Financial Supervisory Authority	209	208
Man years, Bank of Finland	470	446
Turnover rate for those leaving the Bank's service	9%	10%
Turnover rate for those entering the Bank's service	6%	4%
Internal mobility	11%	8%
Number of newly retired employees	21	10
Average effective retirement age	59 yrs	60 yrs
Number of pensions currently paid[2]	1,127	1,158
Staff structure		
Average staff age	45 yrs	46 yrs
Proportion of experts and superiors	67%	66%
Proportion of women	49%	49%
Education level index[3]	5.8	5.8
Salaries and bonuses		
Salaries in relation to market salaries[4]	98%	99%
Fixed increases in pay	1%	2.1%
General increase	1%	1.2%
Performance-based increase	–	0.9%
Bonuses as a proportion of payroll	0.50%	0.35%
Average pay for women / average pay for men	99%	100%
Pensions		
Pensions paid[5]	EUR 22 m	EUR 23 m
Competence		
Training costs/payroll	3.6%	2.7%
Training days/man-year	3.3	3.4
Wellness at work		
Absence rate	2.7	2.9
Employee satisfaction index	–	3.4

1 *Figures refer to Bank of Finland, unless otherwise mentioned. Figures referring to the Financial Supervisory Authority are published in the FIN-FSA Annual Report.*
2 *Includes pensions paid to the retired employees of the FIN-FSA.*
3 *Education level index is calculated from the basic level of education of staff. The index varies between 1 and 8.*
4 *The Bank of Finland's (incl. FIN-FSA's) reference group in the HAY market salary survey is made up of organisations representing the banking and financial sectors, public sector, and industrial and service sectors. The Bank of Finland's remuneration policy is targeted at the median level of the HAY market salary survey for all organisations (basic salary + benefits).*
5 *Includes pensions paid to the retired employees of the FIN-FSA.*

rises represented 0.9% of the negotiated pay rise. On 1 January 2011 there was a structural pay increase of 0.31% and on 1 November 2011 of 0.5 % of the departments' payrolls.

In 2011, working groups were set up in connection with the collective bargaining negotiations to review the practices for fixed-term appointment of permanent staff members. On the basis of the working group's findings, the Board of the Bank of Finland made specifications to the scale of how the practices are implemented and to the employee's position once the fixed-term contract is over.

The Bank of Finland and the Financial Supervisory Authority personnel, along with their families, were invited to an open doors day in the Bank's head office, in April 2011. A magician kept the guests entertained in the staff restaurant.

Photo: Peter Mickelsson.

Budget and operative costs

Table 6.
Budget for the Bank of Finland, EUR m

	Outturn 2011	*Budgeted 2012*
1. Operating expenses and income		
EXPENSES		
Staff expenses	*33.9*	*34.2*
Pension fund contributions	*30.5*	
Staff-related expenses	*2.9*	*4.1*
Other expenses	*21.7*	*25.2*
DEPRECIATION	*7.9*	*8.2*
Total	***96.9***	***71.7***
Banknote acquisition costs	*4.0*	*4.5*
Cash depot system	*0.6*	*1.0*
Banking service expenses	*4.0*	*4.7*
Total operating expenses	***105.5***	***81.9***
INCOME		
Banking service income	*2.8*	*2.9*
Real estate	*9.4*	*10.3*
Other income	*0.5*	*0.1*
Services to FIN-FSA	*2.7*	*2.8*
Total income	***15.4***	***16.1***
NET	***90.1***	***65.8***
2. Investment		
Real estate investment	*3.2*	*2.2*
Head office premises	*1.0*	*0.8*
Vantaa premises	*1.7*	*1.1*
Other premises	*0.5*	*0.3*
IT-equipment and software	*4.8*	*5.9*
Money handling machines	*0.1*	*0.2*
Security equipment	*0.6*	*1.2*
Other	*0.1*	*0.1*
Total investment	***8.8***	***9.6***

Totals/sub-totals may not add up because of rounding.

The cost efficiency of the Bank of Finland's operations is promoted by the objectives-driven Budgetary and Staffing Framework, efficient acquisitions procedures for goods and services and effective monitoring procedures. The budgetary framework covers planning of direct staff expenses, staff-related expenses, real estate, IT and other costs. In autumn 2011 the Bank's budget for the period 2012–2014 was drawn up and, of these, the Board has ratified the budget for 2012. The budgets for 2013–2014 are to be ratified at a later date. Efficient tender procedures and framework agreements have enabled the Bank to manage their operative costs and meet the budgetary framework operative cost objectives. The Board of the Bank of Finland evaluates how well the budget has been achieved every quarter while the supervisors' budgetary situation is monitored on a real-time basis, through the Bank's reporting system. The Bank of Finland Board also ratified the budget drawn up for the Financial Supervisory Authority.

Bank of Finland's budget

In 2011, the Bank of Finland's operating expenses totalled EUR 105.5 million (the previous year expenses totalled EUR 83.1 million). Operating expenses include a contribution of EUR 30.5 million to the Bank's pension fund. Budgeted operating income amounted to EUR 15.4 million. The Bank of Finland's net operating expenses totalled EUR 90.1 million (the previous year's expenses totalled EUR 68.7 million).

Investment expenses amounted to EUR 8.8 million in 2011. Investment expenditure on renovations totalled EUR 3.2 million. The majority of real estate investments concerned the premises in Vantaa. Other long-term acquisitions totalled EUR 5.6 million.

In respect of other costs, the most notable budgeted increases relate to purchases of services, use and licence fees and real estate costs. Other notable budgetary items relate to the costs incurred as the end of the obligatory markka redemption period draws near and the increased traffic exchanging markka for euro as well as banknote acquisition costs. With falling staff numbers, staff expenses are estimated to decrease slightly. In 2012, investment expenditure is estimated at EUR 9.6 million, with the majority relating to Vantaa premises and IT equipment and software.

Pension fund's budget

The pension fund's operating expenses for 2011 totalled EUR 25.4 million. Pensions paid (EUR 22.7 million) was the largest cost item. Operating income amounted to EUR 44.8 million, including the pension fund contribution of EUR 32.0 million.

The pension fund's expenses are estimated to increase in the three coming years, which is largely due to growth in pensions paid.

Investment expenditure arising from the renovation of pension fund premises totalled EUR 0.3 million in 2011.

Table 7.
Budget for the Bank of Finland's pension fund, EUR m

	Outturn 2011	*Budgeted 2012*
1. Operating expenses and income		
EXPENSES		
Staff expenses	0.1	0.2
Pension fund activities expenses	0.5	0.6
Pension fund real estate espenses	0.9	0.9
DEPRECIATION	1.2	1.2
PENSIONS		
Pensions paid	22.7	24.3
Total expenses	***25.4***	***27.2***
INCOME		
Employment pension contribution	9.8	9.8
Pension fund contributions	32.0	
Rents	1.1	1.2
Internal rents	1.9	2.0
Total income	***44.8***	***13.0***
NET	***19.4***	***–14.2***
2. Investment		
Real estate of the pension fund	0.3	0.3
Total investment	***0.3***	***0.3***

Totals/sub-totals may not add up because of rounding.

Table 8.
Budget for the Financial Supervisory Authority, EUR m

	Outturn 2011	*Budgeted 2012*
1. Operating expenses and income		
EXPENSES		
Staff expenses	*18.5*	*19.2*
Staff-related expenses	*0.9*	*1.0*
Other expenses	*3.9*	*4.1*
DEPRECIATION	*0.1*	*0.4*
SERVICES FROM THE BANK OF FINLAND	*2.7*	*2.8*
Total operating expenses	***26.1***	***27.5***
FUNDING OF OPERATIONS		
Supervision fees	*23.5*	*23.9**
Processing fees	*1.0*	*1.0*
Bank of Finland contribution to funding	*1.3*	*1,4*
Surplus/deficit transferred from last year	*2.9*	*2.6*
Total income	***28.7***	***28.9***
Surplus transferred to next year	*2.6*	*1.4*

Totals/sub-totals may not add up because of rounding.
** supervision fees finalised after drawing up the budget*

Renovation expenditure in 2012 is estimated at EUR 0.3 million.

The pension fund's activities are presented in the fund's own annual report.

Financial Supervisory Authority's budget

EUR 26.1 million was used in expenditure in 2011. Staff expenses include a contribution of EUR 1.5 million paid to the pension fund. Funding of operations amounted to EUR 28.7 million. Operating income is estimated at EUR 24.5 million, of which the Bank of Finland's contribution to funding accounts for EUR 1.3 million. The surplus for the period was EUR 2.6 million. The surplus will be taken into account in the following accounting period, when setting the supervisory and processing fees. Investment expenditure totalled EUR xx million.

Operating expenses for 2012 are estimated at EUR 27.5 million. Operating income is estimated at EUR 28.9 million, of which the Bank of Finland's contribution to funding accounts for EUR 1.4 million. Investment expenditure is estimated at EUR 0.5 million.

Financial Supervisory Authority's operations are presented in the authority's own annual report.

Environment

The Bank of Finland ensures that it meets its environmental responsibilities through measures such as improving energy consumption and other material efficiencies. Environmental matters are systematically monitored in the Bank's daily activities through the application of the Eco-Management and Audit Scheme (EMAS), an EU regulation-based scheme. In line with EMAS guidelines, the Bank of Finland pays attention to meeting regulatory requirements, identification of environmental impact of the Bank's various operations and risk prevention, staff training and clear definition of areas of responsibility, extensive documentation of activities and practices as well as continuous improvement of the organisations' environmental performance.

The Bank monitors the environmental effects from its operations using two environmental performance indicators that are proportionate to operating expenses: the relative amount of carbon dioxide emissions and the total amount of waste with the objective of reducing the relative volume of both. In 2011, for every thousand euro of operating expenses, the Bank created 1.67 kg of waste and 72.49 kg of CO2 emissions. In 2010, the equivalent volumes were 1.77 kg of waste and 80 kg of CO2 emissions. Of the total waste, office paper waste was down in volume by close on half over the previous year. A milder year meant that heating costs were reduced in the Bank's facilities by 15%.

The main environmental impact of the Bank of Finland's activities arises from heat and electricity consumption. The Bank's environmental performance was enhanced by installing a number of motion sensor light switches. Heat generated by the Bank's condensers is recycled back into the heating system. The Bank's air conditioning equipment has been renewed meaning that environmentally damaging freon is no longer used. Also, the increased use of cloud computing has had an impact on IT

Table 9.
Bank of Finland's environmental performance

	Volume 2009	2010	2011
Electric energy consumption (MW)	*21,470*	*10,798*	*11,537*
Heat energy consumption (MW)	*14,430*	*14,029*	*11,510*
Water consumption (m^3)	*38,680*	*41,412*	*27,334*
Waste (ton)	*168*	*164*	*157*
Office paper and publications consumption (ton)	*37*	*40*	*40*
CO_2 emission from business trips (ton)	*1,810*	*1,948*	*1,912*
CO_2 emission balance (ton)	*9,540*	*7,420*	*6,829*

Source: Bank of Finland.

technology energy consumption. Additionally, an increase in the use of mobile work station equipment has had an impact on the level of paper consumption in the Bank's offices. Print runs of the paper versions of Euro & talous, and the English equivalent the Bank of Finland Bulletin, were cut back from seven publications a year to five. There was an increased uptake in the use of electronic Christmas greetings cards and similarly the use of paper Christmas cards fell to a third of the previous year's volume. From the point of view of climate impact, the Bank has contracted to purchase carbon neutral postal deliveries, which has an additional positive effect on emissions. On average, emissions from the Bank's vehicles were reduced and the Bank acquired its first vehicle with a bio fuel cell for making deliveries. The service provider of the Bank's head office staff restaurant was able to stay within the strict daily food waste limits imposed on them in their contract with the Bank.

In August 2011, a symposium on the economic history of the Baltic area was arranged in Turku.

Photo: Peter Mickelsson.

Total risk exposure

Central banking always entails risks, which are involved in the management of financial assets, monetary policy operations and operational activities. Risks may also arise from market changes, disruptions and exceptional conditions. Procedures for managing and preparing for risks aim at ensuring that the performance of central banking tasks is not jeopardised under any circumstances.

In 2011, risks related to Bank of Finland financial assets increased against the backdrop of deteriorating sovereign debt markets. In addition, securities purchases by the ECB and the Eurosystem as a whole, with a view to ensuring monetary policy transmission, increased the Bank of Finland's risks. Assessment of the risks overall includes all these risks related to the Bank's own financial assets and Eurosystem operations.

The risks arising from the management of Bank of Finland financial assets and monetary policy operations can be divided into market and credit risks. Market risks include risks stemming from changes in interest rates and exchange rates. For the balance sheet, the most significant risk is caused by exchange rate volatility. Changes in the price of gold are also reflected in market risk, but owing to large revaluation accounts the assessment of gold price risk is separated from other risk assessment.[1] Credit risk includes risks related to changes in the debtor's creditworthiness or difficulties in servicing payments.

As a rule the Bank of Finland is responsible, according to its relative share based on the capital allocation key, for risks involved in the Eurosystem's monetary policy refinancing operations and purchase programmes related to monetary policy.[2] For this reason, the total Eurosystem balance sheet needs to be examined in order to identify the impact of the operations on the Bank of Finland's balance sheet.

In refinancing operations, counterparties are required to submit adequate and separately defined collateral, which are marked to market on a daily basis and are subject to valuation haircuts. As regards the Covered Bond Purchase Programmes, the bonds normally have the highest possible credit rating and are backed by a collateral pool. Preparing for risks related to the Securities Markets Programme, in turn, means ensuring that adequate capital buffers in the balance sheet are in place to provide coverage. The size of the operations and purchase programmes at the end of 2011 and the Bank of Finland's share, according to the capital key, of the exposures are presented in table 10.

Balance sheet risks are assessed using well-established market and credit risk models and different scenarios and balance sheet simulations. Risk

[1] In the Financial statements section 'Notes on risk management' (p. 122), risks related to gold are included in the overall assessment. The way of presentation in the Notes enables comparison with the assessment in the 2010 Annual Report.

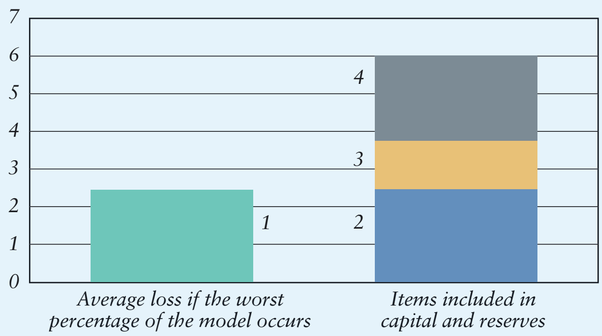
[2] Monetary policy refinancing operations, the Covered Bond Purchase Programmes and the Securities Markets Programme are discussed in greater detail in the Annual Report section on the implementation of monetary policy.

Table 10.
Monetary policy operations at the end of 2011

EUR m	*Monetary policy refinancing*	*Covered bond purchase*	*Securities Markets Programme*
Eurosystem	*863,568*	*61,907*	*211,947*
Bank of Finland's contribution	*15,475*	*1,007*	*3,479*

Source: Bank of Finland

Chart 20.
Bank of Finland's total risk exposure, capital and reserves excl. gold price risk and gold revaluation accounts
EUR bn



1. *Market and credit risk*
2. *Provisions*
3. *Revaluation accounts*
4. *Capital and reserves, excl. provisions and revaluation accounts*

Source: Bank of Finland.

assessment focuses on worst-case scenarios. Although the models are well-established, they fail to fully capture total risk exposure. Models use standard assumptions and, accordingly, the magnitude of risk assessments may vary depending on chosen assumptions. Of the outcomes of the model, the worst percentage is taken under review.

With all risks to the Bank of Finland's balance sheet added up excluding gold, total risk exposure is estimated at about EUR 2.5 billion in annual terms. The Bank of Finland's primary capital and reserve fund total EUR 2.2 billion, provisions (excl. pension provision and provision for ESCB monetary policy risks) EUR 2.5 billion and revaluation accounts (excluding revaluation account for gold) EUR 1.3 billion (Chart 20). Gold price risk assessed in a similar fashion, is about EUR 0.9 billion in annual terms, compared with the gold revaluation account of EUR 1.5 billion. All items incorporated in capital and reserves – including the gold revaluation account – amount to EUR 7.5 billion. A more detailed analysis of the structure of the balance sheet is provided in Financial statements.

Central banks may incur losses in safeguarding the stability and functioning of the financial system. This makes it necessary for the Bank of Finland to prepare for risks in its balance sheet by ensuring balance sheet strength. Maintenance of a strong balance sheet means reducing risks associated with the investment reserves, whenever necessary, and accumulating provisions and capital resources. Risks to the Bank of Finland's balance sheet have increased along with the unfolding of the financial crisis. Provisions and capital in the balance sheet are adequate to cover identified risks. All balance sheet items included in capital and reserves ensure good risk absorption capacity for unforeseen risks, too.

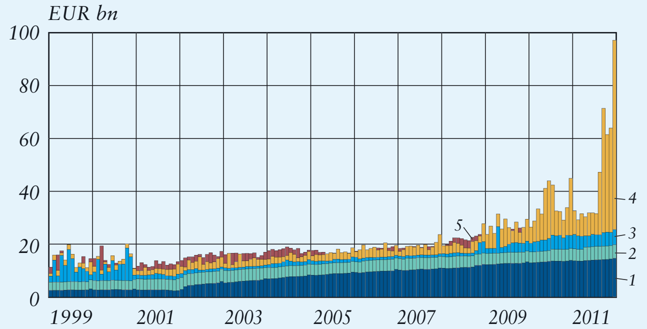
Box 7.

Deficit and surplus positions in payment system traffic between euro area central banks

During the crisis in recent years, large stocks of assets or liabilities have accumulated in the euro area central banks' balance sheets via payment transactions. Developments in the Bank of Finland balance sheet have also been exceptional in this respect. During the year under review, as the Bank of Finland celebrated its 200 years of existence, its balance sheet expanded in the course of the autumn, reaching its highest ever level in the Bank's history. As the balance sheet size has usually stayed between 10% and 15% of Finland's GDP, and during periods of war at 25% to 30%, the Bank of Finland's balance sheet total grew to even approximately 50% of GDP in December 2011 (Charts A and B).

In a monetary union, national central banks act as their respective countries' financial centres at the same time as conducting operations related to the single monetary policy. The effects of these operations are normally reflected in the central banks' balance sheets. Additionally, euro area central banks have mutual positions, such as those included in intra-euro area payment transmission. A key element of euro area-wide activities is, in fact, the processing of intra-area payments mainly via national central banks. This broadly-based, routine

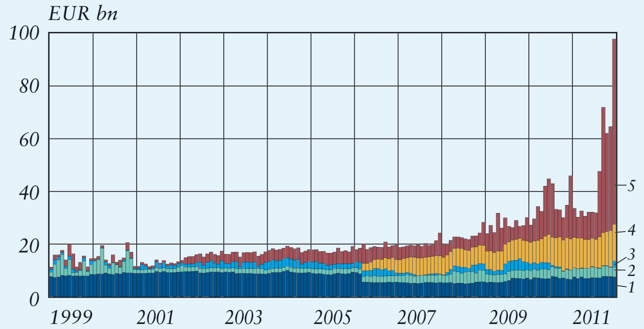
Chart A.
Liabilities in Bank of Finland's balance sheet



1. Banknotes in circulation
2. Provisions, capital and reserves
3. Other liabilities
4. Liabilities to euro area credit institutions
5. Intra-Eurosystem liabilities

Source: Bank of Finland.

Chart B.
Assets in Bank of Finland's balance sheet



1. Gold and claims denominated in foreign currency
2. Other claims
3. Claims on euro area credit institutions
4. Securities
5. Intra-Eurosystem claims

Source: Bank of Finland.

payment transmission between euro area countries generally poses no significant challenge for central banking and related risk management.

The technical IT platform for payments, TARGET2, is an EU-wide automated real-time payment transfer system primarily used by euro area countries. Debtor and creditor relationships that emerge within the system are not legally between the national central banks, but rather the counterparty is the European Central Bank.
A centralised, freely accessible cross-border payment system is an indispensable element of the functioning of a monetary union.

Eurosystem refinancing operations also have an impact on payment transmission. The Eurosystem does not allocate credit on a country-by-country basis, but only imposes general credit terms and conditions. How liquidity is distributed and how payments between central banks are broken down depends on demand from credit institutions in each country. During the crisis, the Eurosystem has supplied unlimited liquidity at its policy rate to credit institutions. Even so, liabilities can only arise if there are adequate eligible collateral assets to cover such credit operations.

In the first years following changeover to the euro, payment transfers mainly evolved in line with ordinary balance of payment fluctuations. Worthy of note were abundant capital flows from countries with current account surpluses into countries with current account deficits. Accordingly, payments in net terms remained relatively small. Several central banks, including the Bank of Finland, were close to balance in respect of payments.

Countries that ended up with economic and financial problems during the crisis have experienced strong payment shortfalls, as abundant private capital inflows came to a standstill and partly even reversed. Large short-term investments have also moved across euro area borders. Meanwhile, strong investment flows have turned towards the financial markets of stable euro area countries. Owing to disruptions in interbank market activity, financially sound banks have received more deposits and monetary financial institutions (MFIs) have also otherwise improved their liquidity via short-term borrowing. These in turn have deposited their funds with the central bank. The German Bundesbank's claim on the ECB, for example, has risen to about 20% of German GDP. The Bank of Finland's claim has occasionally been even larger in relative terms.

On the other hand, the Irish central bank's liability vis-à-vis the Eurosystem has expanded to even close to the country's annual nominal GDP. Greek and Portuguese central bank liabilities have been smaller. The liabilities of the Spanish and Italian central banks did not increase until autumn 2011, following heightened speculation over the countries' sovereign debt markets.

The situation is peculiar in that, despite the financial relationships between the central banks being 'book' relationships within the Eurosystem, they also illustrate – via the ECB – genuine liabilities between euro area economies.

For individual central bank risks, however, it is crucial that the Eurosystem operates as a broadly-based economic entity. Risk sharing related to, and distribution of income from, monetary policy operations are based on the capital key, ie the central banks' shares in the Eurosystem. The Bank of Finland accounts for about 1.8% of entire Eurosystem risks and income.

Exceptional deficit and surplus positions in payments are a problem related to times of crisis. Consequently, along with other suggestions, collateral requirements or ceilings for such positions have been proposed. Restrictions are impossible, as prevention of payments would conflict with the basic principle of a monetary union. The only way of removing the problem is to address the root causes of the imbalances: government debt accumulation, banks' weak financial condition and countries' competitiveness. Remedying these is a slow process, and large TARGET2 positions are therefore likely to still remain in place for a long time.

Financial statements

Balance sheet, EUR million

		31 Dec 2011	31 Dec 2010
ASSETS			
1	***Gold and gold receivables***	***1,918***	***1,664***
2	***Claims on non-euro area residents denominated in foreign currency***	***5,886***	***5,223***
	Receivables from the International Monetary Fund	*1,967*	*1,815*
	Balances with banks and security investments, external loans and other external assets	*3,919*	*3,408*
3	***Claims on euro area residents denominated in foreign currency***	***628***	***712***
4	***Claims on non-euro area residents denominated in euro***	***1,946***	***1,662***
5	***Lending to euro area credit institutions related to monetary policy operations denominated in euro***	***2,311***	***50***
	Main refinancing operations	*10*	*–*
	Longer-term refinancing operations	*2,301*	*50*
6	***Other claims on euro area credit institutions denominated in euro***	***40***	***1***
7	***Securities of euro area residents denominated in euro***	***13,889***	***11,668***
	Securities held for monetary policy purposes	*4,637*	*2,203*
	Other securities	*9,253*	*9,466*
8	***Intra-Eurosystem claims***	***70,348***	***23,921***
	Participating interest in ECB	*120*	*99*
	Claims equivalent to the transfer of foreign reserves	*722*	*722*
	Claims related to TARGET2 and correspondent accounts (net)	*66,008*	*19,686*
	Net claim related to the allocation of euro banknotes within the Eurosystem	*3,497*	*3,414*
9	***Other assets***	***1,171***	***1,090***
	Euro area coins	*25*	*22*
	Tangible and intangible fixed assets	*165*	*171*
	Other current assets	*569*	*551*
	Other	*413*	*346*
	Total assets	***98,138***	***45,990***

Totals/sub-totals may not add up because of rounding.

	31 Dec 2011	31 Dec 2010
LIABILITIES		
1 Banknotes in circulation	***14,649***	***13,880***
2 Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	***71,697***	***21,696***
Current accounts (covering the minimum reserve system)	*1,657*	*9,383*
Overnight deposits	*52,540*	*9,113*
Fixed-term deposits (liquidity-absorbing fine-tuning operations)	*17,500*	*3,200*
3 Liabilities to other euro area residents denominated in euro	***836***	***262***
4 Liabilities to non-euro area residents denominated in euro	***782***	***1,021***
5 Liabilities to euro area residents denominated in foreign currency	***0***	***0***
6 Liabilities to non-euro area residents denominated in foreign currency	***153***	***23***
7 Counterpart of special drawing rights allocated by the IMF	***1,412***	***1,377***
8 Intra-Eurosystem liabilities	***76***	***33***
9 Other liabilities	***178***	***151***
10 Revaluation account	***2,806***	***2,274***
11 Provisions	***3,032***	***2,814***
12 Capital and reserves	***2,262***	***2,175***
Primary capital	*841*	*841*
Reserve fund	*1,421*	*1,334*
13 Profit for the financial year	***254***	***283***
Total liabilities	***98,138***	***45,990***

Profit and loss account, EUR million

		1 Jan–31 Dec 2011	1 Jan–31 Dec 2010
1	*Interest income*	763	597
2	*Interest expense*	–170	–71
3	*NET INTEREST INCOME*	592	526
4	*Foreign exchange rate differences*	5	221
5	*Securities price differences*	63	119
	Valuation losses related to currencies and securities	–59	–50
6	*Change in foreign exchange rate and price difference provision*	–9	–290
	NET RESULT OF FINANCIAL OPERATIONS, WRITE-DOWNS AND RISK PROVISIONS	592	526
7	*FEES AND COMMISSIONS INCOME AND EXPENSE*	–0	–1
8	Net result of pooling of monetary income	–75	–33
9	Share in ECB profit	3	26
10	Provisions in respect of monetary policy operations	22	32
11	Other central banking income	15	9
	CENTRAL BANKING PROFIT	557	560
12	*Other income*	35	34
	Operating expenses	–125	–102
13	Staff costs	–51	–51
14	Pension fund contribution	–32	–10
15	Administrative expenses	–29	–28
16	Depreciation of fixed assets	–8	–7
17	Banknote procurement costs	–4	–6
18	Other expenses	–1	0
	OPERATING PROFIT	467	491
	Profit for the pension fund	19	24
19	Income of the pension fund	63	58
20	Expenses of the pension fund	–44	–34
21	*Changes in provisions*	–232	–232
22	*PROFIT FOR THE FINANCIAL YEAR*	254	283

Appendices to the financial statements, EUR million

	31 Dec 2011	31 Dec 2010
Shares and other interests, nominal value		
Bank for International Settlements (BIS)[1]	22.4 (1.96%)	22.4 (1.96%)
Shares in housing companies	2.5	2.8
Other shares and interests	0.0	0.0
Total	**24.9**	**25.2**
Bank of Finland's liability share in the APK fund	**0.2**	**0.2**
Liability arising from pension commitments		
Bank of Finland's pension liability[2]	543.7	543.3
– of which covered by reserves	543.9	525.8
Customer service office		
Deposits	23.8	22.6
Loans	3.7	3.9

[1] In parentheses, the Bank of Finland's relative holdings of the BIS shares in circulation.
[2] Pension liability excludes indexation of pensions and paid-up policies in 2012.

The Bank of Finland's real estate

Building	*Address*	*Year of completion*	*Volume m³ (approx.)*
Helsinki	*Rauhankatu 16*	*1883/1961/2006*	*52,100*
	Rauhankatu 19	*1954/1981*	*40,500*
	Snellmaninkatu 6[1]	*1857/1892/2001*	*23,600*
	Snellmaninkatu 2[1]	*1901/2003*	*3,200*
	Ramsinniementie 34	*1920/1983/1998*	*4,600*
Kuopio	*Puutarhakatu 4*	*1993*	*13,000*
Oulu	*Kajaaninkatu 8*	*1973*	*17,200*
Tampere	*Hämeenkatu 13 b*[1]	*1942*	*36,000*
Vantaa	*Turvalaaksontie 1*	*1979*	*324,500*
Inari	*Saariseläntie 9*	*1968/1976/1998*	*6,100*

[1] *Transferred to the ownership of the Bank of Finland's pension fund from the beginning of 2002.*

The Board proposes to the Parliamentary Supervisory Council that
EUR 69,483,546.95 of the profit of EUR 254,483,546.95
be transferred to the reserve fund according to section 21,
subsection 2 of the Act on the Bank of Finland and
that the remaining EUR 185,000,000
be made available for the needs of the State.

Helsinki, 22 February 2012

THE BOARD OF THE BANK OF FINLAND

Erkki Liikanen, Chairman

Pentti Hakkarainen Seppo Honkapohja

. /. Arno Lindgren

Accounting conventions

1. General accounting conventions

The Bank of Finland observes the economic-based accounting principles and techniques adopted by the Governing Council of the ECB, and the Bank's annual accounts are drawn up in accordance with these harmonised principles. In accordance with section 11 of the Act on the Bank of Finland, the Parliamentary Supervisory Council confirms, on the proposal of the Board, the principles applied in drawing up the annual accounts.

The Bank of Finland's profit and loss account also comprises incomes and expenses of the Bank's pension fund and of the Financial Supervisory Authority. The pension fund's investment portfolio is valued monthly at the market price of the last day of the month.

2. Revaluation of items denominated in foreign currency and gold

Items denominated in foreign currency and gold are converted into euro at the exchange rate prevailing on the balance sheet date. Foreign currency-denominated items have been revaluated on a currency-by-currency basis. Revaluation differences related to foreign exchange rate movements and securities price movements are treated separately. Unrealised gains are recorded in the revaluation account. Unrealised losses are taken to the profit and loss account if they exceed previous corresponding unrealised revaluation gains registered in the revaluation account. Unrealised losses taken to the profit and loss account are not reversed against any future unrealised gains in subsequent years. In the case of gold, no distinction is made between price and exchange rate differences; rather, a single revaluation is made. Realised gains and losses related to foreign exchange rate movements during the financial year are calculated on the basis of the daily net average cost method. Foreign exchange rates used in the financial statements are presented in the table below.

Currency	*2011*	*2010*
US dollar	*1.2939*	*1.3362*
Japanese yen	*100.2000*	*108.6500*
Australian dollar	*1.2723*	*1.3136*
Norwegian krone	*7.754*	*7.8000*
Danish krone	*7.4342*	*7.4535*
Swedish krona	*8.9120*	*8.9655*
Swiss franc	*1.2156*	*1.2504*
Pound sterling	*0.83530*	*0.86075*
Canadian dollar	*1.3215*	*1.3322*
Special Drawing Rights (SDRs)	*0.8427*	*0.8642*
Gold	*1,216.864*	*1,055.418*

3. Valuation and amortisation of securities

Income and expenses are recognised in the period in which they are earned or incurred. Realised income and expenses are entered in the profit and loss account. The difference between the acquisition price and nominal value of securities is entered as income or expense over the maturity of the security. Gains and losses related to securities price movements have been calculated using the average cost method.

Unrealised gains are recorded in the revaluation account. Unrealised losses are taken to the profit and loss account if they exceed previous corresponding unrealised revaluation gains registered in the revaluation account. Unrealised losses taken to the profit and loss account are not reversed against any future unrealised gains in subsequent years. Both euro-denominated and foreign currency-denominated securities are valued on a security-by-security basis. If unrealised losses are entered in the profit and loss account in respect of a security or a currency, the average price of the security or the net average rate of the currency is adjusted correspondingly before the beginning of the next financial year.

Reverse repurchase agreements, or reverse repos, are recorded as collateralised inward deposits on the assets side of the balance sheet. Repurchase agreements, or repos, are recorded as collateralised outward loans on the liabilities side of the balance sheet. Securities sold under repurchase agreements remain on the Bank's balance sheet.

The pension fund's investment portfolio is valued monthly at the market price of the last day of the month, reported by external portfolio managers.

Marketable securities (other than those classified as held-to-maturity) and similar assets are valued either at the mid-market prices or on the basis of the relevant yield curve prevailing on the balance sheet date, on a security-by-security basis. For 2011, mid-market prices on 30 December 2011 were used.

Marketable securities classified as held-to-maturity, non-marketable securities and illiquid equity shares are all valued at amortised cost subject to impairment.

4. Accounting conventions relating to intra-ESCB balances

Transactions between the national central banks (NCBs) of EU countries are primarily processed via TARGET2, the Trans-European Automated Real-time Gross settlement Express Transfer system. These transactions give rise to bilateral balances in accounts held between EU central banks. These bilateral balances are novated to the ECB daily, leaving each NCB with a single net bilateral position vis-à-vis the ECB only.

5. Valuation of fixed assets

As from the beginning of the financial year 1999, fixed assets have been valued at acquisition price less depreciation. Depreciation is calculated on a straight-line basis over the expected economic lifetime of an asset, starting from the second calendar month following acquisition.

The counteritem of buildings and land capitalised in the 1999 balance sheet at market prices is the revaluation account. Depreciation in respect of buildings and land has been entered by adjusting the revaluation account downwards so that depreciation does not affect the Bank's income or expense.

The economic lifetimes of assets are calculated as follows:

- computers, related hardware and software, and motor vehicles: 4 years
- machinery and equipment: 10 years
- buildings: 25 years.

Fixed assets with a value of less than EUR 10,000 are written off in the year of acquisition.

6. Banknotes in circulation

The ECB and the 17 euro area NCBs, which together comprise the Eurosystem, issue euro banknotes.[1] The total value of euro banknotes in circulation is allocated to the NCBs on the last banking day of each month in accordance with the banknote allocation key.[2] The ECB has been

[1] ECB decision of 13 December 2010, on the issue of euro banknotes (ECB/2010/29), OJ L 35, 9.2.2011, p. 26.

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

allocated a share of 8% of the total value of euro banknotes in circulation, whereas the remaining 92% has been allocated to NCBs according to the banknote allocation key. This is disclosed under the balance sheet liability item 'Banknotes in circulation'. The difference between the value of euro banknotes allocated to each NCB in accordance with the banknote allocation key and the value of euro banknotes that it actually puts into circulation also gives rise to remunerated intra-Eurosystem balances. These claims or liabilities, which incur interest,[3] are disclosed under the sub-item 'Intra-Eurosystem claims/ liabilities: Net claim/ liability related to the allocation of euro banknotes within the Eurosystem'. In the Bank of Finland's balance sheet, the item is on the asset side.

The monetary income on euro banknotes is allocated in proportion to the NCBs' paid-up shares in the capital of the ECB. The interest income and expense on these balances is cleared through the accounts of the ECB and is disclosed under 'Net interest income'. The ECB's capital key is adjusted every five years and whenever a new Member State joins the European Union.

The income accruing to the ECB on the share of 8% of the total value of euro banknotes in circulation is generally distributed to the NCBs.[4]

7. Changes in accounting conventions

There were no changes in accounting conventions in the financial year 2011.

Key for subscription of the ECB's capital, 1 January 2011

	ESCB, %	Eurosystem, %		ESCB, %
Nationale Bank van België/ Banque Nationale de Belgique	2.4256	3.4666	*Българска народна банка (Bulgarian National Bank)*	0.8686
Deutsche Bundesbank	18.9373	27.06469	*Česká národní banka*	1.4472
Eesti Pank	0.179	0.25582	*Danmarks Nationalbank*	1.4835
Central Bank of Ireland	1.1107	1.58738	*Latvijas Banka*	0.2837
Bank of Greece	1.9649	2.80818	*Lietuvos bankas*	0.4256
Banco de España	8.304	11.86786	*Magyar Nemzeti Bank*	1.3856
Banque de France	14.2212	20.32457	*Narodowy Bank Polski*	4.8954
Banca d'Italia	12.4966	17.85981	*Banca Naţională a României*	2.4645
Central Bank of Cyprus	0.1369	0.19565	*Sveriges Riksbank*	2.2582
Banque centrale du Luxembourg	0.1747	0.24968	*Bank of England*	14.5172
Central Bank of Malta	0.0632	0.09032	***Subtotal for non-euro area NCBs***	***30.0295***
De Nederlandsche Bank	3.9882	5.69983		
Oesterreichische Nationalbank	1.9417	2.77503	***Total***	***100.0000***
Banco de Portugal	1.7504	2.50163		
Banka Slovenije	0.3288	0.46991		
Národná banka Slovenska	0.6934	0.99099		
Suomen Pankki – Finlands Bank	1.2539	1.79204		
Subtotal Eurosystem	***69.9705***	***100.0000***		

[3] ECB decision of 6 December 2001 on the allocation of monetary income of the national central banks of participating Member States from the financial year 2002 (ECB/2001/16).

[4] ECB decision of 6 November 2005 on the issue of euro banknotes (ECB/2005/11).

8. Monetary income

Monetary income accruing to NCBs in the performance of monetary policy functions in the ESCB is calculated and allocated to NCBs in accordance with the Statute and any decisions by the ECB's Governing Council.

Interim profit distribution
The Governing Council of the ECB has decided that the seigniorage income of the ECB, which arises from the 8 % share of euro banknotes allocated to the ECB, and the ECB's (net) income arising from securities purchased under the Securities Markets Programme (SMP) shall be due in full to the NCBs in the same financial year it accrues. The ECB shall distribute this income in January of the following year in the form of an interim distribution of profit.[5] The amount of the ECB's income on euro banknotes in circulation may be reduced in accordance with any decision by the Governing Council in respect of expenses incurred by the ECB in connection with the issue and handling of euro banknotes. Before the end of the year the Governing Council decides whether all or part of the ECB's income arising from SMP securities and, if necessary, all or part of the ECB's income on euro banknotes in circulation should be retained to the extent necessary to ensure that the amount of the distributed income does not exceed the ECB's net profit for that year.

The Governing Council may also decide to transfer all or part of the ECB's income arising from SMP securities and if necessary, all or part of the ECB's income on euro banknotes in circulation to a provision for foreign exchange rate, interest rate, credit and gold price risks.

[5] ECB decision of 25 November 2010 on the interim distribution of the income of the European Central Bank on euro banknotes in circulation and arising from securities purchased under the Securities Markets Programme (ECB/2012/24), OJ L 6, 11.1.2011, p. 35.

9. Pension fund

In 2001 the decision was made to create a pension fund in the Bank of Finland's balance sheet for the management of the Bank's pension liability. The purpose of this measure, which came into force from the beginning of 2002, is to ensure that the funds related to the coverage of the pension liability are invested in a lucrative manner. A separate annual report will be prepared on the pension fund of the Bank of Finland. The assets of the pension fund are recorded in the Bank of Finland's balance sheet item 'Other assets'.

The ECB guideline on accounting and financial reporting does not regulate accounting for the pension fund. The pension fund's investments are valued at market price, and revaluations are recognised in profit or loss. The fund's financial statements are drafted using market prices prevailing in the last day of the year. The pension fund's real estate is recorded in the balance sheet at value prevailing on transfer date less annual depreciation. If the balance sheet value of real estate has been covered by revaluation, the corresponding depreciation is recorded by reversing the revaluation so that depreciation has no impact on the pension fund's income or expense.

10. Recording of provisions

Provisions can be made in the annual accounts, if they are necessary for safeguarding the real value of Bank's funds or for smoothing out variations in profit and loss arising from changes in exchange rates or market value of securities.

Provisions can be made, as necessary, to cover the Bank's pension liabilities.

11. Off-balance sheet items

Gains and losses arising from off-balance sheet items are treated in the same manner as gains and losses arising from on-balance sheet items. Forward foreign exchange transactions are taken into account when the net average cost of a currency position is calculated.

Notes on the balance sheet

Assets

1. Gold and gold receivables

The Bank's holdings of gold total 1,576,476 troy ounces (1 troy ounce = 31.103 g). In the annual accounts, gold has been valued at market price. At the beginning of 1999 the Bank of Finland – and the other NCBs participating in the Eurosystem – transferred about 20% of its gold holdings to the ECB.

Gold	*31 Dec 2011*	*31 Dec 2010*
Holdings (troy ounces, million)	1.6	1.6
Price: euro per troy ounce	1,216.9	1,055.4
Market price (EUR m)	1,918.4	1,663.8
Change in market value (EUR m)	254.6	455.7

2. Claims on non-euro area residents denominated in foreign currency

The item consists of claims on non-euro area residents denominated in foreign currency and included in the Bank's foreign reserves, and holdings of special drawing rights (SDRs) allocated by the International Monetary Fund (IMF).

2.1 Receivables from the IMF

Breakdown of receivables from the IMF denominated in foreign currency

	31 Dec 2011		*31 Dec 2010*	
	EUR m	*SDR m*	*EUR m*	*SDR m*
Reserve tranche in the IMF	460.9	388.4	297.4	257.0
SDRs	1,327.6	1,118.7	1,380.0	1,192.5
Other receivables from the IMF	178.4	150.4	138.0	119.3
Total	***1,966.9***	***1,657.4***	***1,815.3***	***1,568.8***

EUR/SDR exchange rate in financial years 2010 and 2011

	2011	*2010*
End-March	0.90	0.89
End-June	0.90	0.83
End-September	0.86	0.88
End-December	0.84	0.86

Finland's quota in the IMF amounts to SDR 1,263.8 million. The reserve tranche is the part of the Bank's quota that has been paid to the IMF in foreign currency. Another part of the quota was formerly paid to the IMF in Finnish markka. The IMF has lent this part back to the Bank of Finland. The net effect of the Finnish markka quota on the Bank's balance sheet is zero, since the above-mentioned receivables and the liability are included in the same balance sheet item.

The Bank of Finland's SDR allocation amounts to EUR 1,327.6 million. The SDRs are reserve assets created and allocated by the IMF to its member countries. They are used in currency transactions as normal currency units. The value of 'Receivables from the IMF' changes on the basis of foreign exchange transactions between the member countries. In addition, its value is affected by interests earned and paid as well as remuneration on the Bank's claims in the IMF.

The Bank of Finland's receivables from the IMF total EUR 1,966.9 million.

In summer 2010, the Accounting and Monetary Income Committee (AMICO) of the ESCB made a decision on the treatment of SDR hedging trades which differs from the general currency-specific valuation principle. Sales of SDR component currencies made for hedging against the SDR exchange rate risk are regarded as reductive items in calculating the amount and market valuation of SDR items. Hence, such sales do not decrease the amount of component currencies and do not have an effect on the market valuation of the respective currencies.

2.2 Other claims on non-euro area residents denominated in foreign currency

This item includes foreign currency-denominated balances with banks and security investments, as well as external loans and other external assets.

Breakdown of claims on non-euro area residents denominated in foreign currency

	31 Dec 2011	31 Dec 2010
	EUR m	EUR m
Deposits	324.5	79.7
Coupon bonds	3,587.4	3,198.0
Discount papers	0.0	127.1
Other	7.0	2.9
Total	**3,918.9**	**3,407.7**

Currency breakdown of securities of non-euro area residents denominated in foreign currency

Currency	31 Dec 2011		31 Dec 2010	
	EUR m	%	EUR m	%
Pound sterling	517.2	14.4	547.9	16.5
US dollar	2,608.8	72.7	2,248.9	67.6
Japanese yen	461.4	12.9	528.3	15.9
Total	**3,587.4**	**100.0**	**3,325.1**	**100.0**

Maturity breakdown of securities of non-euro area residents denominated in foreign currency

Maturity	31 Dec 2011		31 Dec 2010	
	EUR m	%	EUR m	%
Up to 1 year	376.0	10.5	849.4	25.5
Over 1 year	3,211.3	89.5	2,475.7	74.5
Total	**3,587.4**	**100.0**	**3,325.1**	**100.0**

3. Claims on euro area residents denominated in foreign currency

This item consists of balances with banks, security investments and other claims on euro area residents denominated in foreign currency.

Breakdown of claims on euro area residents denominated in foreign currency

	31 Dec 2011	31 Dec 2010
	EUR m	EUR m
Deposits	196.0	32.9
Coupon bonds	437.8	675.8
Discount papers	0.0	0.0
Other	–5.7	2.8
Total	**628.1**	**711.6**

Currency breakdown of securities of euro area residents denominated in foreign currency

Currency	31 Dec 2011		31 Dec 2010	
	EUR m	%	EUR m	%
Pound sterling	131.7	30.1	161.1	23.8
US dollar	293.0	66.9	493.2	73.0
Japanese yen	13.1	3.0	21.4	3.2
Total	**437.8**	**100.0**	**675.8**	**100.0**

Maturity breakdown of securities of euro area residents denominated in foreign currency

Maturity	31 Dec 2011		31 Dec 2010	
	EUR m	%	EUR m	%
Up to 1 year	213.5	48.8	226.2	33.5
Over 1 year	224.3	51.2	449.6	66.5
Total	**437.8**	**100.0**	**675.8**	**100.0**

4 Claims on non-euro area residents denominated in euro

This item includes balances with banks outside the euro area, denominated in euro, coupon bonds and discount papers issued outside the euro area as well as euro-denominated receivables from the Bank for International Settlements (BIS).

Claims on non-euro area residents denominated in euro

	31 Dec 2011	31 Dec 2010
	EUR m	EUR m
Deposits	988.6	1,046.4
Coupon bonds	956.9	615.2
Discount papers	0.0	0.0
Other	0.3	0.0
Total	**1,945.8**	**1,661.5**

Maturity breakdown of securities of non-euro area residents denominated in euro

Maturity	31 Dec 2011		31 Dec 2010	
	EUR m	%	EUR m	%
Up to 1 year	219.6	22.9	164.0	27.0
Over 1 year	737.4	77.1	451.2	73.0
Total	**956.9**	**100.0**	**615.2**	**100.0**

5. Lending to euro area credit institutions related to monetary policy operations denominated in euro

This item consists of claims relating to monetary policy instruments used by the Bank of Finland to implement monetary policy as part of the Eurosystem. The item includes claims (+ interest) on Finnish credit institutions, and the amount recorded is determined by credit institutions' liquidity needs.

Main refinancing operations are liquidity-providing operations which are conducted weekly in the form of reverse transactions and executed through standard tenders. They play a pivotal role in fulfilling the objectives of Eurosystem's market operations and provide the bulk of refinancing to the banking sector. At the end of 2011 claims on main refinancing operations totalled EUR 10.0 million.

Longer-term refinancing operations are liquidity-providing transactions that are executed once a month in the form of reverse transactions and carried out through standard tenders. Claims on longer-term refinancing operations totalled EUR 2,301.0 million.

The Eurosystem's total claims on monetary policy operations amount to EUR 836,568 million, of which the Bank of Finland holds EUR 2,311 million on its balance sheet. In accordance with Article 32.4 of the Statute, any risks from monetary policy operations, if they were to materialise, should eventually be shared in full by the Eurosystem NCBs, in proportion to the prevailing ECB capital key shares.

Lending to euro area credit institutions related to monetary policy operations denominated in euro

	31 Dec 2011	31 Dec 2010
	EUR m	EUR m
Main refinancing operations	10.0	0
Longer-term refinancing operations	2,301.0	50.0
Total	**2,311.0**	**50.0**

6. Other claims on euro area credit institutions denominated in euro

This item consists of euro-denominated deposits and balances with euro area credit institutions. The balance sheet total for this item was EUR 40.3 million in the financial year 2011, compared with EUR 0.6 million in the previous year.

7. Securities of euro area residents denominated in euro

In order to report securities held for monetary policy purpose separately, the item 'Securities of euro area residents denominated in euro' has been divided into two sub-positions: 'Securities held for monetary policy purposes' and 'Other securities'.

7.1 Securities held for monetary policy purposes
As at 31 December 2011 this item consisted of securities acquired by the Bank of Finland within the scope of the covered bond purchase programmes (CBPP and CBPP2) and the securities markets programme.

Securities held for monetary policy purposes

	31 Dec 2011 EUR m	31 Dec 2010 EUR m	Change EUR m
Covered bond purchase programme (CBPP)	947.8	964.9	–17.1
Second covered bond purchase programme (CBPP2)	59.3	–	59.3
Securities Markets Programme	3,629.7	1,237.8	2,391.9
Total	**4,636.8**	**2,202.7**	**2,434.1**

Securities held for monetary policy purposes

Maturity	31 Dec 2011		31 Dec 2010	
	EUR m	%	EUR m	%
Up to 1 year	436.7	9.4	164.9	7.5
Over 1 year	4,200.1	90.6	2,037.8	92.5
Total	**4,636.8**	**100.0**	**2,202.7**	**100.0**

The purchases under the first CBPP programme were fully implemented by the end of June 2010. The accounting amortisation of premium/discounts in 2011 resulted in a net decrease of the reported balance.

On 6 October 2011 the Governing Council announced a second covered bond purchase programme. Under this programme the ECB and the NCBs started to purchase euro-denominated covered bonds issued in the euro area within the objective to ease funding conditions for credit institutions and enterprises as well as encourage credit institutions to maintain and expand lending to their clients. The purchases are expected to be fully implemented by the end of October 2012.

Under the Securities Markets Programme, established in May 2010, the ECB and the NCBs may purchase euro area public and private debt securities in order to address the malfunctioning of certain segments of the euro area debt securities markets and to restore the proper functioning of the monetary policy transmission mechanism. The net increase in the balance in 2011 was due to further purchases that more than offset the redemptions in 2011.

Securities purchased under the Securities Markets Programme and the covered bond purchase programmes are classified as held-to-maturity and reported on an amortised cost basis subject to impairment (see 'Valuation and amortisation of securities' in the notes on accounting conventions). Annual impairment tests are conducted on the basis of the information available and recoverable amounts estimated as at the reporting date.

The total Eurosystem NCB's holdings of SMP securities amounts to EUR 194,155 million, of which the Bank of Finland holds EUR 3,629.7 million on its balance sheet. In accordance with Article 32.4 of the Statute, any risks from holdings of SMP securities, if they were to materialise, should eventually be shared in full by the Eurosystem NCBs, in proportion to the prevailing EXB capital key shares.

In this context, the Governing Council considered the launch in 2011 of the so called Private Sector Involvement (PSI) initiative, proposing a restructuring of part of the debt issued by the Hellenic Republic, to secure debt sustainability in the long term. Part of the Bank of Finland's holdings under the Securities Markets Programme has been issued by the Hellenic Republic. However, given that the PSI was designed as to voluntarily restructure debt held by the private sector no changes were expected to all future contractual cash flows associated with the Bank of Finland's holdings on these securities. As at 31 December 2011, the Governing Council considered that there was no evidence to assume that the PSI initiative was not going to be successfully implemented and therefore no impairment losses were recorded at year end.

In relation to the other securities purchased under the Securities Markets Programme and the securities bought under the two covered bond purchase programmes no impairment was recorded.

The Governing Council assesses on a regular basis the financial risks associated with the securities held under the SMP and CBPP portfolios.

Post-balance-sheet events

In February 2012 the Eurosystem central banks exchanged their holdings of Greek government bonds purchased under the Securities Markets Programme for new securities issued by the Hellenic Republic. The newly acquired securities have the same characteristics as those purchased under the Securities Markets Programme in terms of their nominal values, coupon rates, interest payment dates and redemption dates. The new securities were not included on the list of eligible securities that were subject to restructuring in the context of the PSI initiative.

7.2 Other securities

This item includes coupon bonds and discount papers issued in the euro area.

Breakdown of other securities of euro area residents denominated in euro

	31 Dec 2011	31 Dec 2010
	EUR m	EUR m
Coupon bonds	9,068.9	9,048.8
Discount papers	183.6	417.0
Total	**9,252.5**	**9,465.8**

Maturity breakdown of other securities of euro area residents denominated in euro

Maturity	31 Dec 2011		31 Dec 2010	
	EUR m	%	EUR m	%
Up to 1 year	2,219.4	24.0	2,556.5	27.0
Over 1 year	7,033.1	76.0	6,909.2	73.0
Total	**9,252.5**	**100.0**	**9,465.8**	**100.0**

8. Intra-Eurosystem claims

This balance sheet item includes the following claims:

- participating interest in ECB
- claims equivalent to the transfer of foreign reserves
- claims related to TARGET2 and correspondent accounts (net)
- net claims related to the allocation of euro banknotes within the Eurosystem
- share in ECB's income derived from banknotes and securities purchased under the Securities Markets Programme
- net result of pooling of monetary income.

The share in the ECB's capital of each NCB participating in the Eurosystem is determined on the basis of a so-called capital key. The capital key is calculated relative to the population and gross-domestic product of each country. It is adjusted every five years and when new members join the EU. The Bank of Finland's percentage share in the ECB's capital has been 1.2539% since 1 January 2009.

The ECB increased its subscribed capital by EUR 5 billion from EUR 5.76 billion to EUR 10.76 billion with effect from 29 December 2010.

NCB's paid-up share in the ECB's increased capital

	Subscribed capital since 29 December 2010	***Paid-up capital 31 December 2010***	***Paid-up capital 1 January 2011***	***Paid-up capital since 28 December 2011***
Nationale Bank van België/ Banque Nationale de Belgique	*261,010,385*	*180,157,051*	*180,157,051*	*220,583,718*
Deutsche Bundesbank	*2,037,777,027*	*1,406,533,694*	*1,406,533,694*	*1,722,155,361*
Eesti Pank	*19,261,567*	*722,308*	*13,294,901*	*16,278,234*
Central Bank of Ireland	*119,518,566*	*82,495,233*	*82,495,233*	*101,006,900*
Bank of Greece	*211,436,059*	*145,939,392*	*145,939,392*	*178,687,726*
Banco de España	*893,564,576*	*616,764,576*	*616,764,576*	*755,164,576*
Banque de France	*1,530,293,899*	*1,056,253,899*	*1,056,253,899*	*1,293,273,899*
Banca d'Italia	*1,344,715,688*	*928,162,355*	*928,162,355*	*1,136,439,021*
Central Bank of Cyprus	*14,731,333*	*10,168,000*	*10,168,000*	*12,449,666*
Banque centrale du Luxembourg	*18,798,860*	*12,975,526*	*12,975,526*	*15,887,193*
Central Bank of Malta	*6,800,732*	*4,694,066*	*4,694,066*	*5,747,399*
De Nederlandsche Bank	*429,156,339*	*296,216,339*	*296,216,339*	*362,686,339*
Oesterreichische Nationalbank	*208,939,588*	*144,216,254*	*144,216,254*	*176,577,921*
Banco de Portugal	*188,354,460*	*130,007,793*	*130,007,793*	*159,181,126*
Banka Slovenije	*35,381,025*	*24,421,025*	*24,421,025*	*29,901,025*
Národná banka Slovenska	*74,614,364*	*51,501,030*	*51,501,030*	*63,057,697*
Suomen Pankki – Finlands Bank	*134,927,820*	*93,131,154*	*93,131,154*	*114,029,487*
Subtotal for euro area NCBs*	***7,529,282,289***	***5,143,359,697***	***5,196,932,289***	***6,363,107,289***
Българска народна банка/ (Bulgarian National Bank)	*93,467,027*	*3,505,014*	*3,505,014*	*3,505,014*
Česká národní banka	*155,728,162*	*5,839,806*	*5,839,806*	*5,839,806*
Danmarks Nationalbank	*159,634,278*	*5,986,285*	*5,986,285*	*5,986,285*
Latvijas Banka	*30,527,971*	*1,144,799*	*1,144,799*	*1,144,799*
Lietuvos bankas	*45,797,337*	*1,717,400*	*1,717,400*	*1,717,400*
Magyar Nemzeti Bank	*149,099,600*	*5,591,235*	*5,591,235*	*5,591,235*
Narodowy Bank Polski	*526,776,978*	*19,754,137*	*19,754,137*	*19,754,137*
Banca Națională a României	*265,196,278*	*9,944,860*	*9,944,860*	*9,944,860*
Sveriges Riksbank	*242,997,053*	*9,112,389*	*9,112,389*	*9,112,389*
Bank of England	*1,562,145,431*	*58,580,454*	*58,580,454*	*58,580,454*
Subtotal for non-euro area NCBs*	***3,231,370,113***	***121,176,379***	***121,176,379***	***121,176,379***
Total*	***10,760,652,403***	***5,305,536,076***	***5,318,108,669***	***6,484,283,669***

** Due to rounding, subtotals and totals may not correspond to the sum of all figures.*

In accordance with the legal acts adopted by the Governing Council on the increase of the subscribed capital of the ECB on 29 December 2010 and the pay-up of the increase via three instalments,[6] the Bank of Finland paid up an additional EUR 20,898,333.33 to the ECB on 28 December 2011, representing the second instalment of its contribution to the increase in the ECB's capital.

Item 'Claims equivalent to the transfer of foreign reserves' includes the share of foreign reserve assets transferred by the Bank of Finland to the ECB when Finland joined the Eurosystem. The claims are remunerated at the latest available marginal rate for the Eurosystem's main refinancing operations, adjusted to reflect a zero return on the gold component. They are denominated in euro at a value fixed at the time of their transfer.

This item also consists of net balances of NCBs' TARGET2 accounts if the Bank of Finland has had a claim against the Eurosystem in the period under review.

Net claim related to the allocation of euro banknotes within the Eurosystem consists of a so-called CSM item (Capital Share Mechanism) relating to the subscription of ECB's capital, less the so-called ECB issue figure. The amount of euro banknotes in circulation under the CSM is adjusted in the balance sheet to correspond to the ECB's capital key. The figure for ECB issue represents the ECB's share (8%) of euro banknotes in circulation. For both figures, the counter entry is recorded under the balance sheet liability item 'Banknotes in circulation'.[7]

9. Other assets

This item consists of the Bank of Finland's holdings of euro coins, fixed assets (buildings, machinery and equipment) and investment assets (shares and other equity). The item also includes pension fund asset and investment items, valuation results of off-balance sheet items, accruals and other assets.

Tangible fixed assets

Book value	*31 Dec 2011*	*31 Dec 2010*
	EUR m	*EUR m*
Land	8.8	8.6
Buildings	139.5	146.5
Machinery and equipment	8.4	9.1
Art and numismatic collection	0.4	0.4
Total	***157.1***	***164.6***

Intangible fixed assets

Book value	*31 Dec 2011*	*31 Dec 2010*
	EUR m	*EUR m*
IT systems	7.8	6.3
Total	***7.8***	***6.3***

[6] Decision ECB/2010/26 of 13 December 2010 on the increase of the European Central Bank's capital, OJ L 11, 15.1.2011, p. 53; Decision ECB/2010/27 of 13 December 2010 on the paying-up of the increase of the European Central Bank's capital by the national central banks of Member States whose currency is the euro, OJ L 11, 15.1.2011, p. 54, Decision ECB/2010/34 of 31 December 2010 on the paying-up of capital, transfer of foreign reserve assets and contributions by Eesti Pank to the European Central Bank's reserves and provisions, OJ L 11, 15.1.2011, p. 58; Agreement of 31 December 2010 between Eesti Pank and the European Central Bank regarding the claim credited to Eesti Pank by the European Central Bank under Article 30.3 of the Statute of the European System of Central Banks and of the European Central Bank, OJ C 12, 15.1.2011, p. 6.

[7] According to the accounting regime chosen by the Eurosystem on the issue of euro banknotes, a share of 8% of the total value of the euro banknotes in circulation is allocated to the ECB on a monthly basis. The remaining 92% of the value of the euro banknotes in circulation are allocated to the NCBs also on a monthly basis, whereby each NCB shows in its balance sheet a share of the euro banknotes issued corresponding to its paid-up share in the ECB's capital. The difference between the value of the euro banknotes allocated to the NCB according to the aforementioned accounting regime, and the value of euro banknotes put into circulation, is recorded as a 'Net Intra-Eurosystem claim/liability related to the allocation of euro banknotes within the Eurosystem'.

Other holdings and sundry assets

	31 Dec 2011 EUR m	31 Dec 2010 EUR m
Euro area coins	24.8	21.6
Shares and other equity	24.9	25.2
Pension fund's investments	543.9	525.7
Accruals	404.0	337.9
Other sundry assets	8.5	8.4
Total	**1,006.1**	**918.8**

In the table below, land and buildings also include land (EUR 5.5 million) and buildings (EUR 30.3 million) owned by the Bank of Finland's pension fund. These are included in other holdings and sundry assets. Intangible assets also include shares and other equity.

Tangible and intangible fixed assets

EUR m	Land	Buildings	Machinery and equipment	Art and numisma-tic collection	Intangible assets	Total
Acquisition cost 1 Jan 2011	14.1	300.1	30.6	0.4	50.5	**395.6**
Additions	0.2	3.3	2.1	0.02	4.4	**10.0**
Deductions	–	–	0.2	–	0.3	**0.5**
Acquisition cost 31 Dec 2011	14.4	303.4	32.4	0.4	54.5	**405.1**
Depreciation during financial year	–	12.0	2.9	–	2.9	**17.6**
Accumulated depreciations 31 Dec 2011	–	133.6	24.1	–	21.8	**179.5**
Book value 31 Dec 2011	14.4	169.8	8.4	0.4	32.7	**225.6**
Book value 31 Dec 2010	14.1	178.4	9.1	0.4	31.5	**233.5**

Liabilities

1. Banknotes in circulation

This item consists of the Bank of Finland's share, in accordance with the ECB's capital key and adjusted for the share allocated to the ECB, of the total amount of euro banknotes in circulation. In 2011 the Bank's share of euro banknotes in circulation was EUR 14,649.0 million.

Banknotes in circulation	*31 Dec 2011 EUR m*	*31 Dec 2010 EUR m*
EUR 5	*107.1*	*108.2*
EUR 10	*32.9*	*48.6*
EUR 20	*2,257.6*	*2,109.3*
EUR 50	*5,500.0*	*4,803.3*
EUR 100	*–171.5*	*–53.0*
EUR 200	*380.2*	*364.9*
EUR 500	*3,058.1*	*3,085.1*
Total	*11,164.3*	*10,466.3*
ECB issue	*–1,274.0*	*–1,206.9*
CSM figure	*4,758.7*	*4,620.9*
Banknotes in circulation in accordance with the ECB's capital key	***14,649.0***	***13,880.3***

2. Liabilities to euro area credit institutions related to monetary policy operations denominated in euro

This item consists of interest bearing liabilities to credit institutions and includes credit institutions' minimum reserve account balances, overnight deposits and fixed-term deposits. The item results for the Bank of Finland from the performance of monetary policy functions as part of the Eurosystem. The minimum reserve system aims at stabilising money market interest rates and increasing the structural liquidity needs of the banking system. The average of credit institutions' daily minimum reserve account balances must be at least as high as the reserve requirement during a maintenance period.

3. Liabilities to other euro area residents denominated in euro

This item consists of euro-denominated liabilities to the public sector and credit institutions other than those subject to the reserve requirement.

4. Liabilities to non-euro area residents denominated in euro

This item consists of balances of international organisations and non-euro area banks with the Bank of Finland and repurchase agreements with non-euro area counterparties.

5. Liabilities to euro area residents denominated in foreign currency

This item consists of assets denominated in foreign currency deposited by the State Treasury for its own payments.

6. Liabilities to non-euro area residents denominated in foreign currency

This item includes foreign currency-denominated repurchase agreements entered into for the purpose of managing foreign reserves.

7. Counterpart of special drawing rights allocated by the IMF

This item is the counteritem of SDRs (cf. item on the asset side). Originally the amount of SDRs and their counteritem were equal. As a result of transactions, the Bank of Finland's claims related to SDRs were smaller than their counteritem on the liabilities side of the balance sheet at the end of 2011. On the liabilities side, the counteritem was SDR 1,189.5 million. In the balance sheet, the item is presented in euro, valued at the rate prevailing on the last day of the year (EUR 1,411.5 million).

8. Intra-Eurosystem liabilities

This item includes the net balances of other central banking accounts and the ECB account relating to TARGET2, if the Bank of Finland has a net liability against the Eurosystem in the period under review. Intra-Eurosystem liabilities and claims have been elaborated on in more detail in the notes on the balance sheet under assets item 'Intra-Eurosystem claims'. At the end of financial year 2011, the Bank of Finland had intra-Eurosystem liabilities relating to the redistribution of monetary income in an amount of EUR 76.1 million.

9. Other liabilities

Other liabilities	*31 Dec 2011* *EUR m*	*31 Dec 2010* *EUR m*
Finnish markka banknotes in circulation	*125.4*	*127.1*
Accruals	*18.1*	*16.5*
Accounts payable	*0.9*	*0.0*
Other	*33.7*	*7.6*
Total	***178.1***	***151.2***

10 Revaluation account

This item includes revaluations of land and buildings and other valuation differences arising from changes in accounting practice in 1999. The item also includes unrealised valuation gains arising from the market valuation of foreign currency-denominated items and securities.

11. Provisions

Under section 20 of the Act on the Bank of Finland, provisions can be made in the annual accounts, if they are necessary for safeguarding the real value of the Bank's funds or for smoothing out variations in profit and loss arising from changes in exchange rates or market values of securities. At the end of 2011 these provisions totalled EUR 3,032 million. Provisions consist of a general provision, provision against real value loss, pension liability provision, provision in respect of monetary policy operations as well as foreign exchange rate and price difference provision.

The pension liability provision is made to cover Bank of Finland's pension liabilities. The Bank of Finland's pension liabilities total EUR 543.7 million: 100% of this amount is covered by the pension provision, ie EUR 543.9 million.

In accordance with Article 32.4 of the Statute, the provision against counterparty risks in monetary policy operations is allocated between the NCBs of participating Member States in proportion to their subscribed capital key shares in the ECB prevailing in the year when the defaults have occurred. In accordance with the general accounting principle of prudence, the Governing Council has reviewed the appropriateness of the volume of this provision and decided to reduce the provision by EUR 1.3 billion as at 31 December 2011. The Bank of Finland's share in the provision decrease amounted to EUR 22.5 million. At the end of 2010 the provision amounted to EUR 2.2 billion, of which the Bank's share was EUR 39.4 million.

The respective adjustments are reflected in the NCBs' profit and loss accounts. In the case of the Bank of Finland, the resulting income amounted to EUR 22.5 million in 2011 (see 'Net result of pooling of monetary income' in the notes on the profit and loss account).

12. Capital and reserves

This item consists of the Bank's primary capital and reserve fund. Under section 21 of the Act on the Bank of Finland, the loss shall be covered from the reserve fund, if the annual accounts of the Bank show a financial loss. If the reserve fund is insufficient to cover part of the loss, the uncovered part may be left temporarily uncovered. Any profits in subsequent years shall be used first to cover such uncovered losses.

Capital and reserves (EUR m)	*31 Dec 2011*	*31 Dec 2010*
Primary capital	*840.9*	*840.9*
Reserve fund	*1,421.5*	*1,334.0*
Total	***2,262.4***	***2,174.9***

Profit for the financial year (EUR m)	*2011*	*2010*
Transferred for the needs of the State	*185.0*	*195.0*
Bank of Finland's share of profit (transferred to reserve fund)	*69.5*	*87.5*
Total	***254.5***	***282.5***

13. Profit for the financial year

The profit for the financial year 2011 totalled EUR 254.5 million.

Provisions (EUR m)	*Provisions as at 1 Jan 2010*	*Changes in provisions 2010*	*Total provisions 31 Dec 2010*	*Changes in provisions 2011*	*Total provisions 31 Dec 2011*
Foreign exchange rate and price difference provision	*116*	*290*	***406***	*9*	***415***
General provision	*995*	*100*	***1,095***	*100*	***1,195***
Provision against real value loss	*640*	*109*	***748***	*113*	***861***
Pension liability provision	*503*	*23*	***526***	*19*	***544***
Provision in respect of monetary policy operations	*72*	*–32*	***39***	*–22*	***17***
Total	***2,325***	***489***	***2,814***	***218***	***3,032***

Notes on the profit and loss account

1. Interest income

Interest income received outside the euro area (EUR m)	*2011*			*2010*		
	Euro-denominated	*Foreign currency-denominated*	*Total*	*Euro-denominated*	*Foreign currency-denominated*	*Total*
Gold investments	0.0	1.2	**1.2**	0.0	2.0	**2.0**
Non-euro area coupon bonds	24.5	65.7	**90.2**	15.3	98.6	**113.9**
Non-euro area discount papers	0.1	0.0	**0.1**	0.0	0.1	**0.1**
Non-euro area deposits	8.1	1.0	**9.0**	2.7	0.7	**3.4**
Other	0.0	8.1	**8.1**	0.0	5.7	**5.7**
Total	**32.7**	**76.1**	**108.8**	**17.9**	**107.2**	**125.1**

Interest income received from the euro area (EUR m)	*2011*			*2010*		
	Euro-denominated	*Foreign currency-denominated*	*Total*	*Euro-denominated*	*Foreign currency-denominated*	*Total*
Euro area coupon bonds	223.6	20.6	**244.1**	228.2	37.5	**265.7**
Euro area discount papers	5.8	0.0	**5.8**	5.6	0.0	**5.6**
Euro area deposits	0.5	0.1	**0.6**	0.3	0.1	**0.4**
ESCB items	263.1	0.0	**263.1**	119.8	0.0	**119.8**
Monetary policy items	139.6	0.0	**139.6**	80.4	0.0	**80.4**
Other	0.0	0.6	**0.6**	0.0	0.7	**0.7**
Total	**632.6**	**21.2**	**653.8**	**434.2**	**38.4**	**472.5**

Total interest income (EUR m)	*2011*			*2010*		
	Euro-denominated	*Foreign currency-denominated*	*Total*	*Euro-denominated*	*Foreign currency-denominated*	*Total*
Interest income received outside the euro area	32.7	76.1	**108.8**	17.9	107.2	**125.1**
Interest income received from the euro area	632.6	21.2	**653.8**	434.2	38.4	**472.5**
Total	**665.3**	**97.3**	**762.6**	**452.1**	**145.5**	**597.6**

Interest income from and outside the euro area totalled EUR 762.6 million. Of this, EUR 97.3 million consisted of foreign currency-denominated interest income and EUR 665.3 million on euro-denominated interest income.

Interest income on ESCB items totalled EUR 263.1 million. Of this, EUR 7.7 million consisted of claims on transfers of foreign reserves to the ECB. Interest income due to the claims and liabilities pertaining to the ECB's share of euro banknotes, the application of the ECB capital key and the adjustments, EUR 41.5 million, is entered on a net basis. Interest income on TARGET2 balances totalled EUR 213.8 million.

2. Interest expense

Interest expense paid outside the euro area (EUR m)	*2011*			*2010*		
	Euro-denominated	*Foreign currency-denominated*	*Total*	*Euro-denominated*	*Foreign currency-denominated*	*Total*
Non-euro area deposits	–6.2	–0.4	**–6.6**	–1.9	–0.4	**–2.3**
Other	0.0	–5.4	**–5.4**	0.0	–4.0	**–4.0**
Total	**–6.2**	**–5.8**	**–12.0**	**–1.9**	**–4.4**	**–6.4**

Interest expense paid in the euro area (EUR m)	*2011*			*2010*		
	Euro-denominated	*Foreign currency-denominated*	*Total*	*Euro-denominated*	*Foreign currency-denominated*	*Total*
ESCB items	0.0	0.0	**0.0**	0.0	0.0	**0.0**
Monetary policy items	–155.5	0.0	**–155.5**	–64.1	0.0	**–64.1**
Other	–1.5	–1.1	**–2.6**	–0.3	–0.3	**–0.7**
Total	**–157.0**	**–1.1**	**–158.1**	**–64.4**	**–0.3**	**–64.8**
Total interest expense	**–163.2**	**–6.9**	**–170.1**	**–66.3**	**–4.8**	**–71.1**

Interest expense paid in and outside the euro area totalled EUR 170.1 million. Of this, EUR 55.8 million was paid on minimum reserve deposits, EUR 42.6 million on overnight deposits and EUR 57.1 on fixed-term deposits.

3. Net interest income

Net interest income	*31 Dec 2011 EUR m*	*31 Dec 2010 EUR m*
Interest income		
Financial assets	359.9	397.5
Monetary policy items	139.6	80.4
ESCB claims	263.1	119.8
Total	**762.6**	**597.7**
Interest expense		
Financial assets	–14.6	–7.0
Monetary policy items	–155.5	–64.1
ESCB liabilities	0.0	0.0
Total	**–170.1**	**–71.1**
NET INTEREST INCOME	**592.5**	**526.6**

4. Foreign exchange rate differences

This item includes realised exchange rate gains and losses as well as valuation losses arising from the sale of currency positions. In 2011 gains related to foreign exchange rate movements amounted to EUR 5.2 million.

5. Securities price differences

This item includes realised gains and losses as well as valuation losses arising from the sale of securities. In the accounts, securities are treated on a security-by-security basis. In 2011 the realised gains related to securities price movements totalled EUR 3.5 million.

6. Change in foreign exchange rate and price difference provisions

Realised net gains arising from foreign exchange rate and price differences, EUR 8.8 million, were used to increase provisions in accordance with the financial reporting policy. All provisions have been specified in the notes on the balance sheet under assets.

7. Net result of pooling of monetary income

This item shows the net sum of monetary income paid to and redistributed from the Eurosystem. The amount of each NCB's monetary income is determined by using the actual income that derives from the earmarkable assets that are held against the liability base. The liability base consists of the following items: banknotes in circulation; liabilities to credit institutions related to monetary policy operations denominated in euro; net intra-Eurosystem liabilities resulting from TARGET2 transactions, and net intra-Eurosystem liabilities related to the allocation of euro banknotes within the Eurosystem. Any interest paid on liabilities included within the liability base is to be deducted from the monetary income to be pooled.

Earmarkable assets consist of the following items: lending to credit institutions related to monetary policy operations denominated in euro; securities held for monetary policy purposes; euro-denominated claims equivalent to the transfer of foreign reserves; net claims resulting from TARGET2 transactions; net claims related to the allocation of euro banknotes; and the amount of each NCBs' gold holdings in proportion to each NCB's capital key share. Gold is considered to generate no income. Where the value of earmarkable assets exceeds or falls short of the value of its liability base, income is calculated for the difference by applying the interest rate on main refinancing operations. The monetary income pooled by the Eurosystem is to be allocated among the NCBs according to the subscribed capital key. The actual net result of pooling of monetary income totalled EUR –75.3 million.

8. Share in ECB profit

The ECB distributed EUR 170.8 million profit for the financial year 2010, of which the Bank of Finland's share recorded for the financial year 2011 totalled EUR 3.1 million.

9. Provision in respect of monetary policy operations

In accordance with the general accounting principle of prudence, the Governing Council deemed it appropriate to establish provisions totalling EUR 5.7 billion against the risks arising from transactions with Eurosystem counterparties during 2008. In accordance to Article 32.4 of the Statute, these risks will be shared among all the NCBs of participating Member States in proportion to their subscribed capital key shares in the ECB prevailing in 2008.

As a result, a provision for EUR 102 million equivalent to 1.78603% of the total provision was created.

In the financial statements for 2011, by a decision of the Governing Council, the above-mentioned provision was decreased by EUR 1.3 billion to reflect the increase in collateral prices and payments by the debtor. The Bank of Finland's share of the decrease was EUR 22.5 million.

10. Other central banking income

This item includes income on euro banknotes, EUR 11.7 million, distributed by the ECB in the form of an interim distribution of profit. The item also includes dividend income, EUR 3.5 million, consisting primarily of shares in the Bank for International Settlements.

11. Other income

This item consists of the Financial Supervisory Authority's supervision and processing fees, EUR 24.5 million, income from real estate, EUR 9.5 million, as well as commissions and fees.

12. Staff costs

Staff costs	*31 Dec 2011 EUR m*	*31 Dec 2010 EUR m*
Salaries and fees	40.5	40.6
Employer's payments to the pension fund	7.5	7.6
Other staff-related costs	2.7	2.6
Total	***50.7***	***50.8***

Average staff size	*2011 Number of staff*	*2010 Number of staff*
Bank of Finland	429	456
Financial Supervisory Authority	207	211
Total	***636***	***667***

Basic salaries paid to the members of the Board in 2011

	EUR
Erkki Liikanen	259,062
Pentti Hakkarainen	233,952
Seppo Honkapohja	190,717
Total	***683,731***

Fringe benefits (meal benefit, company-paid telephone and company car) paid to the members of the Board totalled EUR 37,176.

13. Pension fund contribution

Upon approval of the Parliamentary Supervisory Council, the Bank of Finland paid a contribution of EUR 32 million to the Bank's pension fund in 2011 so as to bring the value of the pension fund's assets closer to the targeted pension liability coverage.

	31 Dec 2011 EUR m	*31 Dec 2010 EUR m*
Pension fund contribution	32.0	10.0

14. Administrative costs

Administrative costs	*2011 EUR m*	*2010 EUR m*
Supplies and purchases	*0.8*	*0.7*
Machinery and equipment	*3.4*	*3.0*
Real estates	*11.1*	*10.9*
Staff-related expenses	*3.8*	*3.9*
Purchase of services	*8.5*	*8.0*
Other	*1.5*	*1.3*
Total	***29.1***	***27.9***

This item includes rents, meetings and interest group-related costs, expenses arising from the purchase of services and cost of equipment. Expenses involved in training, travel and recruitment of staff are also recorded under this item.

15. Depreciation of fixed assets

Depreciation of tangible fixed assets	*31 Dec 2011 EUR m*	*31 Dec 2010 EUR m*
Land	–	–
Buildings	*2.2*	*2.1*
Machinery and equipment	*2.8*	*2.9*
Art and numismatic collection	–	–
Pension fund's land and buildings	*1.1*	*1.1*
Total	***6.1***	***6.1***

Depreciations of intangible fixed assets	*31 Dec 2011 EUR m*	*31 Dec 2010 EUR m*
IT systems	*3.1*	*2.4*
Total	***3.1***	***2.4***

Depreciations do not include depreciations arising from the revaluation of land and buildings.

16. Banknote procurement costs

Banknote procurement costs totalled EUR 4.0 million.

17. Other expenses

The bulk of other expenses is related to the use and maintenance of property.

18. Income of the pension fund

This item includes income of the Bank of Finland pension fund's investment activities, EUR 2.7 million. The item also includes the Bank of Finland's and Financial Supervisory Authority's employer contributions as well as employees' share of premium income, EUR 9.8 million. The contribution of EUR 32.0 million paid by the Bank of Finland to the pension fund is also included in this item.

19. Expenses of the pension fund

This item includes expenses of the Bank of Finland pension fund's investment activities, EUR 1.0 million, pensions paid, EUR 23.0 million, management costs and depreciations of fixed assets managed by the pension fund.

20. Changes in provisions

This item includes the increase of the pension liability provision, EUR 19.1 million, the increase of the provision against real value loss, EUR 113.0 million, and the increase of the general provision, EUR 100 million. All provisions have been specified in the notes on the balance sheet under assets.

21. Profit for the financial year

Profit for the financial year 2011 totalled EUR 254.5 million. The Board proposes to the Parliamentary Supervisory Council that EUR 185 million of the profit would be made available for the needs of the State.

Off-balance sheet items

This item contains the Bank of Finland's derivative contracts.

Derivative contracts	*31 Dec 2011 EUR m*	*31 Dec 2010 EUR m*
Nominal value of FX futures contracts		
Purchase agreements	*0*	*0*
Sales agreements	*0*	*0*
Market value of FX swap contracts	*–6.3*	*–2*
Market value of GIRS contracts	*0.1*	*1.3*
Market value of IRS contracts	*0*	*0*
Market value of FX forward contracts	*0*	*0*
Total	***–6.2***	***–0.7***

Five-year review

The following table presents the Bank of Finland's balance sheets and profit and loss accounts for the past five financial years.

BALANCE SHEET (EUR m)	*2011*	*2010*	*2009*	*2008*	*2007*
Assets					
Gold and gold receivables	***1,918***	***1,664***	***1,208***	***980***	***896***
Claims on non-euro area residents denominated in foreign currency	***5,886***	***5,223***	***6,225***	***4,597***	***4,515***
Receivables from the International Monetary Fund	*1,967*	*1,815*	*1,609*	*356*	*260*
Balances with banks and security investments, external loans and other external assets	*3,919*	*3,408*	*4,617*	*4,241*	*4,254*
Claims on euro area residents denominated in foreign currency	***628***	***712***	***1,120***	***2,577***	***1,394***
Claims on non-euro area residents denominated in euro	***1,946***	***1,662***	***845***	***581***	***394***
Lending to euro area credit institutions related to monetary policy operations denominated in euro	***2,311***	***50***	***2,710***	***2,600***	***230***
Main refinancing operations	*10*	*0*	*20*	*350*	*30*
Longer-term refinancing operations	*2,301*	*50*	*2,690*	*2,250*	*200*
Other claims on euro area credit institutions denominated in euro	***40***	***1***	***126***	***0***	***3***
Securities of euro area residents denominated in euro	***13,889***	***11,668***	***8,002***	***7,265***	***6,863***
Securities held for monetary policy purposes	***4,637***	*2,203*	*531*	*–*	*–*
Other securities	***9,253***	*9,466*	*7,471*	*7,265*	*6,863*
Intra-Eurosystem claims	***70,348***	***23,921***	***14,280***	***10,162***	***7,465***
Participating interest in ECB	*120*	*99*	*78*	*73*	*73*
Claims equivalent to the transfer of foreign reserves	*722*	*722*	*722*	*717*	*717*
Claims related to TARGET2 and correspondent accounts (net)	*66,008*	*19,686*	*9,535*	*5,197*	*2,951*
Net claim related to the allocation of euro banknotes within the Eurosystem	*3,497*	*3,414*	*3,945*	*4,174*	*3,724*
Other assets	***1,171***	***1,090***	***1,130***	***1,254***	***1,048***
Euro area coins	*25*	*22*	*19*	*22*	*24*
Tangible and intangible fixed assets	*165*	*171*	*189*	*185*	*196*
Other current assets	*569*	*551*	*528*	*481*	*508*
Other	***413***	*346*	*393*	*566*	*320*
Total assets	***98,138***	***45,990***	***35,646***	***30,016***	***22,809***

BALANCE SHEET (EUR m)	*2011*	*2010*	*2009*	*2008*	*2007*
Liabilities					
Banknotes in circulation	*14,649*	***13,880***	***13,330***	***12,532***	***11,148***
Liabilities to euro area credit institutions related to monetary policy operations denominated in euro	*71,697*	***21,696***	***13,543***	***8,110***	***5,910***
Current accounts (covering the minimum reserve system)	*1,657*	*9,383*	*8,085*	*1,015*	*2,901*
Overnight deposits	*52,540*	*9,113*	*5,458*	*7,095*	*9*
Fixed-term deposits (liquidity-absorbing fine-tuning operations)	*17,500*	*3,200*	*–*	*–*	*3,000*
Liabilities to other euro area residents denominated in euro	*836*	***262***	***14***	***3,009***	***0***
Liabilities to non-euro area residents denominated in euro	*782*	***1,021***	***234***	***37***	***4***
Liabilities to euro area residents denominated in foreign currency	*0*	***0***	***248***	***0***	***0***
Liabilities to non-euro area residents denominated in foreign currency	*153*	***23***	***363***	***–***	***88***
Counterpart of special drawing rights allocated by the IMF	*1,412*	***1,377***	***1,295***	***158***	***153***
Intra-Eurosystem liabilities	*76*	***33***	***–***	***–***	***–***
Other liabilities	*178*	***151***	***155***	***191***	***171***
Revaluation account	*2,806*	***2,274***	***1,703***	***1,622***	***854***
Provisions	*3,032*	***2,814***	***2,325***	***2,092***	***2,368***
Capital and reserves	*2,262*	***2,175***	***2,015***	***1,864***	***1,704***
Primary capital	*841*	*841*	*841*	*841*	*841*
Reserve fund	*1,421*	*1,334*	*1,174*	*1,023*	*863*
Profit for the financial year	*254*	***283***	***420***	***401***	***410***
Total liabilities	*98,138*	***45,990***	***35,646***	***30,016***	***22,809***

PROFIT AND LOSS ACCOUNT (EUR m)	2011	2010	2009	2008	2007
Interest income	763	597	590	844	709
Interest expense	–170	–71	–71	–223	–146
Net interest income	592	526	519	621	563
Foreign exchange rate differences	5	221	15	–485	–379
Securities price differences	4	69	101	37	–34
Change in foreign exchange rate and price difference provision	–9	–290	–116	448	413
Net result of financial operations, write-downs and risk provisions	592	526	519	621	563
Net result of pooling of monetary income	–75	–33	21	26	8
Share in ECB profit	3	26	2	–	–
Provisions in respect of monetary policy operations	22	32	31	–102	–
Other central banking income	15	9	19	25	3
Central banking profit	557	560	590	569	574
Other income	35	34	43	41	29
Operating expenses	–125	–102	–112	–116	–108
Staff costs	–51	–51	–53	–46	–46
Pension fund contribution	–32	–10	–10	–30	–22
Administrative expenses	–29	–28	–31	–27	–26
Depreciation of fixed assets	–8	–7	–7	–8	–8
Banknote procurement costs	–4	–6	–10	–4	–4
Other expenses	–1	0	–1	–2	–2
Operating profit	467	491	521	494	495
Profit for the pension fund	19	24	48	–22	21
Changes in provisions	–232	–232	–149	–71	–106
Profit for the financial year	254	283	420	401	410

Notes on risk management

Decision-making framework for investment of financial assets and risk management

The Board of the Bank of Finland is responsible for decisions on the investment activities objectives, investment policy and risk management principles. Its scope of responsibility includes decisions on the size of own financial assets and foreign reserves, currency distribution of foreign reserves, the size and composition of liquid assets, the strategic benchmark for investment assets by investment category, leeways permitted in investment activities by investment category and the level of interest rate and credit risks.

Within the limits imposed by the Board, the markets committee makes detailed decisions on the investment of the financial assets and the related risk management. Such decisions include criteria for counterparties and issuers and more specific credit risk limits. The chairperson of, and decision-maker in, the markets committee is the Board member responsible for the Bank of Finland's own investments. In the latter half of 2011 the Board changed the market committee's decision-making powers regarding the management of credit risks.

Within the limits imposed by the Board and the markets committee, a small proportion of decisions is delegated to the investment group and the risk group. However, the main focus of these groups is to prepare decisions for consideration by higher decision-making bodies. In addition, the investment group acts as an internal decision-maker within the Banking Operations department and as a coordinator of matters common to the investment and risk control functions. The Head of Banking Operations chairs the investment group and makes decisions within the group. The Head of risk control unit operating under the Banks Administration department chairs the risk group and makes decisions within the group.

Matters related to investment activities and risk management are also discussed in the risk committee which convenes regularly and is chaired by the Board member responsible for risk control. The risk committee does not make actual decisions on investment activities and risk control. Its commission is to conduct independent assessment and control of investment risks and the related risk management. Whenever necessary, the risk committee may submit matters to the Board for information or decision.

Risk control relating to investment activities

The control of risks related to investment activities is the task of the risk control unit operating under the auspices of the Administration department. Risk control is therefore separate from the Bank's actual investment activity, which is the task of the investment unit operating under the Banking Operations department. This organisational separation of the two functions aims at ensuring that risk control is independent of the investment function.

The responsibilities of the risk control unit include control of risks associated with investment activities, monitoring of risk positions, pricing of instruments and reporting on risks and returns. The risk control unit reports on possible cases of non-compliance with the limits imposed and produces risk reports on a daily basis and return reports at monthly intervals. The risks to, and return on, the financial assets are reviewed four times a year by the markets committee and twice a year by the Board.

The risk control unit also maintains an overall risk management framework and investment benchmark indices and develops risk management methods.

Risk measures and breakdowns relating to the Bank of Finland's financial assets

Table 1.
Breakdown of debt securities and deposits in the Bank of Finland's financial assets by credit rating[1]

Credit rating	*31 Dec 2011* %	*31 Dec 2010* %
AAA	*66.8*	*73.7*
AA+	*12.7*	*3.9*
AA	*2.8*	*9.5*
AA-	*9.4*	*2.0*
A+	*1.8*	*4.9*
A	*3.4*	*2.2*
A-	*0.7*	*1.3*
BBB+	*0.6*	*0.0*
BBB	*0.5*	*0.7*
BBB-	*0.4*	*0.0*
below BBB-	*0.2*	*0.6*
No credit rating	*0.6*	*1.2*

[1] Covered bonds have been classified according to their own credit rating and not the credit rating of their issuer. The Bank of Japan and the Federal Reserve are dealt with according to the credit rating of the respective state.

Source: Bank of Finland.

Table 2.
Breakdown of debt securities in the Bank of Finland's financial assets by home state of the issuer (according to market value of debt security)

Country or region	*31 Dec 2011* %	*31 Dec 2010* %
Euro area	***66.7***	***71.5***
Germany	*23.2*	*21.7*
France	*19.3*	*22.1*
The Netherlands	*6.8*	*6.0*
Finland	*6.5*	*6.8*
Austria	*3.4*	*3.4*
Spain	*3.3*	*4.7*
Italy	*2.1*	*3.6*
Belgium	*0.9*	*1.4*
Ireland	*0.5*	*0.6*
Portugal	*0.4*	*0.7*
Greece	*0.2*	*0.6*
Luxembourg[1]	*0.0*	*0.0*
Europe excl. euro area	***8.6***	***7.4***
United Kingdom	*3.8*	*4.0*
Sweden	*2.5*	*2.2*
Norway	*1.3*	*0.5*
Denmark	*1.0*	*0.8*
America	***14.1***	***10.2***
United States	*13.0*	*9.1*
Canada	*1.1*	*1.1*
Asia and Pacific Ocean region	***3.8***	***4.8***
Japan	*3.2*	*4.2*
Australia	*0.4*	*0.6*
Singapore	*0.1*	*0.1*
New Zealand[1]	*0.0*	*–*
International institutions	***6.8***	***6.1***

[1] 0.0 means less than 0.05,
– means zero.

Source: Bank of Finland.

Table 3.
Sensitivity of the Bank of Finland's financial assets to exchange rate and interest rate changes

EUR m	***2011***	***2010***
Change in the value of Bank of Finland's financial assets after appreciation of the euro exchange rate by 15% relative to currencies of foreign reserves as at 31 Dec	*–882*	*–813*
Change in the value of Bank of Finland's financial assets after an interest rate rise of 1%, with the amount, composition and modified duration for the financial assets as at 31 Dec	*–380*	*–370*

Source: Bank of Finland.

Table 4.
VaR figures for the Bank of Finland's financial assets

VaR figures for market risk[1] (one-month horizon, 95% confidence level)

	2011			
EUR m	*Average*	*Highest*	*Lowest*	*31 Dec*
Interest rate risk	120	210	80	95
Exchange rate risk	209	313	138	178
Total risk (excl. gold)	285	458	182	217
Total risk (incl. gold)	402	636	234	234
	2010			
EUR m	*Average*	*Highest*	*Lowest*	*31 Dec*
Interest rate risk	85	128	60	99
Exchange rate risk	215	330	150	193
Total risk (excl. gold)	241	358	174	213
Total risk (incl. gold)	318	510	194	307

VaR figures for credit risk[2] (one-year horizon, confidence levels of 95%, 99% and 99.9%)

	2011			
EUR m	*Average*	*Highest*	*Lowest*	*31 Dec*
Credit risk (95%)	9	12	5	11
Credit risk (99%)	27	34	21	32
Credit risk (99.9%)	84	105	70	91
	2010			
EUR m	*Average*	*Highest*	*Lowest*	*31 Dec*
Credit risk (95%)	6	7	4	6
Credit risk (99%)	22	31	18	22
Credit risk (99.9%)	69	85	56	77

[1] The figures include bonds purchased under the Covered Bond Purchase Programme (CBPP).
[2] The figures exclude bonds purchased under the Covered Bond Purchase Programme (CBPP) and debt instruments issued by states, in domestic currency.
Source: Bank of Finland.

The Bank of Finland's estimated total risk including gold

The Bank of Finland's total risks are discussed in section 'Total risk exposure' (p. 87–88). The figures presented in that section exclude gold owing to its large revaluation account. When all risks – including gold – are added together, the Bank of Finland's total risks are estimated at about EUR 3 billion in annual terms.

Auditor’s report

In our capacity as the auditors elected by Parliament, we have audited the accounting records, financial statements and administration of the Bank of Finland for the financial year 2011 in accordance with generally accepted auditing standards.

During the financial year the Bank’s Internal Audit audited the Bank’s accounting records and activities. We have examined the internal audit reports.

We have read the Bank’s annual report and received representations from the Board concerning the Bank’s activities.

The financial statements have been drawn up in accordance with the principles of financial statements approved by the Parliamentary Supervisory Council and current rules and regulations. The financial statements give a true and fair view of the Bank’s financial position and results.

We propose that the profit and loss account and balance sheet for the financial year audited by us be approved. We recommend that the profit for the financial year be disposed of as proposed by the Board.

Helsinki, 16 March 2012

Esko Kiviranta

Mika Kari

Lenita Toivakka

Eero Prepula
Authorised Public Accountant,
JHTT (Public Administration
Accountant)

Kari Manner
Authorised Public Accountant,
JHTT (Public Administration
Accountant)

. / . Markku Koskela
Authorised Public Accountant

Statement regarding the audit as defined in the Article 27 of the statute of the European System of Central Banks and the European Central Bank

We have audited the accounting records and the financial statements of the Bank of Finland for the year ended 31 December 2011 as defined in the Article 27.1 of the Statute of the European System of Central Banks and the European Central Bank. The financial statements have been prepared in accordance with the Accounting Principles and Methods approved by the Governing Council of the European Central Bank as well as with the Act on the Bank of Finland. The financial statements comprise the balance sheet, the income statement and notes to the financial statements.

The responsibility of the Board

The Board is responsible for the preparation and fair presentation of the financial statements in accordance with the laws and regulations governing the preparation of the financial statements.

Auditor's Responsibility

Our responsibility is to perform an audit in accordance with the International Standards on Auditing and ethical guidance prepared by IFAC (International Federation of Accountants), good auditing practice in Finland as well as the Auditing Act, when applicable, and to express an opinion on these financial statements based on our audit. Good auditing practice requires that we plan and perform the audit to obtain reasonable assurance 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 preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances.

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 performance and financial position of the Bank of Finland in accordance with the Accounting Principles and Methods approved by the Governing Council of the European Central Bank.

Helsinki, 29 February 2012
KPMG Oy Ab

Raija-Leena Hankonen
Authorised Public Accountant

Appendices

Monetary policy measures of the Eurosystem in 2011

January-December	In accordance with the decisions of the Governing Council of the ECB, main refinancing operations and the longer-term regular and non-standard refinancing operations continued to be conducted as fixed-rate tender procedures with full allotment. In all longer-term refinancing operations, the rate applied was fixed at the average of the rates in the main refinancing operations, over the life of the respective operation.
April	On 7 April 2011, the Governing Council of the ECB decided to increase the key interest rates by 0.25 percentage point with effect from 13 April 2011: the interest rate on the main refinancing operations to 1.25% and the interest rates on the marginal lending facility and the deposit facility to 2% and 0.5% respectively.
June	On 29 June 2011, the Governing Council of the ECB decided, in co-operation with the Federal Reserve, to extend the US dollar liquidity swap arrangements in coordination with the Bank of England, the Bank of Japan, the Bank of Canada and the Swiss National Bank up to 1 August 2012. The Governing Council also decided to continue regularly conducting US dollar liquidity-providing operations with a maturity of seven days.
July	On 7 July 2011, the Governing Council of the ECB decided to increase the key interest rates by 0.25 percentage point with effect from 13 July 2011: the interest rate on the main refinancing operations to 1.5% and the interest rates on the marginal lending facility and the deposit facility to 2.25% and 0.75% respectively.
August	On 4 August 2011, the Governing Council of the ECB decided to conduct a supplementary longer-term refinancing operation with a maturity of six months. In the statement issued 7 August 2011, the President of the ECB announced that the Eurosystem will continue to actively implement the Securities Markets Programme. At the end of August, the Governing Council announced that the liquidity swap arrangement with the Bank of England will be extended to 28 September 2012.
September	The Governing Council of the ECB decided, in coordination with other key central banks, to exceptionally conduct three US dollar liquidity-providing operations with a maturity of three months.
October	On 6 October 2011, the Governing Council of the ECB decided to conduct two longer-term refinancing operations with a maturity of approximately 12 months – one in October and another in December. It was also decided to continue applying fixed rate tender procedures with full allotment in regular main refinancing operations, 3-month refinancing operations and operations with a maturity of one maintenance period until 10 July 2012. Furthermore, it was decided to launch a new Covered Bond Purchase Programme. Under the programme, the Eurosystem will purchase covered bonds for an amount of EUR 40 billion in primary and secondary markets from November 2011 to October 2012.

November	On 3 November 2011, the Governing Council of the ECB decided to decrease the key interest rates by 0.25 percentage point with effect from 9 November 2011: the interest rate on the main refinancing operations to 1.25% and the interest rates on the marginal lending facility and the deposit facility to 2% and 0.5% respectively. In addition, on 30 November 2011 it was decided to establish, in cooperation with other key central banks, a temporary network of reciprocal swap lines with the partner central banks until 1 February 2013. The network enables the provision of refinancing in other currencies than US dollar, if needed. It was also decided to reduce the rate on the US dollar swap arrangements. Furthermore, the Governing Council decided to regularly conduct the existing US dollar operations.
December	On 8 December 2011, the Governing Council of the ECB decided to decrease the key interest rates by 0.25 percentage point with effect from 14 December 2011: the interest rate on the main refinancing operations to 1% and the interest rates on the marginal lending facility and the deposit facility to 1.75% and 0.25% respectively. Furthermore, it was decided to conduct two longer-term refinancing operations with a maturity of approximately 36 months – one in December 2011 and another in February 2012 – with an option of early repayment after one year. Counterparties may also repay amounts borrowed in the 12-month refinancing operation allotted in November in full and transfer to the new 36-month operation. The Governing Council decided to discontinue the fine-tuning operations carried out on the last day of each maintenance period. The reserve ratio applicable to minimum reserves was reduced from 2% to 1% as of 18 January 2012.

Key measures affecting the financial markets in 2011

Measures by the European System of Central Banks	
January	The Governing Council of the ECB approved the mandate of the Financial Stability Committee (FSC). This new committee of the Eurosystem and the European System of Central Banks (ESCB) is tasked with assisting the Governing Council of the ECB in the discharge of duties related to financial stability. Responsibility for these tasks lay previously with the Banking Supervision Committee until its abolition in connection with the establishment of the European Systemic Risk Board (ESRB).
March	The Governing Council of the ECB decided to suspend, until further notice, the application of the minimum credit rating threshold in the collateral eligibility requirements for the purposes of the Eurosystem's credit operations in the case of marketable debt instruments issued or guaranteed by the Irish government, irrespective of the time of issuance.
April	The Governing Council of the ECB decided to extend the application of loan-by-loan information requirements for asset-backed securities (ABSs) in the Eurosystem collateral framework to commercial mortgage-backed securities (CMBSs) and small and medium-sized enterprises' (SME) transactions.
May	On 5 May, the Governing Council of the ECB issued a positive assessment of the economic and financial adjustment programme agreed by the Portuguese government earlier on the same day.
June	The Governing Council of the ECB approved legal documentation enabling the central bank of Romania to join TARGET2 in early July 2011.
July	The Governing Council of the ECB decided to suspend, until further notice, the application of the minimum credit rating threshold in the collateral eligibility requirements for the purposes of the Eurosystem's credit operations in the case of marketable debt instruments issued or guaranteed by the Portuguese government, irrespective of the time of issuance.
August	The Governing Council of the ECB published a statement of factors that it considers decisively important for ensuring financial stability in the euro area. The statement underlines the importance for the Heads of State or Government to adhere strictly to the fiscal targets agreed at the summit of 21 July 2011. In addition, the Governing Council calls for a swift implementation of the decisions made, emphasising the need for governments to stand ready to activate the European Financial Stability Facility (EFSF) in the secondary market, once the EFSF is operational. The Governing Council also announces the commencement of the ECB's active implementation of the Securities Markets Programme (SMP).
November	The Governing Council of the ECB decided to postpone the launch of the TARGET2-Securities (T2S) platform from September 2014 to June 2015. The Governing Council approved the publication of an oversight assessment of the EURO1 system, the conclusions of which the Governing Council had adopted in August. EURO1 is a private EU-wide interbank system to settle cross-border and domestic euro-denominated payments.
December	The Governing Council of the ECB decided to increase collateral availability by reducing the rating threshold for asset-backed securities (ABSs) and by allowing national central banks to accept as collateral certain bank loans, at their own risk. At the same time, credit institutions' reserve requirements were eased by a 1 percentage point reduction in the reserve ratio, to 1%.

EU regulatory projects and their implementation in Finland

January	The European Commission's public consultation on stricter regulation of credit rating agencies, now closed. The European Commission's public consultation on regulation related to investment funds, now closed.
February	The European Commission's public consultation on the review of the Markets in Financial Instruments Directive (MiFID), now closed.
March	The European Commission's public consultation on technical details of a possible European crisis management framework, now closed. The aim of the proposal is to ensure that authorities have the potential to address the operations of problem banks ahead of crisis escalation and to enable an orderly resolution of a problem bank. The European Commission's public consultation on Central Securities Depositories and on the harmonisation of certain aspects of securities settlement, now closed. The European Commission's public consultation on possible measures to strengthen bank capital requirements for counterparty credit risk, now closed. Amendments to the Standard of the Financial Supervisory Authority (FIN-FSA) on own funds and their minimum amount entered into force. The amendments are based on the first amendment to the Capital Requirements Directive (CRD 2) and concern hybrid and equity instruments included in Tier 1 capital.
April	A working group set up by the Ministry of Finance to assess local government financing submitted its final report. The working group considers it important that the EU-wide implementation of the Basel III regulatory framework, prepared by the Basel Committee on Banking Supervision, should not significantly constrain the operations of Municipality Finance, a credit institution owned by the local government sector.
June	A new Government was appointed in Finland. As regards the financial markets, the most important items on the Government programme are related to the organisation of macroprudential supervision and the national use of the relevant policy tools, the development of the capital markets, the revision of the Securities Markets Act and the introduction of a bank and financial market tax. The European Commission issued a public admonition to six member states because of defects in the national transposition of the second amendment to the Capital Requirements Directive (CRD 3). The defects concern restrictions related to remuneration in particular. In a letter to the European Commission, seven member states expressed concern that, in the implementation of the Basel III framework, the Commission is proposing as much harmonisation as possible across Europe, meaning the application of the maximum harmonisation principle. Amendments to the Standard of the Financial Supervisory Authority (FIN-FSA) on the capital requirement for counterparty credit risk entered into force.

July	The European Commission published its draft Capital Requirements Directive and Regulation (CRD 4/CRR), mainly focused on the introduction of the Basel III regulatory framework within the EU. The proposal replaces the current Capital Requirements Directives. A Capital Requirements Regulation would make all Pillar 1 requirements directly binding in EU legislation without their transposition into national legislation (maximum harmonisation). The proposed Directive includes requirements for the taking-up and pursuit of business and the provision of services, as well as requirements for supervisory review (Pillar 2) and internal governance. Supervisory responsibility for credit rating agencies was entirely transferred to the European Securities and Markets Authority (ESMA). The European Commission's public consultation on corporate governance, now closed. July saw the entry into force of amendments to the set of regulations and guidelines of the Financial Supervisory Authority (FIN-FSA) concerning industry-wide pension funds, company pension funds, insurance companies, insurance associations, representations of insurance companies from third countries and employee pension insurance companies founded by law.
August	Amendments to the Payment Institutions Act entered into force. The Payment Institutions Act is applied to electronic money issuers. In addition to banks, the right to issue electronic money as defined in law is only permitted to payment institutions authorised to issue electronic money. These amendments serve to implement the Directive on the taking up, pursuit and prudential supervision of the business of electronic money institutions (E-Money Directive).
September	The Government submitted a letter to Parliament concerning the European Commission's proposals for a new Capital Requirements Directive and Regulation (CRD 4/CRR). Finland's position on the proposals is mainly affirmative. The trade reporting obligations of securities intermediaries reporting to the Financial Supervisory Authority (FIN-FSA) were extended to cover OTC derivatives, and reporting of customer identification data became mandatory.
October	The European Commission put forward its proposal for the review of the Markets in Financial Instruments Directive (MiFID). The draft Directive includes measures aimed at ensuring better access to capital markets for small and medium-sized enterprises, limiting disruptions caused by high frequency trading activities, increasing comparability of trading activities across EU countries and providing supervisory authorities with powers to ban trading activities in case of threats to financial stability. The Commission submitted a draft regulation related to insider dealing and market manipulation. The regulation would extend the scope of application of existing provisions to the OTC markets, while reinforcing and harmonising authorities' investigative and sanctioning powers. The EU Council, the European Parliament and the European Commission expressed their support to regulation related to short selling and credit default swaps (CDSs). Such regulation increases transparency, provides authorities with powers to temporarily restrict short selling and CDS trading in crisis situations.

	The European Commission submitted a draft Directive for a financial transaction tax in the EU financial sector. With the proposal, the Commission wants to prevent financial institutions from taking excessive risks and seeks to limit undesirable market behaviour and to ensure that the financial sector makes a fair contribution to covering the benefits received. Another aim is to amend the taxation of the financial sector so as to bring it more in line with that of other sectors and to raise tax revenues for the EU budget. The European Banking Authority (EBA) published its Guidelines on Internal Governance, the purpose of which is to enhance and consolidate supervisory expectations. Current financial sector regulation of the Financial Supervisory Authority (FIN-FSA) mainly corresponds to these Guidelines.
November	The Government proposed amendment of the investment funds Act (Act on Common Funds), where necessary, in connection with the transposition of the new UCITS IV Directive. According to the proposal, a fund management company would be allowed to establish an investment fund outside its home country in another member state belonging to the European Economic Area. The new provisions would also apply to national and cross-border mergers of investment funds. The European Commission submitted a draft Directive and Regulation on toughening the regulatory framework related to credit rating agencies. The proposal has four key objectives: 1) to reduce financial institutions' reliance on credit rating agencies, 2) to improve the quality of the rating process for sovereign debt ratings in the member states, 3) to increase competition and independence and 4) to make credit rating agencies more accountable for their ratings. The Government informed Parliament in a letter of its support to the European Commission's draft Directive concerning an EU-wide financial transaction tax. In accordance with the Government programme, however, the Government supports the introduction of the tax outside the EU, as well. In the summer of 2011, the Financial Supervisory Authority (FIN-FSA) undertook an assessment of the appropriate presentation of investment recommendations issued by six companies and the disclosure of information on the interests and conflicts of interest of the persons who had issued the recommendations. The assessment pointed to generally good compliance with the requirements of Standard (5.5) on investment recommendations. The results were published in November.
December	Amendments to the Standard of the Financial Supervisory Authority (FIN-FSA) on own funds and their minimum amount entered into force. The amendments are based on the second amendment to the Credit Requirements Directive (CRD 3) and concern value adjustments in respect of items subject to fair value measurement. Capital requirements for securitisations under the second amendment to the Capital Requirements Directive (CRD 3) and related FIN-FSA regulations entered into force. An updated version of the FIN-FSA Standard on the capital requirement for market risk entered into force. FIN-FSA issued new regulations and guidelines concerning the organisation and code of conduct for investment fund activities. They entered into force on 1 January 2012.

Other issues

January	Estonia introduced the euro on 1 January 2011, and at the same time the Estonian central bank became the 17th member of the Eurosystem. The European Systemic Risk Board (ESRB) commenced operations at the beginning of the year, convening for the first time on 20 January. The European Commission issued EUR 5 billion worth of bonds via the European Financial Stabilisation Mechanism (EFSM) to finance the support package for Ireland.
February	Staff teams from the European Commission, the ECB and the IMF visited Athens in order to conduct a quarterly review of the Greek government economic programme. A working group that had considered the overhaul of the Securities Markets Act submitted its report. An important aim of the overhaul is to improve the intelligibility of the legislation comprising separate individual parts. The working group also proposes provisions enabling wider use of multi-tiered custody and nominee registration in Finland. However, authorities' access to information must be secured in the multi-tiered custody framework.
March	Euro area Heads of State or Government decided to improve the lending capacity of the European Financial Stability Facility (EFSF) and to amend the loan terms and conditions for Greece so that they correspond to the pricing of loans granted via the EFSF. In accordance with the stability-related decisions of the European Council, it was decided to establish a permanent stability mechanism, the European Stability Mechanism (ESM). The ESM is to replace the current temporary arrangements, ie the European Financial Stability Facility (EFSF) and the European Financial Stabilisation Mechanism (EFSM), from the beginning of July 2013. It was also agreed that a decision on increasing the lending capacity of the EFSF from EUR 250 billion to EUR 440 billion would be made in June. The European Banking Authority (EBA), coordinating EU-wide stress testing, published an overall description of the test and the stress scenario applied.
April	Portugal submitted its official request for financial assistance on 7 April. Staff teams from the European Commission, the ECB and the IMF visited Dublin in order to conduct a quarterly review of the Irish government economic programme.
May	Portuguese authorities published a programme comprising three main elements: 1) fiscal adjustment to ensure fiscal sustainability, 2) reforms to enhance growth and competitiveness and 3) measures to strengthen the financial sector. EU ministers agreed to a financial aid package of EUR 78 billion in loans to Portugal, with financing covered equally between the European Financial Stabilisation Mechanism (EFSM), the European Financial Stability Facility (EFSF) and the IMF.

	The parliamentary Grand Committee announced that, if a euro area country besides Portugal were to request assistance in the form of loans from the European Financial Stability Facility, Finland would be prepared to consider such a request only on condition that the country concerned posts collateral for Finland's loan guarantees.
June	Parliament approved the Finnish Government guarantee for funding by the European Financial Stability Facility (EFSF) necessary for providing loans to Portugal. Staff teams from the European Commission, the ECB and the IMF visited Athens in order to conduct a quarterly review of the Greek government economic programme.
July	European Heads of State or Government decided at their summit meeting of 21 July that the total guarantee commitments for funding by the European Financial Stability Facility (EFSF) would be raised from EUR 440 billion to EUR 780 billion. It was also decided to enhance the effectiveness and flexibility of the EFSF. The European Financial Stability Facility can provide precautionary assistance to euro area member states, it can finance recapitalisation of financial institutions through loans to euro area governments and exceptionally also intervene in the debt markets in order to purchase bonds of euro area governments. The necessary amendments would be included in the Framework Agreement between the euro area countries and the EFSF. The summit also agreed on a second assistance package of EUR 109 billion to Greece, to be financed by the EFSF, the IMF and the private sector. The minimum maturity of EFSF loans was lengthened from 7.5 years to 15 years and the interest rate was lowered from the existing range of 4.8% to 5.5% to about 3.5%. The private sector was offered an opportunity to participate in burden-sharing via measures that would lower the nominal value of exchanged debt by 21%. The European Banking Authority (EBA) and national supervisory authorities published the results of European banks' stress tests on 15 July. Of the 90 participating banks, 8 banks fell below the 5% capital threshold in the stress scenario. These banks were requested to present a plan for remedial measures no later than October 2011. Finland's participating OP-Pohjola Group, the Nordea Group and the Danske Bank Group had adequate levels of capital. Staff teams from the European Commission, the ECB and the IMF visited Dublin in order to conduct a quarterly review of the Irish government economic programme.
August	Staff teams from the European Commission, the ECB and the IMF visited Lisbon in order to conduct a quarterly review of the Portuguese government economic programme.
September	Parliament approved the proposed amendment to the Framework Agreement between the euro area countries and the European Financial Stability Facility (EFSF). The Government gave its approval to the Agreement on the following day.

October	The Eurogroup agreed on the principles and the terms and conditions for the collateral arrangements related to the Greek loan programme. Collateral assets consist of AAA-rated securities. A member state receiving such collateral 1) forgoes potential profits earned by the European Financial Stability Facility (EFSF), 2) accepts that collateral is not paid until a long period has elapsed after the default and 3) pays its share of EFSF capital in one lump sum. Parliament approved the Government's proposal for increasing the guarantee commitments related to the EFSF from just under EUR 8 billion to approximately EUR 14 billion. The EU summit of 26 October made decisions on managing the sovereign debt crisis in the euro area: to set up a new EU-IMF programme of EUR 100 billion for Greece running until 2014, to reduce the Greek debt-to-GDP ratio to 120% by 2020 via a nominal discount of 50% on notional Greek government debt held by private investors, to increase the capacity of the EFSF, to strengthen Tier 1 capital in bank balance sheets by bringing the capital ratio to 9% by June 2012, to improve coordination of economic and fiscal policies and to enhance surveillance of agreed measures. Staff teams from the European Commission, the ECB and the IMF visited Dublin in order to conduct a quarterly review of the Irish government economic programme. Staff teams from the European Commission, the ECB and the IMF visited Athens in order to conduct a quarterly review of the Greek government economic programme. The European Systemic Risk Board (ESRB) published its first recommendation, addressed to the EU member states, national supervisory authorities and the European Banking Authority (EBA) and aimed at ensuring that risks related to foreign-currency lending will not increase so as to threaten the stability of the financial system. In Finland, the Government proposed continuation of preparations for an overhaul of securities markets legislation in two separate projects. The first phase includes proposals for a new Securities Markets Act and a new Investment Firms Act, for an Act on trading in financial instruments, for an Act on the book-entry system and settlement, a proposal for amending the Act on the Financial Supervisory Authority and a proposal for a new Act on securities accounts. The second phase focuses on assessing the possibilities to develop multi-tiered custody for securities. The proposed measures should be completed by the end of May 2012. The Government decided on a temporary (from 15 October 2011 to 31 December 2014) decree amendment under which the interest payable by the borrower will decline from 3.4% to 1.7% in respect of those subsidised loans that are granted for the construction of new rented housing for other than specialised groups. This decree amendment is based on the Government programme.
November	The European Commission submitted proposals for new regulations to strengthen the Stability and Growth Pact. Looking ahead, surveillance of member states' achievement of their medium-term objectives will be more effective, member states with high debt levels must reduce their debt ratios annually, enforcement of budgetary surveillance will improve thanks to new sanction mechanisms, and new preventive and corrective procedures will provide the EU Council with powers to address macroeconomic imbalances and competitiveness gaps.

	The European Commission proposed the launch of Stability Bonds or Eurobonds within euro area countries. The Finnish Government announced its non-acceptance with regard to Stability Bonds involving joint financial responsibility. Staff teams from the European Commission, the ECB and the IMF visited Lisbon in order to conduct a quarterly review of the Portuguese government economic programme. The Government submitted a proposal for improving export companies' chances of providing credit-type export finance. Under the new model, credit from the export credit agency of Finland, Finnvera, will be used to finance long-term export credit organised by a Finnish or foreign bank on OECD terms and conditions. The arrangement is accompanied by Finnvera's export guarantee. The Ministry of Finance decided on appointing Pohjola Bank as the new main intermediary bank for government payment services over an agreement period extending from 1 January 2012 to 30 November 2019. Nordea Bank Finland and Sampo Bank will be acting as ancillary intermediaries for these services. The former main intermediary bank for government payment services was Nordea Bank Finland. The Financial Supervisory Authority (FIN-FSA) proposed that the Ministry of Social Affairs and Health should confirm the amount of the solvency margin applied to insurance portfolio transfers to be 18.4% of technical provisions used for solvency calculation, as from 1 January 2012, instead of the previously applied 23.3%.
December	Euro area Heads of State or Government agreed in connection with the European Council (8 to 9 December) on measures to increase fiscal discipline within the EU. Fiscal rules will be supplemented, in addition to the annual deficit ceiling, with reforms to ensure longer-term fiscal sustainability and the imposition of more automatic sanctions. The rules will be tightened by an inter-governmental treaty. The Heads of State or Government also agreed on accelerating the entry into force of the permanent European Stability Mechanism (ESM) so as to be up and running as early as July 2012. The calculations required from banks by the European Banking Authority (EBA) and national supervisors showed that 31 large European banks need to strengthen their capital positions in order to achieve the 9% capital target. The combined capital shortfall was about EUR 115 billion. The European Commission issued a communication on the application of state aid for banks, starting from January 2012. Temporary aid programmes can be prolonged or approved for a duration of six months. If necessary, the programmes can be renewed or rolled over, subject to the Commission's consent, in mid-2012. The European Commission presented a new strategy to promote better access to finance for small and medium-sized enterprises (SMEs). The strategy includes an action plan to increase support from the EU budget and the European Investment Bank (EIB). It also includes a proposal for a new regulation confirming uniform rules for the marketing of venture capital funds. The Ministry of Employment and the Economy announced continued provision for one year of counter-cyclical finance to SMEs from Finnvera, a specialised financing company and Finland's export credit agency. In addition, the system will be changed so as to enable prolongation of the maximum maturity of granted loans and guarantees up to ten years, instead of the six-year maximum.

Main opinions issued by the Bank of Finland 2011

Opinions concerning legislation on and development of the financial markets

Opinion	*Subject*	*Date*
To the European Commission	Technical details of a possible European crisis management framework	3 Mar
To Euroclear Finland	Amendments to the decision by the managing director of Euroclear Finland 'Registration and settlement timetables'	30 Nov
To the Financial Supervisory Authority	Update of the statement concerning remuneration	7 Feb
	New Standard (6.1) on the provision of payment services and the related reporting Standard (Ra 6.1)	23 Mar
	Revision of the set of regulations and guidelines (investment classification, use of credit ratings in investment classification, safekeeping of documents concerning assets held to cover technical provisions and two individual rules governing assets held to cover technical provisions)	6 May
	Amendment of Standard (4.3k) on the capital requirement for counterparty credit risk	6 May
	Preparation of regulations and guidelines related to the transposition of the UCITS IV directive	15 May
	Marketing of money market funds and the Financial Supervisory Authority's statement concerning marketing in Finland of units other than those of UCITS funds and of undertakings for collective investment	20 May
	Revision of the set of regulations and guidelines (prepayment of housing loans)	17 Jun
	Draft regulation and guideline (auditing)	10 Nov
	Code of conduct for the provision of financial services	15 Nov
	Draft regulation and guideline (management of operational risk)	18 Nov
	Reporting of expenses and income in connection with long-term savings agreements and insurance contracts	23 Nov
	Draft regulation and guideline (outsourcing arrangements)	5 Dec

To the Ministry of Justice	Revision of the Companies Act in order to implement the Second Council Directive concerning the formation of public limited liability companies and the maintenance and alteration of their capital (77/91/EEC) and the Directive (2005/19/EC) amending the Merger Directive (90/434/EEC)	4 Apr
To the Ministry of Finance	Renewed application for authorisation by SIX X-clear AG	6 Apr
	Government Bill for an Act amending the Payment Institutions Act and for certain related Acts (implementation of the E-Money Directive)	20 Apr
	Memorandum of a working group considering the overhaul of securities markets legislation	4 May
	Proposal for an Act amending the investment funds Act (Act on Common Funds) and for certain related Acts (transposition of the UCITS IV Directive)	10 May
	Draft Government Bill to Parliament for an Act amending the Act on the Financial Supervisory Authority and for certain related Acts	8 Jul
	Confirmation of the sum of contributions to Investors' Compensation Fund in 2011	12 Sep
	Application by Euroclear Finland for amendment of the company's rules	14 Sep
	Government letter (U37/2011vp) concerning European Commission proposals for a Capital Requirements Directive and Regulation (CRD IV)	26 Oct

Bank of Finland's publications in 2011

Periodical publications	
Euro & talous	Five issues (in Finnish).
Bank of Finland Bulletin	Five issues.
Research Newsletter	Four quarterly issues of the online research bulletin in Finland (in Finnish and English).
Annual report	Published separately in Finnish, Swedish and English.
Research publications	
Discussion Papers	24 online studies and reports in the areas of macroeconomics and financial markets were published in English.
Studies and reports	8 online studies and reports were published in the *BoF Online series*.
	Two issues of the *Financial Market Report* were published online (in Finnish and English).
	Corporate funding survey, published in January (in Finnish only).
Expository studies	*A:114 Tapio Korhonen* From regulation to market liberalisation. The Bank of Finland's regulatory framework for monetary and exchange rate policy during the period of regulation and liberalisation in the 1970s and the 1980s (in Finnish only).
	A:115 Tapio Korhonen From economic crisis to monetary union. The Bank of Finland's operational framework for monetary and exchange rate policy during the 1990s economic and banking crisis and in the run-up to monetary union (in Finnish only).
Statistical publications	*Financial markets*, a monthly online publication (in Finnish, Swedish and English).
	Finland's balance of payments, a monthly online publication (in Finnish, Swedish and English).
	Finland's balance of payments, *annual review*, published online in September (in Finnish, Swedish and English).
	Finnish bond issues, published online in May (in Finnish, Swedish and English).
	Monetary and banking statistics, a monthly online publication (in Finnish, Swedish and English).
	Financial statistics, *annual review*, published online in February (in Finnish, Swedish and English).
	International Reserves and Foreign Currency Liquidity, a monthly publication (in English).

Studies published by the Institute for Economies in Transition

Research publications	36 online studies were published in the *BOFIT Discussion Papers* series (in English). 8 publications appeared in the *BOFIT Online* series (in Finnish or in English).
Monitoring publications	*BOFIT Viikkokatsaus*, a weekly online publication (in Finnish). *BOFIT Weekly*, a weekly online publication (in English). *BOFIT Venäjä-ennuste*, a bi-annual online publication (in Finnish). *BOFIT Forecast for Russia*, a bi-annual online publication (in English). *BOFIT Venäjä-tilastot*, an online publication (in Finnish). *BOFIT Russia Statistics*, an online publication (in English). *BOFIT Kiina-ennuste*, a bi-annual online publication (in Finnish). *BOFIT Forecast for China*, a bi-annual online publication (in English). *BOFIT Kiina-tilastot*, an online publication (in Finnish). *BOFIT China Statistics*, an online publication (in English).
Orders and subscriptions	A comprehensive list of publications is available on the Bank of Finland's website (http://www.suomenpankki.fi/en/julkaisut/Pages/default.aspx). The Bank of Finland website offers a service where these publications can be subscribed to free of charge. The subscriber will be alerted by email of the release of the desired publication. Online subscriptions can be made at the Bank of Finland's website: Bank of Finland > Publications > Order and Subscribe to electronic publications and reports. The Bank's publications Euro & talous (in Finnish) and Bank of Finland Bulletin as well as the Bank's and ECB's annual reports also appear in print. Online subscriptions to the printed copies can be made at the Bank of Finland's website: Bank of Finland > Publications > Order and subscribe to printed publications. Back copies of printed publications can also be ordered from that same website address.

Supplementary tables

Totals/sub-totals may not add up because of rounding.

0	*less than half the final digit shown*
.	*logically impossible*
..	*data not available*
–	*nil*
_	*change in contents of series*

Table 1.
Monthly balance sheet of the Bank of Finland, EUR m

Assets		Jan	Feb	Mar
1	***Gold and gold receivables***	***1,664***	***1,664***	***1,664***
2	***Claims on non-euro area residents denominated in foreign currency***	***5,885***	***5,392***	***5,867***
2.1	*Receivables from the IMF*	*1,837*	*1,829*	*1,936*
2.2	*Balances with banks and security investments, external loans and other external assets*	*4,048*	*3,564*	*3,932*
3	***Claims on euro area residents denominated in foreign currency***	***695***	***588***	***627***
4	***Claims on non-euro area residents denominated in euro***	***1,587***	***1,871***	***1,681***
4.1	*Balances with bank, security investments and loans*	*1,587*	*1,871*	*1,681*
4.2	*Claims arising from the credit facility under ERM II*	–	–	–
5	***Lending to euro area credit institutions related to monetary policy operations denominated in euro***	***50***	***50***	***50***
5.1	*Main refinancing operations*	–	–	–
5.2	*Longer-term refinancing operations*	*50*	*50*	*50*
5.3	*Fine-tuning reverse operations*	–	–	–
5.4	*Structural reverse operations*	–	–	–
5.5	*Marginal lending facility*	–	–	–
5.6	*Credits related to margin calls*	–	–	–
6	***Other claims on euro area credit institutions denominated in euro***	***101***	***51***	***0***
7	***Securities of euro area residents denominated in euro***	***11,587***	***11,625***	***11,362***
7.1	*Securities held for monetary policy purposes*	*2,254*	*2,284*	*2,243*
7.2	*Other euro-denominated securities*	*9,333*	*9,341*	*9,341*
8	***General government debt denominated in euro***	–	–	–
9	***Intra-Eurosystem claims***	***11,002***	***7,907***	***10,268***
9.1	*Participating interest in ECB*	*99*	*99*	*99*
9.2	*Claims equivalent to the transfer of foreign reserves*	*722*	*722*	*722*
9.3	*Claims related to the issuance of ECB debt certificates*	–	–	–
9.4	*Claims related to TARGET and correspondent accounts (net)*	*6,802*	*3,880*	*6,296*
9.5	*Other intra-Eurosystem claims (net)*	*3,379*	*3,206*	*3,150*
10	***Other assets***	***1,047***	***1,065***	***1,056***
Total assets		***33,618***	***30,214***	***32,575***

Totals/sub-totals may not add up because of rounding.
Source: Bank of Finland.

Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
1,588	***1,588***	***1,588***	***1,645***	***1,645***	***1,902***	***1,902***	***1,902***	***1,918***
5,362	***5,396***	***5,687***	***5,539***	***5,500***	***5,861***	***5,911***	***5,825***	***5,886***
1,870	*1,846*	*1,846*	*1,822*	*1,822*	*1,921*	*1,921*	*1,868*	*1,967*
3,492	*3,550*	*3,841*	*3,718*	*3,677*	*3,940*	*3,989*	*3,957*	*3,919*
522	***462***	***564***	***465***	***395***	***496***	***452***	***480***	***628***
2,166	***1,786***	***2,458***	***2,312***	***2,249***	***2,371***	***2,345***	***1,934***	***1,946***
2,166	*1,786*	*2,458*	*2,312*	*2,249*	*2,371*	*2,345*	*1,934*	*1,946*
–	–	–	–	–	–	–	–	–
50	***50***	***50***	***70***	***100***	***50***	***160***	***160***	***2,311***
–	–	–	–	–	–	–	–	*10*
50	*50*	*50*	*70*	*100*	*50*	*160*	*160*	*2,301*
–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–
6	***391***	***0***	***0***	***0***	***0***	***0***	***0***	***40***
10,907	***10,873***	***10,706***	***10,716***	***11,784***	***12,609***	***13,016***	***13,729***	***13,889***
2,206	*2,186*	*2,143*	*2,146*	*2,925*	*3,748*	*3,969*	*4,469*	*4,637*
8,701	*8,687*	*8,563*	*8,570*	*8,859*	*8,860*	*9,047*	*9,260*	*9,253*
–	–	–	–	–	–	–	–	–
8,825	***10,421***	***9,945***	***10,077***	***24,850***	***47,499***	***37,228***	***39,479***	***70,348***
99	*99*	*99*	*99*	*99*	*99*	*99*	*99*	*120*
722	*722*	*722*	*722*	*722*	*722*	*722*	*722*	*722*
–	–	–	–	–	–	–	–	–
4,813	*6,410*	*5,985*	*6,005*	*20,778*	*43,420*	*33,149*	*35,341*	*66,008*
3,190	*3,190*	*3,138*	*3,251*	*3,251*	*3,257*	*3,257*	*3,317*	*3,497*
1,177	***1,183***	***1,169***	***1,082***	***1,093***	***1,118***	***1,016***	***1,051***	***1,171***
30,601	***32,150***	***32,167***	***31,907***	***47,617***	***71,907***	***62,029***	***64,560***	***98,138***

Table 1.
(cont.)

Liabilities		Jan	Feb	Mar
1	***Banknotes in circulation***	***13,709***	***13,568***	***13,546***
2	***Liabilities to euro area credit institutions related to monetary policy operations denominated in euro***	***8,981***	***6,103***	***8,542***
2.1	*Current accounts (covering the minimum reserve system)*	*5,743*	*1,997*	*3,350*
2.2	*Deposit facility*	*1,058*	*1,327*	*1,992*
2.3	*Fixed-term deposits*	*2,181*	*2,779*	*3,200*
2.4	*Fine-tuning reverse operations*	–	–	–
2.5	*Deposits related to margin calls*	–	–	–
3	***Other liabilities to euro area credit institutions denominated in euro***	–	–	***124***
4	***Liabilities to other euro area residents denominated in euro***	***290***	***282***	***279***
4.1	*General government*	–	–	–
4.2	*Other liabilities*	*290*	*282*	*279*
5	***Liabilities to non-euro area residents denominated in euro***	***1,485***	***1,092***	***739***
6	***Liabilities to euro area residents denominated in foreign currency***	***0***	***0***	***0***
7	***Liabilities to non-euro area residents denominated in foreign currency***	***15***	***33***	***177***
7.1	*Deposits. balances and other liabilities*	*15*	*33*	*177*
7.2	*Liabilities arising from the credit facility under ERM II*	–	–	–
8	***Counterpart of special drawing rights allocated by the IMF***	***1,377***	***1,377***	***1,377***
9	***Intra-Eurosystem liabilities***	***33***	–	–
9.1	*Liabilities related to promissory notes backing the issuance of ECB debt certificates*	–	–	–
9.2	*Liabilities related to TARGET and correspondent accounts (net)*	–	–	–
9.3	*Other intra-Eurosystem liabilities (net)*	*33*	–	–
10	***Other liabilities***	***955***	***1,019***	***1,050***
11	***Revaluation account***	***2,274***	***2,274***	***2,274***
12	***Capital and reserves***	***4,499***	***4,467***	***4,467***
12.1	*Primary capital*	*841*	*841*	*841*
12.2	*Reserve fund*	*1,334*	*1,334*	*1,334*
12.3	*Pension provisions*	*502*	*502*	*502*
12.4	*Other provisions*	*1,822*	*1,790*	*1,790*
Total liabilities		***33,618***	***30,214***	***32,575***

Totals/sub-totals may not add up because of rounding.
Source: Bank of Finland.

Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
13,754	13,807	13,917	14,106	14,060	14,133	14,189	14,339	14,649
7,188	8,713	8,067	7,993	23,645	47,033	36,989	39,527	71,697
4,403	4,543	4,867	5,338	4,805	1,030	939	2,690	1,657
335	320	2,000	1,655	12,402	27,331	19,581	22,170	52,540
2,450	3,850	1,200	1,000	6,438	18,671	16,469	14,667	17,500
–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–
128	103	105	117	105	103	102	101	836
–	–	–	–	–	–	–	–	–
128	103	105	117	105	103	102	101	836
778	753	1,261	777	859	800	913	710	782
0	0	0	0	0	0	0	0	0
229	220	234	250	253	229	228	210	153
229	220	234	250	253	229	228	210	153
–	–	–	–	–	–	–	–	–
1,328	1,328	1,328	1,316	1,316	1,376	1,376	1,376	1,412
–	–	–	–	–	–	–	–	76
–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	–
–	–	–	–	–	–	–	–	76
284	315	345	395	424	537	537	602	432
1,835	1,835	1,835	1,877	1,877	2,618	2,618	2,618	2,806
5,077	5,077	5,077	5,077	5,077	5,077	5,077	5,077	5,294
841	841	841	841	841	841	841	841	841
1,421	1,421	1,421	1,421	1,421	1,421	1,421	1,421	1,421
526	526	526	526	526	526	526	526	544
2,289	2,289	2,289	2,289	2,289	2,289	2,289	2,289	2,488
30,601	32,150	32,167	31,907	47,617	71,907	62,029	64,560	98,138

Table 2.
Key interest rates of the Eurosystem

Fixed rate tenders – Interest rate on main refinancing operations			*Variable rate tenders – Minimum bid rate*		
Decision date	*Effective*	*%*	*Decision date*	*Effective*	*%*
22 Dec 1998	1 Jan 1999	3.00	8 Jun 2000	28 Jun 2000	4.25
8 Apr 1999	14 Apr 1999	2.50	31 Aug 2000	6 Sep 2000	4.50
4 Nov 1999	10 Nov 1999	3.00	5 Oct 2000	11 Nov 2000	4.75
3 Feb 2000	9 Feb 2000	3.25	10 May 2001	15 May 2001	4.50
16 Mar 2000	22 Mar 2000	3.50	30 Aug 2001	5 Sep 2001	4.25
27 Apr 2000	4 May 2000	3.75	17 Sep 2001	19 Sep 2001	3.75
8 Jun 2000	15 Jun 2000	4.25	8 Nov 2001	14 Nov 2001	3.25
			5 Dec 2002	11 Dec 2002	2.75
			6 Mar 2003	7 Mar 2003	2.50
8 Oct 2008	15 Oct 2008	3.75	5 Jun 2003	6 Jun 2003	2.00
6 Nov 2008	12 Nov 2008	3.25	1 Dec 2005	6 Dec 2005	2.25
4 Dec 2008	10 Dec 2008	2.50	2 Mar 2006	8 Mar 2006	2.50
15 Jan 2009	21 Jan 2009	2.00	8 Jun 2006	15 Jun 2006	2.75
5 Mar 2009	11 Mar 2009	1.50	3 Aug 2006	9 Aug 2006	3.00
2 Apr 2009	8 Apr 2009	1.25	5 Nov 2006	11 Oct 2006	3.25
7 May 2009	13 May 2009	1.00	7 Dec 2006	13 Dec 2006	3.50
7 Apr 2011	13 Apr 2011	1.25	8 Mar 2007	14 Mar 2007	3.75
7 Jul 2011	13 Jul 2011	1.50	7 Jun 2007	13 Jun 2007	4.00
3 Nov 2011	9 Nov 2011	1.25	3 Jul 2008	9 Jul 2008	4.25
8 Dec 2011	14 Dec 2011	1.00			

Standing facilities

	Interest rate on deposit facility		*Interest rate on marginal lending facility*
Decision date	*Effective*	*%*	*%*
22 Dec 1998	1 Jan 1999	2.00	4.50
22 Dec 1998	4 Jan 1999	2.75	3.25
21 Jan 1999	22 Jan 1999	2.00	4.50
8 Apr 1999	9 Apr 1999	1.50	3.50
4 Nov 1999	5 Nov 1999	2.00	4.00
3 Feb 2000	4 Feb 2000	2.25	4.25
16 Mar 2000	17 Mar 2000	2.50	4.50
27 Apr 2000	28 Apr 2000	2.75	4.75
8 Jun 2000	9 Jun 2000	3.25	5.25
31 Aug 2000	1 Sep 2000	3.50	5.50
5 Oct 2000	6 Oct 2000	3.75	5.75
10 May 2001	11 May 2001	3.50	5.50
30 Aug 2001	31 Aug 2001	3.25	5.25
17 Sep 2001	18 Sep 2001	2.75	4.75
8 Nov 2001	9 Nov 2001	2.25	4.25
5 Dec 2002	6 Dec 2002	1.75	3.75
6 Mar 2003	7 Mar 2003	1.50	3.50
5 Jun 2003	6 Jun 2003	1.00	3.00
1 Dec 2005	6 Dec 2005	1.25	3.25
2 Mar 2006	8 Mar 2006	1.50	3.50
8 Jun 2006	15 Jun 2006	1.75	3.75
3 Aug 2006	9 Aug 2006	2.00	4.00
5 Oct 2006	11 Oct 2006	2.25	4.25
7 Dec 2006	13 Dec 2006	2.50	4.50
8 Mar 2007	14 Mar 2007	2.75	4.75
7 Jun 2007	13 Jun 2007	3.00	5.00
3 Jul 2008	9 Jul 2008	3.25	5.25
8 Oct 2008	8 Oct 2008	2.75	4.75
8 Oct 2008	9 Oct 2008	3.25	4.25
6 Nov 2008	12 Nov 2008	2.75	3.75
4 Dec 2008	10 Dec 2008	2.00	3.00
15 Jan 2009	21 Jan 2009	1.00	3.00
5 Mar 2009	11 Mar 2009	0.50	2.50
2 Apr 2009	8 Apr 2009	0.25	2.25
7 May 2009	13 May 2009	0.25	1.75
7 Apr 2011	13 Apr 2011	0.50	2.00
7 Jul 2011	13 Jul 2011	0.75	2.25
3 Nov 2011	9 Nov 2011	0.50	2.00
8 Dec 2011	14 Dec 2011	0.25	1.75

Source: European Central Bank.

Table 3.
Reserve base of euro area credit institutions subject to reserve requirements, EUR bn

Reserve base as of:	Total	Liabilities to which a 1% reserve coefficient is applied*		Liabilities to which a 0% reserve coefficient is applied		
		Deposits (overnight, up to 2 years' agreed maturity and notice period)	Debt securities up to 2 years' agreed maturity	Deposits (over 2 years' agreed maturity and notice period)	Repos	Debt securities over 2 years' agreed maturity
	1	2 3 4 5				6
2010						
Dec	18,948.1	9,962.6	644.3	2,683.3	1,335.4	4,322.5
2011						
Jan	19,024.1	9,840.2	651.6	2,780.6	1,395.8	4,356.0
Feb	19,035.7	9,768.4	670.3	2,727.5	1,490.3	4,379.2
Mar	18,872.4	9,700.2	671.9	2,737.5	1,399.8	4,363.0
Apr	18,988.1	9,749.5	662.8	2,744.0	1,475.2	4,356.6
May	19,175.7	9,787.9	677.0	2,764.2	1,538.4	4,408.3
Jun	19,039.4	9,730.8	643.5	2,777.9	1,491.7	4,395.4
Jul	19,046.3	9,695.1	635.0	2,777.7	1,502.7	4,435.8
Aug	19,095.3	9,688.3	645.8	2,782.6	1,557.4	4,421.3
Sep	19,247.9	9,761.9	650.5	2,808.3	1,576.5	4,450.7
Oct	19,126.2	9,718.9	657.4	2,788.5	1,562.7	4,398.7
Nov	19,073.0	9,708.5	673.6	2,776.0	1,509.5	4,405.4
Dec	18,970.1	9,790.9	687.7	2,781.2	1,303.5	4,406.8

*) Until October 2011 the reserve ratio was 2%.
Source: European Central Bank.

Reserve base of Finnish credit institutions subject to reserve requirements, EUR m

Reserve base as of:	Total	Liabilities to which a 1% reserve coefficient is applied*		Liabilities to which a 0% reserve coefficient is applied		
		Deposits (overnight, up to 2 years' agreed maturity and notice period)	Debt securities up to 2 years' agreed maturity	Deposits (over 2 years' agreed maturity and notice period)	Repos	Debt securities over 2 years' agreed maturity
	1	2 3 4 5				6
2010						
Dec	281,947	197,370	19,314	6,459	17,878	40,925
2011						
Jan	285,862	186,531	19,373	6,503	33,071	40,384
Feb	283,953	183,166	19,283	6,591	33,333	41,579
Mar	291,960	185,845	20,001	6,603	38,189	41,322
Apr	292,791	187,853	18,590	6,711	36,960	42,676
May	298,864	189,194	19,028	6,812	37,528	46,303
Jun	305,069	193,573	19,484	6,912	38,639	46,462
Jul	302,235	195,650	19,505	6,493	32,153	48,433
Aug	319,406	207,260	20,252	6,828	34,952	50,114
Sep	339,160	231,352	19,991	7,801	30,566	49,449
Oct	330,583	221,875	20,030	7,965	30,539	50,174
Nov	341,773	232,187	19,636	8,156	31,704	50,089
Dec	360,549	251,193	20,164	9,296	28,502	51,395

*) Until October 2011 the reserve ratio was 2%.
Source: Bank of Finland.

Table 4.
Reserve maintenance of euro area credit institutions subject to reserve requirements, EUR bn

Maintenance period ending in	Required reserves	Actual reserves	Excess reserves	Deficiencies	Interest rate on minimum reserves, %
	1	2	3	4	5
2010					
Dec	211.8	212.5	0.7	0.5	1.00
2011					
Jan	210.5	212.4	1.9	0.0	1.00
Feb	212.3	213.6	1.3	0.0	1.00
Mar	211.6	212.9	1.3	0.0	1.00
Apr	209.3	210.5	1.1	0.0	1.00
May	208.3	209.5	1.2	0.0	1.25
Jun	206.9	209.0	2.0	0.0	1.25
Jul	207.7	210.9	3.1	0.0	1.25
Aug	208.8	211.5	2.7	0.0	1.50
Sep	207.0	209.5	2.5	0.0	1.50
Oct	206.1	208.7	2.6	0.0	1.50
Nov	206.2	208.9	2.8	0.0	1.50
Dec	207.7	212.2	4.5	0.0	1.25
2012					
Jan	207.0	212.3	5.3	0.0	1.00

Source: European Central Bank.

Reserve maintenance of Finnish credit institutions subject to reserve requirements, EUR m

Maintenance period ending in	Required reserves	Actual reserves	Excess reserves	Deficiencies	Interest rate on minimum reserves, %
	1	2	3	4	5
2010					
Dec	3,917	3,931	14.3	0.0	1.0
2011					
Jan	4,141	4,147	6.6	0.0	1.0
Feb	4,302	4,308	6.7	0.0	1.0
Mar	4,086	4,094	7.4	0.0	1.0
Apr	4,017	4,027	10.3	0.0	1.3
May	4,085	4,093	7.2	0.0	1.3
Jun	4,097	4,106	8.5	0.0	1.3
Jul	4,133	4,141	7.7	0.0	1.5
Aug	4,230	4,238	8.4	0.0	1.5
Sep	4,272	4,280	8.2	0.0	1.5
Oct	4,519	4,528	9.2	0.0	1.5
Nov	4,996	5,004	8.5	0.0	1.3
Dec	4,807	4,816	8.6	0.0	1.0
2012					
Jan	2,488	2,505	16.9	0.0	1.0

Source: Bank of Finland.

Table 5.
Euro area monetary aggregate M3 and corresponding items of Finnish monetary financial institutions[1]

	Euro area monetary aggregate M3			Liabilities of Finnish monetary financial institutions included in euro area M3[2]		
	Stock[3]. EUR bn	12-month change[3.4]. %	3-month mov avg of 12-month change[3.4]. %	Stock. EUR bn	12-month change[4]. %	3-month mov avg of 12-month change[4]. %
	1	2 3 4 5				6
2007	8,656.9	11.6	11.9	122.8	19.7	18.7
2008	9,404.7	7.7	7.1	129.2	5.0	5.7
2009	9,344.4	–0.4	–0.2	127.6	–1.7	–1.7
2010	9,540.2	1.7	1.8	137.2	4.8	4.0
2011	9,740.9	1.6	2.0	143.9	6.9	7.7
2011						
Jan	9,526.8	1.7	1.8	135.5	3.7	3.6
Feb	9,576.7	2.2	2.0	133.0	2.3	3.6
Mar	9,589.7	2.2	2.1	135.3	4.9	4.3
Apr	9,595.0	1.9	2.2	136.2	5.6	5.2
May	9,658.5	2.3	2.1	137.8	5.2	5.6
Jun	9,665.4	2.0	2.1	139.0	6.1	5.0
Jul	9,681.5	2.0	2.2	138.1	3.8	6.0
Aug	9,800.4	2.7	2.5	142.1	8.0	7.7
Sep	9,825.1	2.9	2.8	143.7	11.2	9.5
Oct	9,782.5	2.6	2.5	143.2	9.3	9.9
Nov	9,775.6	1.9	2.0	142.3	9.1	8.4
Dec	9,740.9	1.6	2.0	143.9	6.9	7.7

1 Excl. negotiable instruments held by central governments and non-euro area residents.
2 Excl. notes and coins held by the public.
3 Seasonally and calendar effect adjusted.
4 Calculated from monthly differences in stocks adjusted for reclassifications. other revaluations. exchange rate variations and any other changes which do not arise from transactions.
Sources: European Central Bank and Bank of Finland.

Table 6.
Key market interest rates

	Eonia rate	Euribor rates (actual/360)						Yields on Finnish government bonds	
		1-month	2-month	3-month	6-month	9-month	12-month	5-year	10-year
	1	2	3	4	5	6	7	8	9
2007	3.87	4.080	4.194	4.277 4.351 4.406			4.449	4.18	4.29
2008	3.87	4.276	4.484	4.644 4.727 4.774			4.826	3.88	4.30
2009	0.71	0.888	1.057	1.218 1.429 1.529			1.610	2.70	3.74
2010	0.44	0.570	0.663	0.813 1.083 1.223			1.352	1.78	3.00
2011	0.87	1.178	1.260	1.393 1.638 1.826			2.009	2.08	3.00
2011									
Jan	0.66	0.793	0.888	1.017 1.254 1.406			1.550	2.147	3.268
Feb	0.71	0.894	0.968	1.087 1.352 1.537			1.714	2.377	3.411
Mar	0.66	0.903	1.028	1.176 1.483 1.717			1.924	2.733	3.450
Apr	1.01	1.133	1.195	1.325 1.625 1.866			2.089	2.888	3.565
May	1.03	1.243	1.292	1.425 1.707 1.932			2.147	2.654	3.322
Jun	1.12	1.279	1.359	1.489 1.749 1.949			2.144	2.445	3.285
Jul	1.01	1.422	1.479	1.598 1.818 1.994			2.183	2.318	3.164
Aug	0.91	1.373	1.437	1.552 1.755 1.918			2.097	1.731	2.681
Sep	1.01	1.347	1.416	1.536 1.736 1.896			2.067	1.446	2.353
Oct	0.96	1.363	1.437	1.576 1.776 1.942			2.110	1.552	2.513
Nov	0.79	1.227	1.334	1.485 1.706 1.879			2.044	1.502	2.542
Dec	0.62	1.141	1.257	1.425 1.670 1.841			2.003	1.282	2.516

Sources: European Central Bank. Reuters and Bloomberg.

Table 7.
Nominal competitiveness indicators for Finland and the effective exchange rate of the euro calculated by the ECB

	Narrow indicator[1]	Narrow plus euro area indicator [1]	Broad indicator[1]	Effective exchange rate of the euro, narrow group of countries[1]
	January–March 1999 = 100			
	1	2	3	4
2007	108,0	104,0	104,8	113,2
2008	114,5	107,0	107,3	120,7
2009	115,8	107,6	108,8	120,6
2010	107,6	103,6	104,3	111,9
2011	106,7	103,0	104,0	111,2
2011				
Jan	104,8	102,1	102,8	109,1
Feb	105,6	102,5	103,2	110,1
Mar	107,4	103,3	104,1	112,3
Apr	109,6	104,3	105,2	114,8
May	108,5	103,9	104,7	113,4
Jun	108,9	104,1	105,0	113,6
Jul	107,9	103,6	104,5	111,9
Aug	107,4	103,5	104,5	111,3
Sep	105,9	102,7	103,8	110,1
Oct	105,9	102,7	103,9	110,5
Nov	105,2	102,4	103,5	109,7
Dec	103,4	101,4	102,5	107,7

[1] An upward movement of the index represents an appreciation of the euro. The narrow indicator comprises 12 countries, 1999, the narrow plus euro area indicator 23 countries, and the broad indicator 37 countries.
Sources: European Central Bank and Bank of Finland.

Table 8.
Harmonised Index of Consumer Prices for euro area and Finland. annual change, %

	Euro area	Finland
	1	2
2007	2.1	1.6
2008	3.3	3.9
2009	0.3	1.6
2010	1.6	1.7
2011	2.7	3.3
2011		
Jan	2.3	3.1
Feb	2.4	3.5
Mar	2.7	3.5
Apr	2.8	3.4
May	2.7	3.4
Jun	2.7	3.4
Jul	2.5	3.7
Aug	2.5	3.5
Sep	3.0	3.5
Oct	3.0	3.2
Nov	3.0	3.2
Dec	2.7	2.6

Sources: Eurostat and Statistics Finland.

Table 9.
Key euro exchange rates. currency-value of one euro

	US dollar			Japanese yen		
	Low	Average	High	Low	Average	High
	1	2 3 4 5				6
2007	1.2893	1.3705	1.4874	150.93	161.25	168.68
2008	1.2460	1.4708	1.5990	115.75	152.45	169.75
2009	1.2555	1.3948	1.5120	113.65	130.34	138.09
2010	1.1942	1.3257	1.4563	106.19	116.24	134.23
2011	1.2889	1.3920	1.4882	100.20	110.96	122.80
2011						
Jan	1.2903	1.3360	1.3716	107.17	110.38	113.90
Feb	1.3440	1.3649	1.3834	111.42	112.77	113.69
Mar	1.3773	1.3999	1.4211	110.42	114.40	117.61
Apr	1.4141	1.4442	1.4860	118.23	120.42	122.80
May	1.4020	1.4349	1.4882	114.35	116.47	120.85
Jun	1.4088	1.4388	1.4652	113.63	115.75	117.55
Jul	1.3975	1.4264	1.4500	110.59	113.26	117.23
Aug	1.4143	1.4343	1.4487	108.29	110.43	113.24
Sep	1.3430	1.3770	1.4285	102.32	105.75	110.08
Oct	1.3181	1.3706	1.4160	101.08	105.06	109.22
Nov	1.3229	1.3556	1.3809	102.59	105.02	107.78
Dec	1.2889	1.3179	1.3511	100.20	102.55	105.25

	Pound sterling			Swedish krona		
	Low	Average	High	Low	Average	High
	7	8 9		10	11	12
2007	0.65485	0.68434	0.7348	9.0190	9.2501	9.4754
2008	0.74130	0.79628	0.9786	9.2790	9.6152	11.2305
2009	0.84255	0.89094	0.9610	10.0778	10.6191	11.7135
2010	0.81040	0.85784	0.9114	8.9630	9.5373	10.2723
2011	0.83155	0.86788	0.9050	8.7090	9.0298	9.3127
2011						
Jan	0.83155	0.84712	0.86325	8.8435	8.9122	8.9765
Feb	0.83750	0.84635	0.85530	8.7255	8.7882	8.8800
Mar	0.84780	0.86653	0.88370	8.7090	8.8864	8.9922
Apr	0.87285	0.88291	0.89170	8.8885	8.9702	9.0822
May	0.86685	0.87788	0.89990	8.8914	8.9571	9.0682
Jun	0.87530	0.88745	0.90255	8.8890	9.1125	9.2475
Jul	0.87315	0.88476	0.90500	9.0632	9.1340	9.2534
Aug	0.86905	0.87668	0.88565	9.0070	9.1655	9.2947
Sep	0.86015	0.87172	0.88120	8.8945	9.1343	9.3127
Oct	0.85650	0.87036	0.87935	9.0090	9.1138	9.1650
Nov	0.85335	0.85740	0.86570	9.0272	9.1387	9.2597
Dec	0.83230	0.84405	0.86020	8.9120	9.0184	9.1258

Source: European Central Bank.

Table 10.
Other euro exchange rates. currency-value of one euro, average

	Czech koruna	Danish krone	Hungarian forinti	Lithuanian litas	Latvian lats	Puolan zloty
	1	2	3	4	5	6
2007	27.766	7.451	251.357	3.453	0.700	3.784
2008	24.946	7.456	251.512	3.453	0.703	3.512
2009	26.435	7.446	280.327	3.453	0.706	4.328
2010	25.284	7.447	275.480	3.453	0.709	3.995
2011	24.590	7.451	279.373	3.453	0.706	4.121
2011						
Jan	24.449	7.452	275.326	3.453	0.703	3.890
Feb	24.277	7.455	271.153	3.453	0.704	3.926
Mar	24.393	7.457	270.890	3.453	0.707	4.014
Apr	24.301	7.457	265.287	3.453	0.709	3.969
May	24.381	7.457	266.958	3.453	0.709	3.940
Jun	24.286	7.458	266.871	3.453	0.709	3.970
Jul	24.335	7.456	267.681	3.453	0.709	3.995
Aug	24.273	7.450	272.367	3.453	0.709	4.120
Sep	24.556	7.446	285.047	3.453	0.709	4.338
Oct	24.841	7.444	296.790	3.453	0.706	4.352
Nov	25.464	7.441	309.151	3.453	0.702	4.432
Dec	25.514	7.434	304.188	3.453	0.698	4.477

	Turkish lira	Australian dollar	Canadian dollar	Chinese yuan renminbi	Hong Kong dollar	Indonesian rupiah	South Korean won
	14	15	16	17	18	19	20
2007	1.786	1.635	1.468	10.418	10.691	12528.325	1272.988
2008	1.906	1.742	1.559	10.224	11.454	14165.164	1606.087
2009	2.163	1.773	1.585	9.528	10.811	14443.740	1772.904
2010	1.997	1.442	1.365	8.971	10.299	12041.705	1531.821
2011	2.338	1.348	1.376	8.996	10.836	12206.510	1541.234
2011							
Jan	2.092	1.342	1.328	8.815	10.395	12077.466	1495.503
Feb	2.170	1.354	1.348	8.984	10.631	12165.925	1524.991
Mar	2.211	1.385	1.367	9.190	10.909	12263.182	1568.054
Apr	2.197	1.366	1.383	9.427	11.227	12493.481	1567.516
May	2.260	1.344	1.388	9.320	11.155	12290.330	1555.990
Jun	2.308	1.357	1.406	9.316	11.202	12327.023	1555.318
Jul	2.365	1.325	1.364	9.212	11.110	12171.265	1510.293
Aug	2.515	1.365	1.407	9.186	11.185	12249.948	1542.014
Sep	2.474	1.346	1.379	8.799	10.733	12118.494	1544.042
Oct	2.509	1.352	1.398	8.731	10.662	12150.543	1578.175
Nov	2.457	1.341	1.390	8.615	10.549	12214.985	1537.425
Dec	2.463	1.300	1.348	8.356	10.250	11965.395	1513.264

Sources: European Central Bank and Bank of Finland.

	Swiss franc	Icelandic krona	Norwegian krone	Bulgarian lev	Croatian kuna	Romanian leu	Russian rouble
	7	8	9	10	11	12	13
2007	1.643	87.634	8.017	1.956	7.337	..	35.018
2008	1.587	..	8.224	1.956	7.224	..	36.421
2009	1.510	..	8.728	1.956	7.340	..	44.138
2010	1.380	..	8.004	1.956	7.289	..	40.263
2011	1.233	..	7.793	1.956	7.439	..	40.885
2011							
Jan	1.278	..	7.820	1.956	7.401	4.262	40.256
Feb	1.297	..	7.821	1.956	7.415	4.246	39.947
Mar	1.287	..	7.829	1.956	7.391	4.162	39.806
Apr	1.298	..	7.807	1.956	7.364	4.100	40.536
May	1.254	..	7.838	1.956	7.405	4.114	40.057
Jun	1.209	..	7.830	1.956	7.406	4.194	40.267
Jul	1.177	..	7.783	1.956	7.432	4.241	39.834
Aug	1.120	..	7.788	1.956	7.462	4.250	41.295
Sep	1.201	..	7.724	1.956	7.494	4.284	42.324
Oct	1.230	..	7.747	1.956	7.485	4.324	42.857
Nov	1.231	..	7.787	1.956	7.492	4.356	41.808
Dec	1.228	..	7.745	1.956	7.514	4.328	41.569

	Malaysian ringgit	New Zealand dollar	Philippine peso	Singapore dollar	Thai baht	South African rand	IMF SDRs
	21	22	23	24	25	26	27
2007	4.708	1.863	63.026	2.064	44.214	9.660	0.895
2008	4.889	2.077	65.172	2.076	48.475	12.059	0.930
2009	4.908	2.212	66.338	2.024	47.804	11.674	0.904
2010	4.267	1.838	59.739	1.806	42.014	9.698	0.869
2011	4.256	1.760	60.260	1.749	42.429	10.097	0.882
2011							
Jan	4.089	1.744	59.089	1.719	40.827	9.265	0.864
Feb	4.154	1.793	59.558	1.742	41.918	9.813	0.873
Mar	4.248	1.888	60.870	1.776	42.506	9.686	0.886
Apr	4.350	1.833	62.361	1.802	43.434	9.720	0.904
May	4.327	1.802	61.953	1.776	43.398	9.846	0.898
Jun	4.359	1.767	62.468	1.776	43.923	9.781	0.899
Jul	4.272	1.688	60.961	1.736	42.949	9.700	0.894
Aug	4.282	1.711	60.836	1.734	42.875	10.153	0.893
Sep	4.246	1.693	59.322	1.723	41.902	10.396	0.873
Oct	4.296	1.736	59.412	1.749	42.297	10.919	0.872
Nov	4.276	1.758	58.743	1.748	41.969	11.055	0.867
Dec	4.164	1.710	57.537	1.707	41.099	10.783	0.852

Table 11.
Irrevocable euro conversion rates as from 1 Jan 1999

Country	Currency	Units of currency per euro	Euro since	Country	Currency	Units of currency per euro	Euro since
Austria	schilling	13.7603	1 Jan 1999	Netherlands	guilder	2.20371	1 Jan 1999
Belgium	franc	40.3399	1 Jan 1999	Portugal	escudo	200.482	1 Jan 1999
Germany	mark	1.95583	1 Jan 1999	Greece	drakma	340.750	1 Jan 2001
Spain	peseta	166.386	1 Jan 1999	Slovenia	tolar	239.640	1 Jan 2007
Finland	markka	5.94573	1 Jan 1999	Cyprus	pound	0.585274	1 Jan 2008
France	franc	6.55957	1 Jan 1999	Malta	lira	0.429300	1 Jan 2008
Ireland	pound	0.787564	1 Jan 1999	Slovakia	koruna	30.1260	1 Jan 2009
Italy	lira	1936.27	1 Jan 1999	Estonian	kroon	15.6466	1 Jan 2011
Luxembourg	franc	40.3399	1 Jan 1999				

Source: European Union.

Table 12.
Exchange rate mechanism ERM II

Currency	Central rate EUR 1 =	Fluctuation band. %	Upper rate*	Lower rate*	Valid from
	1	2	3	4	5
Danish krone	7.46038	± 2.25	7.62824	7.29252	4 Jan 1999
Lithuanian litas	3.45280	± 15	3.97072	2.93488	28 Jun 2004
Latvian lats	0.702804	± 15	0.808225	0.597383	2 May 2005

* *Intervention at the margin, is in principle, automatic and unlimited.*
Source: European Central Bank.

Table 13.
Banknotes sorted at the Bank of Finland, number in millions

Euro banknotes		2006	2007	2008[1]	2009	2010	2011
500	euro	1.5	1.7	2.4	2.1	1.9	1.8
200	"	1.2	1.2	1.3	1.3	1.2	1.1
100	"	5.2	5.7	6.8	6.5	6.8	6.9
50	"	79.6	83.9	86.6	84.5	84.3	86.9
20	"	180.7	191.3	188.4	177.5	176.3	168.2
10	"	31.1	32.0	40.0	42.4	40.9	39.6
5	"	38.8	39.0	49.2	52.8	48.3	47.1
Total		**338.1**	**354.7**	**374.7**	**366.9**	**359.6**	**351.6**

[1] *Deductions from 2008 figures mainly accounted for by banks' own sorted banknote packages, intended for use in ATMs, returned to the same cash handler and not sorted by the Bank of Finland.*
Source: Bank of Finland.

Organisation of the Bank of Finland

11 March 2011

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