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## **Výroční zpráva České národní banky za rok 2011**

Česká národní banka  
2012

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ANNUAL REPORT

1

2011



# ANNUAL REPORT

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## MANDATE OF THE CZECH NATIONAL BANK

- to maintain price stability,
- to oversee the stability of the financial system,
- to ensure smooth circulation of money and smooth payments,
- to support the balanced and smooth development of the Czech financial market.

- Through monetary policy we seek to preserve price stability, i.e. low and stable inflation. Maintenance of stability of the financial system as a whole, which we pursue through macroprudential policy, is a necessary condition for the fulfilment of this objective. Through the joint action of monetary policy and macroprudential policy, we contribute to maintaining confidence in the value of the Czech koruna and safeguarding the stability of the macroeconomic environment.
- By supervising the financial market, issuing prudential rules and rules of conduct towards clients and conducting financial market operations we care for the stability and development of the financial system and protect its clients.
- By managing the payment system and issuing banknotes and coins we ensure smooth payments and cash flows.
- We administer the foreign exchange reserves.

### What we build upon

#### INDEPENDENCE

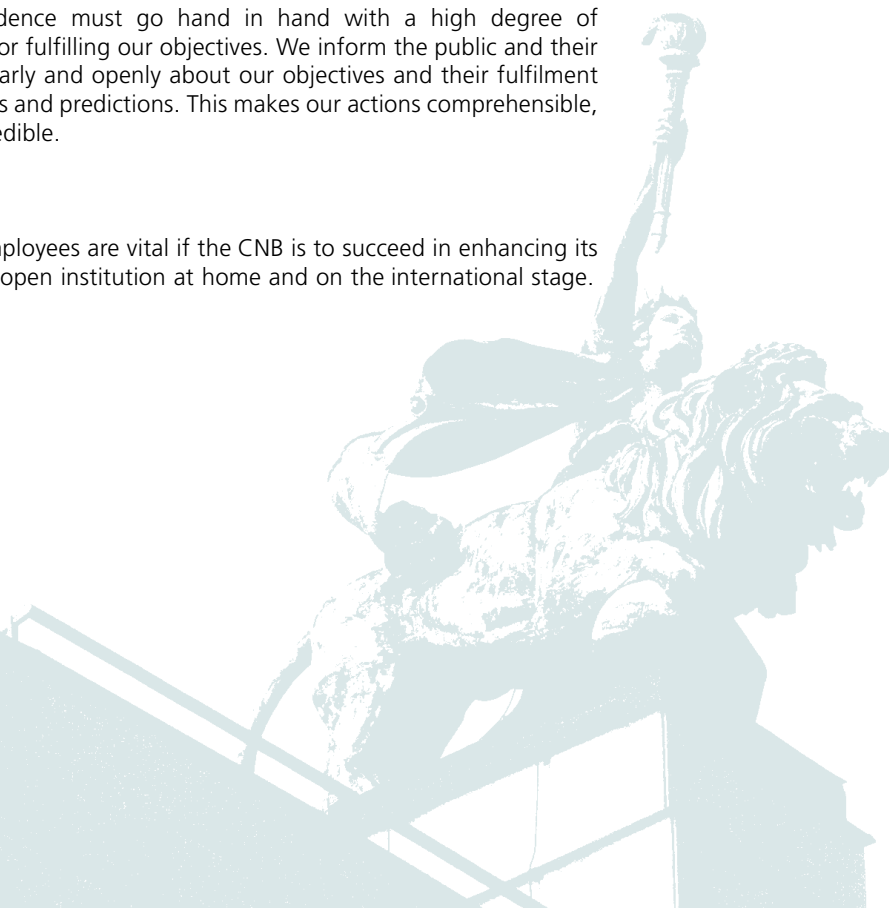
Broad independence of the central bank is a key condition for successful implementation of monetary policy, i.e. for sustained non-inflationary growth of the economy, as well as for objective supervision of the financial market.

#### OPENNESS AND CREDIBILITY

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

#### PROFESSIONALISM

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





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- Monetary-policy relevant inflation (headline inflation adjusted for the first-round effects of changes to indirect taxes) was close to the 2% target for most of 2011. At the end of the year inflation rose above the 2% level, mainly because of the partial advance pass-through of the VAT increase planned for 1 January 2012 to food prices in the final months of 2011.
- Czech economic growth gradually slowed during the year owing to the adverse external situation and continued domestic consolidation of public budgets. In 2011 as a whole the growth amounted to 1.7%. The external outlook deteriorated sharply in the autumn, when the debt crisis escalated in the southern countries of the euro area. The debt crisis increased risk aversion, and this, coupled with a worse outlook for external demand, was reflected in a marked depreciation of the koruna in late 2011.
- The CNB kept its interest rates unchanged, with the key two-week repo rate remaining at 0.75%. The forecasts drawn up during the year gradually postponed the start of interest rate growth. Whereas the first two forecasts expected market interest rates to rise at the end of 2011, the end-2011 forecast postponed the rise to late 2012/early 2013.
- The banking sector stress tests, which the CNB conducts every quarter, confirmed in 2011 that the banking sector is sufficiently resilient to potential adverse shocks. The capitalisation of the sector as a whole remained above the regulatory minimum of 8% even in highly stressful and implausible scenarios.
- The CNB started to publish the Graph of Risks to the Inflation Projection (GRIP), which is one of the key materials for the monetary policy decision-making of the Bank Board members at meetings at which no new forecast is available.
- In 2011, the CNB was actively involved in the work of the three new European Supervisory Authorities (ESAs) and the creation of their structures. As part of their activities, the CNB will contribute, among other things, to the preparation



of binding technical standards and non-binding recommendations and general guidelines. The CNB continued to work to prevent draft regulations that it judged to be unjustified and excessive.

- The Bank Board decided to leave its liquidity-providing facilities (two-week liquidity-providing repo operations and foreign exchange swaps) in effect for an indefinite period of time. These facilities were launched by the CNB in October 2008 in response to the financial crisis. Although they were not used actively by banks in 2011, the CNB considers it appropriate to keep them available given the volatility in the financial markets.
- The President of the Czech Republic appointed Lubomír Lízal as a member of the CNB Bank Board with effect from 13 February 2011. Mr Lízal replaced Robert Holman, whose mandate expired on 12 February 2011.
- The CNB underwent a comprehensive reorganisation between January 2011 and the end of February 2012. This resulted in a decrease of 6.6% in the number of job positions, to 1,403.
- The 2011 reorganisation led not only to a drop in the number of job positions and employees, but also to an overall decline in personnel expenses of 1.8% compared to 2010.
- The CZK 50 banknote ceased to be legal tender on 31 March 2011. Since 1 April 2011, only coins of that denomination have been valid. The invalid CZK 50 banknotes can be exchanged at the Czech National Bank until 31 March 2017.
- In their *Assessment of the Fulfilment of the Maastricht Convergence Criteria and the Degree of Economic Alignment of the Czech Republic with the Euro Area*, the Czech National Bank and the Ministry of Finance recommended not to set a target date for adopting the euro yet and thus not to attempt to enter ERM II during 2012.
- An IMF Financial Sector Assessment Program (FSAP) mission took place in the Czech Republic in November and December 2011. The mission focused on assessing the stability of the Czech financial system, identifying the risks faced by the financial sector and evaluating existing tools and procedures for resolving systemic problems in the financial sector.
- At the end of 2011, the public was able to vote for the first time on the design of a commemorative silver coin on the CNB's website. The coin will be issued in 2013 to mark the 20th anniversary of the establishment of the Czech central bank and the Czech currency. A total of 4,000 people voted. Based on the result, the Bank Board recommended the design by Vladimír Oppl for realisation.



The escalation of the European debt crisis, slower growth abroad and continuing domestic fiscal consolidation were the most important factors that affected the Czech economy in 2011. As a result of those factors, domestic growth slowed and demand-pull inflation pressures disappeared. This allowed us to keep the monetary policy settings unchanged throughout the year. The CNB contributed to domestic economic growth by stabilising inflation close to the inflation target for most of the year and by maintaining the stability of the financial system, which is supervised by the CNB. At a time of cost-cutting in the public and private sectors, the central bank did not shy away from its responsibilities. By making savings and changing its organisational structure it boosted its efficiency and thereby helped maintain its reputation as a condition of its independence.

The situation in the euro area changed during 2011. In the first half of the year it seemed that the foundations for economic growth were strengthening, but during the summer and autumn the overall outlooks started to worsen again, to such an extent that the situation could be described as serious to critical at the year-end. This deterioration was due to a sharp rise in uncertainty stemming from Greece's unsustainable debt and adverse outlooks for the other most indebted European countries, the only slowly recovering European financial sector, the inability of European institutions to find effective solutions to the crisis, and the numerous negative feedback effects between the real economy, the financial sector and insufficiently consolidated budgets. Several summits attended by top European politicians and repeated promises to strengthen rescue funds usually had a calming effect on the financial markets for a few days, but before long the doubts would again start to proliferate and the uncertainty would rise. This resulted in steady growth in the differences in yields between Greek, Portuguese, Spanish and Italian bonds and German bonds. The European Central Bank calmed the situation in the euro area in late 2011 by providing the European banking sector with a huge liquidity injection.

Compared to the dramatic situation in the euro area, the Czech environment can be assessed as having been fairly calm in 2011. However, the Czech economy was not spared adverse impacts of the crisis. The economic growth observed in 2010 slowed in the first half of 2011 and the economy switched to a shallow recession in the second half of the year. This was due not only to weakening external demand, but also to fiscal consolidation, which reduced government expenditure and curbed household consumption growth. Our fiscal policy started to have a pro-cyclical effect on the economy back in 2010, and that effect persisted in 2011. The impacts of fiscal policy on the economy were thus similar to those in numerous other European countries. The substantial fall in the risk of demand-pull inflation enabled monetary policy to remain expansionary, a position to which it had switched in 2010. Monetary policy decision-making was governed to a large extent by assessments of the impacts of cost pressures related to high prices of food and commodities and also to the exchange rate depreciation in the last few months of 2011, caused by increased risk aversion as a result of the escalating debt crisis. As in 2008 and 2009, the exchange rate of the koruna therefore acted as a buffer against external adverse shocks without significantly affecting inflation. The generally low inflation risks, supported by well-anchored inflation expectations, allowed the CNB to leave monetary policy rates unchanged throughout 2011.

As regards the fulfilment of the inflation target (set in terms of headline inflation of 2% since 2010), 2011 was the most successful year since the introduction of inflation targeting. Inflation was very close to the inflation target for most of the year, rising by around half a percentage point above the target in the last two months of the year as retailers incorporated the higher VAT rate into food prices in advance (even though this measure did not take effect until the start of 2012).

Unlike the European banking sector, domestic banks are in good condition. Despite some losses suffered as a result of investing in Greek debt, the Czech banking sector as a whole remains highly profitable, very liquid and exceptionally resilient to adverse shocks. This is confirmed by the results of regular stress tests simulating large and very implausible shocks. Although in 2011 banks did not make active use of the liquidity-providing operations introduced shortly after the onset of the financial crisis in 2008, the CNB decided to leave these operations in effect for an indefinite period of time.

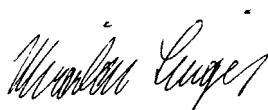
As regards the central bank's many other activities, I would like to mention the following: (i) the CNB's active involvement in the work of the three new European Supervisory Authorities (ESAs), where we are trying to prevent unjustified and excessive regulation of the financial market; (ii) the IMF's Financial Sector Assessment Program (FSAP) mission to the Czech Republic, which focused on assessing the stability of the financial sector; (iii) the fact that CZK 50 banknotes ceased to be legal tender and were replaced by coins; and (iv) the upgraded functionality, enhanced structure and revamped design of the CNB's website, which we consider a key instrument for our transparency.

Quite a major reorganisation took place at the CNB in 2011. It was based on an in-depth analysis of what the bank should be doing itself and what work could be outsourced and done more efficiently that way. The streamlining process led to organisational changes and a 6.6% reduction in the workforce. The central bank will be leaner and more efficient in the years ahead and I am confident it will be better prepared for our future challenges.

The six-year mandates of two Bank Board members expired in February 2011. Pavel Režábek was appointed by the President of the Czech Republic for a second six-year term, while Robert Holman was replaced by Lubomír Lízal.

It is my firm belief that 2011 was a successful year for the CNB. This is evidenced by the consistently high public confidence the CNB has been enjoying in recent years. This confidence is the reward for all the work that we and our predecessors have put in. It is something I truly value, as it was hard and painfully won. I believe that if we remain at least as demanding of ourselves in the future as we were in 2011, the central bank will maintain its high level of credibility.

Miroslav Singer  
Governor





BANK BOARD





**The Bank Board as of 31. December 2011**

Pavel Řežábek, Eva Zamrazilová, Lubomír Lízal,  
Vladimír Tomšík, Miroslav Singer, Mojmír Hampl, Kamil Janáček



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

The Bank Board sets monetary policy and the instruments for implementing this policy and decides upon the fundamental monetary policy measures of the Czech National Bank and measures in the area of financial market supervision. The Bank Board also sets forth the principles for the activities and transactions of the Czech National Bank, approves the budget of the CNB, sets forth the organisational structure and fields of competence of the organisational units of the CNB, defines the types, amounts and uses of the CNB's funds, and executes the rights and duties arising from employment relations in respect of the staff of the CNB. The Governor, or, in his absence, a Vice-Governor nominated by him, chairs the meetings of the Bank Board. The Bank Board acts by a simple majority of the votes cast.

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

Membership of the Bank Board is incompatible with any activity which might cause any conflict of interest between the performance of this activity and membership of the Bank Board.





THE CNB IN 2011



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## MONETARY POLICY AND STATISTICS

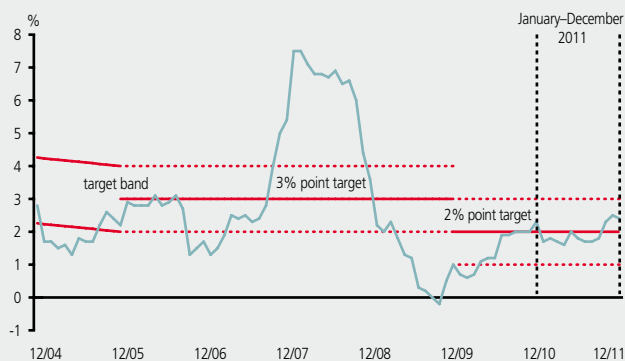
### Monetary policy and economic developments

The CNB's primary monetary policy objective as laid down in the Act on the CNB is to maintain price stability. Since January 1998, this has been achieved under an inflation targeting regime in which the CNB tries to keep inflation close to a declared target. Since the start of 2010, the CNB's inflation target in terms of the consumer price index (CPI) has been set at 2% with a tolerance band of  $\pm 1$  percentage point.

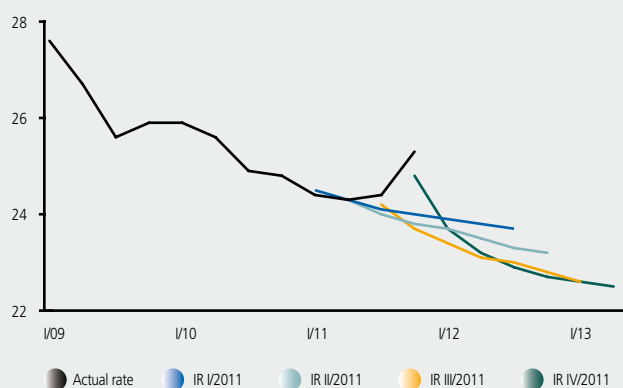
Inflation was close to the CNB's target for most of 2011. At the end of the year, inflation rose above the 2% level, mainly because of the partial advance pass-through of the VAT increase planned for 1 January 2012 to food prices in the final months of 2011. The inflation rate for 2011 as a whole was 1.9%. Czech economic growth slowed gradually during the year owing to adverse external developments, related increased uncertainty and continued domestic consolidation of public budgets. Growth of 1.7% was recorded for the year as a whole. The external outlook deteriorated sharply in the autumn, when the debt crisis escalated in the southern countries of the euro area. The debt crisis increased risk aversion. This – together with a worse external demand outlook – gave rise to a marked depreciation of the koruna in the closing months of 2011. Domestic interest rates were unchanged during the year, but the expected start of upward rate movements shifted significantly. The first two forecasts expected market interest rates to rise at the end of 2011, whereas the forecast in Inflation Report IV/2011 postponed the rise in rates to late 2012/early 2013.

In the first half of 2011, the domestic economy to a large extent continued the trend established in 2010. Economic growth continue to rise in Q1, but – as expected – started to slacken in Q2 as a result of fiscal restriction, fading investment in inventories and slowing growth in external demand. The economic recovery in previous quarters was reflected in renewed modest growth in employment, a gradual decline in unemployment and faster wage growth in the private sector with the usual time lag. The domestic inflation pressures remained contained, however, and inflation fluctuated just below the 2% target. Low inflation was fostered by gradual appreciation of the exchange rate of the koruna, which partially offset the effects of the high world food and commodity prices.

Fulfilment of the inflation target



Forecasts for the koruna-euro exchange rate



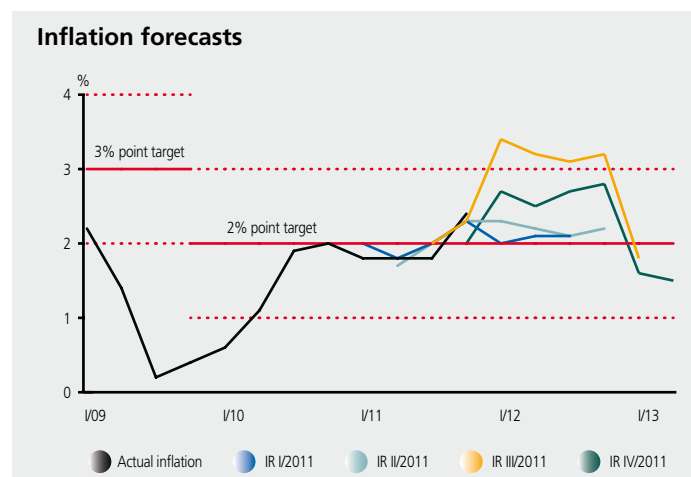
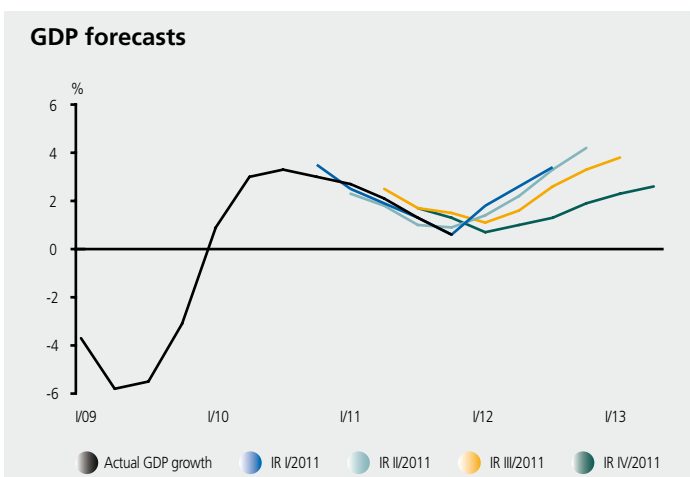
The macroeconomic forecasts in the first half of 2011 were based on an outlook of continued recovery in the euro area accompanied by a gradual rise in ECB interest rates. The external recovery, coupled with a modest recovery in domestic demand

and rising wage growth, was expected to lead to a rise in economic growth to about 3% in 2012. The recovery in economic activity and faster wage growth were expected to gradually increase domestic inflationary pressures. However, these pressures were expected to be partially offset by lower import prices, affected by an expected cooling of prices in commodity markets and appreciation of the koruna. The expected gradual appreciation of the koruna was chiefly due to a favourable outlook for net exports, a declining risk premium owing to domestic fiscal consolidation and – in the longer run – the expected renewal of real convergence.

Consistent with the forecasts compiled in the first half of 2011 was stability of market interest rates close to their current level and a gradual rise in rates from the end of 2011 onwards. The predicted rate stability at the start of the forecast horizon was a result of the opposing effects of foreign inflationary and domestic anti-inflationary pressures. The forecasted rate growth in the longer run was a result of a gradual renewal of domestic inflationary pressures and expected interest rate growth in the euro area.

Both forecasts were surrounded by a high degree of uncertainty, connected mainly with external developments. For this reason, several alternative scenarios for future external developments, simulating the impacts of different external demand and commodity price developments, were drawn up at the start of the year. The Inflation Report II/2011 forecast contained an alternative scenario capturing the potential impacts of the planned increase in the reduced VAT rate, which became reality in January 2012. At its meetings in the first half of the year, the Bank Board assessed the risks to the forecast as being balanced and, in line with the message of the forecast, decided to leave interest rates unchanged.

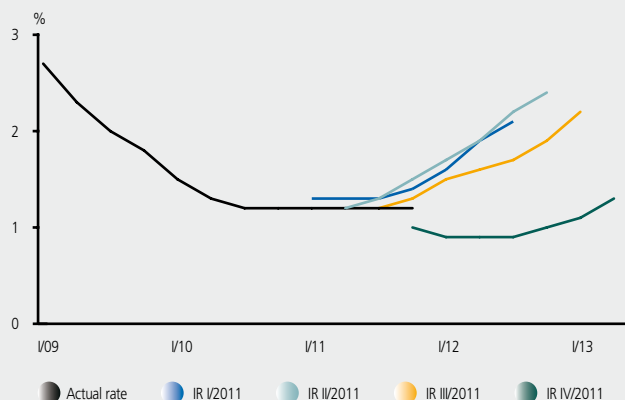
Bad news started coming in from abroad, and especially from the euro area, in the second half of the year. The ECB raised its key rate by 0.25 percentage point to 1.5% in July as expected, but the renewed escalation of the debt crisis in some euro area countries forced it to lower rates in two steps in the remainder of the year and take new unconventional monetary measures. The deepening debt crisis led to worsening outlooks for economic growth in the euro area. The outlooks for interest rates were reduced and the euro depreciated against the dollar. These changes in foreign outlooks caused the CNB to revise the outlook for domestic economic activity downwards in its forecasts in the second half of the year. Compared to the forecasts from the first half of the year, which had expected economic growth of roughly 3% in 2012, the growth forecast for 2012 was lowered in the second half of 2011 to about 1% in Inflation Report IV/2011. The lower outlook for foreign rates and domestic economic activity led to a decrease in the projected domestic interest rate path. The Inflation Report IV/2011 forecast postponed the expected rise in rates to late 2012/early 2013.



In the second half of 2011, the forecasts incorporated a government-approved rise in the reduced VAT rate from 10% to 14% in January 2012. The headline inflation forecast for 2012 thus went up by roughly one percentage point and was close to 3%. However, the forecast for monetary-policy relevant inflation<sup>1</sup> was little changed, staying close to the 2% inflation target, because the impacts of the VAT increase on inflation expectations and wages were not expected to be significant. In 2011, as in the past, escape clauses were applied to the expected first-round effects of the VAT changes and so interest rates did not react to them.

Owing to a significant deterioration of the outlooks, external developments continued to be surrounded by considerable uncertainty. For this reason, an alternative scenario assuming stagnation in the euro area countries on average (taking into account their weight in Czech foreign trade) was drawn up in Inflation Report IV/2011. This scenario led to a modest decline in the domestic economy, but also to a weaker exchange rate of the koruna and, as a result, to slightly higher domestic interest rates than in the baseline scenario of the forecast. In light of the forecasts and their heightened risks, the Bank Board kept interest rates unchanged in the second half of the year. The CNB's key two-week interest rate therefore ended the year where it started, at 0.75%.

Forecasts for 3M PRIBOR rates



More detailed information on economic developments and monetary policy implementation can be found in the quarterly Inflation Reports.<sup>2</sup>

At the end of 2011, the CNB in cooperation with the Ministry of Finance prepared for the Government the regular *Assessment of the Fulfilment of the Maastricht Convergence Criteria and the Degree of Economic Alignment of the Czech Republic with the Euro Area*. This document, which is available on the CNB website, resulted in a recommendation not to set a target date for adopting the euro yet and thus not to attempt to enter the ERM II during 2012. This recommendation was based on a whole range of factors – the fiscal problems in the euro area and the way these are being dealt with, the persisting elevated global financial market volatility and the insufficient preparedness of the Czech Republic to adopt the euro in a situation where it is first necessary to complete the public budget consolidation process and increase the flexibility of the labour market.

<sup>1</sup> Monetary-policy relevant inflation is the inflation to which monetary policy reacts. It is defined as headline inflation adjusted for the first-round effects of changes to indirect taxes.

<sup>2</sup> The Inflation Reports are available on the CNB website (*Monetary policy > Inflation reports*).

## Statistics

In 2011, the development of statistics was again directed at providing a high-quality database, at conducting methodological work and on efficient and respondent-friendly collection of the underlying data for the compilation of statistics.

The most significant event for the CNB's analysts was a revision of the balance of payments based on consistent application of the resident approach linked to the creation of value added in the national accounts. In coordination with the Czech Statistical Office, the CNB published revised time series of both the balance of payments and national accounts during 2011. As regards other statistical products, the monetary and financial statistics data were optimised so as to achieve a balanced breakdown of the individual sets and to rule out the possibility of disclosure of confidential data.

CNB statisticians were again involved in developing harmonised statistics at the European level in both the standard structures and in specially created expert teams tasked with integrating statistical and supervisory reporting and improving access to statistical products. Work on the methodological purity of government finance statistics, especially as regards data consistency and classification of units in the general government sector, was an important task in light of the debt crisis in numerous EU countries.

The collection of underlying data continued to be focused on primary, non-aggregated data. Collection of such data from non-bank investment firms was commenced in 2011. A project to introduce automated exchange of data from respondents between the CZSO and the CNB was implemented. This made it possible to eliminate some of the CZSO's statistical surveys. Preparations for the use of existing administrative data continued as well.

The project to prepare a joint statistical survey of non-financial corporations by the CNB and the Confederation of Industry of the Czech Republic entered the implementation phase. The survey results were used for the first time to draw up the short-term economic forecast.

## FINANCIAL STABILITY

The Act on the CNB defines financial stability as one of the CNB's primary objectives. The Czech National Bank defines financial stability as a situation where the financial system operates with no serious failures or undesirable impacts on the present and future development of the economy as a whole, while showing a high degree of resilience to shocks.

The CNB's financial stability analyses try to identify risks to the functioning of the financial system in the future and simulate the effects of potential domestic and external adverse shocks. The main tools used to communicate the risks identified and their potential effects to the public are the Financial Stability Report and financial sector stress tests. The CNB publishes the Financial Stability Report on its website and also provides information about its content at a press conference given by the CNB Governor and at a special public seminar. The Report is submitted to the Chamber of Deputies (the lower house of the Czech Parliament) as required by law. Its conclusions are also discussed with the members of the Committee on National Economy, Agriculture and Transport of the Senate of the Czech Parliament.

The CNB conducted stress tests of the banking sector on a quarterly basis and published their results on its website. Like the analyses in the Financial Stability Report, the stress test findings were communicated to the public via presentations and publications given by CNB representatives.



The Financial Stability Report aims to identify new risks arising from domestic economic developments or the external environment. Another key objective is to assess the ability of the domestic financial system to withstand the impacts of existing sources of financial instability in stress tests of banks, insurance companies and pension funds. Financial Stability Report 2010/2011, published in June 2011, pointed out that, despite the good starting position of the domestic financial sector, there are still risks to its stability, primarily as a result of the uncertainty surrounding global economic developments. This uncertainty is closely related to the fiscal problems in a number of European countries and weaker economic growth in the Czech Republic's key trading partners. In 2011, the risks to financial stability were monitored on a quarterly basis in "macrofinancial panels", in which the members of the CNB Bank Board met with experts from key departments to assess a wide range of information on developments in the domestic financial system and abroad.

Given the multinational nature of many significant financial institutions and the close links between national financial systems, the CNB is increasingly involved in international cooperation, particularly in relation to the European System of Financial Supervisors (ESFS). In the area of financial stability and macroprudential policy this includes the active participation of the Governor and one other Bank Board member at the regular meetings of the General Board of the European Systemic Risk Board (ESRB) and the involvement of CNB representatives in the ESRB's Advisory Technical Committee (ATC) and working groups.

A regular IMF Financial Sector Assessment Program (FSAP) mission took place in the Czech Republic in November and December 2011. The mission focused on assessing the stability of the Czech financial system, identifying the risks faced by the financial sector and evaluating existing tools and procedures for resolving systemic problems in the financial sector.

### FINANCIAL MARKET SUPERVISION

The CNB supervises the financial market, analyses the evolution of the financial system, sees to the sound operation and development of the financial market in the Czech Republic and contributes to the stability of the Czech financial system as a whole to the extent stipulated by law.<sup>3</sup>

<sup>3</sup> The CNB provides detailed information about financial market supervision in its annual Financial Market Supervision Report – see *CNB > Supervision > Aggregate information on the financial sector > Financial market supervision reports*.

### *Financial market regulation*

The enhancement of financial market stability and transparency through the implementation of new regulatory frameworks is a long-term process linked with changes to European law. In 2011, the CNB contributed to the implementation of the EU's rapidly changing regulations in the financial market area and to changes in the regulatory framework in the Czech Republic. It worked with the Ministry of Finance and other state authorities to prepare new laws regulating the business of financial institutions and other entities subject to its regulation and supervision. The CNB also prepared a number of decrees and explanatory and methodological opinions interpreting the application of regulatory requirements pertaining to financial market participants.

One major legislative change was an amendment to the Act on Banks, the Credit Unions Act and the Capital Market Undertakings Act transposing the amended capital requirements directives (Directives 2006/48/EC and 2006/49/EC, known as CRD III) and defining new powers of the CNB (relating, for example, to the determination of the significance of branches, remedial measures to ensure a sufficient amount and appropriate structure of capital, and activities of supervisory colleges).

Two important new laws are the Act on Retirement Savings and the Act on Supplementary Pension Savings, which form part of the pension reform and regulate the transformation of existing pension funds and the establishment of new pension management companies and lay down conditions for the participation of the public in retirement and participation funds and the rules for their operation.

The CNB issued seven decrees in 2011 on the basis of authorisations laid down in individual laws. These decrees related mostly to new laws in the financial market area. The CNB also published ten official information documents providing financial market participants with important information about the application of legal rules.<sup>4</sup>

### *European regulation*

Intensive work continued in 2011 at the level of the European Commission, the Council and the European Parliament on new or amended European financial market regulations aimed at eliminating the causes of the global economic crisis and maintaining the EU's growth and competitiveness. The CNB paid close attention to the Commission's proposals and prepared critical opinions on them. CNB representatives actively promoted the CNB's opinions in EU committees and working groups.

The CNB was particularly involved in the discussions on the proposed directive and regulation on capital requirements (CRD IV), the draft implementing measure for the Solvency II directive, and the draft Omnibus II directive, which amends the Solvency II directive in connection with the establishment of the European Insurance and Occupational Pensions Authority (EIOPA) and defines the areas in which the EIOPA is authorised to submit proposals for binding technical standards to the Commission.

The CNB also prepared comments on the proposal for a new directive on markets in financial instruments (MiFID II) and a new regulation on markets in financial instruments (MiFIR), i.e. regulations intended to replace the existing Directive 2004/39/EC on markets in financial instruments.

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<sup>4</sup> A complete and up-to-date list of the CNB's decrees, provisions, official information and opinions relating to the financial market can be found on the CNB website at *CNB > Financial market supervision > Legislation*.



### *International cooperation*

The new European institutions which, together with national financial market supervisors, form the European System of Financial Supervision (ESFS) started up on 1 January 2011. In addition to national supervisors, the ESFS comprises the European Systemic Risk Board (ESRB) and the European Supervisory Authorities (ESAs). The ESAs are: the European Banking Authority (EBA),<sup>5</sup> the European Securities and Markets Authority (ESMA)<sup>6</sup> and the European Insurance and Occupational Pensions Authority (EIOPA)<sup>7</sup> and their Joint Committee (JC), which serves as a forum for cooperation between the ESAs. The ESFS represents a significant change in the institutional structure of financial market supervision.

CNB representatives were involved in the ESAs' activities at all levels, including membership of the boards of the individual ESAs and, in the case of the EBA, also of the Management Board. At the expert level, CNB representatives contributed to the preparation of all the ESAs' documents, including regulatory technical standards, technical advice for the Commission on future implementing measures for directives, opinions on the Commission's legislative proposals, EBA, ESMA and EIOPA guidelines and other regulatory outputs, assessments of the implementation of existing European rules and their operation in practice at national level, comparisons of supervisory practices, and financial market analyses.

As part of its work in the ESRB and ESAs, the CNB – in cooperation with the Ministry of Finance in EU policy committees and with the supervisory authorities of EU Member States – strived to prevent the gradual shift of national supervisors' powers to European authorities (and thus also the separation of powers from responsibility for a functioning and stable financial market), to limit the growth in excessive regulation, to reduce the administrative burden on national supervisory authorities and financial institutions, to strengthen financial institutions and enhance their supervision, and to appropriately resolve cross-border issues in the financial market area.

CNB representatives worked within the structures of the ECB and were also involved in other international institutions and associations. They regularly attended meetings of supervisory colleges for important banking groups and also meetings of coordination committees for supervisors of insurance groups. In the capital market area, cooperation continued between the CNB and other supervisors based on IOSCO and ESMA (CESR) multilateral memoranda of understanding. The CNB also worked closely with financial market supervisors from Central and Eastern European countries, mainly in order to exchange information and coordinate the opinions of national supervisory authorities in the region.

### *Financial market supervision*

The CNB supervises the financial market by means of both off-site surveillance (continuous monitoring of the stability of the individual supervised sectors) and on-site inspections.

Off-site surveillance consists in continuously monitoring the activity and financial performance of the individual entities operating on the financial market and assessing the evolution of the market as a whole and its key segments. Owing to the global financial market situation and some euro area countries' debt financing

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<sup>5</sup> The EBA is the legal successor of the Committee of European Banking Supervisors (CEBS).

<sup>6</sup> The ESMA is the legal successor of the Committee of European Securities Regulators (CESR).

<sup>7</sup> The EIOPA is the legal successor of the Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS).

problems, the CNB paid increased attention to the performance and investments of institutions subject to off-site central bank surveillance.<sup>8</sup> In this context, the portfolios of the supervised institutions were analysed in more detail and their exposures to risky entities and instruments were determined.

In supervising banks, the CNB – given the financial market situation – concentrated mainly on credit portfolio quality, provisioning, the adequacy of capital for covering potential losses, and liquidity and overall performance. The exposures of Czech banks to their foreign parent banks were also assessed continuously by means of a special reporting duty. In addition, extraordinary monitoring of the situation of building societies continued in connection with changes to the conditions for building savings schemes.

Turning to the supervision of insurance companies, greater attention was devoted to the adequacy of motor third party liability insurance premiums and of the technical reserves of some insurance companies in this category. Also of significance were the preparations for the future Solvency II regulation in terms of both supervisors' knowledge of the principles and rules of the regulation and methodological preparation. The results of a second round of stress tests of selected domestic insurance companies confirmed that the sector as a whole has sufficient capital to cope with relatively substantial changes in selected risk factors.

As regards the investment firms sector, the CNB continuously assessed compliance with information and disclosure duties. It checked exposure limit compliance and capital adequacy calculations and regularly reviewed significant changes in the volume and structure of client assets.

In accordance with the legislation in force, on-site inspections are focused on checking compliance with the regulatory rules laid down in legal and implementing regulations. The inspections focus either on verifying all the relevant activities of the examined entity (comprehensive inspections) or on verifying selected areas thereof (partial inspections). In addition to on-site inspections, supervisors are responsible for approving advanced methods for calculating capital requirements. Given the interconnectedness of financial markets, the CNB is systematically stepping up its cooperation with regulators in other countries.

#### *Licensing, approval and authorisation activities in the financial market area*

In 2011, the CNB conducted 55 administrative proceedings concerning regulated credit institutions (12 banks and 43 credit unions), in which it issued 46 administrative decisions. The granting of a banking licence to Air Bank a.s. was one of the most important decisions.

The CNB conducted 80 administrative proceedings and issued 67 administrative decisions in the insurance sector. The largest number of decisions (58) related to the granting of prior consent to membership of a statutory or supervisory body of an insurance or reinsurance company.

A total of 278 administrative proceedings were conducted and 203 decisions were made in the collective investment area. The most frequent were those regarding the approval of changes in the statutes of collective investment funds (86).

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<sup>8</sup> These institutions comprise banks, foreign bank branches, insurance companies, pension funds, building societies, credit unions, payment institutions, electronic money institutions and issuers, management companies, investment funds and investment firms.

<b>Numbers of entities providing services on the financial market</b>				
	As of 31 Dec. 2010	Additions	Losses	As of 31 Dec. 2011
Credit institutions, total	55	3	0	58
Banks	22	1	0	23
of which: building societies	5	0	0	5
Branches of foreign banks (operating under the single licence regime)	19	2	0	21
Credit unions	14	0	0	14
Insurance companies (including branches and reinsurance companies)	53	1	0	54
Domestic insurance undertakings (excluding the CIB)	35	0	0	35
Branches of insurance companies from EU/EEA	17	1	0	18
Reinsurance companies	1	0	0	1
Management companies	23	3	5	21
Investment funds	49	14	3	60
Open-end mutual funds	149	17	10	156
of which: standard funds	37	0	0	37
Closed-end mutual funds	1	0	0	1
Pension funds	10	0	1	9
Depositories	8	0	0	8
Investment firms	37	2	4	35
Non-bank investment firms	25	2	4	23
Investment firms – banks	12	0	0	12
Issuers of listed securities	65	5	6	64
of which: foreign	18	1	1	18
Regulated market operators	3	0	0	3
Settlement systems	3	0	0	3
Central depository	1	0	0	1
Payment institutions	0	12	0	12

The CNB received 37 applications for the opening of administrative proceedings from the private pension sector. Decisions on two of them had not been issued by the end of 2011. Most of the proceedings concerned the approval of persons to pension fund bodies.

The CNB closed 258 administrative proceedings in the area of investment services provision in 2011. The largest number of decisions (229) related to the withdrawal of registration of investment intermediaries. A total of 214 decisions were issued and 15 proceedings were discontinued by resolution.

The CNB conducted 134 administrative proceedings in the area of securities issues, securities registers and regulated markets. Most of the decisions (126) concerned the approval of documents relating to new securities issues.

During 2011, the CNB received 452 announcements by foreign regulators of notifications (under the single licence regime) of provision of services in the Czech Republic, of which 25 from banks, 13 from electronic money institutions, 57 from payment institutions, 48 from insurance companies, 159 from collective investment funds, four from management companies and 268 from investment services providers.

#### *Enforcement*

Activity in the penalty proceedings area was an integral part of financial market supervision. It consisted in the investigation of petitions for the opening of administrative proceedings, decision-making on the opening of administrative proceedings or the deferral of cases, and the conduct of first-instance administrative proceedings, within which fines and remedial measures were imposed, licences revoked and registrations cancelled. Administrative proceedings are conducted with both regulated entities and entities that provide services on the financial market without the relevant licence. The work also includes communication with law

enforcement authorities, including the preparation of documents and opinions, and communication with the Finance Ministry's Financial Analytical Unit (FAU) on money laundering and terrorist financing.

Statistics on administrative penalty proceedings conducted in 2011		
	Numbers of administrative penalty proceedings opened	Total fines imposed (in CZK thousands)
Supervision of credit institutions	11	3,315
Capital market supervision	45	22,265
Insurance supervision	24	1,575
Violation of forex regulations	42	2,049
Consumer protection	8	350

### Central Credit Register

The Central Credit Register (CCR) is an information system administered by the CNB since 2002 which enables banks and foreign bank branches operating in the Czech Republic to share information on the credit commitments and payment discipline of businesses. In 2011, the CCR's activity concentrated mainly on the CNB's involvement in international data sharing across the credit registers of EU countries. The construction of a data warehouse continued in parallel. The new warehouse will facilitate better use of aggregated and anonymised CCR data for sectoral and financial stability analyses. A new communication system allowing banks to make ad hoc inquiries on the current credit commitments of their clients via internal applications and to process aggregate credit information on their debtors' portfolios more flexibly was also put into full operation.

Main operational characteristics of CCR				
	12/2008	12/2009	12/2010	12/2011
Number of registered debtors	461,277	497,726	539,540	576,583
of which: natural persons (entrepreneurs)	271,770	291,458	313,129	330,372
legal entities	189,507	206,268	226,411	246,211
Total volume of loans outstanding (CZK billions)	1,265	1,200	1,219	1,307
Number of CCR application users	2,516	2,245	2,362	2,569
Ad hoc credit commitment enquiries (thousands per year)	180	205	213	215
Number of pieces of credit commitment information in monthly reports (thousands per year)	2,800	3,038	3,640	3,198
Number of extracts made for clients (per year)	278	453	492	514

### Consumer protection

The Consumer Protection Department (CPD, at [spotrebitel@cnb.cz](mailto:spotrebitel@cnb.cz)) receives and investigates consumers' complaints in accordance with competences arising under the Consumer Protection Act and now also the Consumer Credit Act. In 2011, the CPD received a total of 866 consumer complaints. Of this number, 273 related to shortcomings in credit institutions, 319 were against insurance companies and insurance intermediaries, 25 concerned shortcomings in the operation of the capital market and the remainder fell into none of the above categories. Most of the complaints related to inadequate provision of information on products. In second place were product costs, including insufficient information on fees. Some of the complaints were answered by means of explanations; these are cases where it is not necessary to contact the supervised entity because the information referred to in the complaint is available in product terms and conditions and in agreements and consumers have merely not read them properly. Such complaints are then assessed as unjustified. The complaints that the CNB finds justified are resolved by communication with the supervised entity and steps are taken to make sure that the entity adopts remedial measures that will result in the elimination of the shortcoming and will guarantee that it does not arise again.

## CURRENCY AND PAYMENTS

### Currency in circulation

Under the Act on the CNB, the CNB has the exclusive right to put banknotes and coins, including commemorative coins, into circulation and to manage the circulation of currency. The payment system legislation underwent a major change in 2011 when the Parliament of the Czech Republic passed the Act on the Circulation of Banknotes and Coins. This law was promulgated under No. 136/2011 in the Collection of Laws and, with the exception of one provision, took effect on 1 July 2011. The Act changes some of the rules for cash circulation (e.g. money changing, banknote and coin processing, and protection against acceptance of counterfeits) for the Czech National Bank, commercial banks and other legal entities and natural persons, including the general public.

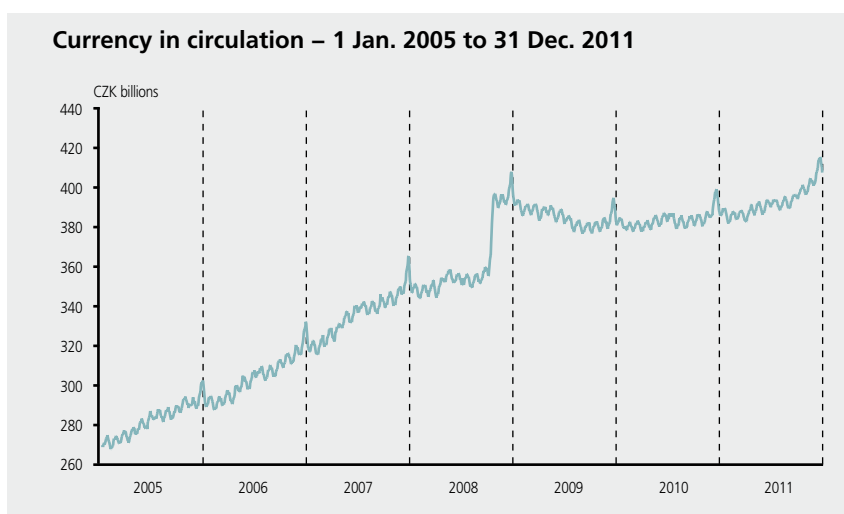
At the decision of the Bank Board, the CZK 50 banknote ceased to be legal tender on 31 March 2011 and was replaced in circulation by coins of the same denomination. Between 1 April 2012 and 31 March 2017, CZK 50 banknotes will be exchangeable only at the Czech National Bank.

In 2011, the CNB put into circulation four CZK 200 commemorative silver coins, one CZK 500 silver coin and two CZK 5,000 gold coins. After the Industrial Heritage Sites cycle ended, the central bank launched a new five-year cycle of gold coins entitled "Bridges in the Czech Republic" in 2011. The first two coins depict the Gothic bridge in Písek and the Renaissance bridge in Střibro.



The denomination of the gold coins in the cycle was increased from CZK 2,500 to CZK 5,000. In total, 97,000 commemorative silver coins with a nominal value of CZK 24.8 million and 19,500 gold coins with a nominal value of CZK 97.5 million were produced in 2011.

Cash turnover at the CNB's branches amounted to CZK 1,379.1 billion in 2011, up by 3.7% year on year. The CNB's cash offices received 688.1 million banknotes and 433.8 million coins and issued 698.4 million banknotes and 488.3 million coins, representing a total of 6,682 tonnes of money (26.4 tonnes a day).



The value of currency in circulation was CZK 412.0 billion on 31 December 2011, up by CZK 20.3 billion on a year earlier. Despite this rise, the value of currency in circulation in the Czech Republic is still slightly below the long-term upward trend. However, nominal GDP has been even further below its long-term trend in the last three years. The ratio of currency to the nominal value of economic output therefore increased at the start of 2009 compared to its pre-2008 values and remained at this elevated level in 2011.

Denomination	In CZK millions		In millions of pieces	
	2010	2011	2010	2011
CZK 5,000	120,676.0	124,915.3	24.1	25.0
CZK 2,000	111,154.2	124,666.5	55.6	62.3
CZK 1,000	122,600.6	123,681.3	122.6	123.7
CZK 500	10,372.3	10,699.6	20.7	21.4
CZK 200	10,228.9	10,600.4	51.1	53.0
CZK 100	4,841.6	5,028.1	48.4	50.3
CZK 50	824.2	606.9	16.5	12.1
CZK 20	104.3	104.2	5.2	5.2
<b>Banknotes, total</b>	<b>380,802.1</b>	<b>400,302.3</b>	<b>344.3</b>	<b>353.0</b>
CZK 50	3,135.5	3,614.6	62.7	72.3
CZK 20	2,922.5	2,952.8	146.1	147.6
CZK 10	1,685.4	1,729.4	168.5	172.9
CZK 5	973.9	1,006.4	194.8	201.3
CZK 2	684.5	709.8	342.2	354.9
CZK 1	417.2	434.7	417.2	434.7
CZK 0.50	183.4	183.3	366.9	366.5
<b>Coins in circulation, total</b>	<b>10,002.4</b>	<b>10,630.9</b>	<b>1,698.5</b>	<b>1,750.3</b>
Precious metal coins	889.1	1,019.5	1.8	1.9
<b>Total</b>	<b>391,693.6</b>	<b>411,952.7</b>	<b>2,044.6</b>	<b>2,105.2</b>

### Non-cash payments

The Czech National Bank keeps the accounts of the state and operates systems for transfers of interbank payments and for the settlement of short-term securities transactions. Non-cash payment transactions are executed through the CERTIS, SKD and ABO systems.

In 2011, the CNB actively assisted the Ministry of Finance in completing an amendment to Act No. 284/2009 Coll., on the Payment System, which arose because of the need to transpose amendments to European legislation (on electronic money, settlement finality, etc.) into national legislation.

Following the amendment of the Payment System Act, the CNB prepared an amendment to Decree No. 140/2011 Coll., on payment systems with irrevocability of transactions, and a new Decree No. 169/2001 Coll., stipulating the rules for creating account numbers in the payment system. Decree No. 141/2011 Coll., on the pursuit of business of payment institutions, electronic money institutions, small-scale payment service providers and small-scale electronic money issuers, and Decree No. 142/2011 Coll., stipulating the content, form, time limits and manner of reporting by these institutions to the Czech National Bank, were also issued.

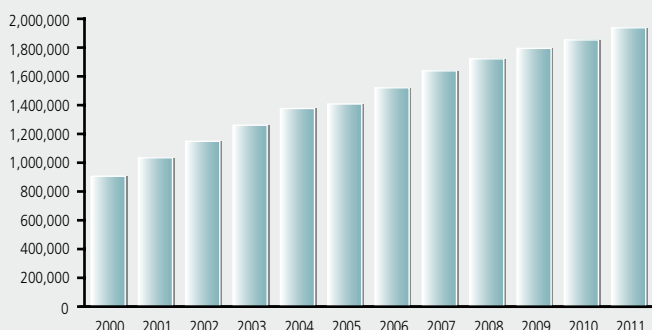
#### *CERTIS – interbank payment system*

The CERTIS system processes interbank payments in the Czech Republic. Banks, credit unions and foreign bank branches are participants in this system. As of 1 December 2011, CERTIS comprised 49 direct participants (for which accounts are maintained in the system) and 6 third parties (for example, card payment clearing houses and securities clearing and settlement institutions).

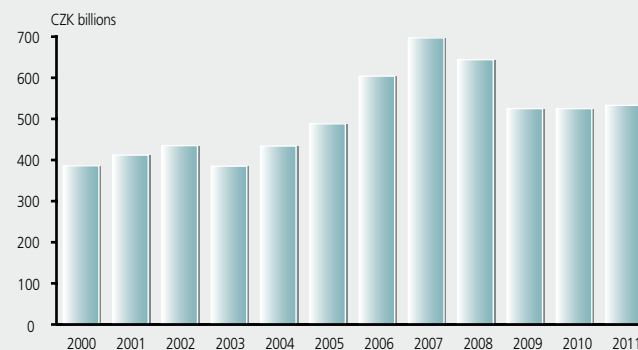
CERTIS processed 490 million transactions in 2011 (up by 4.5% year on year) with a total value of CZK 134,909 billion (up by 1.5%). It processed a daily average of 1.94 million transactions, with a value of CZK 533 billion.

The following charts show the number of transactions processed and the volume of funds transferred in CERTIS since 2000.

**Average daily number of transactions**



**Average daily turnovers**



#### *SKD – short-term securities settlement system*

The short-term securities settlement system operated by the CNB is a separate register of securities and a securities settlement system. Since 2011, certificates



issued by accredited providers of certification services have been used for electronic signatures.

As of 31 December 2011, a total of 151 owner accounts – belonging to 109 clients (securities owners) – were registered in SKD. In all, 20 agents and 9 custodians use the system. In this case, agents are banks that provide securities settlement services to their clients. They have direct interactive access to the SKD system. Custodians administer securities accounts owned by persons other than custodians, i.e. customers of custodians.

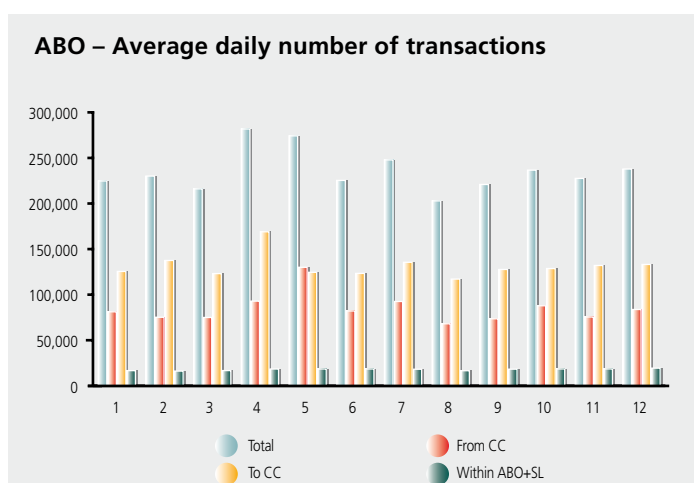
SKD records bonds issued by the Czech National Bank and government bonds issued by the Ministry of Finance with a maturity of up to one year. The securities recorded in SKD are used, among other things, as collateral for intraday credit, which the CNB extends to banks for smooth accounting purposes within CERTIS. They are also used for the CNB's repo operations and by the Ministry of Finance for daily liquidity management of the Single Treasury Account. Only 43 transactions a day were processed in SKD on average in 2011, but the average daily value of these transactions was CZK 135 billion.

#### *ABO – the CNB's accounting and payment system*

The CNB keeps the accounts of its clients and the internal accounts of the central bank in the ABO system. As of the end of 2011, the system maintained almost 39,000 accounts, more than 21,000 of which came under the Single Treasury Account, on which state budget revenues and expenditures and other financial operations of the state are realised.

Most clients use the ABO-K internet banking system to manage their accounts. The CNB offered an additional level of protection to clients in 2011 based on text message confirmation. The ABO-K system had 3,939 registered users at the end of 2011. A total of 149,000 transfer orders are processed on average every day. 99.7% of transfer orders are submitted through ABO-K, and only 0.3% are submitted in writing. The system processes a daily average of 85,000 incoming payments.

The following chart shows the average daily number of accounting transactions processed in 2011. The total number of transactions increased by 2.5% compared to 2010.



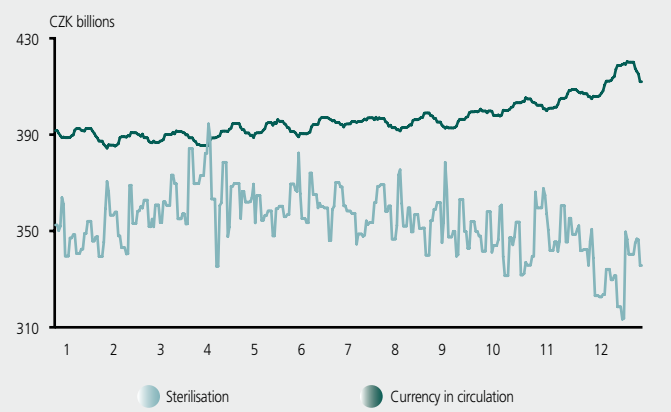


### FINANCIAL MARKET OPERATIONS

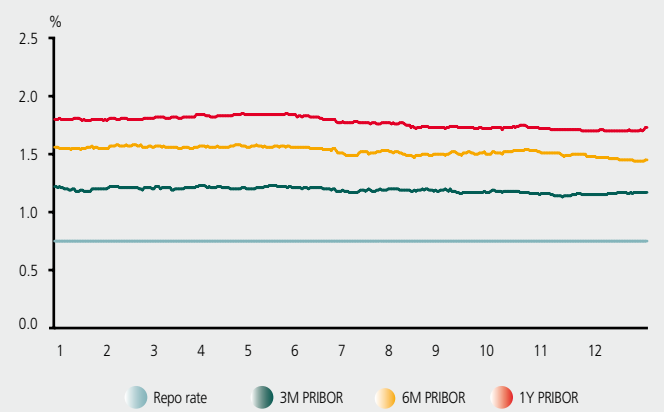
The CNB implements monetary policy using instruments comprising mainly financial market operations, automatic facilities and reserve requirements. The CNB Bank Board sets three interest rates: the two-week repo rate, the discount rate and the Lombard rate. The main monetary policy rate is the two-week repo rate. A change in these interest rates transmits through financial market operations to short-term interest rates on the interbank market. The discount and Lombard rates provide the floor and ceiling respectively for short-term interest rates on the money market. In 2011, the repo rate stood at 0.75%, the discount rate at 0.25% and the Lombard rate at 1.75%.

The CNB manages the liquidity of the banking sector through money market operations so as to maintain an optimum liquidity level for compliance with the reserve requirement. This ensures that short-term interest rates are stable at the desired level. The main instrument for managing short-term interest rates is the repo, announced three times a week with a maturity of 14 days. Repos are used for absorbing excess liquidity from the banking sector. The liquidity absorbed in monetary operations in 2011 varied between CZK 313 billion and CZK 395 billion, the average being CZK 353 billion. The average amount of liquidity absorbed fell by approximately CZK 5 billion relative to the 2010 average.

Excess liquidity in 2011



Interest rates in 2011



The CNB's instruments also included two "automatic" facilities – the marginal lending facility and the deposit facility. Under the lending facility, the CNB lends overnight funds to banks in the form of a repo operation at the Lombard rate. The deposit facility gives banks the option of making overnight deposits with the CNB at the discount rate. These operations are only supplementary. The CNB also executed collateral exchanges. The aim of these operations was not to affect the banking sector's excess liquidity, but to provide securities to banks that can be used, for instance, for obtaining intraday credit.

#### Liquidity-providing operations

The CNB launched these operations (two-week liquidity-providing repo operations and foreign exchange swaps) in October 2008 as a result of the outbreak of the financial crisis. These instruments are important for the stability of the domestic financial market. Although they were not used actively by banks in 2011, the CNB considers it appropriate to keep them available given the volatility in the financial

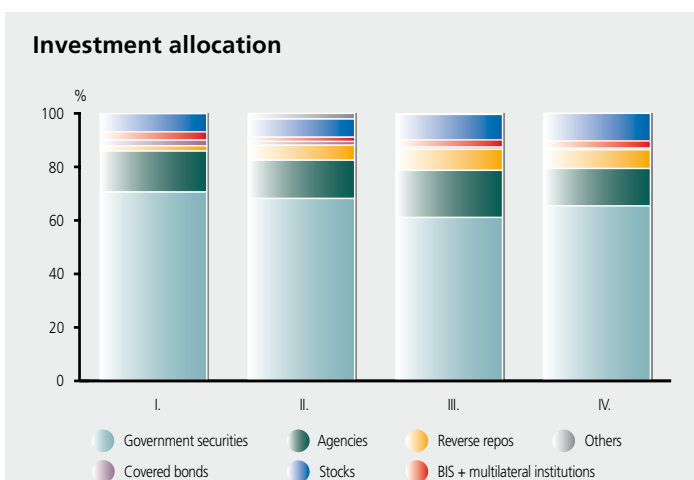
markets. For this reason the Bank Board decided to leave its liquidity-providing operations in effect for an indefinite period of time. The CNB reserves the option to adjust the parameters of these operations in response to market developments.

### International reserves management

International reserves are the CNB's foreign assets in convertible currencies. They are used mainly to support the CNB's independent monetary and exchange rate policy-making and as a source of foreign exchange liquidity for CNB clients. At the end of 2011, international reserves accounted for 97% of the assets in the CNB's balance sheet and the income on them was the CNB's most significant revenue.

The CNB regularly publishes the volume and structure of the reserves in the *Financial markets* section of the CNB website. At the close of 2011, the international reserves totalled CZK 803 billion. The actively managed portfolio accounts for around 95% of the international reserves. The remainder consists of passively held assets – SDR (3%), passively held gold (1%) and reserve positions with the IMF (1%). The actively managed international reserves portfolio can be divided roughly into a euro portfolio, a US dollar portfolio, a Canadian dollar portfolio, a Swedish krona portfolio and an Australian dollar portfolio. The US dollar portfolio is partly diversified into the Japanese yen and the British pound using currency forwards. The Australian dollar portfolio was created in December 2011 by transferring part of the euro portfolio.

Portfolio managers invest the international reserves in particular instruments in compliance with the principles of the CNB's reserve management policy and subject to investment opportunities and the situation on the relevant markets. The largest part of the reserve portfolio is invested in debt securities issued by selected governments of OECD countries, selected government-guaranteed bonds or securities issued by eligible multilateral institutions. Given the continued sovereign debt crisis in the EU, the CNB responded to the latest developments in 2011, as in 2010, by tightening the limits for the government bonds concerned. Other eligible instruments for international reserves management include repos, reverse repos, specific covered bonds, shares, futures, and interest rate, currency and equity swaps. All derivative transactions are collateralised.

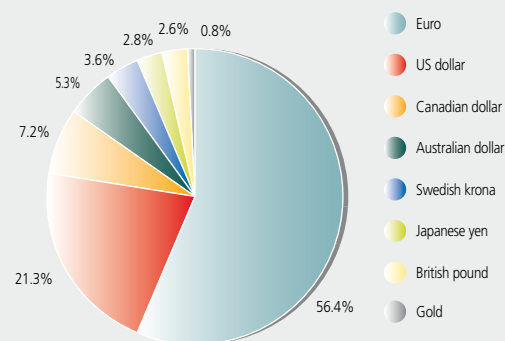


The market value of the CNB's actively managed international reserves portfolio was CZK 755 billion at the end of 2011. The international reserves recorded a year-on-year rise in koruna terms due to portfolio returns (+CZK 13.7 billion) and depreciation

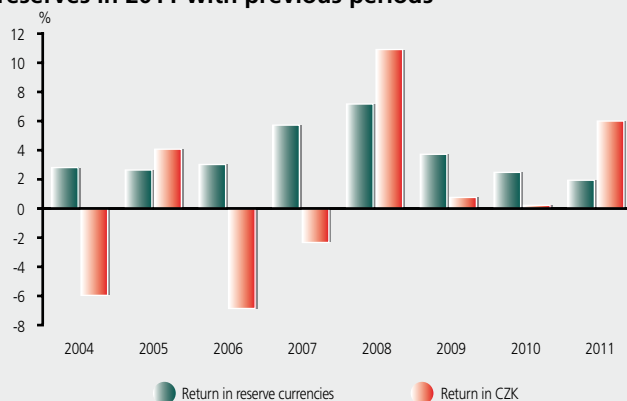
of the koruna against reserve currencies (+CZK 27.8 billion). By contrast, the sell-off of returns (-CZK 24.8 billion) and other external flows<sup>9</sup> (-CZK 17.4 billion) fostered a decrease in the reserves. No foreign exchange interventions were made in 2011.

The individual portfolios recorded the following returns in 2011: euro 1.25%, US dollar 2.53%, Canadian dollar 3.44%, Swedish krona 5.34% and Australian dollar 0.05%. The weighted average of the return on the portfolios in reserve currencies was 1.94%. The return in koruna terms, including exchange rate gains and losses, was 6.00%.

**Currency structure of the actively managed portfolio as of 30 December 2011**



**Comparison of the total return on international reserves in 2011 with previous periods**



In 2011, the CNB gradually expanded the equity portfolios to their target volume, namely 10% of the market value of the international reserves. Analyses have shown that roughly this percentage of equity in the portfolios corresponds to the optimum diversification strategy for market risk management. BlackRock and State Street manage the majority external equity portfolios, with the MSCI Euro, S&P 500, FTSE 100 and Nikkei 225 indices as benchmarks. The internal portfolios are made up of equity swaps.

In 2011, the International Monetary Fund drew six credit tranches totalling SDR 68.4 million under a bilateral loan agreement signed in 2010. As of the end of 2011, the total size of the loan since the contract began represented around 13.5% of the total credit line of EUR 1.03 billion.

### The CNB as the bank of the state

The Czech National Bank provides banking services, i.e. maintains accounts and provides payment services, for the state and the public sector under Act No. 6/1993 Coll., on the Czech National Bank, and Act No. 218/2000 Coll., on Budgetary Rules. The main clients of the CNB are state organisational units, the Czech Social Security Administration, labour offices, and revenue and customs offices. The Czech National Bank also maintains accounts for business entities that receive subsidies from the state budget and for subsidised organisations and state funds, and also accounts connected to the budget of the European Communities. The number of accounts maintained for these clients exceeded 25,000 at the end of 2011. The accounts were used for tens of thousands of transactions daily.

<sup>9</sup> External flows originate from purchases/sales of foreign currency from/to CNB clients and client deposits in foreign currency.

### *Support for Treasury liquidity management*

The CNB has been working with the Ministry of Finance on a Treasury development project since 2000. This work intensified in 2011, since the Ministry of Finance has been building a state budget preparation and implementation system and discussing a draft amendment to the Act on Budgetary Rules which will lay down mandatory use of this system by organisational units of the state.

The CNB is responsible for daily consolidation of state funds on the Single Treasury Account<sup>10</sup> and works closely with the Ministry of Finance to continuously manage intra-day liquidity on this account. Every morning, an estimate of Treasury revenues and expenditures and an outlook for the coming days are compiled. During the day, current-day expenditures are compared with their coverage on the state accounts in the CNB's settlement and payment system. Real-time monitoring of movements on Treasury accounts allows appropriate operations to be chosen so that current expenditures can be covered and effective use can be made of any free Treasury liquidity. Although billions of korunas pass through the Treasury accounts every day, the daily balance on the Single Treasury Account is maintained at around CZK 7 million thanks to good liquidity management.

### *Support for state debt financing*

The CNB acts as fiscal agent for the Ministry of Finance in the area of state debt management. This involves organising and carrying out primary sales of both short-term and long-term government bonds and administering those bonds. The CNB organised 31 auctions of T-bills with maturities of 3, 6, 9 and 12 months on behalf of the Ministry of Finance in 2011. The total volume of T-bills sold was CZK 297 billion. In 2011, the CNB organised 25 auctions of medium-term and long-term government bonds on behalf of the Ministry of Finance in the area of long-term debt. Government bonds totalling almost CZK 159 billion were sold in these auctions. As the administrator of government bond issues, the CNB made coupon payments to government bond holders for 17 issues. One issue was redeemed.

The volume of medium-term and long-term government bonds issued increased from CZK 1,163.3 billion in 2010 to CZK 1,244.9 billion in 2011, while the volume of T-bill issues rose from CZK 113.3 billion to CZK 162.6 billion. Savings bonds with maturities of 1 and 5 years, which are also administered by the CNB, were issued for the first time in 2011. They totalled more than CZK 20 billion.

## **ECONOMIC RESEARCH**

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

In 2011, the CNB published a total of 18 internationally reviewed articles in the CNB Working Paper Series and the CNB Research and Policy Notes and ten research papers in prestigious professional journals such as the *Journal of International Economics* and the *Journal of Comparative Economics*. Two review issues of the *Economic Research Bulletin* also came out. Experts from foreign central banks,

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<sup>10</sup> The Single Treasury Account is defined in Act No. 218/2000 Coll., on Budgetary Rules and on the Amendment of Some Related Acts (Budgetary Rules), as amended, which specifies the accounts subject to consolidation. Above all, they include revenue and expenditure accounts of the state budget, revenue offices' accounts, state financial assets accounts, accounts of funds of state organisational units and Treasury liquidity management accounts.

multilateral organisations and major universities collaborate with CNB economists on research projects. The relevance and quality of research outputs were assessed and internationally compared in a document entitled *CNB Economic Research in 2011*.

The research project coordinators are involved in the monetary policy-making process through the preparation of opinions on the situation reports on economic developments and the minutes and transcripts of monetary policy meetings. The topics raised during monetary policy discussions are taken into account when setting research priorities. Research project outputs are regularly used in CNB documents.

In 2011 the CNB held its seventh Research Open Day, at which it regularly presents the results of its economic research to a broader professional audience and presents the Economic Research Department Award for the best research paper. In 2011, the CNB organised a seminar jointly with the Czech Economic Society and the Centre for Economic Research and Graduate Education (CERGE-EI). The speaker was Laurent Clerc (Banque de France). The CNB was actively involved in the Eurosystem Macroeprudential Research Network (MaRs), which focuses on incorporating financial stability models and indicators into the decision-making processes of central banks.

The Research Advisory Committee is an advisory body to the CNB Bank Board in the area of research. The Committee's main role is to provide recommendations for the Bank Board's decisions on research projects. The members of the Committee include foreign experts.





## EUROPEAN AND INTERNATIONAL RELATIONS

### *European Central Bank, European System of Central Banks and European Systemic Risk Board*

Four times a year, the CNB Governor and Vice-Governor attend meetings of the General Council of the European Central Bank (ECB), where the governors of all the NCBs of the EU countries are represented. Documents concerning macroeconomic, monetary and financial developments around the world and in the EU (broken down into euro area and non-euro area countries) were discussed in 2011. The debt crisis deepened especially in the peripheral countries, adversely affecting the real economy. At the close of 2011, therefore, the ECB lowered its GDP growth forecasts for the period ahead. A discussion took place regarding the methodology of the Convergence Reports (to be published on 30 May 2012). CNB representatives were actively involved in the work of 13 committees of the European System of Central Banks (ESCB) and numerous sub-committees and working groups; in addition to material issues, they presented proposals to improve working practices, streamline procedures and comply with approved working methods.

The CNB processed 120 documents in written consultations on European and national legislation. In 33 cases the CNB made comments in the form of a Governor's letter to the President of the ECB. The CNB consulted the ECB on two regulations – a provision on the terms and conditions for creating minimum reserves and a decree implementing the Act on the Circulation of Banknotes and Coins.

The European Systemic Risk Board (ESRB) commenced its activities in 2011. In the first half of the year it dealt mainly with institutional issues and in the second half it focused on systemic financial market problems, which escalated significantly in this period. In particular, the ESRB analysed and assessed systemic risk in the EU, European stress tests, foreign currency lending (especially in US dollars), the Capital Requirements Directive and the principles of operation of macroprudential supervision. The ESRB issued several recommendations and warnings to the European Council and the European Commission, and in September 2011 it published a press release concerning risks to the stability of the EU financial system.

### *Relations with EU Council, EU Committee*

The CNB has no direct representation in the EU Council except in some of its advisory bodies, especially the Economic and Financial Committee (EFC). Therefore, it works with the relevant government departments and contributes to the coordination of European issues through the EU Committee at the government level, the level of deputy ministers and the working level. At all these levels, the CNB actively commented on topics of relevance, especially in the areas of economic and monetary union and the financial markets.

### *International Monetary Fund*

During 2011, the IMF focused mainly on addressing the global economic situation. The issue of further streamlining of the IMF's operations, including the reform of governance, significantly affected the Czech Republic. On 15 December 2010, the IMF Board of Governors adopted Resolution No. 66-2, under which the Emerging Markets and Developing Countries (EDMCs) will have greater representation in exchange for a reduction of two executive directors in the representation of advanced Europe. The aim is to complete these reforms in time for the autumn 2012 IMF/World Bank meeting. In the course of the year, the CNB was actively involved in the debate on the possibility of creating a new Central European constituency.

In June 2011, in line with the CNB's position, the Executive Board rejected a new SDR allocation, calling it premature. A revision of credit instruments was completed in November. At the same time, it was decided that the assessment and potential expansion of the SDR basket should be based on the existing criteria. At the Annual Meeting, the Managing Director of the IMF Christine Lagarde presented an action plan containing a broad range of future reforms.

At the request of the Czech Republic, an FSAP mission took place in the fourth quarter of 2011. The mission was aimed at providing an independent and in-depth assessment of the condition of the financial sector. In 2011, a total of EUR 82.4 million was drawn from the bilateral loan of EUR 1.03 billion provided to the IMF by the CNB.

#### *CNB activities in other international organisations*

In 2011, the CNB Governor continued to attend the regular meetings of central bank governors of the member countries of the Bank for International Settlements (BIS) held every two months. The CNB was also represented at the regular meeting of vice-governors and at meetings of the Central Bank Governance Group and the Basel Consultative Group (BCG), which is part of the Basel Committee on Banking Supervision. At the expert level, the CNB was involved in the activities of the Working Party on Monetary Policy in Central and Eastern Europe. The CNB also regularly participates in the meetings of a number of OECD working bodies, particularly the Economic Policy Committee and the Committee on Financial Markets. The CNB contributed to the preparation of the OECD's regular economic review of the Czech Republic and the examination of the economic review of Switzerland. CNB representatives attended the meeting of the European Bank for Reconstruction and Development in Astana, Kazakhstan.

#### **Foreign technical assistance**

A total of 33 events took place in 2011: ten seminars for 147 experts from 42 central banks and supervisory authorities, and 13 consultations for 49 participants from Albania, Azerbaijan, Croatia, Kazakhstan, Macedonia, Mozambique, Serbia, Ukraine and Vietnam. The CNB also provided expert assistance in the form of consultations and lectures abroad. Within the ESCB, it continued to implement a banking supervision project for Egypt's central bank and joined a project to prepare Serbia's central bank for ESCB entry. Together with the Deutsche Bundesbank the CNB participated in a European Commission project for the central bank of Croatia in the field of banknote counterfeit deterrence.

In 2011 the CNB organised ten ESCB training events for a total of 122 participants (106 of whom were non-Czechs). On the other hand, 73 CNB employees took part in ESCB events abroad.



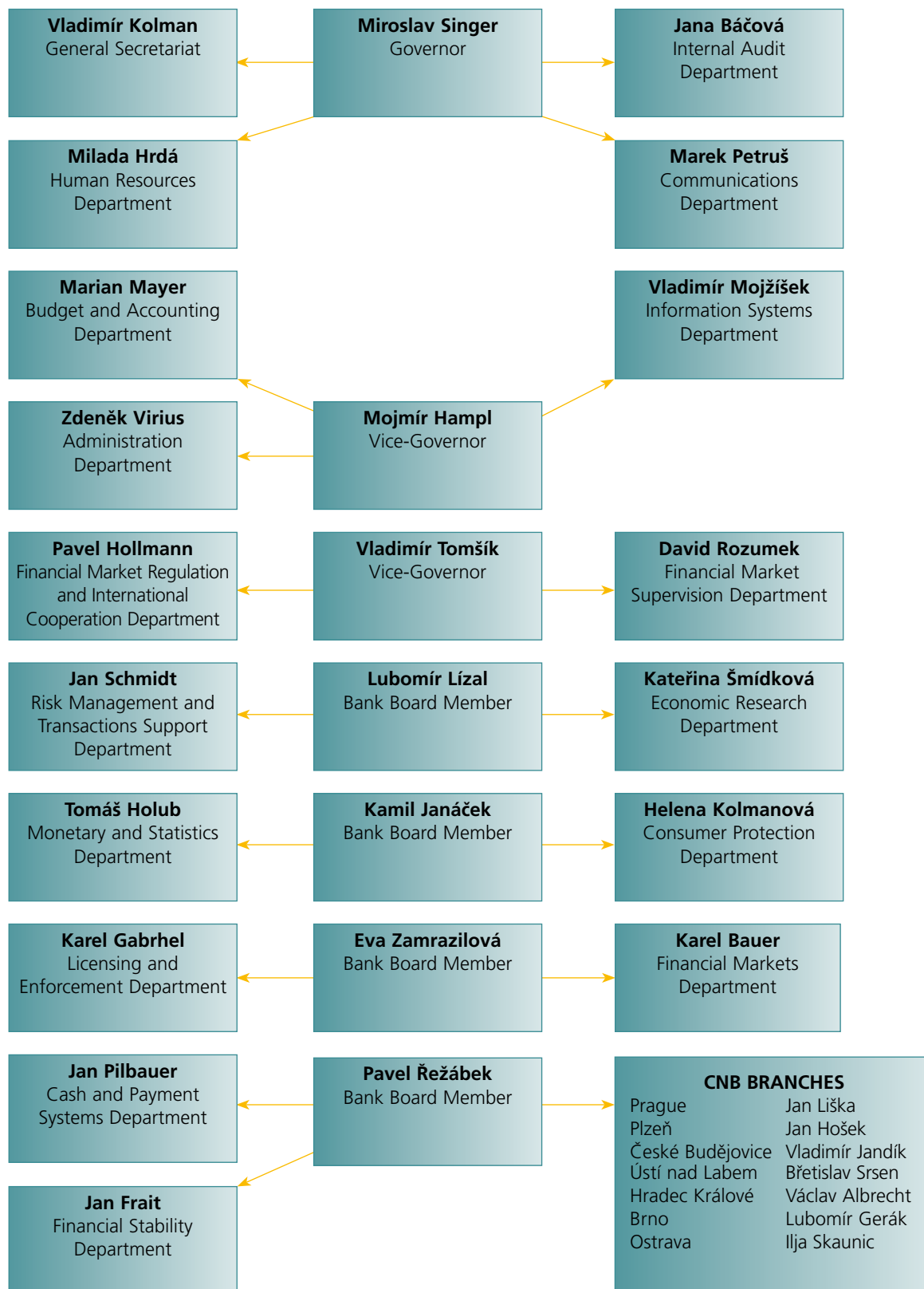




# MANAGEMENT AND ORGANISATION



## ORGANISATIONAL CHART AS OF 31 DECEMBER 2011



The CNB's organisational structure consists of a headquarters in Prague and seven branches in Prague, České Budějovice, Plzeň, Ústí nad Labem, Hradec Králové, Brno and Ostrava.

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

#### *Bank Board*

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



The term of office of Bank Board Member Robert Holman expired on 12 February 2011. The President of the Czech Republic appointed Lubomír Lízal as a new member of the Bank Board with effect from 13 February 2011. As of the same date, Board member Pavel Režábek was appointed for a second six-year term. In this connection, the Bank Board decided to re-allocate the Bank Board members' responsibilities for overseeing the activities performed by the CNB's organisational units at its headquarters and branches.

#### *Executive directors of departments and branches*

These senior officers of the CNB carry out the decisions taken by the Bank Board and are responsible – subject to the CNB's development strategy and plans for individual areas of the competence of the CNB – for the performance of the activities of the units they manage as defined in the Organisational Statute.

The executive directors set targets and tasks for the staff under them and perform the employer's rights and duties under labour law in respect of those employees. Their powers and responsibilities relate not only to direct management activities, but also to methodological management activities in their competence, cooperation with other organisational units of the bank and with external partners in the Czech Republic and abroad, and to the submission of proposed solutions to issues of fundamental significance to the Bank Board.

#### *Headquarters*

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

Several amendments to EU legislation and new legal regulations affected the competences of the CNB and its organisational units in 2011. In accordance with the applicable regulations of the European Parliament and of the Council (EU), the performance of work relating to the establishment and activities of the European Systemic Risk Board and European Supervisory Authorities was incorporated into the Organisational Statute. The Organisational Statute was also revised to include supervision of compliance with Act No. 145/2010 Coll., on Consumer Credit, by financial market entities subject to CNB supervision, and supervision of processors of domestic banknotes and coins under Act No. 136/2011 Coll., on the Circulation of Banknotes and Coins, under which the CNB also assumed legal responsibility for performing the functions of the National Counterfeit Centre and National Analysis Centre. Under Act No. 180/2011 Coll., amending the Act on the Financial Arbitrator, the financing of the Office of the Czech Financial Arbitrator was transferred from the CNB to the state and the support activities provided to the Financial Arbitrator by the CNB were discontinued.

The Bank Board decided to re-organise the Financial Market Supervision Department. Responsibility for financial education was transferred from the Consumer Protection Department to the Communication Department. The Financial Market Regulation and Analyses Department – the supervisory department responsible for external relations – was re-named the Financial Market Regulation and International Cooperation Department. Following a personnel audit, internal organisational changes were carried out in headquarters units, including the abolition of several divisions.

#### *Branches*

The CNB's branches represent the bank in their regions of jurisdiction and are contact points for the CNB's relations with state and local authorities and legal and natural persons that have registered offices or residence addresses in the relevant region when dealing with the CNB under the relevant legal rules. This does not affect the right of the said entities to deal with the CNB's headquarters in Prague.

The CNB's branches are responsible mainly for managing money reserves (with the exception of the branches in České Budějovice and Ústí nad Labem), maintaining accounts of the state budget and other CNB clients falling within their fields of competence, and making payments for them. To a specified extent they also perform supervision and foreign exchange inspections of financial market entities, including supervision in the area of consumer protection. They collect, check and process data for business surveys. They receive suggestions, enquiries and notifications from the public and deal with them within their defined areas of competence.

### **HUMAN RESOURCES**

The Czech National Bank strives constantly to achieve a reasonable level of spending on its staff and on developing their skills. A sustained emphasis on the traditional values of CNB employees, in particular credibility and a high level of expertise, is a precondition for maintaining the CNB's reputation.

### *Numbers of positions and employees*

Between January 2011 and the end of February 2012, the CNB underwent a comprehensive reorganisation consisting of 25 organisational changes. This resulted in a decrease of 96 positions, which represents a fall of 6.6% compared to 1 January 2011. As of 31 December 2011, the CNB had 1,415 employees, down by 62 from 31 December 2010. A total of 168 employees left the CNB during 2011, 129 of which at its headquarters and 39 at branches. In 2011, 68 more employees left the CNB than in 2010, of which 48% left for organisational reasons, 19% left without giving any reasons, 16% retired and the remaining 17% gave other reasons. The Office of the Financial Arbitrator was transferred with all its employees



to the Ministry of Finance on 1 July 2011. The total staff turnover rate, including employees whose positions were eliminated due to organisational changes, was 11.6%. The average length of employment at the CNB was 13.3 years, slightly lower than in 2010 (13.4 years).

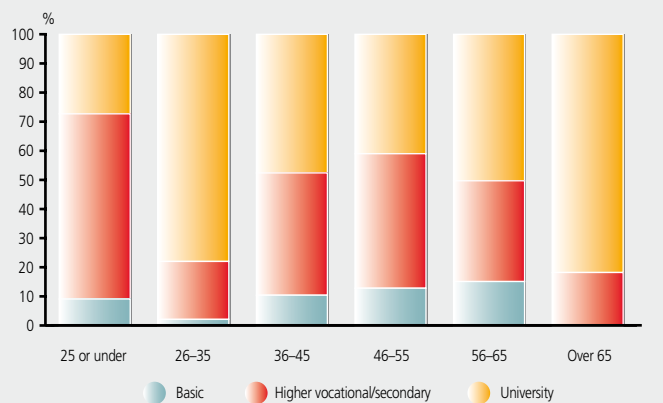
### *Recruitment and selection*

The CNB performs numerous tasks relating to financial market supervision, maintenance of monetary and price stability and consumer protection, plays a specific role in licensing and penalty proceedings, and is actively involved in the work of international organisations, primarily in the area of financial market regulation and supervision. To perform these tasks well, it is important to seek and recruit highly skilled employees. To fill vacancies, the CNB uses external selection procedures and directly contacts people who register an interest in working for the CNB. To increase the efficiency of its personnel processes it also makes use of internal mobility. In addition to the traditional advertising of job offers in the daily press (e.g. *Hospodářské noviny* and *Mladá fronta Dnes*) and via internet portals (e.g. *Jobs.cz*), targeted cooperation with universities has proved successful.

### *Education, age and gender structure*

The number of university-educated employees (which made up 52.4% of the total CNB workforce in 2011) is increasing slightly, in line with the bank's objectives and tasks. Employees with higher vocational training or secondary school education ending with a school leaving exam (including vocational training ending with a school leaving exam) accounted for 37.3%, and employees with vocational training without a school leaving exam or with basic education recorded a 10.3% share.

Age and education structure of employees



Representation of men and women



The CNB's equal opportunities policy for all employees and job applicants is reflected in equal representation of employees across the individual age and gender categories. A positive aspect of the CNB's stable staff structure is that it provides an opportunity to create work teams with the optimal composition and thereby minimise the risks arising from generational turnover. The average age of the CNB's workforce as of 31 December 2011 was 44.9 years, the same as in 2010. At the end of 2011, the ratio of men to women was 1:1.

#### Incentive system

Staff assessment and remuneration are key instruments affecting the fulfilment of the CNB's mission. Regular feedback provided by managers within work teams is an integral part of the incentive system. Managers – as salary administrators of their divisions and departments – are motivated within the system to continuously streamline all activities and optimise all processes.

The 2011 reorganisation resulted not only in a decrease in the number of job positions and employees, but also in an overall decline in personnel expenses of 1.8% compared to the previous year. These expenses, which comprise wage costs, including temporary sick leave payments, obligatory insurance contributions and other social expenses (pension insurance, health care and food allowances), training expenses and employee benefits, amounted to CZK 1,238 million in 2011.

#### The salaries of Bank Board members were as follows:

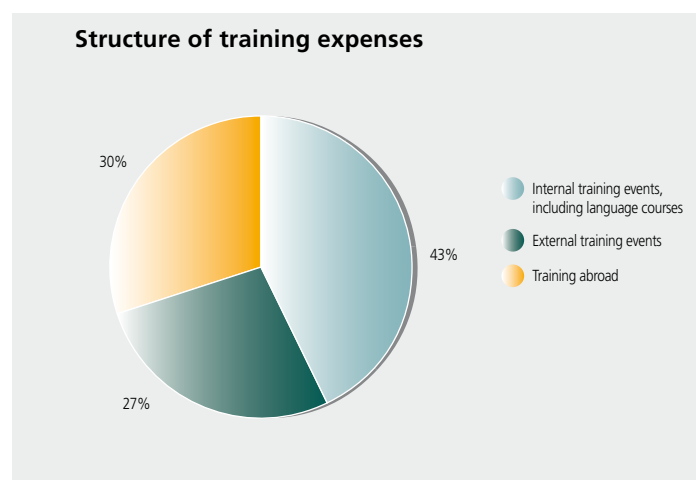
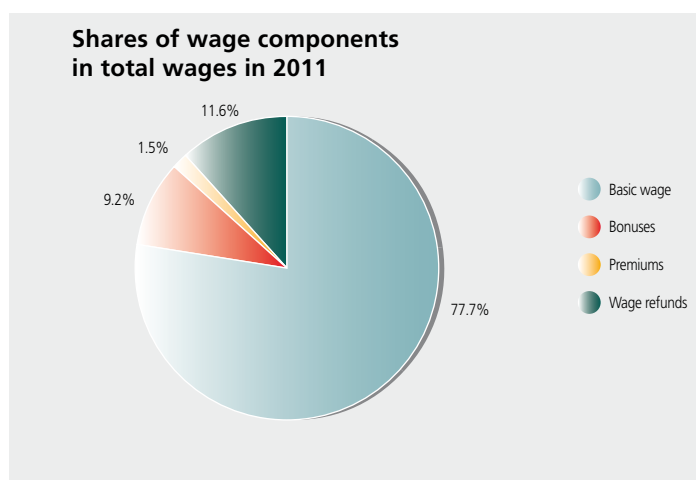
	Gross salary in CZK <sup>1)</sup>	Net salary in CZK <sup>2)</sup>
Miroslav Singer	4,299,275	3,414,446
Mojmír Hampl	3,429,969	2,675,536
Vladimír Tomšík	3,482,962	2,673,732
Kamil Janáček	2,927,914	2,201,941
Lubomír Lízal <sup>3)</sup>	2,624,528	1,963,763
Pavel Režábek	2,914,652	2,214,308
Eva Zamrazilová	2,916,763	2,250,914
Robert Holman <sup>4)</sup>	713,813	502,562

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

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

3) Lubomír Lízal was appointed CNB Bank Board member as from 13 February 2011.

4) Robert Holman's term of office ended on 12 February 2011. He left the CNB on 31 March 2011.



#### Professional development

In addition to the systematic professional development of all employees, the CNB pays special attention to enhancing managerial skills and preparing selected employees for the positions of top specialists and managers. Spending on CNB staff training totalled CZK 28 million in 2011.

Specialised courses focusing on enhancing skills in individual CNB business areas accounted for a significant part of the internal training event structure. At the request of supervisory units and in partnership with KPMG, a series of seminars on international financial reporting standards and other accounting regulations was held. A major three-year training project entitled *Development of corporate culture and soft skills of CNB staff* was completed successfully in the second half of 2011. It was financed by the European Social Fund within Operational Programme Prague Adaptability. Short-term external training events organised in the form of seminars and workshops were used to acquire knowledge of new legislation and practices and to train specialists, for example in the IT area.

As for training abroad, cooperation continued between the CNB and partner central banks, the International Monetary Fund, the Joint Vienna Institute and the Financial Stability Institute. The most popular training events were seminars and workshops in the fields of financial stability, economic modelling and the financial markets. In 2011, CNB staff were actively involved in the ESCB training programme. There was a further increase in the number of financial market regulatory and supervisory staff attending seminars organised by the ESMA, EBA and EIOPA. Extension of knowledge and experience in the form of consultations and short-term exchange study visits between central bank staff and financial market regulatory and supervisory institutions in the EU was an important element of specialised training.

The CNB again organised long-term and intensive language courses focusing mainly on enhancing knowledge of specialised terminology and communication skills. Regular complementary e-learning also continued in 2010. The language courses also concentrated on meeting language skills requirements for managerial positions and specialised professions for which such requirements are prescribed. A total of 52% employees proved their language skills by passing standardised language examinations.





# PUBLIC RELATIONS



### EXTERNAL COMMUNICATIONS

In 2011, the CNB commemorated the 85th anniversary of the foundation of its predecessor, the National Bank of Czechoslovakia. Its establishment on 21 March 1926 was the culmination of efforts by Czechs and Slovaks to create their own stable currency, whose value was to be guarded by an autonomous bank of issue. The values that applied at its birth in the 1920s, when the NBC took over the care of the Czechoslovak koruna from Finance Minister Karel Engliš, the CNB acknowledges to this day. This is why it consistently builds on its reputation as an independent, competent and open institution in its communication with the public. The traditionally high public confidence in the central bank's activity was confirmed by a STEM survey conducted in February 2011, according to which 77% of Czechs trust the CNB (according to an updated survey published in March 2012 the figure is now 78%).

The CNB fulfils its mandate by informing the public regularly, and as openly as possible, about its activities relating to maintaining confidence in the value of the Czech currency and the financial system.



As regards monetary policy issues, the CNB is one of the most transparent central banks in the world. The CNB strengthened this position in 2011 when it started to publish the Graph of Risks to the Inflation Projection (GRIP), one of the key materials for the monetary policy decision-making of the Bank Board members at meetings at which no new forecast is made available.

The CNB's website ([www.cnb.cz](http://www.cnb.cz)) is its most important means of communication. The design and functions of the site were changed in 2011. Its current look, with new navigational elements and more intuitive ordering of sections, is in line with the practices of similar institutions in Europe and around the world and is consistent with long-term analyses of visitor traffic. In 2011, the CNB website had 179,000 visitors and 1.6 million page loads a month on average.

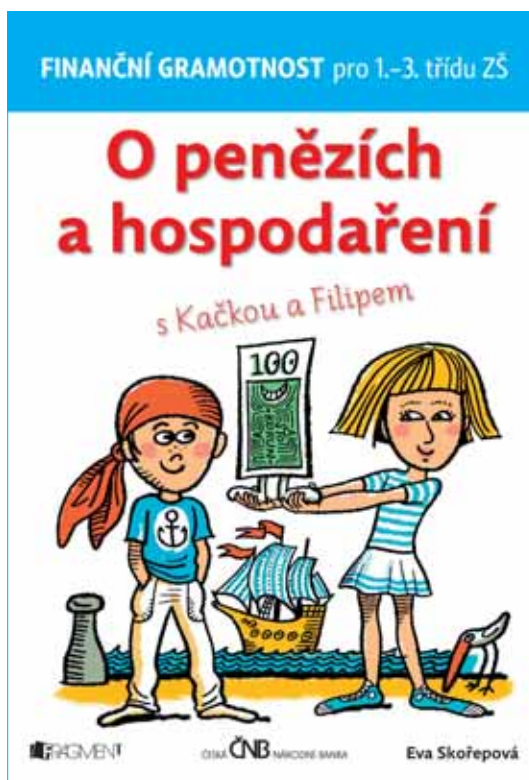
At the end of 2011, the public were able to vote for the first time on the design of a commemorative silver coin on the CNB's website. The coin will be issued in 2013 to mark the 20th anniversary of the establishment of the Czech central bank and the Czech currency. A total of 4,000 people voted. Based on the result, the Bank Board recommended the design by Vladimír Oppl for realisation.



The CNB's profiles on Twitter and, since 2011, on YouTube are additional internet communication tools. Consistent fulfilment of the CNB's mandate is also aided by suggestions from the public. In 2011, the central bank processed 10,952 submissions through the CNB Information Service. The CNB dealt with 5,793 telephone calls, 4,497 e-mails and 662 letters in 2011.

#### FINANCIAL EDUCATION

Financial literacy affects the behaviour of consumers in the world of finance. For this reason, the CNB has long supported projects to improve the skills and confidence of the general public in actively using products offered on the financial market.







Financial education should be a routine part of the educational process from the first grades of primary schools. During 2011, the CNB therefore distributed more than 10,000 financial literacy workbooks to primary schools for the first to third grades to help teachers educate their youngest pupils. The workbook, entitled *Money and Finance with Katie and Philip*, is based on the educational programmes of the Ministry of Education. It teaches schoolchildren where money comes from and how to recognise the protective elements of Czech banknotes. They also “visit” a bank, learn about the function of advertising, and learn that goods can be returned.

An animated film *Of Money and Men* – targeted not at only teachers and schoolchildren, but also at the wider public – has been available on YouTube since September 2011. In addition to basic economic and financial terms, the film presents some interesting facts about the history of money and the CNB’s activities.

The central bank’s activities are not aimed solely at schoolchildren. The website [www.cnbprovsechny.cnb.cz](http://www.cnbprovsechny.cnb.cz) (“CNB for All”) provides guidance for anyone interested in managing their personal finances sensibly. This site, like the official CNB website, acquired a new design and navigation elements in 2011.

The CNB’s branches were also involved in financial education in 2011. In collaboration with high schools and universities they organised lectures and competitions for school pupils and students and, together with other partners in selected regions, helped to train field social workers who come into contact with socially disadvantaged or excluded people.

## EXHIBITION

The CNB Exhibition, located in a former strong-room, celebrated its 10th birthday in 2011. More than 150,000 registered visitors, mostly school pupils and students, have visited the permanent exhibition *People and Money* since it opened.

The history, mission and tasks of the central bank are presented in, among other things, an introductory documentary called *The Bank of Its Country*, an animated film entitled *Of Money and Men* and 66 showcases containing exhibits that are regularly supplemented and updated. The exhibition is open Tuesday to Friday. Tours are organised at 9 a.m., 11 a.m. and 1.30 p.m. each day, and also at 4 p.m. on Thursday. More information is available in the *People and Money* section of the CNB website.



## SPECIAL LIBRARY

The primary mission of the CNB's special library is to provide CNB staff and outside specialists with information. The library offers lending, advisory, reference, bibliographic and research services. Its highly specialised collection and access to numerous electronic sources allow users to obtain information in the fields of banking and economics in general, law and computer technology and to some extent in other areas as well. The electronic catalogue is integrated into the Single Information Gateway operated by the National Library of the Czech Republic. The library is open Monday to Thursday from 9 a.m. to 5 p.m. and Friday from 9 a.m. to 3 p.m. The library can be contacted by e-mail at [lib@cnb.cz](mailto:lib@cnb.cz). All information, including the electronic catalogue, is available in the *CNB special library* section of the CNB website.

## ARCHIVE

The CNB Archive cares for the archive documents produced by the CNB and its legal predecessors. Archive tools in book and electronic form (268,810 detailed entries) are made accessible to researchers via archive collections. The CNB Archive's research room is open all year subject to prior consultation. Anyone interested in studying in the CNB Archive should visit the CNB website (About the CNB > Archive of the CNB) or e-mail [archiv@cnb.cz](mailto:archiv@cnb.cz)

In 2011, the CNB Archive organised an internal exhibition entitled *The Beauty of Banking Shares* and also lent out archive documents for an exhibition entitled *First Ladies – Fate, Mission, Destiny?* organised by the Central Bohemian Museum in Roztoky u Prahy.

#### CONGRESS CENTRE

The CNB Congress Centre, located in the listed building of the former Commodity Exchange, is a traditional venue for meetings between the CNB's top management and representatives of other central banks, deputies and senators of the Parliament of the Czech Republic, financial market representatives, trade unions, analysts and journalists. The CNB's specialised units hold conferences, lectures, presentations, seminars, ECB committee and working group meetings, quarterly insurance intermediaries' examinations and training sessions there. The Congress Centre, which is equipped with modern audio-visual conference technology, is also hired by external institutions for professional and social events. More information is available on the CNB website at [About the CNB > Organisational structure > CNB headquarters building](#).









# FINANCIAL REPORT



(Translation of a report originally issued in Czech.)

## INDEPENDENT AUDITOR'S REPORT

To the Bank Board of Česká národní banka:

- I. We have audited the financial statements of Česká národní banka as at 31 December 2011 presented on the enclosed CD-ROM and our audit report dated 24 February 2012 stated the following:

"We have audited the accompanying financial statements of Česká národní banka, which comprise the balance sheet as at 31 December 2011, and the income statement for the year then ended, and a summary of significant accounting policies and other explanatory notes. For details of Česká národní banka see Note 1 to the financial statements.

### *Management's Responsibility for the Financial Statements*

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the Czech Republic, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

### *Auditor's Responsibility*

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with the Act on Auditors and International Standards on Auditing as amended by implementation guidance of the Chamber of Auditors of the Czech Republic. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance 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 an assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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

### *Opinion*

In our opinion, the financial statements present fairly, in all material respects, the financial position of Česká národní banka as at 31 December 2011, and its financial performance for the year then ended in accordance with accounting principles generally accepted in the Czech Republic."

- II. We have also audited the consistency of the annual report with the financial statements described above. The management of Česká národní banka is responsible for the accuracy of the annual report. Our responsibility is to express, based on our audit, an opinion on the consistency of the annual report with the financial statements.

We conducted our audit in accordance with International Standards on Auditing and the related implementation guidance issued by the Chamber of Auditors of the Czech Republic. Those standards require that we plan and perform the audit to obtain reasonable assurance as to whether the information presented in the annual report that describes the facts reflected in the financial statements is consistent, in all material respects, with the financial statements. We have checked that the accounting information presented in the annual report in section 5 "Financial report" is consistent with that contained in the audited financial statements as at 31 December 2011. Our work as auditors was confined to checking the annual report with the aforementioned scope and did not include a review of any information other than that drawn from the audited accounting records of the Company. We believe that our audit provides a reasonable basis for our opinion.

Based on our audit, the accounting information presented in the annual report is consistent, in all material respects, with the financial statements described above.

A stylized signature of the Ernst & Young firm, written in black ink.

Ernst & Young Audit, s.r.o.  
License No. 401  
Represented by Partner

A handwritten signature of Magdalena Soucek, written in black ink.

Magdalena Soucek  
Auditor, License No. 1291

24 February 2012  
Prague, Czech Republic

## FINANCIAL STATEMENTS

<b>ASSETS</b>			
in CZK million			
		31 Dec. 2011	31 Dec. 2010
<b>1.</b>	<b>Gold</b>	<b>755</b>	<b>770</b>
<b>2.</b>	<b>Receivables from the International Monetary Fund</b>	<b>57,337</b>	<b>48,499</b>
<b>3.</b>	<b>Receivables from abroad, including securities</b>	<b>758,856</b>	<b>761,500</b>
3.1.	Deposits at foreign banks and financial institutions	71,767	11,749
3.2.	Loans provided to foreign banks	52,671	44,222
3.3.	Securities	634,315	705,450
3.4.	Other receivables from abroad	103	79
<b>4.</b>	<b>Receivables from domestic banks</b>	<b>3,500</b>	<b>1,500</b>
<b>5.</b>	<b>Fixed assets</b>	<b>4,413</b>	<b>4,692</b>
5.1.	Tangible fixed assets	4,390	4,657
5.2.	Intangible fixed assets	23	35
<b>6.</b>	<b>Other assets</b>	<b>7,245</b>	<b>6,689</b>
6.1.	Other financial assets	3,883	3,478
6.2.	Other	3,362	3,211
	<b>TOTAL ASSETS</b>	<b>832,106</b>	<b>823,650</b>

<b>LIABILITIES AND EQUITY</b>			
in CZK million			
		31 Dec. 2011	31 Dec. 2010
<b>1.</b>	<b>Notes and coins in circulation</b>	<b>411,953</b>	<b>391,694</b>
<b>2.</b>	<b>Liabilities to the International Monetary Fund</b>	<b>44,830</b>	<b>41,358</b>
<b>3.</b>	<b>Liabilities abroad</b>	<b>4,984</b>	<b>6,180</b>
3.1.	Loans from foreign banks	4,818	5,153
3.2.	Other liabilities abroad	166	1,027
<b>4.</b>	<b>Liabilities to domestic banks</b>	<b>389,520</b>	<b>394,275</b>
4.1.	Loans received	328,046	339,838
4.2.	Bank monetary reserves	50,317	40,256
4.3.	Other liabilities to banks	11,157	14,181
<b>5.</b>	<b>Liabilities to the state and other public institutions</b>	<b>76,000</b>	<b>123,690</b>
5.1.	Liabilities to the state	70,906	119,318
5.2.	Other liabilities	5,094	4,372
<b>6.</b>	<b>Provisions</b>	<b>229</b>	<b>215</b>
<b>7.</b>	<b>Share capital</b>	<b>1,400</b>	<b>1,400</b>
<b>8.</b>	<b>Funds</b>	<b>8,050</b>	<b>8,050</b>
<b>9.</b>	<b>Revaluation reserve</b>	<b>12,239</b>	<b>8,667</b>
<b>10.</b>	<b>Accumulated losses from previous periods</b>	<b>-161,836</b>	<b>-152,102</b>
<b>11.</b>	<b>Net loss / profit for the period</b>	<b>35,425</b>	<b>-9,734</b>
<b>12.</b>	<b>Other liabilities</b>	<b>9,312</b>	<b>9,957</b>
	<b>TOTAL LIABILITIES AND EQUITY</b>	<b>832,106</b>	<b>823,650</b>

<b>OFF-BALANCE SHEET</b>			
in CZK million			
		31 Dec. 2011	31 Dec. 2010
<b>1.</b>	<b>Guarantees issued</b>	<b>158,120</b>	<b>158,135</b>
<b>2.</b>	<b>Issued loan commitments</b>	<b>17,482</b>	<b>24,690</b>
<b>3.</b>	<b>Receivables from spot, term and futures transactions</b>	<b>143,467</b>	<b>173,097</b>
<b>4.</b>	<b>Liabilities from spot, term and futures transactions</b>	<b>143,462</b>	<b>174,542</b>
<b>5.</b>	<b>Guarantees received</b>	<b>156,952</b>	<b>156,952</b>
<b>6.</b>	<b>Collateral received</b>	<b>77,841</b>	<b>68,065</b>
<b>7.</b>	<b>Values taken into custody and values in own custody</b>	<b>0</b>	<b>292</b>

<b>INCOME STATEMENT</b>			
in CZK million		31 Dec. 2011	31 Dec. 2010
<b>1.</b>	<b>Interest income and similar income</b>	<b>9,836</b>	<b>10,552</b>
1.1.	Interest from fixed income securities	9,133	10,288
1.2.	Other	703	264
<b>2.</b>	<b>Interest expense and similar expense</b>	<b>-3,380</b>	<b>-4,024</b>
<b>3.</b>	<b>Income from shares and other interests</b>	<b>1,277</b>	<b>1,232</b>
<b>4.</b>	<b>Fee and commission income</b>	<b>354</b>	<b>309</b>
<b>5.</b>	<b>Fee and commission expense</b>	<b>-70</b>	<b>-74</b>
<b>6.</b>	<b>Gains less losses from financial operations</b>	<b>29,258</b>	<b>-15,503</b>
6.1.	Net foreign exchange gains / losses and foreign exchange spread	29,818	-16,386
6.2.	Other	-560	883
<b>7.</b>	<b>Other operating income</b>	<b>438</b>	<b>262</b>
7.1.	Income from money issue	239	124
7.2.	Other	199	138
<b>8.</b>	<b>Other operating expense</b>	<b>-354</b>	<b>-452</b>
8.1.	Expenses for production of notes and coins	-276	-414
8.2.	Other	-78	-38
<b>9.</b>	<b>Administration expense</b>	<b>-1,593</b>	<b>-1,640</b>
9.1.	Personnel expenses	-1,238	-1,262
9.1.1.	Wages and salaries	-863	-872
9.1.2.	Social and health security	-290	-297
9.1.3.	Training and employee benefits	-85	-93
9.2.	Other administration expenses	-355	-378
<b>10.</b>	<b>Depreciation and amortisation of fixed assets</b>	<b>-345</b>	<b>-398</b>
<b>11.</b>	<b>Reversal of provisions for receivables and guarantees, income from receivables already written off</b>	<b>168</b>	<b>4,953</b>
<b>12.</b>	<b>Write offs, additions and utilisation of provisions for receivables and guarantees</b>	<b>-164</b>	<b>-4,951</b>
<b>13.</b>	<b>Net loss / profit for the period</b>	<b>35,425</b>	<b>-9,734</b>

The full version of the financial statements of the Czech National Bank as of 31 December 2011, including the notes thereto, is available on the CNB website [www.cnb.cz](http://www.cnb.cz) (About the CNB > Performance > Financial statements) and on the attached CD-ROM.

The structure of income and expenses used in the following text corresponds to the main activities arising from Act No. 6/1993 Coll., on the CNB. Compared to the structure of the standard financial statements, which provide an overview of income and expenses primarily with regard to type, this view provides information with regard to the purpose of the bank's expenditure. The following review of income and expenses lists the individual areas of the central bank's financial performance in 2011.

in CZK millions

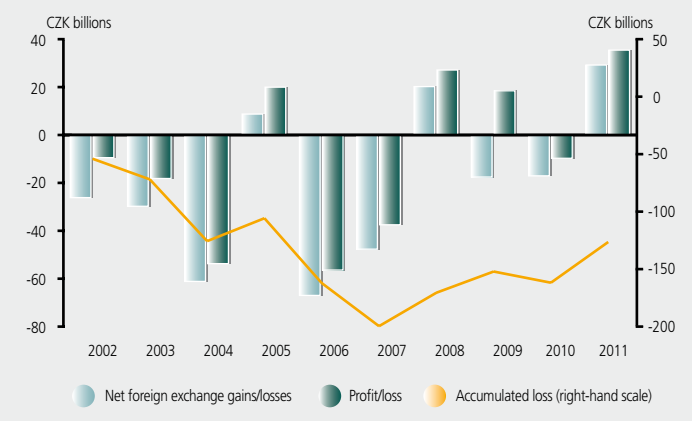
	Expenses	Income	Net	y-o-y change
Monetary area	33,345	70,617	37,272	44,784
• monetary policy-making	3,072	4	-3,068	400
• international reserves management	28,918	39,365	10,447	-2,019
• valuation changes	954	30,161	29,207	46,263
• client operations	374	1,048	674	138
• other operations	27	39	12	2
Currency issuance and management	276	258	-18	257
Operations	1,991	162	-1,829	118
<b>Total</b>	<b>35,612</b>	<b>71,037</b>	<b>35,425</b>	<b>45,159</b>

The CNB recorded a profit of CZK 35,425 million in 2011. This was due mainly to international reserves management and to exchange rate gains recorded by the CNB as a result of the year-on-year depreciation of the Czech currency. 2011 was a specific year with regard to the nominal exchange rate, since the koruna depreciated against all reserve currencies in year-on-year terms. The depreciation was largely associated with nervousness on financial markets due to the persisting debt crisis in some euro area countries. The CNB's main monetary policy instruments remained unchanged in 2011, with key interest rates being left at historical lows. As a result, the sharp decline in sterilisation costs seen in previous years was not repeated.

In order to ensure smooth money circulation, the CNB every year purchases new coins and banknotes from its suppliers. The total purchased volume decreased in 2011. In combination with higher sales of numismatic material, net costs in this area recorded a substantial decline. The significant year-on-year decrease in the bank's operating expenses is due to targeted pressure to streamline all the activities delegated to the CNB. In 2011, increased attention was paid to personnel expenses, which make up a large part of the bank's operating expenses. As a result of a reorganisation, the number of CNB staff declined. This was accompanied by a decrease in the bank's total wage costs.

In line with financial management principles, the profit was used in full to reduce accumulated losses from previous periods. After this payment, the bank's balance sheet will continue to show an accumulated loss of CZK 126.4 billion.<sup>11</sup>

The CNB's performance 2002–2011



The CNB's performance in 2011



<sup>11</sup> A more comprehensive analysis of the CNB's performance in 2011 is available on the CNB website (*About the CNB > Performance > Financial Reports*).







PROVISION OF INFORMATION UNDER  
ACT NO. 106/1999 COLL.



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

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

The CNB's procedure for complying with the duties ensuing from the Act, and in particular its procedure for accepting and dealing with applications for information in compliance therewith, is regulated by Czech National Bank Directive No. 55 of 13 December 2002, on the communication of the Czech National Bank, as amended.

#### **A) Information provided in 2011 on the basis of applications:**

1. Number of applications for information submitted in compliance with the Act: 19
2. Number of decisions refusing an application: 5.
3. Number of appeals submitted against decisions: 1
4. Transcript of the relevant parts of each court judgement concerning the examination of the legality of an obliged entity's decision refusing an application for information and an overview of all expenses incurred by the obliged entity in connection with court proceedings on rights and obligations under this Act, including its own staff expenses and legal representation costs: 0
5. Number of exclusive licences granted, including justification of the necessity to grant exclusive licences: 0
6. Number of complaints submitted under Article 16a, reasons for their submission and a brief description of the manner in which they were dealt with: 2
  - 6.1. A complaint about the CNB's procedure when dealing with the complainant's application for information regarding the type of power under which it was decided about the prohibition of the sale of commemorative coins at a CNB branch to natural persons which do not carry on business, including an application for the provision of a copy of a document by which this was implemented. The complainant was not provided with the document, as it was a document meant only for the CNB's internal use. The CNB Bank Board in its decision about the complaint upheld the CNB's previous procedure as correct.
  - 6.2. A complaint about the CNB's procedure when dealing with the complainant's application for the submission of a document for the CNB Bank Board regarding the reorganisation in the Financial Market Supervision Department. The complainant was not provided with the requested documents, as in the CNB's opinion these documents and the related decision are considered employment facts. They cannot therefore be subject to Act No. 106/1999 Coll., on Freedom of Information, as amended. The CNB Bank Board in its decision about the complaint upheld the CNB's previous procedure as correct.
7. Other information relating to application of the Act: 0

#### **B) Information provided by way of public disclosure:**

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



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