



growth, being higher than that in the external environment, created leeway for sustainable appreciation of the real exchange rate without disrupting the economy's equilibrium. However, the REER had followed a depreciating trend in

previous years. The improvement in Slovakia's trade balance and increase in its exports as a share of global trade points to growing competitiveness.

2 EUROSYSTEM MONETARY POLICY

2.1 MONETARY POLICY OPERATIONS

The ECB's Governing Council adjusted key ECB interest on two occasions in 2013, so as to ensure price stability in the medium term amid low underlying price pressures and to support gradual economic recovery. At the monetary policy meeting in May the Governing Council decided to reduce the main refinancing rate, by 25 basis points, and the marginal lending rate, by 50 basis points, with effect from 8 May 2013, while keeping the deposit facility rate unchanged at 0.00%. At November's meeting the Governing Council decided to decrease both the main refinancing rate and marginal lending rate by 25 basis points, with effect from 13 November, and to leave the deposit facility rate unchanged. Overall in 2013 the main refinancing rate and marginal lending rate were cut, respectively, by 50 basis points and 75 basis points, to 0.25% and 0.75%, and the deposit facility rate stayed at 0.00%.

The EONIA remained below the main refinancing rate throughout the year except during end-month fluctuations. The composition of banks' deposits with the ECB altered slightly. Of the total, only 32% on average were held in the overnight deposit facility while the rest were held in current accounts with the ECB.

The European Central Bank implements monetary policy through the national central banks of the Eurosystem by means of various monetary policy instruments. The most widely used of these instruments are main refinancing operations, longer-term refinancing operations (LTROs), fine-tuning operations (FTOs), and standing facilities, which include the deposit facility (DF) and marginal lending facility (MLF).

During 2013 the Governing Council approved the continuation of selected non-standard monetary measures in order to enhance the transmission of accommodative monetary policy to the real economy in the medium term. In May the Governing Council announced that main refinancing operations (MROs) would continue to be conducted as fixed rate tender procedures with full allotment at least until the end of the sixth reserve maintenance period of in July 2015 (as at present).

The same procedure would remain in use for the Eurosystem's special-term refinancing operations with a maturity of one maintenance period, which will be conducted as long as necessary, but at least until the end of the second quarter of 2014, or 2015. The fixed rate in these special-term refinancing operations would be the same as the MRO rate prevailing at the time. Furthermore, it was decided to conduct the three-month longer-term refinancing operations (LTROs) as fixed rate tender procedures with full allotment until the end of the second quarter of 2014 or 2015. The rates in these three-month operations would be fixed at the average rate of the MROs over the life of the respective LTRO.

At its first monetary policy meeting in July the Governing Council engaged in forward guidance for the first time, announcing its expectation that the key ECB interest rates would remain at present or lower levels for an extended period of time. This expectation was based on the overall subdued outlook for inflation extending into the medium term, given the broad-based weakness in the real economy and subdued monetary dynamics. The Governing Council added that in the period ahead it would monitor all incoming information on



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economic and monetary developments and assess any impact on the medium-term outlook for price stability. After its monetary policy meeting in November, the Governing Council announced that its monetary policy stance would remain accommodative for as long as necessary, as announced in its forward guidance in July 2013. The Governing Council reiterated its expectation that the key ECB interest rates would remain at present or lower levels for an extended period.

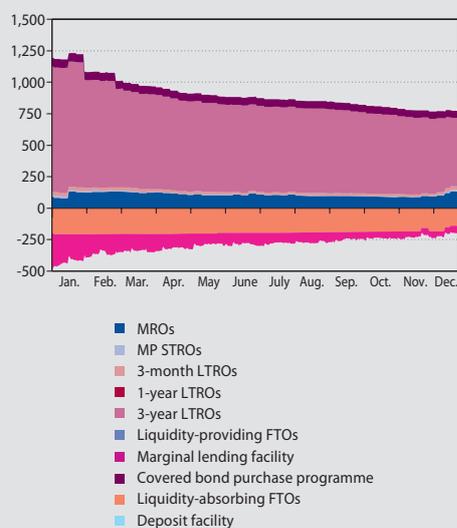
Early in 2013 euro area banks began invoking the option of early repayment of three-year LTRO funds obtained from two operations settled in 2011 and 2012 with a total allotment of more than €1 billion. Banks also reduced their borrowing in special-term refinancing operations with a maturity of one maintenance period as well as in three-month LTROs. Longer-term funding as a share of the total fell to an average of 84%. The lower uptake of longer-term funds in comparison with the previous year was partially offset by increased participation in short-term MROs. The reduction in banks' borrowing from the ECB was associated with increasing stability in the euro area and with measures taken in several euro area countries to support banking sector stability.

The utilisation of US dollar liquidity swap arrangements maintained by the ECB with the Federal Reserve System showed a falling tendency. The euro area banking sector substantially reduced its participation in seven-day US dollar liquidity-providing operations, presumably owing to banks' improved conditions for obtaining dollar funding from wholesale markets. Insofar as they used the ECB's dollar swap arrangements, euro area banks participated mainly in three-month operations. On average they borrowed only USD 0.3 billion, as against USD 4 billion in the previous year.

In 2013 the ECB along with the Federal Reserve, the Bank of Canada, the Bank of England, the Bank of Japan, and the Swiss National Bank announced that their existing temporary bilateral liquidity swap arrangements were being converted to standing arrangements, i.e. arrangements that will remain in place until further notice. The ECB's US dollar liquidity swap arrangements had previously been due to end at the end of February 2014.

In October the ECB and the People's Bank of China established a bilateral currency swap agreement that will be valid for three years. From the perspective of the ECB, the arrangement ensures

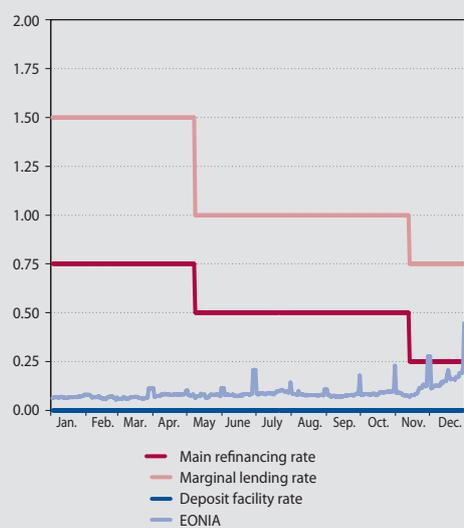
Chart 7 Eurosystem operations in 2013 (EUR billions)



Source: ECB.

Note: MP STRO – special-term refinancing operation with a maturity of one maintenance period.

Chart 8 Key ECB interest rates and the EONIA in 2013 (percent per annum)



Source: ECB and Bloomberg.



that euro area banks will have continuous access to yuan funding. The maximum size of the swap line is 350 billion yuan and €45 billion.

During the year the ECB continued with operations to absorb the liquidity injected through the Securities Markets Programme (SMP), thereby neutralising the SMP's impact on the monetary stance. The SMP programme for purchasing sovereign bonds of selected countries had run from 2010 until September 2012, when it was terminated concurrently with the announcement of the new programme of Outright Monetary Transactions (OMT). In essence, the OMT programme is a means of purchasing unlimited amounts of one-year to three-year government bonds issued by countries participating in an appropriate EFSF/ESM programme, with the ECB fully sterilising the OMTs (just as it absorbed liquidity injected by the SMP). A precondition for initiating OMT is that a euro area country applies for a loan from the EFSF. As at the end of 2013, no country had requested such assistance and therefore no OMTs had been activated. Nevertheless, the announcement of the programme has in itself helped significantly to reduce risk premia in periphery bond markets.

2.2 FOREIGN EXCHANGE OPERATIONS

The exchange rate of the euro against the US dollar was volatile during 2013. It reflected market expectations for euro area monetary policy, volatility in foreign exchange markets, and anticipation of the US Federal Reserve System's

Chart 9 USD/EUR exchange rate in 2013



Source: Bloomberg.

monetary policy decisions. The euro was positively affected by preparations for a euro area banking union, which the market sees as a stabilising move. In the second half of the year the exchange rate responded to capital flight from certain emerging economies, as well as to positive activity figures for the euro area. In 2013 the euro traded lowest against the dollar at the end of the first quarter, at 1.2772 USD/EUR, and strongest at the end of October, during the height of the US budget difficulties, when it reached a two-year high of 1.3805 USD/EUR. The euro's trading against the dollar was 4.5% stronger at the end of 2013 than at the end of 2012.

3 FINANCIAL MARKET DEVELOPMENTS⁴

Financial sector developments in Slovakia in 2013 reflected to some extent improvements in the external environment, stemming mainly from the euro area's emergence from recession. In Slovakia, too, economic growth accelerated moderately. This upturn was accompanied by partial stabilisation of the euro area debt crisis, which was largely the result of large-scale liquidity-supporting operations conducted by central

banks. As recent developments have indicated, however, the unwinding of support measures may pose an appreciable risk to the global financial system, particularly given the potential increase in risk premia. Despite the substantial efforts already made, the situation in Europe requires additional, relatively extensive, structural reforms and consolidation measures. In both Slovakia and the euro area as a whole, the labour

⁴ Preliminary data as at 31 December 2013.