

MONETARY BULLETIN 2010

10

Improving competitiveness and renewed demand on external markets alongside with a gradual rise in domestic demand resulted in growth of GDP in the third quarter. According to the flash estimate of the Central Statistical Bureau of Latvia, the gross domestic product expanded quarter-on-quarter as well as year-on-year (by 2.7%, representing positive annual growth for the first time since the first quarter of 2008). The annual rise was primarily determined by the rapidly expanding industrial output (19.7% in manufacturing in September) driven by external demand as well as by the renewal of annual growth also in trade, with the annual increase of retail trade turnover amounting to 6.1% (to 12.5% sales of motor vehicles inclusive) in September. Latvia's foreign trade continued to expand in September, with both exports as well as imports of goods growing (by 30.7% and 30.3% year-on-year respectively) and foreign trade balance improving slightly.

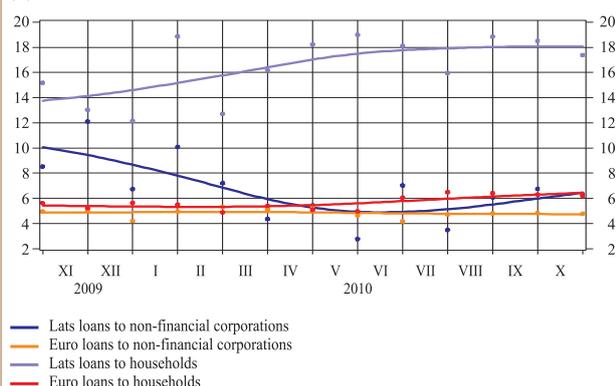
October was the seventh consecutive month witnessing a decline in registered unemployment, to stand at 14.3% of the economically active population at the end of the month. Performance in freight transportation continued to improve. With the domestic and export flows as well as freight transit by road picking up, the overall freight turnover at Latvian ports increased by 1.3% year-on-year, whereas the volume of freight transportation by rail expanded by 2.1%.

Consumer prices climbed by 0.4% in October mainly on account of rising prices on dairy products and cereal products pushed up by the increasing global food prices as well as under the impact of seasonally higher prices on clothing and footwear. Overall, the prices of goods grew by 0.6%, whereas the average price level of services declined by 0.3%. In October, the 12-month average harmonised index of consumer prices (HICP) used for the Maastricht criterion decreased by 1.8%, whereas the annual price rise stood at 1.0%.

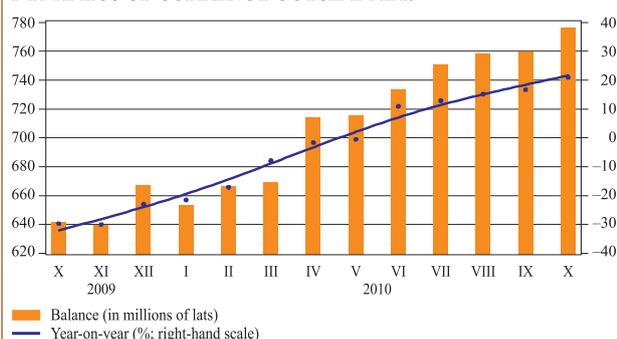
The consolidated general government budget ran a 55.9 million lats deficit in October. Consequently, the deficit accumulated from the beginning of the year reached 349.7 million lats in comparison with 514.5 million lats recorded in the corresponding period of the previous year. The central government basic budget, central government social security budget and the consolidated local government budget all recorded deficits. The consolidated general government budget revenue shrank by 14.6% year-on-year as a result of smaller foreign financial assistance inflows and central government budget transfers, although the growth of tax revenue at the same time accelerated to 8.5% on account of higher revenue from the value added tax and personal income tax (growth of 37.6% and 18.4% respectively). Budget expenditure contracted by 6.1% year-on-year in October due to subsidies and grants posting a 32.8% decline. The general government debt increased to 5 002.5 million lats in October as a result of receiving 200 million euro from the European Commission within the framework of the international assistance programme. An issue of five-year Treasury bonds in the amount of 30 million lats also had an upward effect on the central government debt.

October data on money supply point to continued stability of the Latvian financial system. Although M3 decreased by 1.9%

WEIGHTED AVERAGE INTEREST RATES ON NEW LOANS TO RESIDENT NON-FINANCIAL CORPORATIONS AND HOUSEHOLDS (%)



DYNAMICS OF CURRENCY OUTSIDE MFIs



month-on-month in October, the annual growth of M3 at 11.0% was significant. Against the background of the pick-up in industry, exports and retail trade reported in 2010, deposits by non-financial corporations continued to expand in October, whereas household deposits shrank moderately reflecting higher consumption. The most liquid segments of money supply posted a rise, with the overnight deposits received by banks growing by 1.1% and currency outside MFIs by 2.2%; consequently, M1 also continued to expand by 20.7% which is the steepest climb since July 2007. Nevertheless, the aggregate money supply was affected by a 3.1% decline in deposits of resident financial institutions, non-financial corporations and households, with financial intermediary deposits with an agreed maturity shrinking reflecting a one-off effect (restructuring of funding within a financial group).

The amount of new loans was smaller than that of matured and written-off loans; therefore, the outstanding loans of resident financial institutions, non-financial corporations and households shrank by 1.1%, with loans granted to non-financial corporations and those to households decreasing to a similar extent and the annual rate of decline of loans standing at 8.2% in October.

External financing of the banking sector increased by 265.4 million lats in October, with liabilities to foreign parent banks expanding by 188.0 million lats and non-resident non-MFI deposits by 144.5 million lats. The increase in the banks' foreign assets was smaller (140.6 million lats), thus the negative net foreign assets of MFIs (except the Bank of Latvia) improved slightly.

The monetary base M0 shrank by 88.6 million lats in October. The central bank's money supply was compressed by banks increasingly resorting to the deposit facility with the Bank of Latvia in the context of ample liquidity (monthly growth of 95.6 million lats), at the same time demand deposits by banks contracted. Consequently, the annual growth of the monetary base M0 decelerated to 5.6%. An increase in the government deposit in lats with the Bank of Latvia also had a downward effect on the money supply of the central bank.

The Bank of Latvia's net foreign assets grew by 2.0% in October totalling 4.2 billion lats. At the end of the month, the backing of the national currency with the Bank of Latvia's net foreign assets was 251.1%. Net reserves expanded mainly on account of the growing government deposit in foreign currency with the Bank of Latvia following the receipt of the current loan instalment from the European Commission on 20 October. At the same time, minor euro selling interventions had a compressing effect on the Bank of Latvia's foreign reserves.

Interest rates remained low on the interbank market. The weighted average rate on overnight loans was 0.54% in October (0.50% in September), whereas the average RIGIBOR on overnight loans was 0.67% during the month, unchanged from September. 3-month, 6-month and 12-month RIGIBOR continued to decrease by 2, 30 and 46 basis points, to 1.22%, 1.58% and 2.42% respectively.

Interest rates on most loans granted to non-financial corporations and households, including those on loans for house purchase, declined in October, with minor growth reported only for the rates on foreign currency loans granted to non-financial corporations. The lats deposit rates also posted a decline.

The depreciation of the US dollar on the global market supported a fall in the US dollar/lats exchange rate set by the Bank of Latvia by 1.5% in October. The British pound sterling depreciated against the lats by 1.8%, whereas the Japanese yen appreciated by 0.8%.

| MACROECONOMIC INDICATORS | 2010 | |
|--|---------|---------|
| | IX | X |
| Volume index of industrial output (working-day adjusted annual rate of change; %) | 19.0 | * |
| Changes in the CPI | | |
| Month-on-month basis (%) | 0.4 | 0.4 |
| Average annual inflation rate (HCPI) of last 12 months (%) | -1.8 | -1.6 |
| Year-on-year basis (%) | 0.4 | 1.0 |
| Annual rate of core inflation ¹ (%) | -2.5 | -1.5 |
| Number of registered unemployed persons (at end of period) | 165 386 | 162 497 |
| Unemployment rate (%) | 14.6 | 14.3 |
| General government consolidated budget financial deficit/surplus (in millions of lats) | -293.8 | -349.7 |
| Foreign trade (in millions of lats) | | |
| Exports | 460.7 | * |
| Imports | 547.6 | * |
| Balance | -86.9 | * |

¹ Source: Bank of Latvia.

* Figure available at a later date.

Source: Central Statistical Bureau of Latvia and Ministry of Finance.

| MONETARY INDICATORS (at end of period; in millions of lats) | 2010 | |
|--|----------|----------|
| | IX | X |
| MFI ¹ | | |
| M3 | 6 332.9 | 6 212.5 |
| Repurchase agreements | 0 | 0 |
| Money market fund shares and units | 94.6 | 92.3 |
| Debt securities issued with maturity of up to 2 years | 20.6 | 20.6 |
| M2 | 6 217.7 | 6 099.6 |
| Deposits with agreed maturity of up to 2 years | 2 573.7 | 2 405.4 |
| Deposits redeemable at notice of up to 3 months | 235.1 | 239.6 |
| M1 | 3 408.9 | 3 454.5 |
| Currency outside MFIs | 760.1 | 776.6 |
| Overnight deposits | 2 648.8 | 2 677.9 |
| Net external assets | -1 320.1 | -1 360.5 |
| Credit to resident financial institutions, non-financial corporations and households | 12 808.1 | 12 669.6 |
| Credit to general government | 503.1 | 518.8 |
| Deposits of central government | 2 050.6 | 2 121.9 |
| Longer-term financial liabilities | 2 322.5 | 2 299.9 |
| Bank of Latvia | | |
| M0 | 1 771.2 | 1 682.6 |
| Currency in circulation | 866.8 | 885.5 |
| Deposits with the Bank of Latvia in lats | 887.8 | 777.4 |
| Deposits with the Bank of Latvia in foreign currencies | 16.6 | 19.7 |
| Net foreign assets | 4 139.8 | 4 224.2 |
| Net domestic assets | -2 368.6 | -2 541.6 |
| Credit | -1 327.7 | -1 399.7 |
| To MFIs | 0 | 0 |
| To central government (net) | -1 327.7 | -1 399.7 |
| Other items (net) | -1 041.0 | -1 141.9 |
| International reserves (at end of period; in millions of euro) | 5 853.22 | 6 080.20 |
| Gold | 240.06 | 238.62 |
| Special Drawing Rights | 138.10 | 145.69 |
| Reserve position in the IMF | 0.06 | 0.06 |
| Foreign convertible currencies | 5 475.00 | 5 695.83 |
| International reserves (at end of period; in millions of US dollars) | 7 956.81 | 8 395.26 |
| Gold | 326.34 | 329.46 |
| Special Drawing Rights | 187.73 | 201.17 |
| Reserve position in the IMF | 0.09 | 0.09 |
| Foreign convertible currencies | 7 442.65 | 7 864.54 |

¹ In accordance with the methodology of the European Central Bank.

| EXCHANGE RATES SET BY THE BANK OF LATVIA AND INTEREST RATES | 2010 | |
|---|--------|--------|
| | IX | X |
| Weighted average interest rate on domestic interbank loans in lats | 0.5 | 0.5 |
| Interest rates on loans to resident non-financial corporations and households | | |
| Loans to non-financial corporations (in lats) | 6.8 | 6.3 |
| Loans to households (in lats) | 18.5 | 17.4 |
| incl. for house purchase | 10.1 | 7.2 |
| Loans to non-financial corporations (in foreign currencies) | 4.6 | 4.8 |
| Loans to households (in foreign currencies) | 5.4 | 4.9 |
| incl. for house purchase | 3.8 | 3.7 |
| Interest rates on deposits of non-financial corporations and households | | |
| Time deposits of non-financial corporations (in lats) | 0.8 | 0.6 |
| Demand deposits of non-financial corporations (in lats) | 0.2 | 0.3 |
| Time deposits of households (in lats) | 2.4 | 2.0 |
| Demand deposits of households (in lats) | 0.8 | 0.6 |
| Time deposits of non-financial corporations (in foreign currencies) | 0.7 | 0.8 |
| Demand deposits of non-financial corporations (in foreign currencies) | 0.3 | 0.3 |
| Time deposits of households (in foreign currencies) | 1.8 | 1.7 |
| Demand deposits of households (in foreign currencies) | 0.5 | 0.5 |
| The Bank of Latvia's refinancing rate (at end of period; %) | 3.5 | 3.5 |
| Exchange rates of foreign currencies (at end of period) | | |
| LVL/USD | 0.5170 | 0.5090 |
| LVL/GBP | 0.8190 | 0.8040 |
| LVL/100 JPY | 0.6180 | 0.6230 |
| LVL/EUR | 0.7028 | 0.7028 |

| AGGREGATED BALANCE SHEET OF MFIs (EXCLUDING THE BANK OF LATVIA) (at end of period; in millions of lats) | 2010 | |
|---|--------------|--------------|
| | IX | X |
| MFI reserves | 1 740.1 | 1 730.2 |
| Vault cash in national currency | 106.7 | 108.9 |
| Deposits with the Bank of Latvia | 1 633.4 | 1 621.3 |
| Foreign assets | 4 579.5 | 4 720.1 |
| Vault cash in foreign currencies | 64.1 | 68.9 |
| Claims on MFIs | 2 464.5 | 2 603.9 |
| Claims on non-MFIs | 1 941.0 | 1 904.2 |
| Other assets | 109.9 | 143.2 |
| Claims on central government | 441.0 | 456.0 |
| Claims on local government | 62.1 | 62.9 |
| Claims on public non-financial corporations | 418.6 | 425.9 |
| Claims on financial institutions and private non-financial corporations | 6 746.1 | 6 665.0 |
| Claims on households | 5 854.9 | 5 798.2 |
| Unclassified assets | 870.4 | 918.5 |
| Fixed assets | 90.2 | 120.5 |
| Items in transit | 13.2 | 16.5 |
| Other assets | 502.5 | 497.7 |
| Claims on resident MFIs (incl. investments) | 264.5 | 283.8 |
| Total assets | 20 712.6 | 20 776.8 |
| <i>Memo item: Trust assets</i> | <i>439.1</i> | <i>446.9</i> |
| Overnight deposits in lats | 1 439.8 | 1 462.9 |
| Public non-financial corporations | 67.8 | 83.8 |
| Financial institutions and private non-financial corporations | 689.5 | 687.1 |
| Households | 682.5 | 692.0 |
| Time deposits and deposits redeemable at notice in lats | 1 241.4 | 1 182.3 |
| Public non-financial corporations | 245.5 | 215.2 |
| Financial institutions and private non-financial corporations | 459.3 | 461.3 |
| Households | 536.6 | 505.8 |
| Foreign currency deposits of residents | 2 749.1 | 2 617.2 |
| Public non-financial corporations | 55.8 | 61.1 |
| Financial institutions and private non-financial corporations | 1 020.5 | 888.0 |
| Households | 1 672.7 | 1 668.2 |
| Deposits of central government | 723.0 | 722.2 |
| Deposits of local government | 200.6 | 204.6 |
| Foreign liabilities | 10 039.4 | 10 304.8 |
| Liabilities to MFIs | 6 372.8 | 6 494.6 |
| Liabilities to non-MFIs | 3 527.6 | 3 672.1 |
| Other liabilities (incl. subordinated liabilities) | 138.9 | 138.0 |
| Liabilities to the Bank of Latvia | 0 | 0 |
| Debt securities issued | 196.2 | 193.8 |
| Money market fund shares and units | 94.9 | 92.7 |
| Capital and reserves | 1 634.9 | 1 638.6 |
| Residents | 357.0 | 354.0 |
| Non-residents | 1 277.9 | 1 284.5 |
| Provisions | 1 807.4 | 1 788.8 |
| Unclassified liabilities | 586.0 | 569.0 |
| Items in transit | 120.5 | 96.3 |
| Other liabilities (incl. subordinated liabilities) | 226.0 | 210.9 |
| Liabilities to resident MFIs | 239.5 | 261.7 |
| Total liabilities | 20 712.6 | 20 776.8 |
| <i>Memo item: Trust liabilities</i> | <i>439.1</i> | <i>446.9</i> |

The IMF's Dissemination Standards Bulletin Board (<http://dsbb.imf.org>) disseminates the release dates for monetary indicators of the Latvian banking system, monetary indicators of the Bank of Latvia and international reserves. The data are first made available on the Bank of Latvia's website (<http://www.bank.lv>).