

# MONETARY BULLETIN 2008

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In January, the slowdown of economic growth became more pronounced. A more subdued GDP growth in the fourth quarter of 2007 (9.6% according to preliminary data), development of retail trade and real estate market, a further moderation of the increase in lending suggested a deceleration of domestic demand and moving towards more sustainable levels in the long run.

Yet, driven by the supply side factors, inflation continued to move upward. With a 2.8% consumer price increase in January, the year-on-year inflation reached 15.8%, while the average annual inflation was 10.8%. In January, consumer prices were mostly affected by the increase of excise tax on tobacco, leading to a price surge of 38.1% month-on-month, and by an escalation of fuel prices (by 5.0%). Food product prices, especially those of milk and dairy products, continued to rise. A number of administered prices went up (public transportation fares, several public utility service prices, natural gas tariffs for retail clients). At the same time, the decrease of clothing and footwear prices had a dampening effect on inflation.

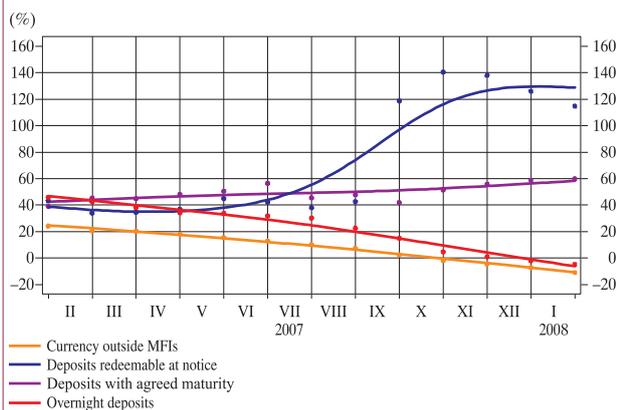
In December of 2007, retail trade turnover (including sales of motor vehicles and automotive fuel retailing) dropped 3.4% year-on-year. In December, the output in manufacturing reported an annual decline of 7.5%. The seasonally adjusted volume index of industrial output went down 5.4%. In January, the volume of rail freight increased by 36.1%, while freight turnover at Latvian ports grew by 26.5%. Unemployment rate rose somewhat (to 5.0%).

In January, the financial surplus of the general government consolidated budget was 92.1 million lats (a 61.8 million lats year-on-year decline). A financial surplus was reported both by the central government consolidated budget (63.9 million lats) and the local government consolidated budget (27.0 million lats). However, the general government consolidated budget revenue grew by a mere 4.1% year-on-year in January. The notable slowdown in revenue growth was on account of a reduction in foreign financial aid (by 66.4%; in January 2007, there was a substantial increase in EU funding). The tax revenue growth rate dropped to 14.0%, while the non-tax revenue diminished by 7.2%. The general government consolidated budget expenditure demonstrated a more accelerated growth (29.3%). With the central government domestic debt lowering, the general government total debt shrank by 13.3 million lats in January, to stand at 1 145.3 million lats at the end of the month.

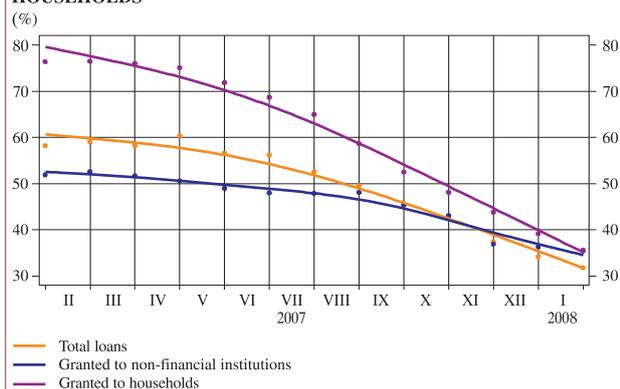
In January, the annual growth of monetary aggregates continued on its downward path, with money supply exhibiting a seasonal decline as well. Broad money M3 shrank by 41.1 million lats, with its annual rate of increase declining by 1.3 percentage points (to 13.3%). Intermediate monetary aggregate M2 declined by 49.1 million lats (a 13.1% year-on-year growth). Narrow monetary aggregate M1 declined by 165.5 million lats (6.2% down year-on-year).

The changes in domestic deposits were relatively small. In January, deposits of financial institutions, non-financial corporations and households diminished by 22.5 million lats, with its annual growth rate losing 0.9 percentage point, down to 16.0%.

ANNUAL CHANGES IN CURRENCY IN CIRCULATION AND DEPOSITS (%)



**ANNUAL CHANGES IN LOANS TO RESIDENT FINANCIAL INSTITUTIONS, NON-FINANCIAL CORPORATIONS AND HOUSEHOLDS**



MACROECONOMIC INDICATORS	2007	2008
	XII	I
Changes in the seasonally adjusted volume index of industrial output (year-on-year basis; %)	-5.4	*
Changes in the CPI		
Month-on-month basis (%)	0.7	2.8
Average annual inflation rate (HCPI) of last 12 months (%)	10.1	10.8
Year-on-year basis (%)	14.1	15.8
Annual rate of core inflation <sup>1</sup> (%)	13.0	15.2
Number of registered unemployed persons (at end of period)	52 321	53 325
Unemployment rate (%)	4.9	5.0
General government consolidated budget financial deficit/surplus (in millions of lats)	94.0	92.1
Foreign trade (in millions of lats)		
Exports	328.0	*
Imports	593.0	*
Balance	-265.0	*

<sup>1</sup> Source: Bank of Latvia.

\* Figure available at a later date.

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

Deposits in foreign currency increased by 33.4 million lats, whereas those in lats fell by 55.9 million lats. Household deposits contracted by 2.1 million lats (an 11.9% annual increase), while those of financial institutions and non-financial corporations decreased by 20.4 million lats (a 22.6% annual increase).

Lending continued to moderate. In January, domestic credit grew by 118.8 million lats only (the tiniest month-on-month growth recorded since December 2004). The annual growth rate of domestic credit declined by 2.4 percentage points (to 31.8%; the lowest growth rate since September 2000). Lending to non-financial corporations demonstrated a notable pickup of 100.8 million lats. The increase in loans to households amounted to 51.8 million lats. The annual growth of all major loans slowed down, with loans for house purchase demonstrating the steepest drop (to 39.8%), while industrial credit and loans for purchasing consumer goods were the ones with the smallest decline (to 38.5% and 41.1% respectively). Loans granted in lats continued to decrease (by 76.1 million lats in January) and accounted for only 13.0% to loans outstanding, with loans in euro contributing 84.1%.

Funding from foreign banks continued to grow modestly (by 96.2 million lats, including 109.2 million lats from parent banks). A decline in deposits by non-resident non-MFIs, determined a fall of funds placed with foreign credit institutions. The negative net foreign assets of MFIs grew by 157.5 million lats.

In January, the demand for cash decreased due to seasonal factors, albeit at a quicker pace than accustomed. At the end of January, currency in circulation shrank by 90.6 million lats over the end of December, posting a 8.5% year-on-year decline. Although the banks' overnight deposits with the Bank of Latvia grew with the increase in minimum reserve requirements, the monetary base M0 decreased by 39.0 million lats. The central bank's money supply expanded on account of the intensifying lending to banks and the increase in currency swaps (18.1 million lats and 20.0 million lats respectively), and declined on account of an increase in the Government deposits with the Bank of Latvia. The Bank of Latvia's net foreign assets grew by 31.0 million lats or 1.1%. At the end of January, the backing of the national currency with the Bank of Latvia's net foreign assets was 115.4%.

RIGIBOR on longer-term loans continued to go down. At the end of January, RIGIBOR on 3-month loans stood at 8.08%, posting a 245 basis point decline month-on-month. RIGIBOR on 6-month loans shrank by 187 basis points (to 9.37%). Following the steep drop to 2.72% during the last days of the minimum reserve maintenance period, RIGIBOR on overnight loans once again stepped over 7% at the end of the month. The average rate of RIGIBOR (4.44%) was 80 basis points lower than in December.

In January, the weighted average interest rate on loans in lats extended to non-financial corporations and to households for house purchase decreased by 1.8 and 1.5 percentage points respectively. The weighted average interest rate on loans in foreign currency extended to non-financial corporations and to households for house purchase posted a minor decline (0.6 and 0.1 percentage point respectively).

According to the Bank of Latvia exchange rate, both the US dollar and the British pound sterling depreciated against the lats by 1.7% in January, whereas the Japanese yen appreciated by 5.2%.

<b>MONETARY INDICATORS</b> (at end of period; in millions of lats)	2007	2008
	XII	I
<b>MFIs<sup>1</sup></b>		
<b>M3</b>	6 311.6	6 270.5
Repurchase agreements	0	0
Money market fund shares and units	41.3	48.4
Debt securities issued with maturity of up to 2 years	28.2	29.2
<b>M2</b>	6 242.0	6 192.9
Deposits with agreed maturity of up to 2 years	1 971.9	2 086.3
Deposits redeemable at notice of up to 3 months	335.0	336.9
<b>M1</b>	3 935.2	3 769.7
Currency outside MFIs	900.0	850.2
Overnight deposits	3 035.2	2 919.5
Net external assets	-4 482.8	-4 640.3
Credit to resident financial institutions, non-financial corporations and households	13 050.6	13 169.4
Credit to general government	313.6	309.6
Deposits of central government	189.3	259.7
Longer-term financial liabilities	2 346.9	2 403.7
<b>Bank of Latvia</b>		
<b>M0</b>	2 471.2	2 432.2
Currency in circulation	1 049.5	958.9
Deposits with the Bank of Latvia in lats	1 412.4	1 466.0
Deposits with the Bank of Latvia in foreign currencies	9.3	7.3
Net foreign assets	2 776.0	2 807.0
Net domestic assets	-304.9	-374.8
Credit	-164.4	-203.6
To MFIs	6.9	25.0
To central government (net)	-171.2	-228.6
Other items (net)	-140.5	-171.2
International reserves (at end of period; in millions of euro)	3 965.49	3 997.73
Gold	141.05	155.18
Special Drawing Rights	0.12	0.12
Reserve position in the IMF	0.06	0.06
Foreign convertible currencies	3 824.26	3 842.37
International reserves (at end of period; in millions of US dollars)	5 758.18	5 902.55
Gold	204.81	229.12
Special Drawing Rights	0.17	0.17
Reserve position in the IMF	0.09	0.09
Foreign convertible currencies	5 553.11	5 673.17

<sup>1</sup> In accordance with the methodology of the European Central Bank.

<b>EXCHANGE RATES SET BY THE BANK OF LATVIA AND INTEREST RATES</b>	2007	2008
	XII	I
Weighted average interest rate on domestic interbank loans in lats	5.1	4.0
Interest rates on loans to resident non-financial corporations and households		
Loans to non-financial corporations (in lats)	9.7	7.9
Loans to households (in lats)	17.3	18.3
incl. for house purchase	12.0	10.5
Loans to non-financial corporations (in foreign currencies)	7.2	6.6
Loans to households (in foreign currencies)	6.8	6.5
incl. for house purchase	6.4	6.3
Interest rates on deposits of non-financial corporations and households		
Time deposits of non-financial corporations (in lats)	7.3	7.2
Demand deposits of non-financial corporations (in lats)	2.0	2.4
Time deposits of households (in lats)	8.7	8.4
Demand deposits of households (in lats)	0.6	0.6
Time deposits of non-financial corporations (in foreign currencies)	4.1	3.9
Demand deposits of non-financial corporations (in foreign currencies)	1.6	1.6
Time deposits of households (in foreign currencies)	4.4	4.4
Demand deposits of households (in foreign currencies)	1.7	1.7
The Bank of Latvia's refinancing rate (at end of period; %)	6.0	6.0
Exchange rates of foreign currencies (at end of period)		
LVL/USD	0.4840	0.4760
LVL/GBP	0.9630	0.9470
LVL/100 JPY	0.4240	0.4460
LVL/EUR	0.7028	0.7028

AGGREGATED BALANCE SHEET OF MFIs (EXCLUDING THE BANK OF LATVIA) (at end of period; in millions of lats)	2007	2008
	XII	I
MFI reserves	1 566.3	1 568.0
Vault cash in national currency	149.5	108.7
Deposits with the Bank of Latvia	1 416.8	1 459.3
Foreign assets	5 474.8	5 041.8
Vault cash in foreign currencies	72.5	62.0
Claims on MFIs	3 578.1	3 178.3
Claims on non-MFIs	1 756.9	1 727.7
Other assets	67.3	73.9
Claims on central government	253.4	249.0
Claims on local government	60.3	60.6
Claims on public non-financial corporations	250.0	252.8
Claims on financial institutions and private non-financial corporations	6 866.8	6 936.9
Claims on households	5 988.8	6 040.6
Unclassified assets	1 041.5	983.3
Fixed assets	174.8	178.1
Items in transit	23.6	29.4
Other assets	190.0	175.8
Claims on resident MFIs (incl. investments)	653.2	600.1
<b>Total assets</b>	<b>21 501.9</b>	<b>21 133.0</b>
<i>Memo item: Trust assets</i>	369.6	283.6
Overnight deposits in lats	1 652.0	1 554.4
Public non-financial corporations	117.1	95.8
Financial institutions and private non-financial corporations	748.1	708.9
Households	786.8	749.7
Time deposits and deposits redeemable at notice in lats	1 078.0	1 119.8
Public non-financial corporations	176.2	185.9
Financial institutions and private non-financial corporations	299.5	311.7
Households	602.3	622.2
Foreign currency deposits of residents	2 541.2	2 574.6
Public non-financial corporations	42.4	40.7
Financial institutions and private non-financial corporations	779.2	799.2
Households	1 719.6	1 734.7
Deposits of central government	18.1	31.1
Deposits of local government	211.7	222.4
Transit funds	4.0	4.0
Foreign liabilities	12 733.6	12 489.1
Liabilities to MFIs	7 905.2	8 001.4
Liabilities to non-MFIs	4 513.0	4 163.2
Other liabilities (incl. subordinated liabilities)	315.4	324.5
Liabilities to the Bank of Latvia	6.9	25.0
Debt securities issued	314.7	317.8
Money market fund shares and units	41.3	48.4
Capital and reserves	1 744.1	1 772.3
Residents	998.9	1 027.1
Non-residents	745.2	745.2
Provisions	116.4	120.1
Unclassified liabilities	1 039.9	854.1
Items in transit	270.1	142.7
Other liabilities (incl. subordinated liabilities)	185.1	180.3
Liabilities to resident MFIs	584.7	531.1
<b>Total liabilities</b>	<b>21 501.9</b>	<b>21 133.0</b>
<i>Memo item: Trust liabilities</i>	369.6	283.6

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>).