

# MONETARY BULLETIN 2009

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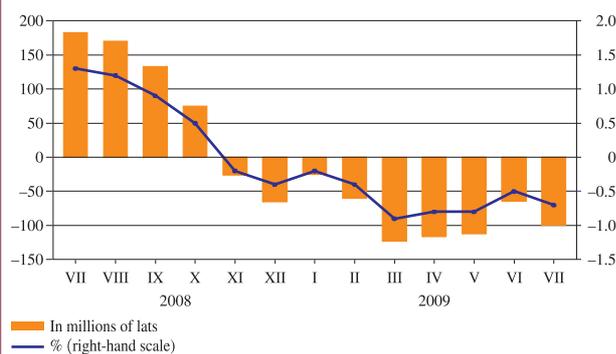
Almost all macroeconomic indicators continued to follow a downward trend. According to a flash estimate of the Central Statistical Bureau of the Republic of Latvia, GDP decreased by 19.6% year-on-year in the second quarter; moreover, a slowdown in economic activity persisted in all sectors of the economy. Weak external and domestic demand had a negative impact on both the goods and services sectors. Retail trade turnover recorded a sharper year-on-year decline than in the first quarter – it shrank by 5.1% in June in comparison with May, posting a 25.4% annual decrease. The construction and real estate sectors weakened rapidly, the financial sector indicators deteriorated and the amount of collected taxes decreased. Nevertheless, signs indicating that the slowdown in economic activity had reached a low and started to abate were also observed. Manufacturing recorded a slight improvement – the real output grew during the quarter, recording a less pronounced year-on-year decline than before (in June, manufacturing output grew by 0.9% month-on-month, thus posting a 20.6% decrease over the year). In the second quarter, some freight transportation services also improved; in July, however, the year-on-year freight turnover contracted again (freight transportation by rail shrank by 5.1%, whereas freight turnover at Latvian ports dropped 5.5%). With the fall in imports of goods notably exceeding that in exports, foreign trade deficit continued on a downward trend; according to preliminary data and taking into account also the income account developments, the current account surplus of the balance of payments was 481.8 million lats in the second quarter. In July, unemployment rate continued to move up, rising to 11.8%, the general government consolidated budget deficit expanded slightly, lending posted a further decline, and money supply decreased.

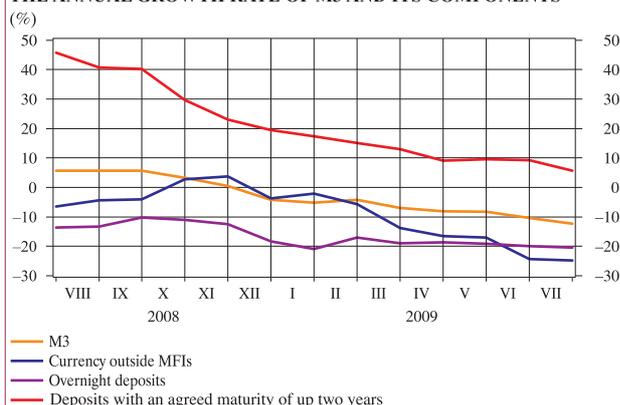
In July, consumer prices dropped 0.6%, while the annual inflation of consumer prices abated by 0.9 percentage point, to 2.5%. A weak demand (it pushed down food prices and prices of clothing and footwear) and a decrease in administered prices underpinned the monthly downslide of prices. On the backdrop of still declining natural gas trading prices, heating tariffs recorded a reduction of 2.4% and natural gas tariffs for households fell by 23.8%. The rise in alcoholic beverage prices, stemming from a higher excise tax rate, had the most pronounced upward effect (6.0% on average). The annual core consumer price inflation declined to 1.8% and accounted for 1.4 percentage points of total inflation.

When Latvia received the second instalment of the EC loan in the amount of 1.2 billion euro, financial market tensions eased substantially. The market was stabilised and the lats liquidity increased by the Bank of Latvia's interventions by selling lats, resulting in a drop in interest rates on the money market that contributed to shrinking interest rates also on transactions with the non-bank sector.

In July, the general government consolidated budget ran a deficit of 3.8 million lats (428.9 million lats deficit accumulated from the beginning of the year). The central government basic budget and the local government consolidated budget recorded deficits, while the social security budget was in surplus. The overall decrease in revenue amounted to 26.1% year-on-year, with tax revenue shrinking by 25.5%. Revenues from the corporate income tax, personal income tax and value added tax contracted most (by 84.3%, 34.1% and 22.9% respectively).

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



**THE ANNUAL GROWTH RATE OF M3 AND ITS COMPONENTS**


MACROECONOMIC INDICATORS	2009	
	VI	VII
Volume index of industrial output (working-day adjusted annual rate of change; %)	-18.5	*
Changes in the CPI		
Month-on-month basis (%)	-0.5	-0.6
Average annual inflation rate (HCPI) of last 12 months (%)	10.2	9.1
Year-on-year basis (%)	3.4	2.5
Annual rate of core inflation <sup>1</sup> (%)	2.0	1.8
Number of registered unemployed persons (at end of period)	129 269	132 519
Unemployment rate (%)	11.5	11.8
General government consolidated budget financial deficit/surplus (in millions of lats)	-425.2	-428.9
Foreign trade (in millions of lats)		
Exports	285.3	*
Imports	352.5	*
Balance	-67.2	*

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

\* Figure available at a later date.

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

With the decreasing compensation to employees, purchases of goods and services, subsidies and grants, as well as capital expenditure, the budget expenditure fell sharply year-on-year in July (by 34.4%). The government received the second instalment of the EC loan and issued Treasury bills and the total debt of the general government expanded by 926.8 million lats in July, to 3 990.0 million lats.

In July, loans to resident financial institutions, non-financial corporations and households continued to shrink (by 99.6 million lats), with the annual rate of change in lending amounting to -2.2%. Loans to households contracted slightly (by 24.1 million lats or 0.4%), while loans to non-financial corporations and financial institutions recorded a more pronounced decline (46.6 million lats or 0.7% and 28.8 million lats or 4.3% respectively). The annual rate of change in loans to non-financial corporations remained positive (2.2%) but that of loans to households shrank to -1.6%. In July, commercial credit, consumer credit, industrial credit and loans for house purchase decreased by 1.7%, 0.8%, 0.6% and 0.3% respectively.

The persisting downside of economic activity accounted for the weakening of the money demand. In July, M1, M2 and M3 decreased by 40.5 million lats, 113.3 million lats and 111.5 million lats respectively, thus also posting higher annual rates of decrease (-21.5%, -11.6% and -12.3% respectively). During the summer holiday season, the demand for cash stabilised whereas the drop in deposits in all maturity groups was more pronounced than before. Overnight deposits, deposits with an agreed maturity of up to two years and deposits redeemable at notice decreased (by 1.9%, 2.6% and 2.7% respectively). In previous months, only deposits in lats contracted, while in July deposits in euro also declined. The annual rate of change in deposits of resident financial institutions, non-financial corporations and households was -7.7%.

In July, Latvian bank liabilities to foreign banks shrank by 204.2 million lats or 2.5% (in a similar amount as in June) on account of decreasing liabilities to affiliated banks and repaid syndicated loans. Non-resident non-bank deposits posted a slight drop (26.2 million lats or 0.9%). The negative net foreign assets of MFIs (excluding the Bank of Latvia) diminished by 64.3 million lats.

The negative annual rate of change in monetary base M0 amounted to 35.5%, with minimum reserves falling, bank demand deposits with the Bank of Latvia shrank and loans of the central bank were used by banks to a lesser extent. Net foreign assets of the Bank of Latvia grew by 906.6 million lats or 46.1% in July as a result of the purchase of foreign currencies and the second instalment of the EC loan received by the government. The backing of the national currency with net foreign assets of the Bank of Latvia expanded from 124.1% at the end of June to 183.4% at the end of July.

Higher lats liquidity in July supported a decrease in RIGIBOR. RIGIBOR on overnight loans was 6.9% at the beginning of the month, dropping to 1.9% in the middle of the month and averaging 4.08% in July. At the same time, 3-, 6-, and 12-month RIGIBOR decreased by 5–8 percentage points (to 16%–19%). The stabilising conditions in the lats money market also underpinned a sharp drop in interest rates on loans in lats to non-financial corporations and households, and on deposits, while interest rates on transactions in foreign currencies remained broadly unchanged.

In July, the exchange rates of the US dollar and the British pound sterling set by the Bank of Latvia against the lats depreciated by 0.2% and 0.7% respectively, while that of Japanese yen remained unchanged.

MONETARY INDICATORS (at end of period; in millions of lats)	2009	
	VI	VII
<b>MFIs<sup>1</sup></b>		
M3	5 829.2	5 717.7
Repurchase agreements	0	0
Money market fund shares and units	59.0	60.7
Debt securities issued with maturity of up to 2 years	1.7	1.7
M2	5 768.6	5 655.3
Deposits with agreed maturity of up to 2 years	2 490.0	2 424.8
Deposits redeemable at notice of up to 3 months	285.1	277.5
M1	2 993.5	2 953.0
Currency outside MFIs	661.0	664.9
Overnight deposits	2 332.4	2 288.1
Net external assets	-4 946.9	-3 976.0
Credit to resident financial institutions, non-financial corporations and households	14 076.1	13 976.5
Credit to general government	626.8	710.7
Deposits of central government	1 059.1	1 973.2
Longer-term financial liabilities	2 174.1 <sup>2</sup>	2 274.0
<b>Bank of Latvia</b>		
M0	1 584.8	1 566.8
Currency in circulation	758.5	767.1
Deposits with the Bank of Latvia in lats	808.5	792.0
Deposits with the Bank of Latvia in foreign currencies	17.7	7.7
Net foreign assets	1 967.3	2 873.9
Net domestic assets	-382.5	-1 307.1
Credit	-138.2	-1 053.3
To MFIs	258.9	255.0
To central government (net)	-397.0	-1 308.3
Other items (net)	-244.3	-253.7
International reserves (at end of period; in millions of euro)	2 810.83	4 093.17
Gold	166.15	164.56
Special Drawing Rights	0.46	0.46
Reserve position in the IMF	0.06	0.06
Foreign convertible currencies	2 644.16	3 928.09
International reserves (at end of period; in millions of US dollars)	3 943.06	5 753.39
Gold	233.08	231.30
Special Drawing Rights	0.64	0.64
Reserve position in the IMF	0.09	0.09
Foreign convertible currencies	3 709.25	5 521.36

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

<sup>2</sup> Data have been revised.

EXCHANGE RATES SET BY THE BANK OF LATVIA AND INTEREST RATES	2009	
	VI	VII
Weighted average interest rate on domestic interbank loans in lats	22.3	2.8
Interest rates on loans to resident non-financial corporations and households		
Loans to non-financial corporations (in lats)	33.4	14.6
Loans to households (in lats)	19.1	17.7
incl. for house purchase	10.4	8.4
Loans to non-financial corporations (in foreign currencies)	5.4	5.6
Loans to households (in foreign currencies)	5.5	5.4
incl. for house purchase	4.5	4.4
Interest rates on deposits of non-financial corporations and households		
Time deposits of non-financial corporations (in lats)	20.0	8.5
Demand deposits of non-financial corporations (in lats)	2.6	1.1
Time deposits of households (in lats)	14.7	12.0
Demand deposits of households (in lats)	1.0	0.9
Time deposits of non-financial corporations (in foreign currencies)	1.4	1.2
Demand deposits of non-financial corporations (in foreign currencies)	0.3	0.3
Time deposits of households (in foreign currencies)	3.1	3.0
Demand deposits of households (in foreign currencies)	0.9	0.8
The Bank of Latvia's refinancing rate (at end of period; %)	4.0	4.0
Exchange rates of foreign currencies (at end of period)		
LVL/USD	0.5010	0.5000
LVL/GBP	0.8260	0.8200
LVL/100 JPY	0.5260	0.5260
LVL/EUR	0.7028	0.7028

**AGGREGATED BALANCE SHEET OF MFIs (EXCLUDING THE BANK OF LATVIA)** (at end of period; in millions of lats)

	2009	
	VI	VII
MFI reserves	923.0	894.1
Vault cash in national currency	97.5	102.2
Deposits with the Bank of Latvia	825.5	791.9
Foreign assets	4 602.2	4 444.3
Vault cash in foreign currencies	64.6	72.0
Claims on MFIs	2 657.2	2 479.3
Claims on non-MFIs	1 775.0	1 786.2
Other assets	105.4	106.8
Claims on central government	552.5	634.4
Claims on local government	74.2	76.3
Claims on public non-financial corporations	382.9	382.9
Claims on financial institutions and private non-financial corporations	7 598.4	7 523.2
Claims on households	6 257.0	6 232.9
Unclassified assets	988.4	951.7
Fixed assets	166.9	164.8
Items in transit	22.2	19.1
Other assets	362.9	375.6
Claims on resident MFIs (incl. investments)	436.3	392.2
<b>Total assets</b>	<b>21 378.7</b>	<b>21 139.8</b>
<i>Memo item: Trust assets</i>	353.7	349.5
Overnight deposits in lats	1 041.9	1 042.5
Public non-financial corporations	65.3	66.7
Financial institutions and private non-financial corporations	439.7	455.2
Households	536.9	520.6
Time deposits and deposits redeemable at notice in lats	1 101.8	1 052.7
Public non-financial corporations	176.6	163.5
Financial institutions and private non-financial corporations	407.7	375.8
Households	517.5	513.4
Foreign currency deposits of residents	2 933.2	2 871.5
Public non-financial corporations	51.6	45.2
Financial institutions and private non-financial corporations	1 051.6	1 012.4
Households	1 829.9	1 813.8
Deposits of central government	662.1	664.9
Deposits of local government	189.4	180.1
Transit funds	3.2	3.2
Foreign liabilities	11 516.4	11 294.2
Liabilities to MFIs	8 066.4	7 862.2
Liabilities to non-MFIs	2 977.3	2 951.2
Other liabilities (incl. subordinated liabilities)	472.7	480.9
Liabilities to the Bank of Latvia	258.9	255.0
Debt securities issued	160.5	160.7
Money market fund shares and units	59.0	60.7
Capital and reserves	1 580.0	1 669.2
Residents	807.0	758.9
Non-residents	773.1	910.3
Provisions	1 020.1	1 105.1
Unclassified liabilities	852.2	780.1
Items in transit	90.3	74.4
Other liabilities (incl. subordinated liabilities)	363.3	346.7
Liabilities to resident MFIs	398.5	359.0
<b>Total liabilities</b>	<b>21 378.7</b>	<b>21 139.8</b>
<i>Memo item: Trust liabilities</i>	353.7	349.5

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>).