2026 Q2 assessment of the systemic cyclical risk and applicable countercyclical capital buffer rate

2026 | June

The countercyclical capital buffer (hereinafter – the CCyB) is a macroprudential tool that aims at strengthening the capitalisation of credit institutions so that they are adequately equipped to absorb losses in times of crisis. When risks materialise, the CCyB rate is partially or fully released to help credit institutions continue to offer funding to the economy, thereby reducing the length of crises and their impact on the economy.

Latvijas Banka, in its capacity as the designated authority for the application of the CCyB requirement, evaluates the cyclical systemic risk on a quarterly basis pursuant to Section 35.5 of the Credit Institution Law and, if necessary, sets or adjusts the CCyB rate applicable to credit institution exposures to residents of the Republic of Latvia. Latvijas Banka publishes quarterly assessments of the cyclical systemic risk and the applicable CCyB rate. If the CCyB rate remains unchanged, the previous decision regarding the applicable CCyB rate remains in force.

On 18 December 2023, the Council of Latvijas Banka decided to implement a positive neutral CCyB approach. According to this approach the CCyB rate is set at positive basis level (above zero) already in a standard risk environment or at the neutral stage of the financial cycle when cyclical systemic risk is neither elevated nor subdued. Latvijas Banka has estimated 1% to be an appropriate base level of the CCyB rate. In accordance with the Council's decision of 18 December 2023, a 1% CCyB rate will take effect from 18 June 2025.

As cyclical risk increases, the CCyB rate should be raised proportionally to the intensity of the risk, starting already from the base rate. Thus, the total CCyB requirement consists of the base rate and the cyclical component, which is assessed on a quarterly basis. In times of crisis, as well as during the recovery period following a crisis, the CCyB rate may be reduced or released.

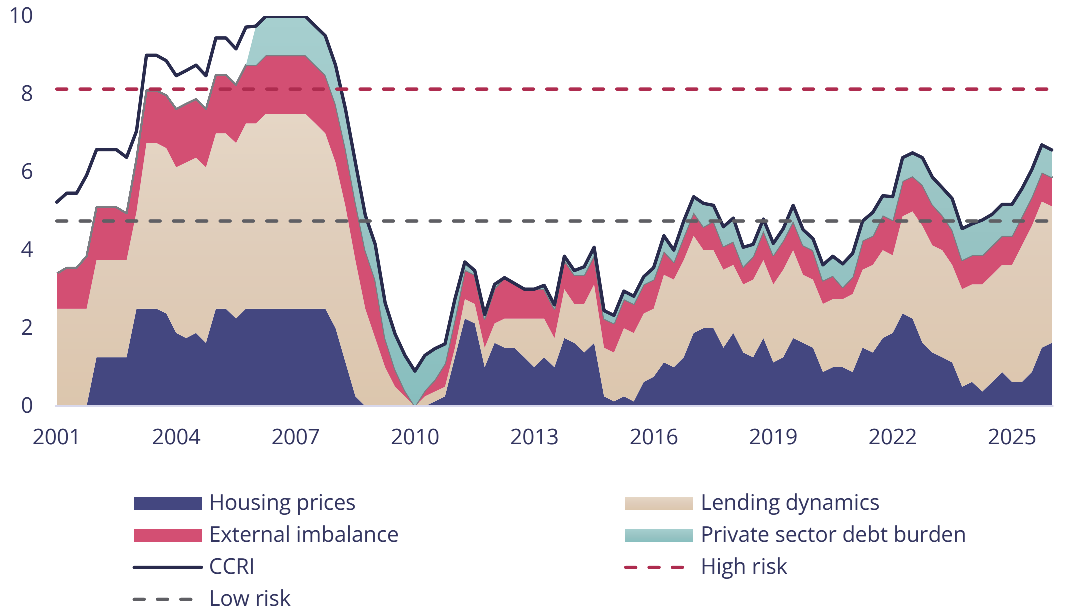
In accordance with the cyclical risk assessment for 2026 Q2, **Latvijas Banka has decided not to increase the cyclical component of the CCyB.**

The decision of Latvijas Banka regarding the applicable CCyB rate, adopted on December 18, 2023, remains in force.

The cyclical risk level continues to increase, mainly driven by the expansion of lending activity. However, the pick-up in lending is taking place from a persistently low base and is partly influenced by the temporarily introduced solidarity contribution. The real estate market is transitioning from moderate growth to more uneven developments across housing market segments: following a period of stronger growth, activity is stabilizing, while house price growth is accelerating. Economic growth in 2026 may not exceed the pace recorded in 2025, as businesses and households remain cautious in the context of still elevated geopolitical risks.

Further escalation of military conflict in the Middle East could lead to weaker external demand, higher energy costs and overall price levels, as well as supply chain disruptions. These developments could adversely affect economic activity, labor market conditions, and the financial position of borrowers, while also weakening borrower and lender sentiment.

Composite cyclical risk indicator (CCRI)



Composite cyclical risk indicator (CCRI) reached 6.6 points in 2026 Q1, which is 1.4 points higher than a year ago. The increase in the CCRI was driven by a pick-up in lending activity and rising house prices. The CCRI is within the medium risk range.

For more details on the CCRI, see Latvijas Bankas 2025 Financial Stability Report.

Sources: Latvijas Banka, Central Statistical Bureau of Latvia (CSB), Latvijas Banka's calculations

The credit-to-GDP gap of the private non-financial sector calculated using the additional credit measure has turned positive for the first time since the introduction of the CCyB methodology. **The buffer guide is 0%.**

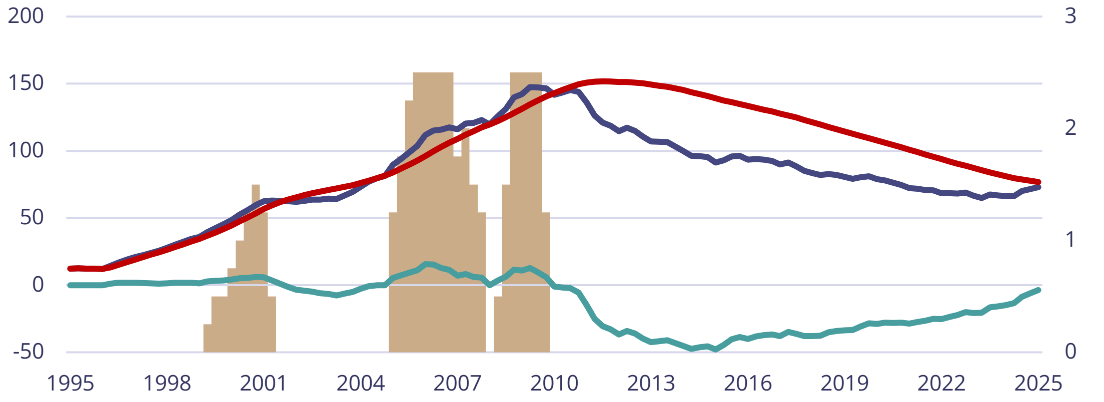
	Standardised credit definition 2025 Q4	**Additional** credit definition 2026 Q1
Credit-to-GDP ratio (%)	73.0	33.4
Credit-to-GDP gap (pp)	-3.8	0.2
Benchmark buffer rate (% from TREA)	0	0

Standardized credit definition – liabilities of non-financial corporations (hereinafter – NFCs) and households to credit institutions, as well as their loans from non-bank financial institutions or other NFCs.

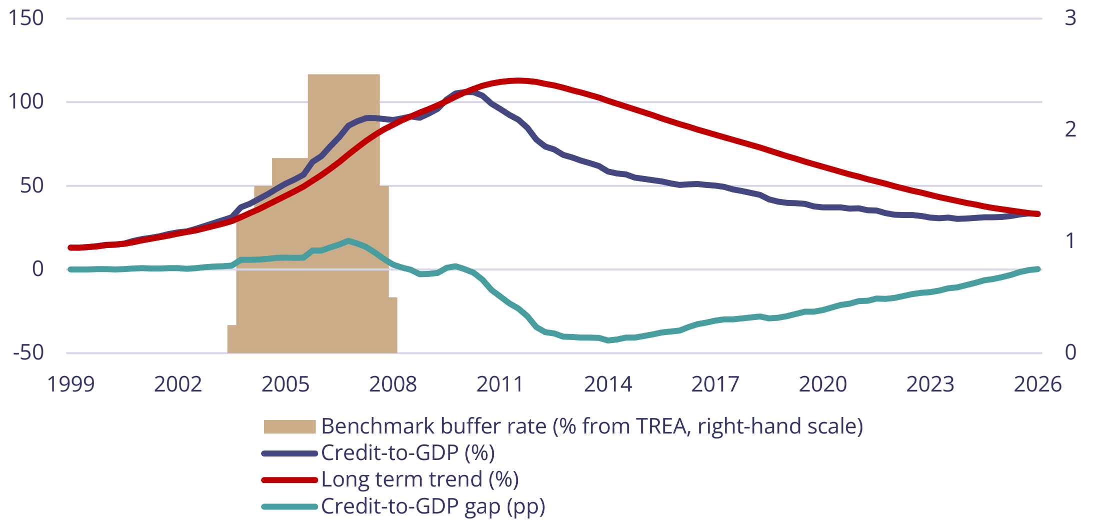
Additional credit definition – bank loans to NFCs and households, and holdings of NFCs debt securities, and loans granted by banks' leasing subsidiaries.

The benchmark buffer rate calculated from the additional credit definition has been chosen as the buffer guide. The data is available sooner, and the benchmark buffer rate calculated from the additional credit measure aligns better with the historically required CCyB rate.

Standardised credit-to-GDP gap

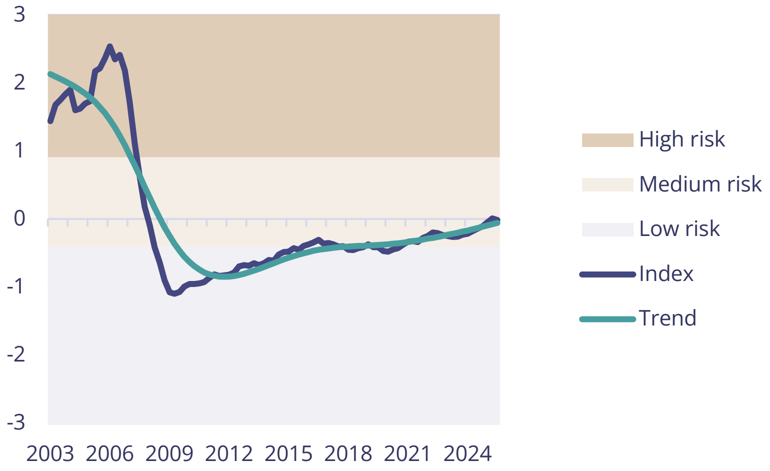


Additional credit-to-GDP gap

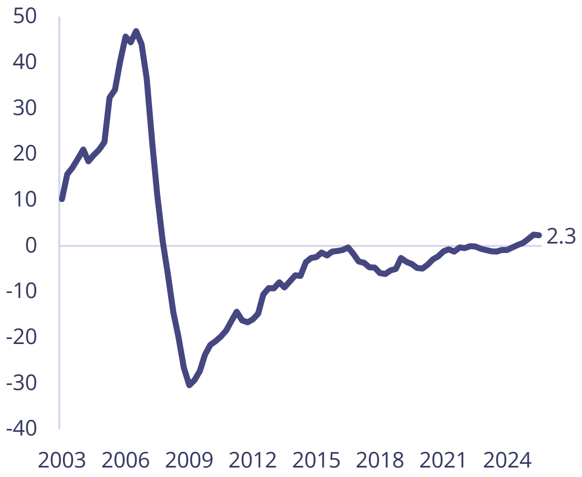


Sources: Latvijas Banka, CSB, Latvijas Banka's calculations

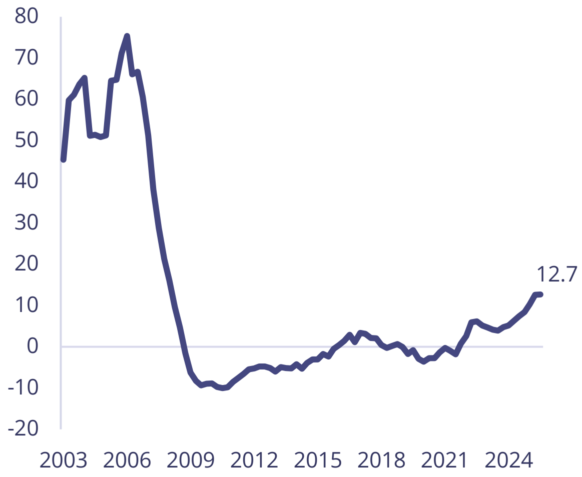
Credit developments index



Additional credit measure to 7-year GDP annual difference, percentage points



Additional credit measure annual growth rate*, %

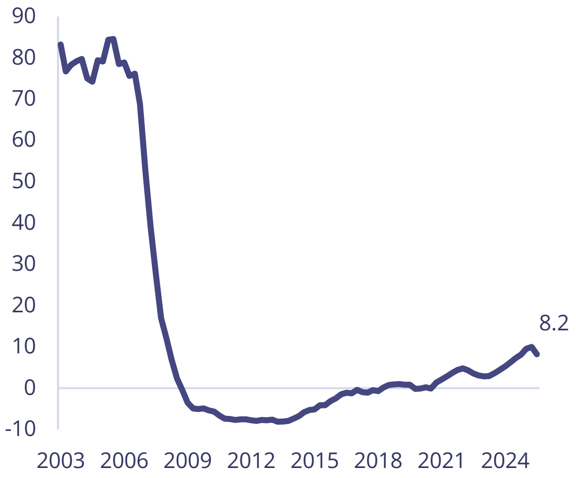


Domestic lending continues to grow at a significant pace despite increasing uncertainty stemming from the military conflict in the Middle East, as well as weaker economic growth prospects. In 2026 Q1 and in May, the outstanding loans issued to households and NFCs* increased year-on-year by 11.8 % and 12.4 %, respectively (including 10.3 % and 10.5 % for households, and 13.3 % and 14.4 % for NFCs).

Lending growth continues to be driven primarily by the expansion of long-term loans. The pace of mortgage lending growth is gradually increasing, supported by sustained improvements in household creditworthiness and a substantial stock of liquid financial assets. Corporate lending is developing alongside strong investment activity, including in renewable energy projects and residential construction, where investment levels had remained low for an extended period. Credit supply continues to be supported by the Solidarity Contribution Law, which allows credit institutions to receive a contribution discount if specific credit portfolio growth targets are met. It cannot be ruled out that lending growth may moderate once the application period of the solidarity contribution ends.

Further developments in lending may be constrained by external factors, including geopolitical risks.

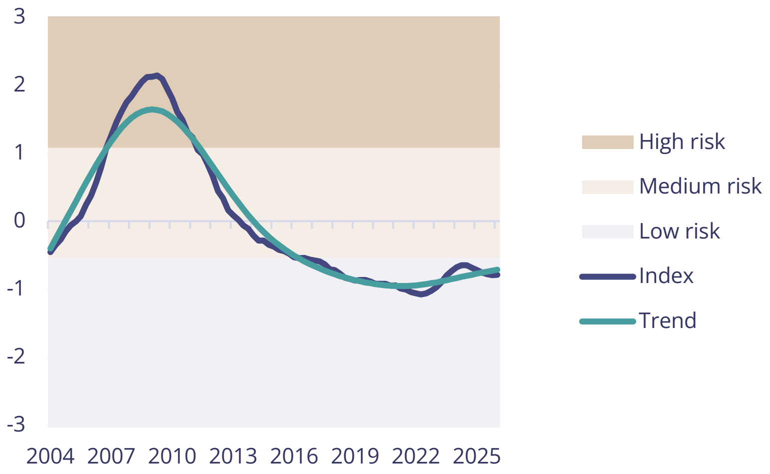
Household credit annual growth rate*, %



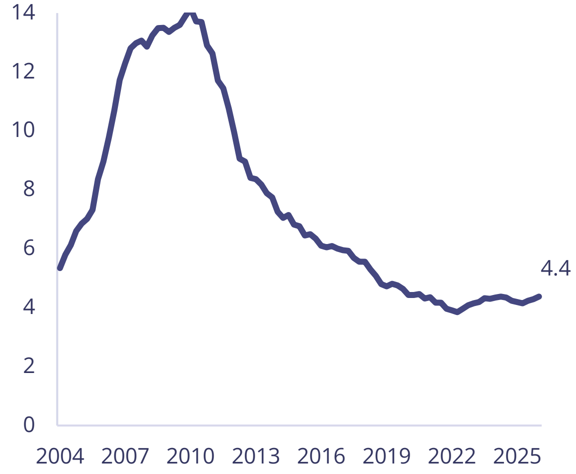
* Reclassifications and other one-time effects are excluded from the loan growth rate, but the effect of written-off loans is not excluded.

Sources: Latvijas Banka, CSB, Latvijas Banka's calculations

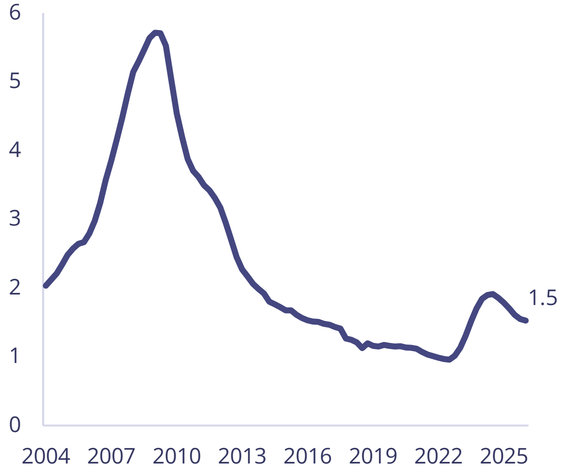
Private sector debt burden index



Household and NFC debt service ratio*, %



Household and NFC annual interest payments to GDP, %



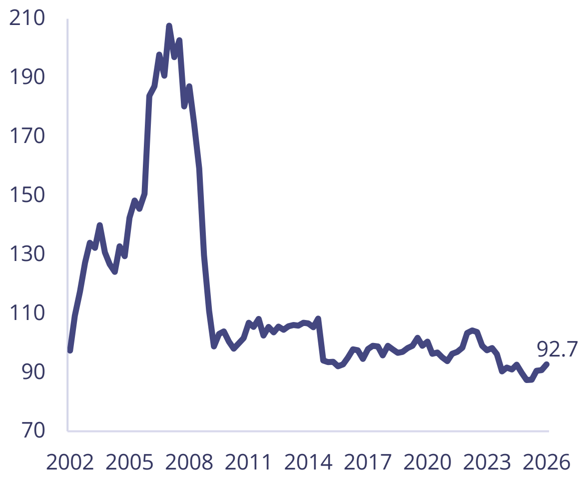
The debt of the private non-financial sector is low. Along with the gradual decrease in interest rates, the ratio of interest payments on private non-financial sector loans to GDP has also slightly decreased. The financial resilience of borrowers remains good.

*The calculation of the Debt Service Ratio (DSR) is based on an equal-payment (annuity) approach, which accounts for both interest payments and principal amortization burden: $DSR = \frac{i_t * D_t}{(1-(1+i_t)^{-s_t}) * Y_t}$, where *D* represents the measure of additional credit measure or the total private non-financial sector debt volume, *i* is the sector's average interest rate, income *Y* is replaced by GDP, and the average loan term *s* is assumed to be 10 years. This methodology allows for assessing the debt servicing burden at the macro level.

Sources: Latvijas Banka, CSB, Latvijas Banka's calculations

Potential overvaluation of property prices index

House prices-to-average net wages index, 2010 = 100



CSB's house price annual growth rate, %

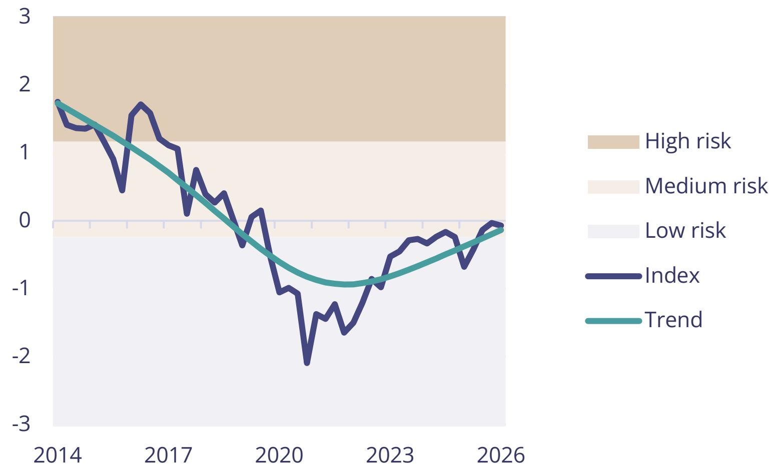
Activity in the real estate market in 2026 Q1 was lower than a year earlier for the second consecutive quarter. This continued to reflect a high base effect following the recovery in market activity driven by declining interest rates. The total number of real estate purchase transactions decreased by 5.7 %, including a 10.7 % decline in land purchase transactions and a 2.1 % decrease in the housing segment. At the same time, the annual rate of change in the housing market improved during 2026 Q1: following declines in January and February, the number of transactions increased by 2.1 % in March. In the apartment market, activity remained broadly close to the level observed in 2025 Q1, with the number of transactions decreasing by only 0.9 %. In the standard-type apartment segment, the number of transactions increased by 1.7 %, while activity declined in other housing segments. In the new project segment, the number of transactions fell by 6.1 %, while in the primary market the decline moderated to 16.4 %.

The annual growth rate of **housing prices** has remained elevated since the second half of 2025, while quarterly price growth has become more moderate. According to CSB data, overall housing prices increased by 10.9 % year-on-year in 2026 Q1 (10.5 % in the previous quarter), while quarter-on-quarter growth slowed to 1.2 % (1.5 % in the previous quarter). House price dynamics continued to be driven by divergent developments in the new and existing housing segments. Faster growth was mainly driven by existing housing, with prices increasing by 12.2 % year-on-year and by 1.9 % quarter-on-quarter (1.8 % in the previous quarter). In contrast, price growth in the new housing segment was significantly weaker, at 4.0 % year-on-year, while prices declined by 2.1 % during the quarter, reflecting lower market activity.

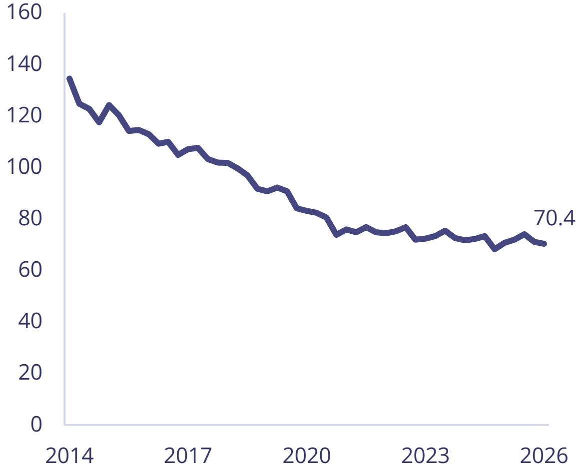
Housing affordability has started to deteriorate in the existing housing market, as wage growth has slowed and housing prices have continued to increase, while in the new housing segment affordability continues to show positive dynamics.

Sources: CSB, Latvijas Banka's calculations

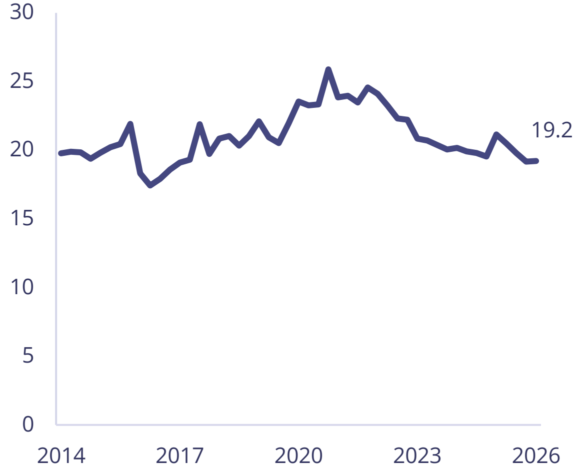
Strength of bank balance sheets index



The ratio of domestic credit to deposits, %



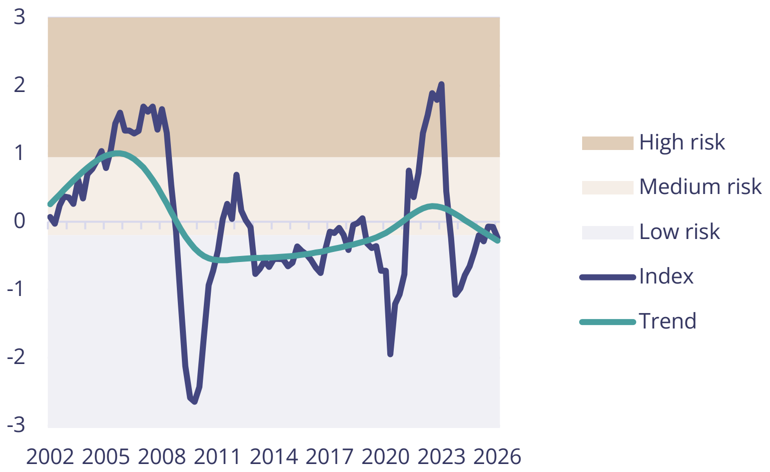
CET1 ratio, %



Bank balance sheet resilience indicators – bank capitalization, as well as profitability and asset quality – are very strong. The ratio of bank loans to deposits remains consistently low.

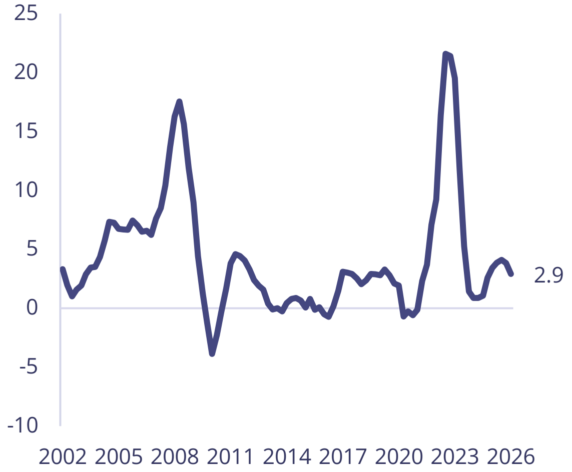
Sources: Latvijas Banka, Latvijas Banka's calculations

Macroeconomic environment index



Real GDP annual growth rate, %

HICP annual growth rate, %



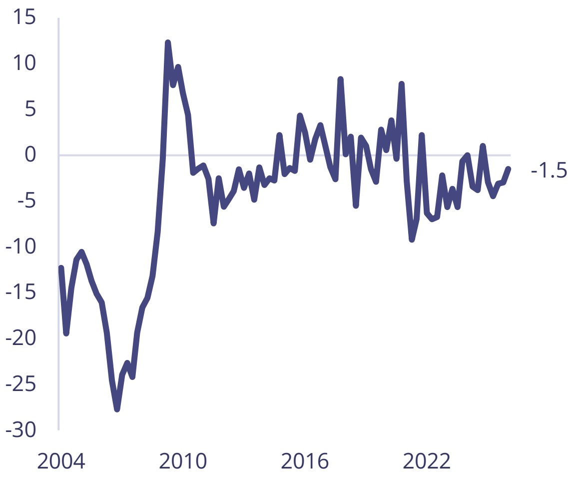
Economic growth in 2026 may not exceed the pace recorded in 2025, as the deterioration in the geopolitical environment is hampering a stronger recovery in external demand and maintaining cautious sentiment among economic agents. In 2026 Q1, Latvia's GDP increased by 0.6 % quarter-on-quarter (seasonally adjusted data).

Investment activity was the main driver of growth, in line with increasing construction activity and the need to strengthen defence capabilities. Despite elevated uncertainty, previously launched projects continue to advance, while new projects are being announced in both infrastructure and residential construction. Export growth in Q1 was driven mainly by the services sector. At the same time, the recovery of private consumption remains gradual (with growth below that of GDP overall): on the one hand, this reflects caution stemming from geopolitical developments, while on the other hand it is constrained by slow growth in purchasing power. Although inflation during the first months of the year was more moderate than expected, gains in purchasing power were held back by slower-than-projected growth in labour income.

Economic sentiment deteriorated in April and May. While survey data currently suggest that concerns about material shortages in manufacturing have not increased significantly, the Latvian economy remains highly dependent on the consumption of petroleum products.

Sources: CSB, Latvijas Banka's calculations

Current account balance-to-GDP, %



In 2026 Q1, the **current account** deficit decreased to 1.5 % of GDP. The improvement was mainly supported by stronger service exports and changes in secondary income flows.

The increase in EURIBOR since 2022 has directly contributed to a reduction in margins, as the overall interest rate on loans rose less than EURIBOR, while the funding costs for banks did not increase as rapidly as EURIBOR.

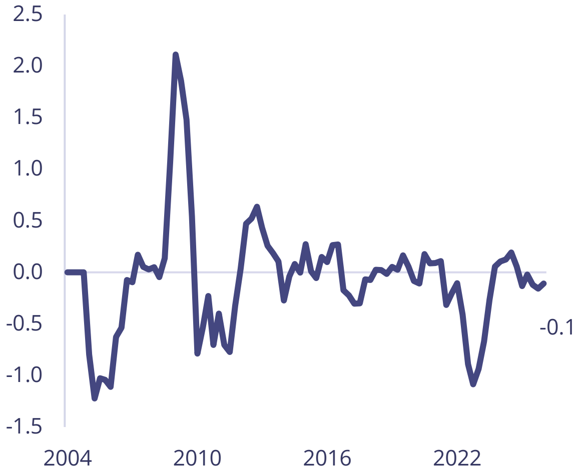
Margins continued to decrease in 2025. Although the ECB no longer adjusted policy interest rates, the lending environment became more favorable: competition among lenders intensified, and households made more active use of lower refinancing costs.

The decline in margins has also been supported by policy measures aimed at promoting competition in the banking sector and stimulating lending.

The ECB raised interest rates in June 2026 for the first time since 2023, but the pass-through to borrowers' overall lending rates remained limited.

Difference between interest rate on newly issued housing loans to households and 6-month EURIBOR, pp

Difference between interest rate on newly issued housing loans to households and 6-month EURIBOR, annual change pp



Sources: Latvijas Banka, CSB, Latvijas Banka's calculations, The European Money Markets Institute.