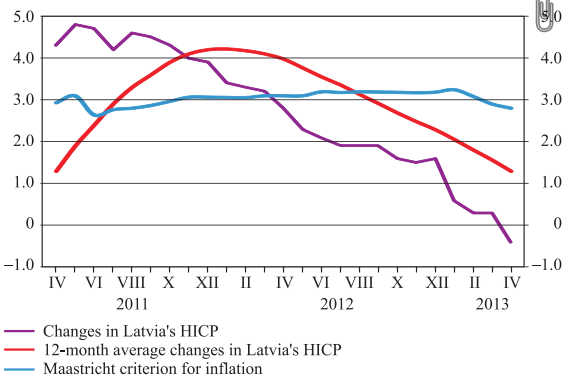
1. Highlights

Inflation low, Latvia meets Maastricht criterion with wide margin

Inflation in Latvia and the Maastricht criterion for inflation
(%)



Source: Eurostat.

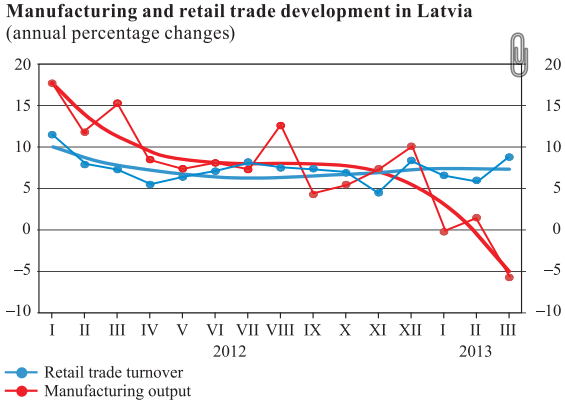
In April 2013, annual inflation turned negative (-0.4%). This low level of inflation is still rooted in both cost and other factor dynamics of the basis period. For instance, in April 2012, fuel prices hiked dramatically on account of high oil prices. However, in April 2013, they declined and thus alleviated cost pressures in many sectors.

This persistently low inflation has allowed Latvia to comply with the Maastricht inflation rate criterion with a comfortable margin.

At the same time, it is quite likely that the lowest level of the current year's annual inflation has already been reached. In the coming months, the effects stemming from low fuel prices, the reduction of the value added tax in July 2012, and the lowering of heating costs in November 2012 will all gradually disappear. On the other hand, prices in the electricity market are likely to be liberalised later than initially planned, thus reducing the scope for price increases this year. Moreover, potential price hikes for a number of widely used goods and services are likely to be curbed by the on-going price observation activities related to the expected euro changeover.

GDP growth slower due to manufacturing, but retail trade still holding up

Manufacturing and retail trade development in Latvia
(annual percentage changes)



Source: CSB.

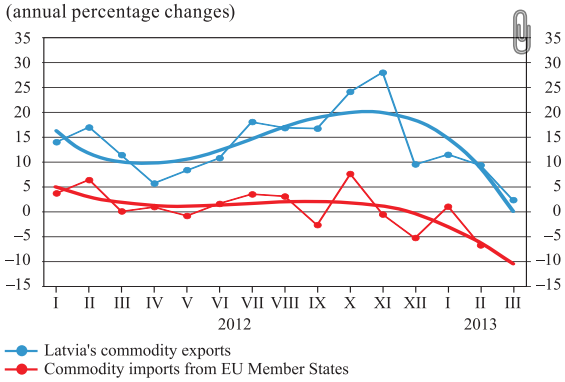
According to the CSB flash estimate, in the first quarter of 2013, the annual growth rate of gross domestic product (GDP) was 3.1%. This is a decline in comparison with the previous year; nevertheless, considering the unfavourable developments both in the external and the domestic environment, economic growth has moderated only slightly.

Looking by sector, however, the performance is uneven. While the manufacturing output shrank by 3.6% quarter-on-quarter in the first quarter, retail trade continued to report significant growth.

Even assuming that the domestic demand will continue to develop at a stable pace in 2013, it is unlikely that GDP growth will reach the levels observed in 2012 and 2011. Experience suggests that the domestic demand in Latvia will be unable to sustain the economic growth in the longer term in the absence of a recovery in the external demand.

Exports slow down amid stagnating external demand

Export development in Latvia and external demand
(annual percentage changes)



Source: CSB.

In March 2013, Latvia's foreign trade turnover grew by 10% despite the generally low external demand.

Although the annual growth of the commodity exports remained positive in March (2.6%), as a result of the weakening demand in the markets of partner countries and the base effect, the rate of growth decelerated significantly. The rises in the exports of products of the chemical industry, agricultural and food products, paper and articles of paper, building materials, machinery and equipment contributed positively to the annual growth of the commodity exports. Conversely, the annual growth rate of exports was dampened by a decline in the exports of transport vehicles and mineral products.

Latvia's export trends for the coming months should be viewed with caution because of the data reported from manufacturing in the most recent months as well as the external developments. The confidence indicators published by the European Commission also show deterioration in the outlook on new export orders in April for the second consecutive month for Latvia's ESI. On the other hand, a positive contribution to exports in the future could be made by the signing of the Trade and Investment Partnership Agreement between the European Union and the USA.