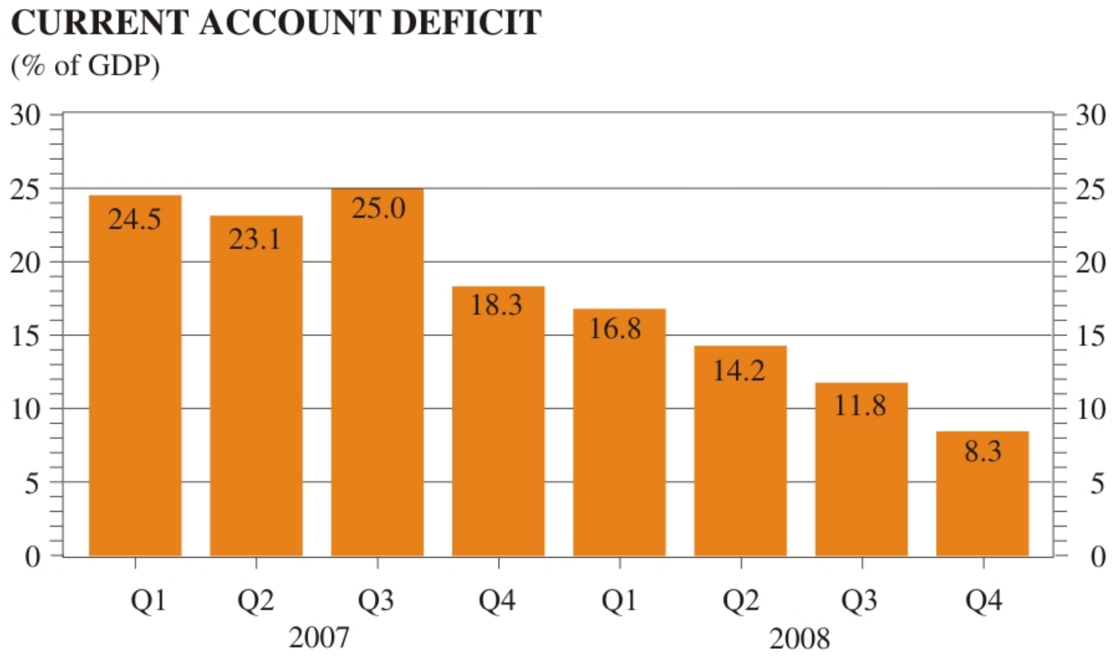
PRESS RELEASE

Riga, 26 March 2009
Latvia's Balance of Payments in the Fourth Quarter of 2008

The current account deficit of Latvia's balance of payments continued to shrink, **in the fourth quarter of 2008** decreasing to 348.1 million lats or 8.3% of GDP (771.4 million lats or 18.3% of GDP in the corresponding period of the previous year).



The goods deficit to GDP decreased notably (by 5.0 percentage points), with the annual slowdown in exports and imports of goods at 7.0% and 14.7% respectively. The income balance turned positive, translating into a 4.3 percentage point decrease in the current account deficit as non-resident direct investment companies in Latvia incurred losses. At the same time, net foreign direct investment in Latvia was negative in the fourth quarter, at 2.3% of GDP. The services surplus to GDP increased, with services exports growing faster than services imports. The current transfers surplus to GDP contracted.

Progressively narrowing in the course of the year, the current account deficit in **2008 as a whole** reversed to the level of 2005 (12.6% of GDP; 22.5% of GDP in 2006 and 2007). This improvement in the current account was primarily on account of a smaller goods deficit to GDP. All other items to GDP also improved somewhat.

Net inflow of foreign direct investment dropped in the sectors which previously had recorded the largest inflows (trade, real estate activities, and financial intermediation), whereas manufacturing recorded stable inflows. In 2008 as a whole, foreign direct investment in Latvia recorded net inflows in the amount of 4.0% of GDP.

As in the previous years, in 2008 net inflows of long-term other capital covered the current account deficit. An increase in long-term debt was triggered by bank borrowing in the first three quarters of 2008 and government borrowing (offsetting substantial outflows of short-term capital from banks) in the fourth quarter.

As a result of Bank of Latvia's interventions in the foreign exchange market, the reserve assets decreased both in the fourth quarter and the year 2008 as a whole (by 320.2 million lats).

Evaluation and Outlook

With foreign demand weakening and credit availability becoming more restricted in the context of the global financial crisis, exports of goods contracted substantially in the fourth quarter of 2008. The steep fall in exports and domestic demand caused a sharp drop in imports of intermediate goods. At the same time, imports of capital goods also shrank due to the narrowing in corporate investment and household spending for durable goods against the backdrop of tighter credit conditions and falling wages and salaries. In the situation of slow economic activity and heightened competition, the exporters should anticipate declines in demand and lower prices in external markets also in 2009. As incomes fall, household purchases of imported goods are expected to shrink further, albeit at a slower pace, whereas respective corporate purchases will depend on exports.

It is essential for successful development of the economy that exporting businesses retain their capacity and ability to compete when the external demand resumes its force. Hence it is vital how quickly and to what extent the government will be able to implement a consistent cost-cutting policy, maintaining and supporting exports as a priority at the same time.

Mārtiņš Grāvītis
Press secretary
Bank of Latvia

Telephone: +371 670 22 349
Mobile: +371 265 10 385
Martins.Gravitis@bank.lv
www.bank.lv