

# MONETARY BULLETIN 2006

## 11

The data on the gross domestic product in the third quarter of 2006 published by the Central Statistical Bureau of Latvia confirmed rapid growth and the significant role of the domestic demand in the development of the Latvian economy. Latvia's economic growth rate remained the highest among the Baltic States and amounted to 11.8%. Sectoral developments point to imbalanced growth. Trade and business activities with an increase of 19.0% and 18.1% respectively accounted for more than a half of the overall rise. Financial sector, construction, transport, storage and communication, and community and personal service activities also continued to develop buoyantly. A significant increase in the value added (7.4%) supported by external demand was reported in manufacturing.

In October, the seasonally adjusted volume index of industrial output in manufacturing increased by 4.6% year-on-year. Energy recorded slightly lower growth, whereas the overall industrial output expanded by 3.9%. Retail trade turnover (including sale of motor vehicles and retail trade in automotive fuel) grew by 36.7% at constant prices.

The volume of rail freight continued to shrink (by 21.2% in November). Cargo turnover at Latvian ports expanded by 5.8% year-on-year. Unemployment rate remained unchanged at 6.6% in November.

In November, consumer prices increased by 1.0% month-on-month, with the annual inflation rebounding to 6.4%. With the supply side effects increasing rather marginally, the core inflation climbed from 4.8% in October to 5.5% in November, particularly increasing for services that are not administratively regulated. The highest rise was reported for the prices of vegetables, bread and cereal products, which grew by 15.9%, 8.8% and 3.4% respectively, and heating tariffs by 8.8%.

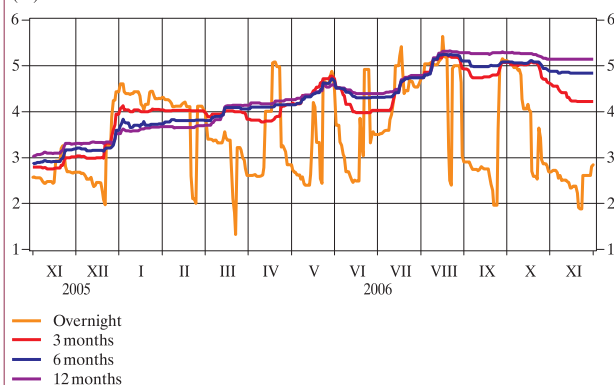
The Bank of Latvia continued to pursue a tight monetary policy warranted by the persistently high inflation, large current account deficit and unsustainable growth spurred by lending. Taking into account the macroeconomic development trends of Latvia and the rising interest rates in the euro area, the Bank of Latvia's Council raised the refinancing rate of the Bank of Latvia by 0.5 percentage point to stand at 5.0% and the interest rates on Lombard loans by 0.5 percentage point as of 17 November 2006.

The financial deficit of the general government consolidated budget amounted to 71.0 million lats in November; thus, the financial surplus of the budget for the first 11 months of 2006 shrank to 235.2 million lats. The central government basic budget reported a more sizeable deficit of 133.5 million lats in November, whereas the social security fund and local government consolidated budget ran a financial surplus of 31.9 million lats and 21.9 million lats respectively. The general government consolidated budget revenue increased by 110.5 million lats or 40.1% and expenditure by 101.3 million lats or 28.5% year-on-year.

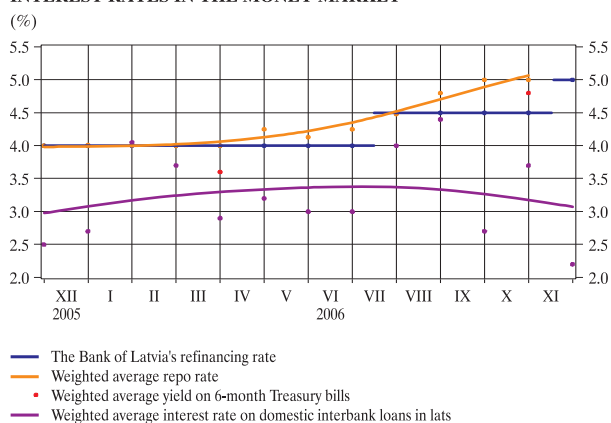
The general government debt expanded by 16.9 million lats month-on-month to stand at 1 108.8 million lats at the end of November, and it was related to an issue of 5-year Government bonds. In November, two competitive multi-price auctions were held on the primary market for these bonds where securities in the amount of 17.4 million lats were sold at the weighted average yield of 5.032%.

**MONEY MARKET INDEX RIGIBOR**

(%)



### INTEREST RATES IN THE MONEY MARKET



In November, the growth in broad money M3 was lower than in October. That was determined by a more subdued increase in resident deposits, with a currency outside MFIs continuing to rise moderately. The growth rate of M3 decelerated year-on-year (from 44.3% in October to 40.4% in November). The annual rate of increase in overnight deposits shrank from 54.1% to 48.7% respectively, whereas that of deposits with agreed maturity of up to 2 years declined from 39.2% to 34.9% and that of deposits redeemable at notice diminished from 42.7% to 41.4%. The growth rate of monetary aggregates M1 and M2 also decelerated year-on-year to stand at 41.8% and 40.1% respectively, whereas that of currency outside MFIs remained broadly unchanged year-on-year (23.6% in November).

The annual rate of increase in deposits made by resident financial institutions, non-financial corporations and households decreased in November by 4.7 percentage points (to 41.7%), with deposits made in foreign currencies expanding faster (by 44.4%).

A rise in loans granted to resident financial institutions, non-financial corporations and households remained broadly unchanged in November. Mortgage lending reported the highest increase and the majority of loans were granted in euro. Unlike the previous months, lending to non-financial corporations accelerated in November. The annual growth rate of loans granted to resident financial institutions, non-financial corporations and households remained at the level of the previous month (58.7%). Lending to business grew by 1.0 percentage point year-on-year (to 46.8%) due to a rise in the annual growth rate of commercial credit and industrial credit, with the annual expansion of mortgage loans granted to financial institutions and non-financial corporations shrinking slightly at the same time. The household lending rate diminished in November to 76.7% year-on-year, with the household loans for house purchase expanding annually by 85.2% and consumer credit – by 62.6%. Loans granted in euro accounted for almost entire increase in lending (a pickup of 430.8 million lats).

Latvian banks continued to borrow abroad in November, hence the negative net foreign assets of MFIs (excluding the Bank of Latvia) grew by 275.4 million lats.

Interest rates on household loans granted in foreign currency continued to increase in November due to a rise in euro money market interest rates (for instance, the weighted average interest rate on household loans rose by 0.1 percentage point – to 5.6%, including that on loans for house purchase growing by 0.2 percentage point to 5.4%), whereas those on loans granted to non-financial corporations as well as to households in lats posted a decline.

With an excess liquidity persisting in the banking sector, the overnight RIGIBOR remained low, fluctuating from 1.88% to 2.80%. RIGIBOR for loans with a 6 month maturity shrank to 4.84% during November, while that for loans with a 12 month maturity remained unchanged (5.15%). Banks reduced the excess liquidity by placing time deposits with the Bank of Latvia, hence, the monetary base M0 decreased substantially. Thus, with the Bank of Latvia foreign reserves remaining broadly unchanged, the backing of the national currency with the central bank's net foreign assets was 123.3% at the end of November.

In November, the US dollar, the Japanese yen and the British pound sterling depreciated against the lats by 2.0%, 1.1% and 0.9% respectively.

MACROECONOMIC INDICATORS	2006	
	X	XI
Changes in the volume index of industrial output (year-on-year basis; %)	3.9	*
Changes in the CPI		
Month-on-month basis (%)	0.5	1.0
Year-on-year basis (%)	5.6	6.4
Annual rate of core inflation <sup>1</sup> (%)	4.8	5.5
Number of registered unemployed persons (at end of period)	70 045	69 705
Unemployment rate (%)	6.6	6.6
General government consolidated budget financial deficit/surplus (in millions of lats)	306.1	235.2
Foreign trade (in millions of lats)		
Exports	294.5	*
Imports	588.9	*
Balance	-294.4	*

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

\* Figure available at a later date.

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

MONETARY INDICATORS (at end of period; in millions of lats)	2006	
	X	XI
<b>MFIs<sup>1</sup></b>		
<b>M3</b>	5 110.7	5 210.5
Repurchase agreements	0	0
Money market fund shares and units	31.1	32.7
Debt securities issued with maturity of up to 2 years	4.9	4.9
<b>M2</b>	5 074.8	5 173.0
Deposits with agreed maturity of up to 2 years	1 183.1	1 198.1
Deposits redeemable at notice of up to 3 months	138.8	141.2
<b>M1</b>	3 752.8	3 833.7
Currency outside MFIs	904.4	921.3
Overnight deposits	2 848.4	2 912.4
Net external assets	-2 131.0	-2 390.4
Credit to resident financial institutions, non-financial corporations and households	8 873.7	9 323.3
Credit to general government	345.3	356.8
Deposits of central government	315.3	343.3
Longer-term financial liabilities	1 729.5	1 752.4
<b>Bank of Latvia</b>		
<b>M0</b>	2 065.1	1 957.2
Currency in circulation	998.0	1 023.8
Deposits with the Bank of Latvia in lats	1 067.1	933.4
Deposits with the Bank of Latvia in foreign currencies	0	0
Net foreign assets	2 397.1	2 413.1
Net domestic assets	-332.1	-455.9
Credit	-258.5	-277.0
To MFIs	0	0
To central government (net)	-258.5	-277.0
Other items (net)	-73.6	-178.8
International reserves (at end of period; in millions of US dollars)	4 349.15	4 460.39
Gold	149.95	157.18
Special Drawing Rights	0.15	0.16
Reserve position in the IMF	0.08	0.08
Foreign convertible currencies	4 198.97	4 302.97

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

EXCHANGE RATES SET BY THE BANK OF LATVIA AND INTEREST RATES	2006	
	X	XI
Weighted average interest rate on domestic interbank loans in lats	3.7	2.2
Interest rates on loans to resident non-financial corporations and households		
Loans to non-financial corporations (in lats)	7.3	6.4
Loans to households (in lats)	11.3	11.0
incl. for house purchase	7.4	7.0
Loans to non-financial corporations (in foreign currencies)	5.9	5.3
Loans to households (in foreign currencies)	5.5	5.6
incl. for house purchase	5.2	5.4
Interest rates on deposits of non-financial corporations and households		
Time deposits of non-financial corporations (in lats)	3.5	3.6
Demand deposits of non-financial corporations (in lats)	1.1	0.8
Time deposits of households (in lats)	3.3	3.7
Demand deposits of households (in lats)	0.5	0.5
Time deposits of non-financial corporations (in foreign currencies)	3.4	3.5
Demand deposits of non-financial corporations (in foreign currencies)	1.5	1.6
Time deposits of households (in foreign currencies)	3.5	3.7
Demand deposits of households (in foreign currencies)	1.3	1.3
The Bank of Latvia's refinancing rate (at end of period; %)	4.5	5.0
Exchange rates of foreign currencies (at end of period)		
LVL/USD	0.5530	0.5420
LVL/GBP	1.0480	1.0390
LVL/100 JPY	0.4710	0.4660
LVL/EUR	0.7028	0.7028

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

	2006	
	X	XI
MFI reserves	1 156.6	1 134.6
Vault cash in national currency	93.5	102.5
Deposits with the Bank of Latvia	1 063.0	1 032.1
Foreign assets	3 531.7	3 502.4
Vault cash in foreign currencies	58.7	56.2
Claims on MFIs	2 073.9	2 032.0
Claims on non-MFIs	1 360.3	1 359.7
Other assets	38.8	54.5
Claims on central government	252.1	263.1
Claims on local government	93.2	93.8
Claims on public non-financial corporations	116.1	113.0
Claims on financial institutions and private non-financial corporations	4 870.7	5 146.9
Claims on households	3 942.0	4 116.9
Unclassified assets	809.8	785.1
Fixed assets	137.2	137.8
Items in transit	22.9	28.4
Other assets	105.5	112.3
Claims on resident MFIs (incl. investments)	544.2	506.7
<b>Total assets</b>	<b>14 772.2</b>	<b>15 155.7</b>
<i>Memo item: Trust assets</i>	<i>455.0</i>	<i>445.2</i>
Overnight deposits in lats	1 624.0	1 645.0
Public non-financial corporations	138.2	97.8
Financial institutions and private non-financial corporations	648.5	690.3
Households	837.4	857.0
Time deposits and deposits redeemable at notice in lats	817.1	824.5
Public non-financial corporations	77.0	73.1
Financial institutions and private non-financial corporations	219.9	210.7
Households	520.2	540.6
Foreign currency deposits of residents	1 724.2	1 766.8
Public non-financial corporations	20.6	21.4
Financial institutions and private non-financial corporations	536.9	538.0
Households	1 166.7	1 207.4
Deposits of central government	56.9	66.3
Deposits of local government	164.5	177.3
Transit funds	4.6	4.4
Foreign liabilities	8 059.9	8 305.9
Liabilities to MFIs	4 808.0	5 098.7
Liabilities to non-MFIs	3 016.4	2 914.8
Other liabilities (incl. subordinated liabilities)	235.4	292.4
Liabilities to the Bank of Latvia	0	0
Debt securities issued	323.5	323.5
Money market fund shares and units	31.1	32.7
Capital and reserves	1 146.3	1 167.2
Residents	696.7	714.8
Non-residents	449.6	452.5
Provisions	91.0	98.5
Unclassified liabilities	729.1	743.6
Items in transit	133.7	166.7
Other liabilities (incl. subordinated liabilities)	98.4	114.2
Liabilities to resident MFIs	497.1	462.7
<b>Total liabilities</b>	<b>14 772.2</b>	<b>15 155.7</b>
<i>Memo item: Trust liabilities</i>	<i>455.0</i>	<i>445.2</i>

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>).