

MONETARY BULLETIN 2006

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The situation in the Latvian economy has remained broadly unchanged, with the domestic demand still the key driver of growth. Inflation continued to soar in Latvia. With consumer prices picking up 0.3% against November, the annual inflation rose to 6.8% in December, at 6.5% for the year on average. The largest contributors to price movements in December were increases in vegetable, bread and public catering prices and a drop in telecommunication service prices. Year-on-year, the seasonally adjusted volume index of industrial output grew by mere 0.7% (including a 1.9% rise in the respective index for manufacturing). The volume of freight transportation by rail kept on shrinking in December (by 16.4%), with a corresponding year-on-year contraction in cargo turnover at Latvian ports (by 15.1%) and in oil product transportation by pipeline (by 19.3%). Retail trade was still developing buoyantly (a 32.4% rise in turnover at constant prices). Overall, the economic growth remained unbalanced, with the high domestic demand putting pressure on imports.

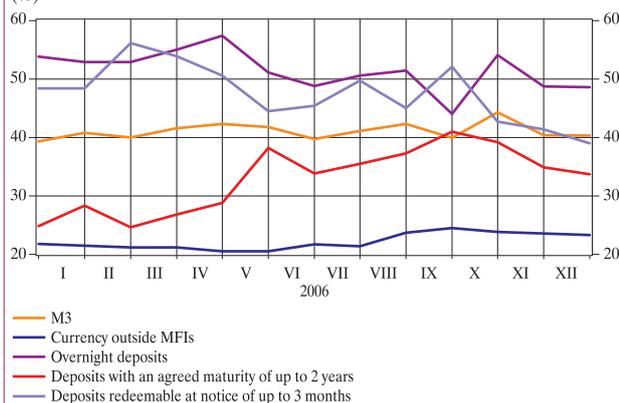
The number of unemployed persons diminished in December, bringing the unemployment rate down to 6.5%.

In December, government expenditure rose sharply, and the financial deficit of the general government consolidated budget surged to 333.7 million lats; in 2006 overall, the financial deficit was 98.6 million lats (113.3 million lats in the previous year overall). The central government basic budget and the local government consolidated budget posted sizeable financial deficits in December, whereas the social security budget continued to record a financial surplus. The general government consolidated budget revenue increased by 27.8% year-on-year. This increase was underpinned by a boost in tax revenue (34.1%), while the revenue from value added tax decelerated (to 27.0%) but that in the revenues from direct taxes and social security contributions accelerated (to 42.1% and 38.9% respectively). Budget expenditure grew by 40.0% on account of increased wages and salaries of the employees (by 50.8%), more costly services and material purchases (by 43.8%), expanding social benefits (by 62.6%), and rising capital investment expenditure (by 49.9%).

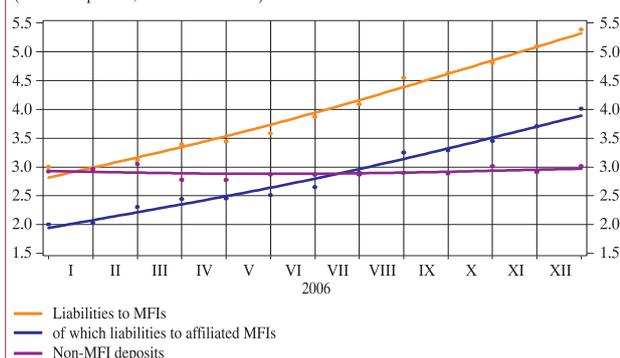
Total debt of the general government (1 115.1 million lats at the end of December) picked up 6.3 million lats month-on-month as a result of an issue of 5-year government bonds. In December, a competitive multi-price auction of these bonds was held on the primary market where securities in the amount of 16.0 million lats were sold at the weighted average yield of 5.237% (11 basis points above the yield of the previous auction).

In December, the increase in broad money M3 was steep due to seasonal factors, with resident deposits increasing substantially and the demand for cash surging. However, the annual growth rate of M3 was broadly unchanged (40.3%) and that of overnight deposits (48.6%) did not deviate much from its November level. At the same time, the growth in deposits with agreed maturity of up to 2 years decelerated from 34.9% in November to 33.7% in December, in deposits redeemable at notice declined from 41.4% to 39.0%, and in currency outside MFIs dropped from 23.6% to 23.3% respectively. The annual growth in monetary aggregates M1 and M2 was 41.7% and 39.7% respectively in December.

THE ANNUAL GROWTH RATE OF BROAD MONEY M3 AND ITS COMPONENTS (%)



CHANGES IN THE MAIN COMPONENTS OF FOREIGN LIABILITIES OF MFIs (EXCLUDING BANK OF LATVIA)
(at end of period; in billions of lats)



With the annual growth rate of deposits in euro decelerating (by 6.0 percentage points; to 65.7%) and the corresponding indicator for deposits in lats remaining broadly unchanged (39.6%), the annual rate of increase in deposits of resident financial institutions, non-financial corporations and households slowed in December by 0.7 percentage point (to 41.0%).

Despite a continued slow deceleration in the growth of loans to resident financial institutions, non-financial corporations and households (58.4% in December; the lowest indicator since September 2005) due to the high basis, lending did not change much in terms of volume and trends. With the annual rate of increase in industrial credit becoming faster, the growth rate of business loans picked up 0.2 percentage point (increasing to 47.0%). A moderate annual acceleration in loans to households for house purchase (to 86.4%) and in consumer credit (to 63.5%) notwithstanding, in December the annual growth rate of loans to households declined by 1.2 percentage points (to 75.5%). Loans granted in euro (a pickup of 379.5 million lats; the annual growth rate of 97.5%) still accounted for almost the entire increase in lending, whereas loans in lats increased only slightly (a pickup of 29.5 million lats; the annual growth rate of 21.5%).

In December, borrowing from abroad continued, and the negative net foreign assets of MFIs (excluding the Bank of Latvia) grew by 245.5 million lats.

With the government budget expenditure rising steeply in the last month of the year, government deposits with banks shrank sharply, and the banking system's net credit to general government increased by 264.4 million lats.

Interest rates on loans to non-financial corporations and on loans to households in foreign currency continued to rise in December, whereas those on loans to households granted in lats declined slightly.

With bank excess liquidity persisting, the overnight RIGIBOR remained low within the range of 2.33%–2.89%. In the course of the month, RIGIBOR on 3-, 6- and 12-month loans changed only by 1–3 basis points to stand at 4.20%, 4.83% and 5.18% respectively at the end of the period.

The central bank's lending facility was not used, and banks reduced their excess liquidity via time deposits with the Bank of Latvia in the amount of 135.3 million lats (3.3 times less than in November). Reflecting the sharply growing budget expenditure, government deposits with the Bank of Latvia shrank by 227.2 million lats in December. Time deposits of credit institutions contracted by 58.4 million lats, whereas bank demand deposits with the Bank of Latvia increased by 241.5 million lats. Cash in circulation grew by 50.1 million lats, and the annual growth in monetary base M0 accelerated by 14.1 percentage points (to 66.5%). The Bank of Latvia's net foreign assets grew by 1.3 million lats, and at the end of December the backing of the national currency with the Bank of Latvia's net foreign assets was 107.4%.

In December, the US dollar and the Japanese yen depreciated against the lats by 1.1% and 3.2% respectively, whereas the British pound sterling appreciated by 0.9%.

To protect depositors' interests, the Board of the Financial and Capital Market Commission at its extraordinary meeting on 21 December 2006 resolved to withdraw the license of the joint stock company *Ogres komercbanka* and to file an application for its liquidation with the Riga Regional Court. On 23 January 2007, the Riga Regional Court ruled to put the joint stock company *Ogres komercbanka* into liquidation.

MACROECONOMIC INDICATORS	2006	
	XI	XII
Changes in the volume index of industrial output (year-on-year basis; %)	0.7	*
Changes in the CPI		
Month-on-month basis (%)	1.0	0.3
Year-on-year basis (%)	6.4	6.8
Annual rate of core inflation ¹ (%)	5.5	5.8
Number of registered unemployed persons (at end of period)	69 705	68 944
Unemployment rate (%)	6.6	6.5
General government consolidated budget financial deficit/surplus (in millions of lats)	235.2	-98.6
Foreign trade (in millions of lats)		
Exports	287.6	*
Imports	591.2	*
Balance	-303.6	*

¹ 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	
	XI	XII
MFIs¹		
M3	5 210.5	5 506.8
Repurchase agreements	0	0
Money market fund shares and units	32.7	46.1
Debt securities issued with maturity of up to 2 years	4.9	4.8
M2	5 173.0	5 456.0
Deposits with agreed maturity of up to 2 years	1 198.1	1 241.9
Deposits redeemable at notice of up to 3 months	141.2	148.2
M1	3 833.7	4 065.8
Currency outside MFIs	921.3	969.3
Overnight deposits	2 912.4	3 096.5
Net external assets	-2 390.4	-2 634.7
Credit to resident financial institutions, non-financial corporations and households	9 323.3	9 722.9
Credit to general government	356.8	333.7
Deposits of central government	343.3	89.8
Longer-term financial liabilities	1 752.4	1 804.9
Bank of Latvia		
M0	1 957.2	2 248.8
Currency in circulation	1 023.8	1 073.9
Deposits with the Bank of Latvia in lats	933.4	1 174.9
Deposits with the Bank of Latvia in foreign currencies	0	0
Net foreign assets	2 413.1	2 414.4
Net domestic assets	-455.9	-165.6
Credit	-277.0	-49.8
To MFIs	0	0
To central government (net)	-277.0	-49.8
Other items (net)	-178.8	-115.8
International reserves (at end of period; in millions of US dollars)	4 460.39	4 509.60
Gold	157.18	156.10
Special Drawing Rights	0.16	0.16
Reserve position in the IMF	0.08	0.08
Foreign convertible currencies	4 302.97	4 353.26

¹In accordance with the methodology of the European Central Bank.

EXCHANGE RATES SET BY THE BANK OF LATVIA AND INTEREST RATES	2006	
	XI	XII
Weighted average interest rate on domestic interbank loans in lats	2.2	2.3
Interest rates on loans to resident non-financial corporations and households		
Loans to non-financial corporations (in lats)	6.4	6.8
Loans to households (in lats)	11.0	9.9
incl. for house purchase	7.0	6.9
Loans to non-financial corporations (in foreign currencies)	5.3	5.9
Loans to households (in foreign currencies)	5.6	5.7
incl. for house purchase	5.4	5.4
Interest rates on deposits of non-financial corporations and households		
Time deposits of non-financial corporations (in lats)	3.6	3.5
Demand deposits of non-financial corporations (in lats)	0.8	0.7
Time deposits of households (in lats)	3.7	3.9
Demand deposits of households (in lats)	0.5	0.5
Time deposits of non-financial corporations (in foreign currencies)	3.5	3.4
Demand deposits of non-financial corporations (in foreign currencies)	1.6	1.7
Time deposits of households (in foreign currencies)	3.7	3.9
Demand deposits of households (in foreign currencies)	1.3	1.4
The Bank of Latvia's refinancing rate (at end of period; %)	5.0	5.0
Exchange rates of foreign currencies (at end of period)		
LVL/USD	0.5420	0.5360
LVL/GBP	1.0390	1.0480
LVL/100 JPY	0.4660	0.4510
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	
	XI	XII
MFI reserves	1 134.6	1 316.8
Vault cash in national currency	102.5	104.5
Deposits with the Bank of Latvia	1 032.1	1 212.3
Foreign assets	3 502.4	3 625.8
Vault cash in foreign currencies	56.2	65.1
Claims on MFIs	2 032.0	2 160.0
Claims on non-MFIs	1 359.7	1 353.6
Other assets	54.5	47.1
Claims on central government	263.1	259.0
Claims on local government	93.8	74.7
Claims on public non-financial corporations	113.0	114.5
Claims on financial institutions and private non-financial corporations	5 146.9	5 359.2
Claims on households	4 116.9	4 303.2
Unclassified assets	785.1	814.8
Fixed assets	137.8	133.9
Items in transit	28.4	16.0
Other assets	112.3	111.1
Claims on resident MFIs (incl. investments)	506.7	553.8
Total assets	15 155.7	15 867.9
<i>Memo item: Trust assets</i>	445.2	432.2
Overnight deposits in lats	1 645.0	1 804.1
Public non-financial corporations	97.8	115.6
Financial institutions and private non-financial corporations	690.3	775.6
Households	857.0	912.8
Time deposits and deposits redeemable at notice in lats	824.5	846.8
Public non-financial corporations	73.1	73.7
Financial institutions and private non-financial corporations	210.7	214.8
Households	540.6	558.4
Foreign currency deposits of residents	1 766.8	1 859.7
Public non-financial corporations	21.4	25.9
Financial institutions and private non-financial corporations	538.0	603.3
Households	1 207.4	1 230.6
Deposits of central government	66.3	40.0
Deposits of local government	177.3	143.4
Transit funds	4.4	4.4
Foreign liabilities	8 305.9	8 674.8
Liabilities to MFIs	5 098.7	5 388.4
Liabilities to non-MFIs	2 914.8	3 016.8
Other liabilities (incl. subordinated liabilities)	292.4	269.6
Liabilities to the Bank of Latvia	0	0
Debt securities issued	323.5	319.8
Money market fund shares and units	32.7	46.1
Capital and reserves	1 167.2	1 212.7
Residents	714.8	758.0
Non-residents	452.5	454.7
Provisions	98.5	92.8
Unclassified liabilities	743.6	823.3
Items in transit	166.7	199.2
Other liabilities (incl. subordinated liabilities)	114.2	117.9
Liabilities to resident MFIs	462.7	506.3
Total liabilities	15 155.7	15 867.9
<i>Memo item: Trust liabilities</i>	445.2	432.2

Note. Due to the exclusion from the List of MFIs of the Republic of Latvia of the joint stock company Ogres komercbanka, the respective indicators are not included in monetary and financial statistics published by the Bank of Latvia as of December 2006.

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>).