

# MONETARY BULLETIN 2008

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In February, the economic developments in Latvia were indicative of a continuous decrease in the domestic demand and slowdown in growth. The rate of GDP growth moderated, reaching 8.0% in the fourth quarter, a low since the first quarter of 2005, and the growth became more balanced. With the increase in the domestic demand subsiding, the growth rate of exports of goods and services expanding considerably and that of imports declining, the contribution of net exports to the GDP was positive in the fourth quarter.

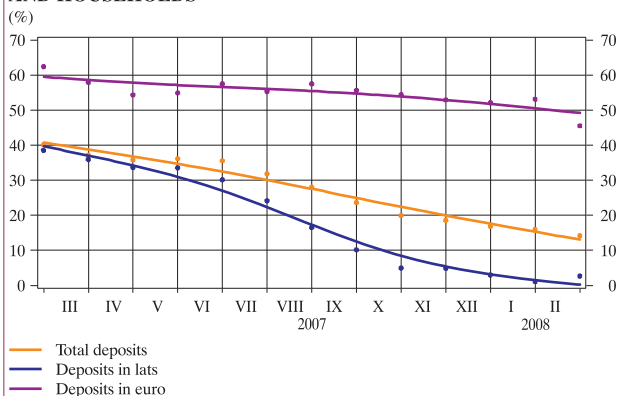
Retail trade continued to develop along the same trends as in the previous months. In January, the retail trade (including sales of motor vehicles and automotive fuel retailing) turnover dropped by 1.3%, suggesting a fall in private consumption. In January, the output in manufacturing decreased by 3.8%. The economic activity was contained by the moderating lending growth (the annual rate of increase in domestic loans fell below 30% for the first time since July 2000). In the central government budget, tax revenue dynamics also suggested a downward trend. In February, freight transportation by rail increased by 14.8%; the freight turnover at Latvian ports also expanded (by 16.7%).

With the supply side effects (particularly on account of administrative decisions) increasing, consumer prices rose by 1.3% in February. The annual inflation reached 16.7% and the 12-month average annual inflation (the harmonised index of consumer prices) stood at 11.6%. Consumer prices were particularly affected by a rise in the administrative prices. Heating tariffs and housing expenditure posted a month-on-month rise of 5.2%. An increase in excise tax rates for tobacco products accounted for a 10.2% upswing in their prices. Food product prices, especially those of milk and dairy products and eggs, also continued to rise.

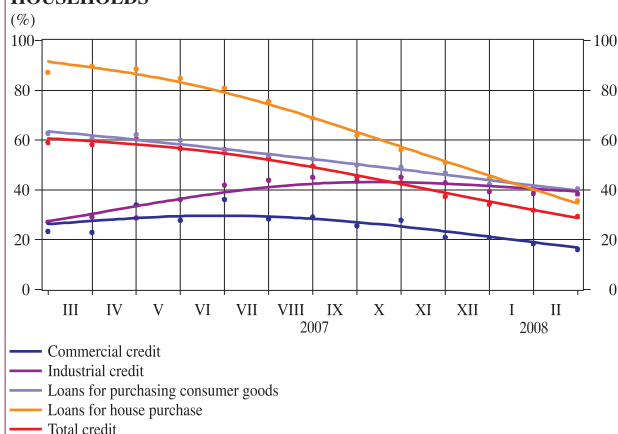
In February, the financial surplus of the general government consolidated budget was 13.6 million lats. Financial surpluses were recorded in the social security fund and local government consolidated budget (33.1 million lats and 7.8 million lats respectively), and the central government basic budget posted a deficit of 28.4 million lats. The general government consolidated budget revenue and expenditure picked up 25.1% and 17.2%, respectively. Revenue expanded on account of a 25.5% rise in tax revenue, with the excise tax revenue recording a particularly rapid surge of 66.7% as a result of an increase in the tax rate. The value added tax revenue grew at a relatively slow rate of 8.6% as a result of a decrease in private consumption. In the first two months of 2008, the financial surplus of the general government consolidated budget totalled 105.6 million lats (141.1 million lats in the corresponding period of 2007). In February, the central government and local government debt shrank by 15.5 million lats totalling 1 129.7 million lats at the end of the month.

In February, the annual growth of monetary aggregates continued on its downward path, with money supply also posting a slight decline. Broad money M3 contracted by 23.3 million lats, with its annual rate of increase declining by 1.4 percentage points (to 11.9%). Intermediate monetary aggregate M2 decreased by 28.2 million lats, recording an 11.5% year-on-year growth. Narrow monetary aggregate M1 shrank by 90.9 million lats, posting a 7.5% year-on-year fall. The decrease in the overnight deposits, which form part of broad money, was still partly offset by an increase in the deposits with an agreed maturity and deposits redeemable at notice, driven by the relatively high interest rates. Overnight deposits dropped by 7.1%

ANNUAL CHANGES IN DEPOSITS OF RESIDENT FINANCIAL INSTITUTIONS, NON-FINANCIAL CORPORATIONS AND HOUSEHOLDS



### ANNUAL CHANGES IN LOANS TO RESIDENT FINANCIAL INSTITUTIONS, NON-FINANCIAL CORPORATIONS AND HOUSEHOLDS



year-on-year. The annual rate of increase in deposits with an agreed maturity of up to 2 years and those redeemable at a period of notice of up to 3 months remained vigorous at 53.7% and 118.7% respectively.

In February, household deposits both in lats and in euro increased by 32.0 million lats and 14.3 million lats respectively. Deposits of financial institutions and non-financial corporations in lats did not post significant changes while those in euro decreased. Overall the annual growth rate of household deposits declined to 10.0% and that of financial institutions and non-financial corporations fell to 21.0%.

Although in February loans granted to financial institutions, non-financial corporations and households posted a slightly higher increase than in January, the annual lending growth moderated by 2.5 percentage points (to 29.3%). Loans granted to non-financial corporations recorded a slightly higher increase than those granted to households (90.7 million lats and 79.8 million lats respectively). The annual growth of all major types of loans slowed down, with loans for house purchase and commercial credit demonstrating the steepest drop (to 35.6% and 16.0% respectively), while industrial credit and loans to households for consumption purposes declined somewhat (to 38.3% and 40.4% respectively). Loans granted in lats continued to decrease (by 43.1 million lats, to 12.5% of total loans).

In February, funding from foreign banks continued to grow modestly (by 21.9 million lats, including an increase of 24.2 million lats from parent banks). The negative net foreign assets of MFIs grew by 180.2 million lats, with the decrease in MFI foreign assets exceeding that of foreign liabilities.

In February, the demand for cash gradually rebounded. Currency in circulation expanded by 10.7 million lats, with its annual rate of change nevertheless remaining negative (-6.0%). Banks' overnight deposits with the Bank of Latvia shrank, and the monetary base M0 recorded a drop of 17.1 million lats. The central bank's money supply decreased on account of a 25.0 million lats fall in loans granted to banks and the net result of the Bank of Latvia's foreign exchange operations as the decrease in the currency swaps exceeded the foreign currency purchased in spot transactions; though positive contribution to money supply was made by a 40.4 million lats drop in the Government deposit with the Bank of Latvia. The Bank of Latvia's net foreign assets contracted by 15.8 million lats or 0.6%. At the end of February, the backing of the national currency with the Bank of Latvia's net foreign assets was 115.6%.

In February, RIGIBOR for loans with longer maturity continued to follow a downward trend. At the end of February, RIGIBOR on 3-month loans stood at 7.09%, posting a 99 basis point month-on-month decline. RIGIBOR on 6-month loans fell by 110 basis points, to 8.27% and 1-year RIGIBOR rate dropped by 28 basis points, to 10.04%. At the beginning and in the middle of the month, overnight RIGIBOR was relatively high (5.9%-7.6%), declining only at the beginning of the minimum reserve maintenance period to 3.7%. Hence, the average overnight RIGIBOR (5.90%) was 146 basis points higher than in January.

In February, the weighted average interest rates on loans to households for house purchase granted in lats and foreign currency moved down by 0.2 percentage point to 10.2% and 6.1% respectively, whereas those on loans granted to non-financial corporations edged up somewhat. Under adequate liquidity conditions, banks considerably reduced the interest rates on deposits made by non-financial corporations and households in lats while those on deposits in foreign currency posted a slight decrease.

In February, the exchange rate of the US dollar, the British pound sterling and the Japanese yen set by the Bank of Latvia depreciated against the lats by 2.3%, 2.5% and 1.8% respectively.

MACROECONOMIC INDICATORS	2008	
	I	II
Changes in the seasonally adjusted volume index of industrial output (year-on-year basis; working-day-adjusted; %)	0.5	*
Changes in the CPI		
Month-on-month basis (%)	2.8	1.3
Average annual inflation rate (HCPI) of last 12 months (%)	10.8	11.6
Year-on-year basis (%)	15.8	16.7
Annual rate of core inflation <sup>1</sup> (%)	15.2	15.8
Number of registered unemployed persons (at end of period)	53 325	53 429
Unemployment rate (%)	5.0	5.0
General government consolidated budget financial deficit/surplus (in millions of lats)	92.1	105.6
Foreign trade (in millions of lats)		
Exports	330.7	*
Imports	578.2	*
Balance	-247.5	*

<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)	2008	
	I	II
<b>MFIs<sup>1</sup></b>		
<b>M3</b>	6 270.5	6 247.2
Repurchase agreements	0	0
Money market fund shares and units	48.4	52.7
Debt securities issued with maturity of up to 2 years	29.2	29.8
<b>M2</b>	6 192.9	6 164.7
Deposits with agreed maturity of up to 2 years	2 086.3	2 142.7
Deposits redeemable at notice of up to 3 months	336.9	343.2
<b>M1</b>	3 769.7	3 678.8
Currency outside MFIs	850.2	852.4
Overnight deposits	2 919.5	2 826.4
Net external assets	-4 640.3	-4 820.5
Credit to resident financial institutions, non-financial corporations and households	13 169.4	13 368.3
Credit to general government	309.6	299.8
Deposits of central government	259.7	259.2
Longer-term financial liabilities	2 403.7	2 440.2
<b>Bank of Latvia</b>		
<b>M0</b>	2 432.2	2 415.1
Currency in circulation	958.9	969.6
Deposits with the Bank of Latvia in lats	1 466.0	1 439.2
Deposits with the Bank of Latvia in foreign currencies	7.3	6.2
Net foreign assets	2 807.0	2 791.2
Net domestic assets	-374.8	-376.1
Credit	-203.6	-188.1
To MFIs	25.0	0
To central government (net)	-228.6	-188.1
Other items (net)	-171.2	-188.0
International reserves (at end of period; in millions of euro)	3 997.73	3 913.28
Gold	155.18	157.49
Special Drawing Rights	0.12	0.12
Reserve position in the IMF	0.06	0.06
Foreign convertible currencies	3 842.37	3 755.61
International reserves (at end of period; in millions of US dollars)	5 902.55	5 914.55
Gold	229.12	238.03
Special Drawing Rights	0.17	0.18
Reserve position in the IMF	0.09	0.09
Foreign convertible currencies	5 673.17	5 676.25

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

EXCHANGE RATES SET BY THE BANK OF LATVIA AND INTEREST RATES	2008	
	I	II
Weighted average interest rate on domestic interbank loans in lats	4.0	5.2
Interest rates on loans to resident non-financial corporations and households		
Loans to non-financial corporations (in lats)	7.9	8.7
Loans to households (in lats)	18.3	18.4
incl. for house purchase	10.5	10.2
Loans to non-financial corporations (in foreign currencies)	6.6	6.7
Loans to households (in foreign currencies)	6.5	6.3
incl. for house purchase	6.3	6.1
Interest rates on deposits of non-financial corporations and households		
Time deposits of non-financial corporations (in lats)	7.2	5.5
Demand deposits of non-financial corporations (in lats)	2.4	1.4
Time deposits of households (in lats)	8.4	7.6
Demand deposits of households (in lats)	0.6	0.9
Time deposits of non-financial corporations (in foreign currencies)	3.9	3.8
Demand deposits of non-financial corporations (in foreign currencies)	1.6	1.7
Time deposits of households (in foreign currencies)	4.4	4.2
Demand deposits of households (in foreign currencies)	1.7	1.6
The Bank of Latvia's refinancing rate (at end of period; %)	6.0	6.0
Exchange rates of foreign currencies (at end of period)		
LVL/USD	0.4760	0.4650
LVL/GBP	0.9470	0.9230
LVL/100 JPY	0.4460	0.4380
LVL/EUR	0.7028	0.7028

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

	2008	
	I	II
MFI reserves	1 568.0	1 564.9
Vault cash in national currency	108.7	117.2
Deposits with the Bank of Latvia	1 459.3	1 447.7
Foreign assets	5 041.8	4 649.3
Vault cash in foreign currencies	62.0	60.8
Claims on MFIs	3 178.3	2 775.9
Claims on non-MFIs	1 727.7	1 737.8
Other assets	73.9	74.8
Claims on central government	249.0	239.3
Claims on local government	60.6	60.5
Claims on public non-financial corporations	252.8	260.5
Claims on financial institutions and private non-financial corporations	6 936.9	7 046.6
Claims on households	6 040.6	6 120.4
Unclassified assets	983.3	1 010.7
Fixed assets	178.1	181.9
Items in transit	29.4	26.2
Other assets	175.8	185.7
Claims on resident MFIs (incl. investments)	600.1	616.9
<b>Total assets</b>	<b>21 133.0</b>	<b>20 952.3</b>
<i>Memo item: Trust assets</i>	283.6	318.8
Overnight deposits in lats	1 554.4	1 537.5
Public non-financial corporations	95.8	104.2
Financial institutions and private non-financial corporations	708.9	667.5
Households	749.7	765.8
Time deposits and deposits redeemable at notice in lats	1 119.8	1 174.2
Public non-financial corporations	185.9	191.5
Financial institutions and private non-financial corporations	311.7	344.5
Households	622.2	638.1
Foreign currency deposits of residents	2 574.6	2 512.1
Public non-financial corporations	40.7	38.9
Financial institutions and private non-financial corporations	799.2	742.3
Households	1 734.7	1 730.8
Deposits of central government	31.1	71.1
Deposits of local government	222.4	225.7
Transit funds	4.0	4.0
Foreign liabilities	12 489.1	12 261.0
Liabilities to MFIs	8 001.4	8 023.3
Liabilities to non-MFIs	4 163.2	3 862.3
Other liabilities (incl. subordinated liabilities)	324.5	375.4
Liabilities to the Bank of Latvia	25.0	0
Debt securities issued	317.8	318.9
Money market fund shares and units	48.4	52.7
Capital and reserves	1 772.3	1 797.7
Residents	1 027.1	1 052.5
Non-residents	745.2	745.2
Provisions	120.1	124.5
Unclassified liabilities	854.1	873.0
Items in transit	142.7	145.6
Other liabilities (incl. subordinated liabilities)	180.3	178.8
Liabilities to resident MFIs	531.1	548.6
<b>Total liabilities</b>	<b>21 133.0</b>	<b>20 952.3</b>
<i>Memo item: Trust liabilities</i>	283.6	318.8

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>).