

# MONETARY BULLETIN 2009

## 12

Despite the still difficult overall macroeconomic situation in the country, positive developments primarily associated with the growing business competitiveness and progressively recovering demand in the majority of external markets continued to surface. In November, the positive shifts in the foreign trade balance and the current account of Latvia's balance of payments were accompanied by the growth in manufacturing. According to seasonally adjusted data, the volume index of industrial output in manufacturing recorded a month-on-month increase of 11.6%. At the same time year-on-year, production contracted notably by 2.6% (working day adjusted data). Following the approval of 2010 budget, monetary aggregates got a positive impetus from easing uncertainty surrounding the future economic outlook and a number of seasonal factors (a rise in public expenditure toward the year's end and attractive interest rates in December).

Consumer prices, underpinned by lower personal income and contracting business costs, declined further in December, recording 0.5% and 1.2% drops month-on-month and year-on-year respectively. Annual consumer price core inflation slid down to -2.0%. While annual deflation was recorded for the third consecutive month, the 2009 average annual inflation remained positive, at 3.5%, whereas the average 12-month growth in HICP, an indicator for the Maastricht criterion, dropped to 3.3%. The prices for clothing and footwear, fuel and food products as well as certain services (housing related and catering) declined markedly in December. In the meantime, administered prices exerted an upward impact on inflation in December primarily due to rising health services prices.

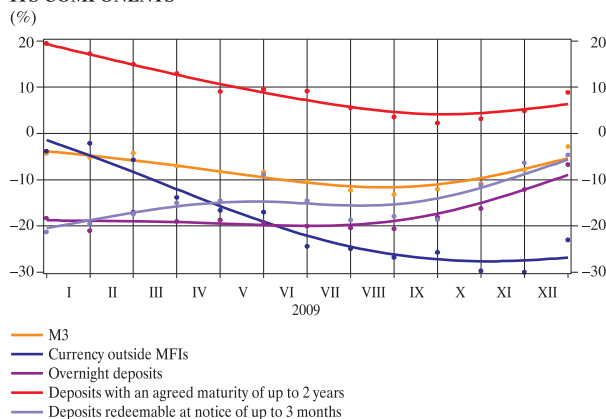
Low domestic demand was a driver behind a further contraction in retail trade whose seasonally adjusted turnover in November shrank by 2.3% month-on-month and 30.2% year-on-year.

In December, Latvia's freight transportation indicators worsened. Freight traffic by rail narrowed by 13.2% year-on-year as a result of contracting transit via Latvian ports. Total freight turnover at Latvian ports decreased by 10.1%. Unemployment soared, standing at 16.0% at the end of December.

In December, the general government consolidated budget recorded a high-level deficit of 304.0 million lats, amounting to 892.1 million lats for 2009 overall. Deficits were registered for all budget levels both in December and the entire 2009. The ongoing downward trend in tax revenue (23.3%) in December triggered a year-on-year drop also in the overall revenue (22.9%). The reductions were most pronounced for corporate income tax, personal income tax and value added tax, 50.1%, 33.3% and 18.5% respectively. Budget expenditure plummeted year-on-year by 6.7% in December and 10.0% in 2009 overall. The largest contribution to December drop came from cuts in compensation of employees and capital expenditure, whereas subsidies and grants grew. The general government debt in December expanded by 25.1 million lats primarily as a result of a Treasury bill issue, and amounted to 4 265.1 million lats.

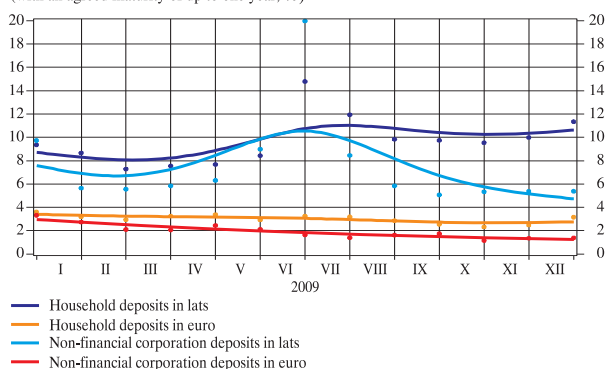
Money supply continued on an upward trend in December, with monetary aggregate M3 picking up 3.9%. The rise of

**THE ANNUAL GROWTH RATE OF BROAD MONEY M3 AND ITS COMPONENTS**



### INTEREST RATES ON DEPOSITS FROM RESIDENTS

(with an agreed maturity of up to one year; %)



4.6% in domestic deposits, with deposits in lats going up significantly and those in euro moderately, had a decisive upward effect on broad money. Deposits by households as well as financial institutions and non-financial corporations recorded a similar increase of 4.5% and 4.7% respectively. Non-resident non-MFI deposits grew at an even faster month-on-month pace (by 7.6%). The increase in domestic deposits in December was the sharpest over two last years, thus a positive annual growth rate of 1.7% was registered for the first time since October 2008, including an 8.9% growth in deposits with an agreed maturity of up to 2 years. Due to seasonal factors currency outside MFIs increased notably (by 4.3%).

Lending to the private sector continued to contract in December (by 1.5%), reflecting banks' prudent lending stances in the circumstances of deteriorating credit portfolio quality and a weak demand for loans. Commercial credit to businesses diminished, contractions in housing loans and consumer credit to households remained moderate, while the industrial credit portfolio was stable.

As a result of syndicated loan repayments, banking sector's liabilities to foreign banks diminished by 144.9 million lats despite slightly growing borrowings from parent banks abroad. With banks opting for investing the attracted funds abroad (banking sector's foreign assets were 8.9% up month-on-month), the negative net foreign assets of MFIs (except the Bank of Latvia) contracted by 336.1 million lats in December.

The monetary base M0 decreased in December by 83.4 million lats even though the demand for cash went up steeply due to seasonal factors. At the end of the year, the monetary base diminished as a result of banks resorting to the deposit facility with the Bank of Latvia in the context of excess liquidity, while the bank demand deposits with the Bank of Latvia shrank simultaneously. Net foreign assets of the central bank in December contracted by 24.9 million lats or 0.7%, whereas the backing of the national currency with the Bank of Latvia's net foreign assets was 201.3% at the end of the month. The slight decrease in the Bank of Latvia net reserves was on account of its expanding foreign liabilities, primarily resulting from larger European Commission funds with the central bank. A decrease in the government deposit in lats with the Bank of Latvia had an upward impact on the monetary base.

Liquidity of the banking sector had been ample over several months, and the interbank market interest rates eased notably, coming closer to the ones set by the Bank of Latvia. RIGIBOR on overnight loans went down on average to 1.46% in December (1.80% in November). Longer term (3-, 6-, and 12-month) RIGIBOR recorded an even steeper fall to 6.8%, 8.8%, and 10.7% at the end of December respectively (9.5%, 12.0%, and 13.1% at the end of November respectively). Such money market interest rate drops pressed down interest rates on loans in lats, with the average weighted interest rate on loans to households declining by 0.8 percentage point, to 12.2%, of which that on loans for house purchase was down to 9.1%; at the same time, the average weighted interest rate on loans to non-financial corporations decreased by 5.4 percentage points, to 6.7%. Interest rates on loans in foreign currencies to non-financial corporations were also down. Meanwhile, as banks engaged in attracting domestic funding more actively, deposit interest rates increased significantly, and the average weighted interest rate on household time deposits in lats reached 11.4%.

In December, the exchange rate of the US dollar and the British pound sterling set by the Bank of Latvia against the lats appreciated by 3.8% and 1.3%, whereas that of the Japanese yen depreciated by 2.6%.

MACROECONOMIC INDICATORS	2009	
	XI	XII
Volume index of industrial output (working-day adjusted annual rate of change; %)	-2.4	*
Changes in the CPI		
Month-on-month basis (%)	-0.7	-0.5
Average annual inflation rate (HCPI) of last 12 months (%)	4.5	3.5
Year-on-year basis (%)	-1.2	-1.2
Annual rate of core inflation <sup>1</sup> (%)	-1.6	-2.0
Number of registered unemployed persons (at end of period)	169 236	179 235
Unemployment rate (%)	15.1	16.0
General government consolidated budget financial deficit/surplus (in millions of lats)	-588.1	-892.1
Foreign trade (in millions of lats)		
Exports	323.3	*
Imports	390.9	*
Balance	-67.6	*

<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)	2009	
	XI	XII
<b>MFIs<sup>1</sup></b>		
M3	5 654.3	5 873.1
Repurchase agreements	0	0
Money market fund shares and units	85.6	76.1
Debt securities issued with maturity of up to 2 years	0.9	0.9
M2	5 567.9	5 796.2
Deposits with agreed maturity of up to 2 years	2 411.8	2 565.2
Deposits redeemable at notice of up to 3 months	253.4	251.6
M1	2 902.6	2 979.3
Currency outside MFIs	639.6	667.3
Overnight deposits	2 263.1	2 312.0
Net external assets	-3 333.2	-3 021.6
Credit to resident financial institutions, non-financial corporations and households	13 718.8	13 514.9
Credit to general government	580.8	590.8
Deposits of central government	2 140.2	1 932.2
Longer-term financial liabilities	2 106.7	2 224.4
<b>Bank of Latvia</b>		
M0	1 729.2	1 645.8
Currency in circulation	739.5	788.2
Deposits with the Bank of Latvia in lats	942.3	837.7
Deposits with the Bank of Latvia in foreign currencies	47.4	19.9
Net foreign assets	3 338.0	3 313.1
Net domestic assets	-1 608.8	-1 667.3
Credit	-1 350.8	-1 151.5
To MFIs	145.2	140.4
To central government (net)	-1 496.0	-1 291.9
Other items (net)	-258.0	-515.8
International reserves (at end of period; in millions of euro)	4 804.51	4 805.37
Gold	195.31	191.18
Special Drawing Rights	130.53	129.82
Reserve position in the IMF	0.06	0.06
Foreign convertible currencies	4 478.61	4 484.31
International reserves (at end of period; in millions of US dollars)	7 169.07	6 906.44
Gold	291.43	274.78
Special Drawing Rights	194.78	186.58
Reserve position in the IMF	0.09	0.09
Foreign convertible currencies	6 682.77	6 444.99

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

EXCHANGE RATES SET BY THE BANK OF LATVIA AND INTEREST RATES	2009	
	XI	XII
Weighted average interest rate on domestic interbank loans in lats	1.4	1.4
Interest rates on loans to resident non-financial corporations and households		
Loans to non-financial corporations (in lats)	12.1	6.7
Loans to households (in lats)	13.0	12.2
incl. for house purchase	9.9	9.1
Loans to non-financial corporations (in foreign currencies)	5.0	4.2
Loans to households (in foreign currencies)	5.2	5.8
incl. for house purchase	4.0	4.5
Interest rates on deposits of non-financial corporations and households		
Time deposits of non-financial corporations (in lats)	5.4	5.4
Demand deposits of non-financial corporations (in lats)	0.6	0.5
Time deposits of households (in lats)	10.2	11.4
Demand deposits of households (in lats)	1.0	1.1
Time deposits of non-financial corporations (in foreign currencies)	1.2	1.3
Demand deposits of non-financial corporations (in foreign currencies)	0.4	0.2
Time deposits of households (in foreign currencies)	2.5	3.1
Demand deposits of households (in foreign currencies)	0.8	0.8
The Bank of Latvia's refinancing rate (at end of period; %)	4.0	4.0
Exchange rates of foreign currencies (at end of period)		
LVL/USD	0.4710	0.4890
LVL/GBP	0.7730	0.7830
LVL/100 JPY	0.5470	0.5330
LVL/EUR	0.7028	0.7028

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

	2009	
	XI	XII
MFI reserves	1 084.3	1 233.0
Vault cash in national currency	99.9	120.8
Deposits with the Bank of Latvia	984.4	1 112.2
Foreign assets	4 458.3	4 854.9
Vault cash in foreign currencies	64.8	63.4
Claims on MFIs	2 643.6	2 983.3
Claims on non-MFIs	1 650.2	1 712.5
Other assets	99.7	95.7
Claims on central government	508.0	519.1
Claims on local government	72.8	71.8
Claims on public non-financial corporations	396.6	395.7
Claims on financial institutions and private non-financial corporations	7 369.3	7 195.0
Claims on households	6 121.0	6 088.2
Unclassified assets	1 031.3	943.5
Fixed assets	154.6	148.5
Items in transit	28.4	16.4
Other assets	451.8	460.4
Claims on resident MFIs (incl. investments)	396.6	318.2
<b>Total assets</b>	<b>21 041.6</b>	<b>21 301.1</b>
<i>Memo item: Trust assets</i>	<i>357.7</i>	<i>391.5</i>
Overnight deposits in lats	1 056.4	1 114.9
Public non-financial corporations	75.9	70.4
Financial institutions and private non-financial corporations	477.6	487.0
Households	502.8	557.5
Time deposits and deposits redeemable at notice in lats	1 067.9	1 171.3
Public non-financial corporations	209.5	201.6
Financial institutions and private non-financial corporations	352.7	426.4
Households	505.7	543.3
Foreign currency deposits of residents	2 803.2	2 866.8
Public non-financial corporations	52.8	50.6
Financial institutions and private non-financial corporations	1 008.9	1 044.2
Households	1 741.5	1 771.9
Deposits of central government	644.1	640.2
Deposits of local government	158.3	133.3
Transit funds	3.2	3.0
Foreign liabilities	11 129.5	11 189.7
Liabilities to MFIs	7 519.2	7 374.2
Liabilities to non-MFIs	3 030.7	3 261.7
Other liabilities (incl. subordinated liabilities)	579.6	553.8
Liabilities to the Bank of Latvia	145.2	140.4
Debt securities issued	153.2	153.5
Money market fund shares and units	85.6	76.1
Capital and reserves	1 506.4	1 624.7
Residents	478.8	392.8
Non-residents	1 027.6	1 231.8
Provisions	1 507.1	1 526.7
Unclassified liabilities	781.7	660.6
Items in transit	126.1	77.1
Other liabilities (incl. subordinated liabilities)	290.8	298.6
Liabilities to resident MFIs	364.8	284.9
<b>Total liabilities</b>	<b>21 041.6</b>	<b>21 301.1</b>
<i>Memo item: Trust liabilities</i>	<i>357.7</i>	<i>391.5</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>).