

# MONETARY BULLETIN 2009

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Although an overall economic recovery in Latvia could not be observed yet, certain macroeconomic stabilisation persisted: in the context of moderating external imbalances, the surplus of the current account of the balance of payments strengthened, inflation continued to abate, and some industries reported recovery. In September, the development trends of the monetary aggregates remained broadly unchanged as almost all aggregates continued to shrink slowly. The seasonal factors and decisions on job cuts, particularly in education, accounted for an increase in unemployment by 0.9 percentage point (to 13.2%). With tax revenue decreasing, the general government consolidated budget grew again in September.

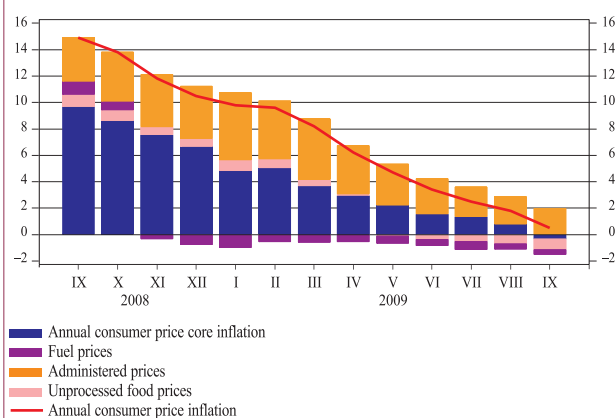
The weakening purchasing power of households, cost optimisation in corporate sector enabling sales price reduction, as well as price falls in the countries wherefrom Latvia imports part of goods supported easing of inflationary pressures. In September, consumer prices shrank by 0.2% month-on-month, with the consumer price annual inflation standing at 0.5%. The relatively insignificant drop in prices in September reflected the impact of seasonal factors on price dynamics rather than suggested a moderating impact of the contracting demand. As usual, new collections of footwear and clothing appeared in the shops as the new season set in, and prices of this group of goods rose by 6.8%. In September, tuition fees were traditionally raised as well (by 8.1%). The drop in food prices (1.3%) continued to have an easing effect on inflation. In September, the annual consumer price core inflation posted a further decline, entering negative territory (-0.4%, contributing -0.3 percentage point to the overall inflation). The 12-month average annual inflation and the harmonised index of consumer prices (HICP), used for the Maastricht criterion, also continued on a downward trend, nevertheless remaining relatively high (6.7% and 6.5% respectively).

In August, the seasonally adjusted industrial output in manufacturing grew by 2.5% month-on-month. The overall sectoral growth resulted from higher output in several sectors, particularly in the manufacture of wood and products of wood and cork, pharmaceutical preparations, other transport vehicles, and chemicals, chemical products and man-made fibres, supported by improvement in external demand and competitiveness. In September, rail freight fell by 9.4% year-on-year, whereas total cargo turnover at Latvian ports contracted by 13.5%.

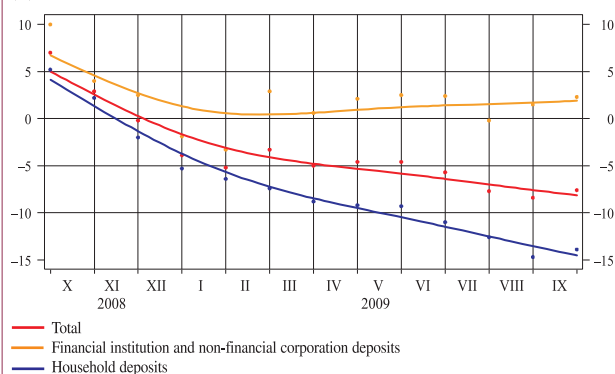
A more attractive price policy for consumers and improvements in consumer and business sentiment ratios notwithstanding, in August the retail trade turnover at constant prices shrank by 3.3% month-on-month and 30.3% year-on-year.

In September, the general government consolidated budget ran a deficit of 77.0 million lats (accrued to 493.7 million lats since the beginning of the year). The central government basic budget and social security budget as well as the local government consolidated budget recorded a deficit. The overall decrease in revenue reached 39.4% year-on-year, mostly on account of increasingly plummeting tax revenues (33.5%). The most pronounced declines were recorded for corporate income tax (by 67.6%), personal income tax (by 36.1%) and value added tax (by 35.3%). Social security contributions also contracted drastically (by 29.6%). At the same time, as the fiscal consolidation achieved as a result of the budgetary amendments made in June continued, the annual rate of

**ANNUAL CONSUMER PRICE INFLATION**  
(by component; in percentage points)



**ANNUAL CHANGES IN RESIDENT FINANCIAL INSTITUTION, NON-FINANCIAL CORPORATION AND HOUSEHOLD DEPOSITS (%)**



decrease in budget expenditure also accelerated (21.3% in September; 17.5% in August). The largest contribution to the expenditure decrease was on account of capital expenditure, compensation to employees and expenditure related to the purchase of goods and services (a fall of 46.5%, 32.3% and 32.5% respectively). In September, the general government debt shrank by 10.3 million lats (to 4 129.5 million lats).

The decrease in total loans resulted both from the particularly cautious lending policy caused by the complex overall financial situation and the low demand from the household and non-financial corporation sectors. In September, loans to resident financial institutions, non-financial corporations and households shrank by 40.8 million lats (the smallest monthly decrease since January), with the annual growth rate moving up by 1.2 percentage points (to -4.9%). In September, loans to households and non-financial corporations contracted somewhat while those granted to financial institutions expanded. Commercial loans slightly increased whereas loans for house purchase and consumer credit posted a fall. As in August, loans granted in lats continued on their downward trend while those granted in euro slowly moved up.

On account of the economic situation in Latvia the demand for the longer-term components of broad money continued to weaken moderately. In September, M3 and M2 shrank by 40.3 million lats and 52.7 million lats respectively. A pickup in overnight deposits accounted for a minor increase (1.3 million lats) in M1. However, the relatively small changes in money supply for the first time during the last seven months resulted in a lower annual rate of decrease in M3, M2 and M1 (12.0%, 11.6% and 19.9%). In September, demand for cash shrank somewhat and the fall in deposits in lats was considerably smaller than before (a mere 7.3 million lats; the household sector even posted an increase). Overnight deposits grew by 0.4% whereas deposits with an agreed maturity of up to 2 years shrank by 1.9%. The annual growth rate of deposits made by resident financial institutions, non-financial corporations and households improved (-7.6%).

In September, foreign funding provided to the banking sector posted a moderate decline. Liabilities to foreign banks decreased by 1.1%, with borrowings from affiliated banks contracting by 1.4%. Non-resident non-bank deposits also shrank (by 3.0%). The negative net foreign assets of MFIs (except the Bank of Latvia) contracted by 61.7 million lats in September.

With the lats liquidity conditions improving, as excess reserves were accrued and demand deposits with the Bank of Latvia grew, monetary base M0 in September increased by 31.0 million lats, with the annual rate of decrease of the monetary base M0 slowing down by 2.6 percentage points (to -31.9%). In September, the net foreign assets of the central bank grew by 50.9 million lats or 1.6%, and at the end of September the backing of the national currency with the Bank of Latvia's net foreign assets was 200.0%. The increase in the net foreign assets of the central bank resulted from the IMF SDR allocation as well as inflows of other foreign funding into the government accounts with the Bank of Latvia.

In September, the situation on the money market was stable, with RIGIBOR on overnight loans averaging 1.99% per month (2.83% in August). 6- and 12-month RIGIBOR fell by approximately one percentage point while 3-month RIGIBOR edged up somewhat.

In September, the exchange rate of the US dollar and the British pound sterling set by the Bank of Latvia against the lats depreciated by 2.0% and 4.0% respectively, while that of Japanese yen appreciated by 2.1%.

MACROECONOMIC INDICATORS	2009	
	VIII	IX
Volume index of industrial output (working-day adjusted annual rate of change; %)	-12.5	*
Changes in the CPI		
Month-on-month basis (%)	-1.0	-0.2
Average annual inflation rate (HCPI) of last 12 months (%)	7.9	6.7
Year-on-year basis (%)	1.8	0.5
Annual rate of core inflation <sup>1</sup> (%)	1.0	-0.4
Number of registered unemployed persons (at end of period)	137 586	147 754
Unemployment rate (%)	12.3	13.2
General government consolidated budget financial deficit/surplus (in millions of lats)	-416.7	-493.7
Foreign trade (in millions of lats)		
Exports	273.0	*
Imports	354.1	*
Balance	-81.1	*

<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	
	VIII	IX
<b>MFIs<sup>1</sup></b>		
M3	5 654.7	5 614.4
Repurchase agreements	0	0
Money market fund shares and units	65.6	78.8
Debt securities issued with maturity of up to 2 years	1.7	0.9
M2	5 587.4	5 534.7
Deposits with agreed maturity of up to 2 years	2 422.1	2 377.2
Deposits redeemable at notice of up to 3 months	270.2	261.0
M1	2 895.2	2 896.5
Currency outside MFIs	658.3	651.5
Overnight deposits	2 236.9	2 244.9
Net external assets	-3 683.8	-3 571.1
Credit to resident financial institutions, non-financial corporations and households	13 921.5	13 880.8
Credit to general government	685.8	663.9
Deposits of central government	2 221.2	2 244.3
Longer-term financial liabilities	2 224.7	2 165.8
<b>Bank of Latvia</b>		
M0	1 573.3	1 604.3
Currency in circulation	756.7	748.7
Deposits with the Bank of Latvia in lats	809.0	841.4
Deposits with the Bank of Latvia in foreign currencies	7.6	14.2
Net foreign assets	3 158.4	3 209.3
Net domestic assets	-1 585.2	-1 605.0
Credit	-1 323.5	-1 338.8
To MFIs	235.0	225.0
To central government (net)	-1 558.5	-1 563.8
Other items (net)	-261.7	-266.3
International reserves (at end of period; in millions of euro)	4 494.90	4 577.17
Gold	164.53	168.67
Special Drawing Rights	103.37	131.09
Reserve position in the IMF	0.06	0.06
Foreign convertible currencies	4 226.94	4 277.35
International reserves (at end of period; in millions of US dollars)	6 447.02	6 701.77
Gold	235.99	246.96
Special Drawing Rights	148.26	191.93
Reserve position in the IMF	0.09	0.09
Foreign convertible currencies	6 062.68	6 262.79

<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	
	VIII	IX
Weighted average interest rate on domestic interbank loans in lats	2.2	1.6
Interest rates on loans to resident non-financial corporations and households		
Loans to non-financial corporations (in lats)	10.6	17.9
Loans to households (in lats)	18.1	15.5
incl. for house purchase	8.4	8.6
Loans to non-financial corporations (in foreign currencies)	4.3	5.2
Loans to households (in foreign currencies)	5.5	5.8
incl. for house purchase	4.3	4.2
Interest rates on deposits of non-financial corporations and households		
Time deposits of non-financial corporations (in lats)	5.9	5.1
Demand deposits of non-financial corporations (in lats)	0.6	0.6
Time deposits of households (in lats)	9.9	9.8
Demand deposits of households (in lats)	0.9	1.0
Time deposits of non-financial corporations (in foreign currencies)	1.4	1.1
Demand deposits of non-financial corporations (in foreign currencies)	0.3	0.3
Time deposits of households (in foreign currencies)	2.7	2.5
Demand deposits of households (in foreign currencies)	0.9	0.9
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	0.4900	0.4800
LVL/GBP	0.7970	0.7650
LVL/100 JPY	0.5230	0.5340
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	
	VIII	IX
MFI reserves	911.1	949.1
Vault cash in national currency	98.4	97.1
Deposits with the Bank of Latvia	812.7	852.0
Foreign assets	4 622.7	4 587.0
Vault cash in foreign currencies	68.1	67.6
Claims on MFIs	2 719.3	2 685.0
Claims on non-MFIs	1 732.6	1 726.3
Other assets	102.8	108.1
Claims on central government	611.1	591.5
Claims on local government	74.7	72.3
Claims on public non-financial corporations	382.5	392.5
Claims on financial institutions and private non-financial corporations	7 491.1	7 469.9
Claims on households	6 211.8	6 185.9
Unclassified assets	944.4	942.5
Fixed assets	160.0	158.4
Items in transit	22.9	24.2
Other assets	394.0	417.8
Claims on resident MFIs (incl. investments)	367.4	342.1
<b>Total assets</b>	<b>21 249.3</b>	<b>21 190.8</b>
<i>Memo item: Trust assets</i>	<i>327.5</i>	<i>316.1</i>
Overnight deposits in lats	1 015.3	1 033.7
Public non-financial corporations	60.9	74.6
Financial institutions and private non-financial corporations	454.5	456.9
Households	499.8	502.1
Time deposits and deposits redeemable at notice in lats	1 060.5	1 034.7
Public non-financial corporations	175.1	180.3
Financial institutions and private non-financial corporations	378.0	348.0
Households	507.5	506.5
Foreign currency deposits of residents	2 838.3	2 803.4
Public non-financial corporations	43.8	29.1
Financial institutions and private non-financial corporations	1 008.4	1 005.6
Households	1 786.1	1 768.7
Deposits of central government	662.8	680.5
Deposits of local government	175.6	173.2
Transit funds	3.2	3.2
Foreign liabilities	11 465.0	11 367.5
Liabilities to MFIs	7 983.0	7 896.3
Liabilities to non-MFIs	3 002.1	2 910.7
Other liabilities (incl. subordinated liabilities)	479.8	560.5
Liabilities to the Bank of Latvia	235.0	225.0
Debt securities issued	157.7	157.0
Money market fund shares and units	65.6	78.8
Capital and reserves	1 615.8	1 549.7
Residents	704.1	535.3
Non-residents	911.7	1 014.4
Provisions	1 178.8	1 334.9
Unclassified liabilities	775.7	749.2
Items in transit	86.3	90.9
Other liabilities (incl. subordinated liabilities)	353.8	348.8
Liabilities to resident MFIs	335.6	309.4
<b>Total liabilities</b>	<b>21 249.3</b>	<b>21 190.8</b>
<i>Memo item: Trust liabilities</i>	<i>327.5</i>	<i>316.1</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>).