

# MONETARY BULLETIN 2005

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Following a more subdued rise during the summer, the growth rate of consumer prices picked up again in September, mainly as a result of the escalation of fuel prices. At the same time, the impact of structural changes (convergence of prices within the EU) and rapid economic growth persisted. In comparison with August, consumer prices increased by 1.5%, whereas the annual inflation reached 7.2%, which is consistent with the autumn 2004 inflation rate. The prices for fuel, clothing and footwear as well as catering services (an increase of 8.8%, 7.0% and 4.6%, respectively) were the most significant contributors to the price rise in September. The price escalation affected almost all groups of consumer goods. Only the prices for vegetables, potatoes and fruit decreased (by 8.6%).

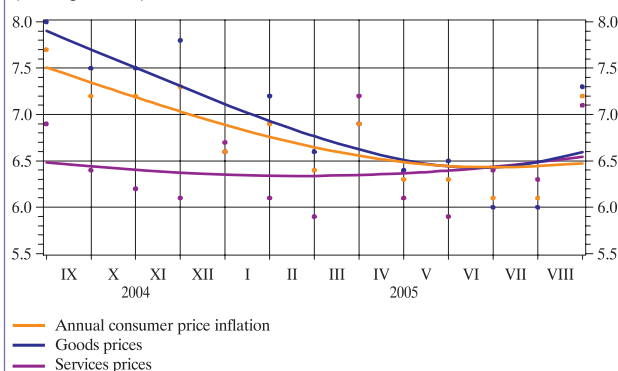
Buoyant economic growth continued. In August, the seasonally adjusted volume index of industrial output in manufacturing increased by 8.8%, whereas industry recorded a 6.8% growth year-on-year. Retail trade turnover increased even more significantly (by 22.6%). In September, freight turnover at rail grew 10.8% year-on-year, whereas cargo turnover at Latvian ports contracted by 5.6%. Unemployment rate declined by 0.1 percentage point (to 7.7%), and the number of unemployed persons registered with the State Employment Agency as at the end of September had decreased by 11.5% year-on-year.

In September 2005, the financial surplus of the general government consolidated budget amounted to 22.7 million lats, with the financial surplus accumulated from the beginning of the year reaching 172.6 million lats (2.5 times more year-on-year). This resulted from a surplus in the central government basic budget and social insurance budget, and only a slight deficit in the consolidated local government budget. In September, the general government consolidated budget revenue grew by 17.5%, whereas expenditure increased by 14.2% year-on-year. The rise in budget revenue was supported by a notable increase in tax collections (32.7%). The highest growth was recorded for revenue from social security contributions (41.8%) and value-added tax collections (27.4%). The increase in budget expenditure over September 2004 was underpinned by raising the childcare benefit in 2005, pension indexation, wage rise for medical staff and provision of co-financing for the EU funds. The EU funds co-financing underlay a significant expansion of public investment (1.9 times over September 2004).

At the end of September, Latvian central government and local government debt totalled 1 003.7 million lats. One auction of 6-month Treasury bills was held on the domestic government securities market in September. Bills in the amount of 4.0 million lats at the weighted average discount rate of 2.353% (47 basis points lower than at the previous auction held in May) were sold at a competitive multi-price auction on the primary market.

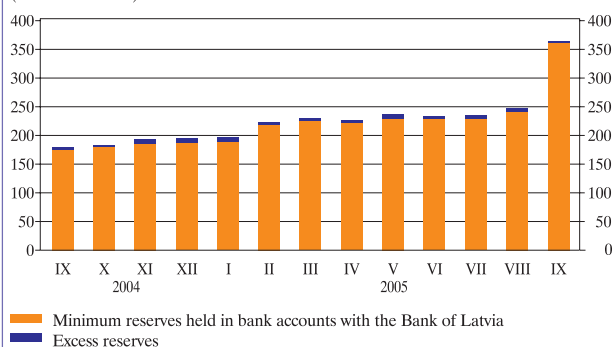
The strong domestic demand was facilitated by the active lending policies implemented by banks. In September, broad money M3 grew by 117.4 million lats. The increase was mainly driven by a rise in overnight deposits (95.1 million lats). Currency in circulation expanded insignificantly (by 9.9 million lats), whereas the deposits with an agreed maturity of up to 2 years and deposits redeemable at notice of up to 3 months grew by 9.6 million lats and 4.2 million lats, respectively. Therefore, the annual growth rate of all money supply aggregates (M1, M2 and M3) accelerated notably (by 4.1 percentage points; to 37.7%, 33.6% and 34.1%, respectively).

**CHANGES IN ANNUAL CONSUMER PRICE INFLATION**  
(annual growth; %)



### BANK RESERVES WITH THE BANK OF LATVIA

(in millions of lats)



MACROECONOMIC INDICATORS	2005	
	VIII	IX
Changes in the volume index of industrial output (year-on-year basis; %)	6.8	*
Changes in the CPI		
Month-on-month basis (%)	-0.1	1.5
Year-on-year basis (%)	6.1	7.2
Annual rate of core inflation <sup>1</sup> (%)	5.1	5.6
Number of registered unemployed persons (at end of period)	83 345	81 889
Unemployment rate (%)	7.8	7.7
General government consolidated budget fiscal deficit/surplus (in millions of lats)	173.2	197.3
Foreign trade (in millions of lats)		
Exports	230.0	*
Imports	408.4	*
Balance	-178.4	*

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

\* Figure available at a later date.

Source: Central Statistical Bureau of Latvia.

In September, the annual growth rate of resident financial institution, non-financial corporation and household deposits (39.3%) stood at the level recorded in mid-1998. The pick-up in deposits made in euro exceeded that of deposits in lats almost twofold. By type of depositor, the deposits of financial institutions and non-financial corporations expanded slightly faster.

The rise in the annual growth rate of bank loans (57.8%) also reached the level of 1998. This stemmed from the all-time-high expansion of loans in September (257.4 million lats) relating to a pick-up in mortgage loans (144.3 million lats; including household loans for house purchase by 97.1 million lats). Commercial credit and industrial credit grew significantly (by 43.9 million lats and 39.2 million lats, respectively). The increase primarily affected loans granted in euro (by 247.4 million lats). The increase in loans granted in lats was also higher than in the preceding months (51.1 million lats). Lending to households, financial institutions and non-financial corporations expanded at a similar rate, with outstanding loans growing by 132.8 million lats and 124.6 million lats in September, respectively. The annual growth rate of both loans granted to households and loans granted to financial institutions and non-financial corporations accelerated (by 78.9% and 46.6% in September, respectively).

With the budget surplus increasing, Government deposits with MFIs exceeded Government borrowing from banks by 8.8 million lats in September.

The weighted average interest rate on household loans for house purchase granted in lats shrank by 0.1 percentage point (to 5.1%), whereas that on foreign currency loans climbed 0.1 percentage point (to 4.5%). The weighted average interest rate on loans granted to non-financial corporations in lats declined to 5.3%, whereas that on loans granted in foreign currencies increased to 4.9%.

Interbank market rates remained low (RIGIBOR on overnight loans stood at 2.5%–2.6%). For a short time, at the end of the reserve maintenance period, they went up to 4.8%, as banks required additional funds for meeting the increased reserve ratio requirement (6%) for the first time. RIGIBOR for loans with a 6 and 12 month maturity remained broadly unchanged (at the end of the period, 2.81% and 2.92%, respectively).

In September, MFI assets expanded by 391.4 million lats, whereas profit amounted to 144.1 million lats in the first nine months of 2005 (1.7 times higher year-on-year).

With the banks' demand deposits with the Bank of Latvia growing and against the background of persistently rather high demand for cash, the monetary base M0 increased by 38.7 million lats. The growth of the central bank's money supply was underpinned by a rise in its net foreign assets (by 64.6 million lats), primarily as a result of the Bank of Latvia purchasing foreign currencies. At the end of September, the backing of the national currency with the Bank of Latvia's net foreign assets was 114.9%. Money supply was reduced by an increase in the banks' time deposits with the central bank by 11.0 million lats and Government deposits with the Bank of Latvia by 16.6 million lats.

Raising of the reserve ratio slightly changed the amounts and structure of the liquidity adjustment operations implemented by the Bank of Latvia in September. Time deposits from banks (93.9 million lats) were 1.9 times lower than in August, whereas the amount of repo loans granted was 3.4 times higher (22.3 million lats). Moreover, demand Lombard loans were granted for the first time since April (22.9 million lats).

In September, the US dollar appreciated by 1.4% against the lats, the exchange rate of the British pound sterling remained unchanged, whereas the Japanese yen depreciated by 0.6%.

MONETARY INDICATORS (at end of period; in millions of lats)	2005	
	VIII	IX
<b>MFIs<sup>1</sup></b>		
<b>M3</b>	3 385.8	3 503.2
Repurchase agreements	0	0
Money market fund shares and units	16.7	15.3
Debt securities issued with maturity of up to 2 years	0	0
<b>M2</b>	3 369.1	3 487.9
Deposits with agreed maturity of up to 2 years	817.6	827.2
Deposits redeemable at notice of up to 3 months	94.4	98.6
<b>M1</b>	2 457.1	2 562.1
Currency outside MFIs	707.2	717.1
Overnight deposits	1 749.9	1 845.0
Net external assets	-690.3	-784.1
Credit to resident financial institutions, non-financial corporations and households	5 095.7	5 353.1
Credit to general government	378.9	382.5
Deposits of central government	274.8	300.7
Longer-term financial liabilities	1 140.3	1 160.1
<b>Bank of Latvia</b>		
<b>M0</b>	1 164.0	1 202.7
Currency in circulation	784.8	800.6
Deposits with the Bank of Latvia in lats	379.2	402.1
Deposits with the Bank of Latvia in foreign currencies	0	0
Net foreign assets	1 317.8	1 382.4
Net domestic assets	-153.8	-179.7
Credit	-61.7	-77.6
To MFIs	4.5	4.7
To central government (net)	-66.2	-82.3
Other items (net)	-92.1	-102.1
International reserves (at end of period; in millions of US dollars)	2 307.39	2 396.84
Gold	108.59	116.85
Special Drawing Rights	0.15	0.14
Reserve position in the IMF	0.08	0.08
Foreign convertible currencies	2 198.57	2 279.77

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

EXCHANGE RATES SET BY THE BANK OF LATVIA AND INTEREST RATES	2005	
	VIII	IX
Weighted average interest rate on domestic interbank loans in lats	2.2	2.9
Interest rates on loans to resident non-financial corporations and households		
Loans to non-financial corporations (in lats)	5.8	5.3
Loans to households (in lats)	6.1	6.3
incl. for house purchase	5.2	5.1
Loans to non-financial corporations (in foreign currencies)	4.4	4.9
Loans to households (in foreign currencies)	4.5	4.5
incl. for house purchase	4.4	4.5
Interest rates on deposits of non-financial corporations and households		
Time deposits of non-financial corporations (in lats)	2.3	2.4
Demand deposits of non-financial corporations (in lats)	0.8	0.7
Time deposits of households (in lats)	2.9	2.8
Demand deposits of households (in lats)	0.4	0.5
Time deposits of non-financial corporations (in foreign currencies)	2.2	2.5
Demand deposits of non-financial corporations (in foreign currencies)	1.0	1.0
Time deposits of households (in foreign currencies)	2.6	2.6
Demand deposits of households (in foreign currencies)	1.2	1.4
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	0.5750	0.5830
LVL/GBP	1.0310	1.0310
LVL/100 JPY	0.5190	0.5160
LVL/EUR	0.7028	0.7028

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

	2005	
	VIII	IX
MFI reserves	477.4	516.8
Vault cash in national currency	77.6	83.6
Deposits with the Bank of Latvia	399.8	433.3
Foreign assets	3 128.3	3 209.5
Vault cash in foreign currencies	65.0	66.1
Claims on MFIs	1 900.2	1 943.4
Claims on non-MFIs	1 129.2	1 155.8
Other assets	33.9	44.2
Claims on central government	205.0	208.3
Claims on local government	75.3	75.2
Claims on public non-financial corporations	127.3	124.3
Claims on financial institutions and private non-financial corporations	3 034.7	3 163.1
Claims on households	1 967.1	2 099.9
Unclassified assets	410.1	419.4
Fixed assets	125.2	125.7
Items in transit	10.4	16.6
Other assets	69.4	69.8
Claims on resident MFIs (incl. investments)	205.2	207.3
<b>Total assets</b>	<b>9 425.2</b>	<b>9 816.6</b>
<i>Memo item: Trust assets</i>	<i>547.4</i>	<i>444.7</i>
Overnight deposits in lats	987.0	1 015.3
Public non-financial corporations	49.6	48.7
Financial institutions and private non-financial corporations	448.7	462.1
Households	488.7	504.5
Time deposits and deposits redeemable at notice in lats	610.5	616.9
Public non-financial corporations	56.9	51.7
Financial institutions and private non-financial corporations	175.5	183.0
Households	378.1	382.2
Foreign currency deposits of residents	1 114.0	1 190.5
Public non-financial corporations	16.2	17.5
Financial institutions and private non-financial corporations	356.0	402.0
Households	741.8	770.9
Deposits of central government	110.0	119.3
Deposits of local government	90.1	90.6
Transit funds	5.1	5.1
Foreign liabilities	5 136.4	5 376.1
Liabilities to MFIs	2 263.9	2 418.4
Liabilities to non-MFIs	2 732.2	2 787.7
Other liabilities (incl. subordinated liabilities)	140.3	170.0
Liabilities to the Bank of Latvia	4.5	4.7
Debt securities issued	162.2	166.7
Money market fund shares and units	16.7	15.3
Capital and reserves	738.3	753.6
Residents	430.2	441.9
Non-residents	308.0	311.7
Provisions	96.9	98.7
Unclassified liabilities	353.5	363.7
Items in transit	102.2	107.9
Other liabilities (incl. subordinated liabilities)	67.1	68.9
Liabilities to resident MFIs	184.2	186.9
<b>Total liabilities</b>	<b>9 425.2</b>	<b>9 816.6</b>
<i>Memo item: Trust liabilities</i>	<i>547.4</i>	<i>444.7</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>).