

# MONETARY BULLETIN 2009

## 10

Economic data pointed to further macroeconomic stabilisation. The current account of the balance of payments recorded a surplus again. In October, annual consumer price deflation was observed in Latvia for the first time since 1991, and the rate of decline in the money supply started to moderate. With recession in several trade partners of Latvia coming to an end, expectations for the recovery of the external demand emerged and have already materialised as upward trends in some industrial sectors. However, due to the generally weak domestic demand the industrial output shrank somewhat, retail trade turnover was low, and the unemployment rate increased by 0.9 percentage point, to 14.1% in October. According to the flash estimate of the Central Statistical Bureau of Latvia, a notable real year-on-year contraction of GDP, albeit smaller than in the previous quarter, persisted in the third quarter (18.4%). The weak demand was also reflected in the continuous tax revenue fall which contributed to a further rise in the general government consolidated budget deficit in October.

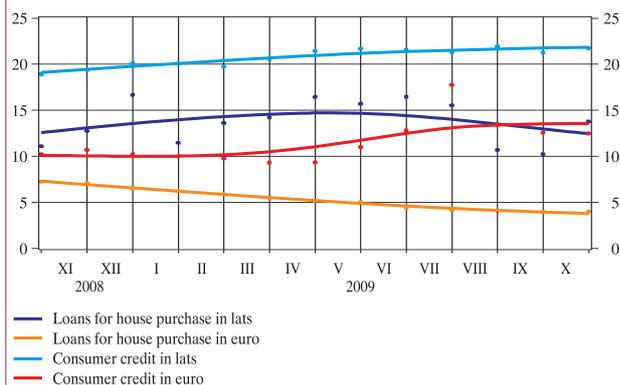
The moderating demand as a result of a decrease in personal income, optimisation of corporate costs as well as dropping prices in those countries wherefrom part of goods is imported accounted for 0.2% and 0.9% consumer price declines in October and year-on-year respectively. Almost all commodity groups posted price falls, with food recording a particular year-on-year price decline of 5.3%. As the price of natural gas decreased notably, gas and heating tariffs were reduced. The price decline moderated on account of the administered prices, e.g. fees for health and social care as well as education services were higher year-on-year. A slower price decrease also resulted from changes in indirect taxes in early 2009. In October, the annual consumer price core inflation reached -0.8%, and the 12-month average annual inflation and the 12-month average growth in the harmonised index of consumer prices (HICP) used for the Maastricht criterion still remained relatively high (5.5% and 5.3% respectively).

In September, the seasonally adjusted industrial output in manufacturing shrank by 1.7% month-on-month while the year-on-year decline (working-day adjusted) was 15.1%. Retail trade turnover also posted respective month-on-month and year-on-year decreases of 1.6% and 34.1%. In October, rail freight contracted notably in comparison with the corresponding period of the previous year (by 17.4%) while the total freight turnover at Latvian ports grew by 3.4%.

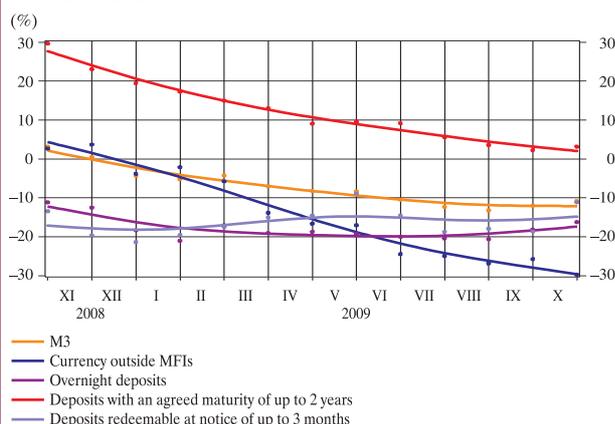
In October, the general government consolidated budget ran a deficit of 20.7 million lats (accrued to 514.5 million lats since the beginning of the year). The central government social security budget and local government consolidated budget recorded a deficit, while the central government basic budget was in surplus. The total revenue drop in comparison with the same period of the previous year was relatively small (5.0%) due to the foreign financial assistance and government budget transfers while tax revenue continued to plummet by 31.2%. Pronounced declines persisted in corporate income tax (64.1%), personal income tax (35.9%), and value added tax (37.7%) revenues; social security contributions contracted by

### INTEREST RATES ON LOANS GRANTED TO RESIDENT HOUSEHOLDS

(with a floating rate and an initial rate fixation of up to 1 year; %)



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



19.2%. As a result of further general government budget deficit-reducing measures, budget expenditure saw more drastic cuts: in October expenditure posted a 34.0% year-on-year decrease (21.3% in September) as all major budget expenditure items contracted (inter alia capital expenditure was down 60.9%, expenditure related to the purchase of goods and services dropped 39.5%, and compensation to employees shrank by 38.4%). Expenditure for social benefits which had been increasing before slightly contracted in October. The general government debt shrank to 4 111.9 million lats.

In October, the development trends of monetary aggregates suggested stabilisation of money supply. Deposits of resident financial institutions, non-financial corporations and households grew by 0.1% while broad money M3 contracted by 0.3%. The demand for cash posted a more notable drop (1.5%) in parallel with an 0.9% increase in deposits with an agreed maturity of up to 2 years, hence this money supply component resulted in a positive annual change rate of 3.2%. For the second consecutive month, the negative annual change rate of deposits of resident financial institutions, non-financial corporations and households and broad money M3 posted a considerable deceleration (to -5.2% and -10.8% respectively).

At the same time, loans to resident financial institutions, non-financial corporations and households continued on their downward trend, dropping 0.6%, with their annual rate of change reaching -5.9%. Each segment of loans – to households, non-financial corporations and financial institutions – contracted in October. As regards the loan breakdown by type, industrial credit posted a minor increase of 0.1% while commercial credit shrank by 1.7%.

In October, the total amount of financing from foreign banks remained almost unchanged while liabilities to foreign banks continued to decrease (by 1.4%), with borrowings from affiliated banks contracting by 0.3%. Conversely, non-resident non-bank deposits grew by 3.3%, reaching a high of the last five months. The negative net foreign assets of MFIs (except the Bank of Latvia) contracted by 85.4 million lats in October.

The monetary base M0 shrank by 10.5 million lats in October due to minor decreases both in the demand for cash and bank deposits with the Bank of Latvia. The annual rate of change in monetary base reached -33.1%. Net foreign assets of the central bank decreased by 1.2% in October, and the backing of the national currency with the Bank of Latvia net foreign assets stood at 198.9% at the end of the month. The decrease in foreign reserves resulted from a drop in foreign exchange swaps with banks. The moderating effect of the above decrease on the central bank money supply, however, was almost offset by the decrease in the government deposit with the Bank of Latvia in lats as loans granted to banks remained broadly unchanged.

In October, the situation in the money market remained stable, with RIGIBOR on overnight loans decreasing somewhat and averaging 1.81% per month (1.99% in September). Longer term RIGIBOR, however, posted a slight increase: 3-month, 6-month, and 12-month RIGIBOR reached 13.9%, 14.8%, and 15.7% respectively at the end of the month. The signs of macroeconomic stabilisation underpinned a fall in interest rates on loans granted to non-financial corporations and households, particularly so on loans granted in lats to non-financial corporations.

According to the exchange rate set by the Bank of Latvia, in October the US dollar and the Japanese yen depreciated against the lats by 0.6% and 1.1% respectively, whereas the British pound sterling appreciated by 2.2%.

MACROECONOMIC INDICATORS	2009	
	IX	X
Volume index of industrial output (working-day adjusted annual rate of change; %)	-15.3	*
Changes in the CPI		
Month-on-month basis (%)	-0.2	-0.2
Average annual inflation rate (HCPI) of last 12 months (%)	6.7	5.5
Year-on-year basis (%)	0.5	-0.9
Annual rate of core inflation <sup>1</sup> (%)	-0.4	-0.8
Number of registered unemployed persons (at end of period)	147 754	157 897
Unemployment rate (%)	13.2	14.1
General government consolidated budget financial deficit/surplus (in millions of lats)	-493.7	-514.5
Foreign trade (in millions of lats)		
Exports	331.3	*
Imports	388.4	*
Balance	-57.1	*

<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	
	IX	X
<b>MFIs<sup>1</sup></b>		
M3	5 614.4	5 598.4
Repurchase agreements	0	0
Money market fund shares and units	78.8	79.1
Debt securities issued with maturity of up to 2 years	0.9	0.9
M2	5 534.7	5 518.4
Deposits with agreed maturity of up to 2 years	2 377.2	2 399.3
Deposits redeemable at notice of up to 3 months	261.0	257.0
M1	2 896.5	2 862.1
Currency outside MFIs	651.5	641.8
Overnight deposits	2 244.9	2 220.3
Net external assets	-3 571.1	-3 525.3
Credit to resident financial institutions, non-financial corporations and households	13 880.8	13 796.7
Credit to general government	663.9	665.0
Deposits of central government	2 244.3	2 181.4
Longer-term financial liabilities	2 165.8	2 141.9
<b>Bank of Latvia</b>		
M0	1 604.3	1 593.8
Currency in circulation	748.7	745.6
Deposits with the Bank of Latvia in lats	841.4	838.9
Deposits with the Bank of Latvia in foreign currencies	14.2	9.3
Net foreign assets	3 209.3	3 169.8
Net domestic assets	-1 605.0	-1 575.9
Credit	-1 338.8	-1 313.0
To MFIs	225.0	226.1
To central government (net)	-1 563.8	-1 539.2
Other items (net)	-266.3	-262.9
International reserves (at end of period; in millions of euro)	4 577.17	4 523.28
Gold	168.67	174.36
Special Drawing Rights	131.09	130.74
Reserve position in the IMF	0.06	0.06
Foreign convertible currencies	4 277.35	4 218.12
International reserves (at end of period; in millions of US dollars)	6 701.77	6 664.53
Gold	246.96	256.90
Special Drawing Rights	191.93	192.63
Reserve position in the IMF	0.09	0.09
Foreign convertible currencies	6 262.79	6 214.91

<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	
	IX	X
Weighted average interest rate on domestic interbank loans in lats	1.6	1.3
Interest rates on loans to resident non-financial corporations and households		
Loans to non-financial corporations (in lats)	17.9	8.5
Loans to households (in lats)	15.5	15.2
incl. for house purchase	8.6	10.6
Loans to non-financial corporations (in foreign currencies)	5.2	5.0
Loans to households (in foreign currencies)	5.8	5.6
incl. for house purchase	4.2	4.2
Interest rates on deposits of non-financial corporations and households		
Time deposits of non-financial corporations (in lats)	5.1	5.4
Demand deposits of non-financial corporations (in lats)	0.6	0.6
Time deposits of households (in lats)	9.8	9.6
Demand deposits of households (in lats)	1.0	1.0
Time deposits of non-financial corporations (in foreign currencies)	1.1	0.9
Demand deposits of non-financial corporations (in foreign currencies)	0.3	0.3
Time deposits of households (in foreign currencies)	2.5	2.3
Demand deposits of households (in foreign currencies)	0.9	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	0.4800	0.4770
LVL/GBP	0.7650	0.7820
LVL/100 JPY	0.5340	0.5280
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	
	IX	X
MFI reserves	949.1	946.8
Vault cash in national currency	97.1	103.8
Deposits with the Bank of Latvia	852.0	843.0
Foreign assets	4 587.0	4 677.4
Vault cash in foreign currencies	67.6	61.6
Claims on MFIs	2 685.0	2 812.1
Claims on non-MFIs	1 726.3	1 712.9
Other assets	108.1	90.8
Claims on central government	591.5	591.7
Claims on local government	72.3	73.3
Claims on public non-financial corporations	392.5	390.5
Claims on financial institutions and private non-financial corporations	7 469.9	7 418.6
Claims on households	6 185.9	6 153.2
Unclassified assets	942.5	949.0
Fixed assets	158.4	156.4
Items in transit	24.2	15.9
Other assets	417.8	432.4
Claims on resident MFIs (incl. investments)	342.1	344.4
<b>Total assets</b>	<b>21 190.8</b>	<b>21 200.4</b>
<i>Memo item: Trust assets</i>	<i>316.1</i>	<i>316.5</i>
Overnight deposits in lats	1 033.7	1 008.0
Public non-financial corporations	74.6	67.2
Financial institutions and private non-financial corporations	456.9	454.3
Households	502.1	486.6
Time deposits and deposits redeemable at notice in lats	1 034.7	1 043.5
Public non-financial corporations	180.3	193.3
Financial institutions and private non-financial corporations	348.0	348.1
Households	506.5	502.1
Foreign currency deposits of residents	2 803.4	2 823.6
Public non-financial corporations	29.1	62.2
Financial institutions and private non-financial corporations	1 005.6	1 007.2
Households	1 768.7	1 754.3
Deposits of central government	680.5	642.3
Deposits of local government	173.2	162.1
Transit funds	3.2	3.2
Foreign liabilities	11 367.5	11 372.5
Liabilities to MFIs	7 896.3	7 788.8
Liabilities to non-MFIs	2 910.7	3 005.5
Other liabilities (incl. subordinated liabilities)	560.5	578.2
Liabilities to the Bank of Latvia	225.0	226.1
Debt securities issued	157.0	154.5
Money market fund shares and units	78.8	79.1
Capital and reserves	1 549.7	1 529.1
Residents	535.3	507.9
Non-residents	1 014.4	1 021.2
Provisions	1 334.9	1 417.2
Unclassified liabilities	749.2	739.2
Items in transit	90.9	81.3
Other liabilities (incl. subordinated liabilities)	348.8	345.5
Liabilities to resident MFIs	309.4	312.4
<b>Total liabilities</b>	<b>21 190.8</b>	<b>21 200.4</b>
<i>Memo item: Trust liabilities</i>	<i>316.1</i>	<i>316.5</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>).