

MONETARY BULLETIN 2006

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The all-time-high GDP growth data (13.1%) for the first quarter published by the Central Statistical Bureau of Latvia in combination with the high inflation and external imbalances caused increasing concern about overheating. Such buoyant growth poses risks to balanced economic development in the long-term, especially if the growth is mainly driven by the domestic consumption based sectors, while the external demand based sectors develop at a more moderate rate. A pronounced increase was observed in construction (17.5%) and the services sector, including trade (17.7%), business activities (18.7%) and other community, social and personal service activities (17.9%). The transport, storage and communication sector as well as manufacturing demonstrated moderate growth (6.0% and 8.8%, respectively). Data on economic growth in April and May also indicate persistence of the above trends. With the industrial growth dampening, the seasonally adjusted volume index of industrial output in manufacturing rose by a mere 3.9% and the total industrial output expanded by 4.3% in April. The volume of rail freight continued to shrink (by 8.1% in May). Cargo turnover at Latvian ports expanded by 5.7% year-on-year. In April, retail trade turnover (including sale of motor vehicles and retail trade in automotive fuel) expanded by 22.3%. In May, the unemployment rate posted a more rapid decline than in previous months (0.3 percentage point, to 7.0%).

With prices of fuel and gas rising (by 7.0% and 18.1%, respectively), consumer prices grew by 1.2% and the annual inflation rate reached 6.6% in May.

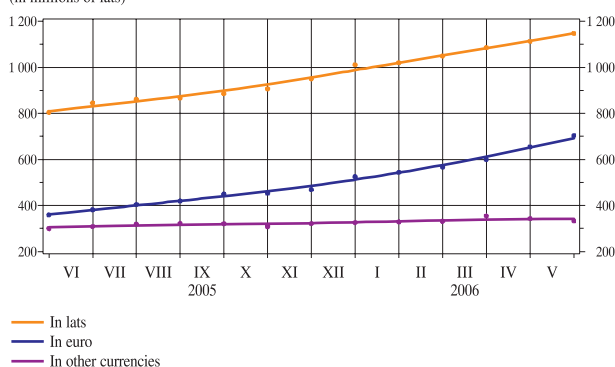
In May 2006, the general government consolidated budget posted a financial surplus of 80.6 million lats (230.6 million lats in the first five months of 2006; 89.2 million lats in the first five months of 2005). The growing tax income and non-tax income as a result of several major companies making payments for using the state capital contributed to the substantial budget surplus in May.

One auction of 12-month Treasury bills was held on the domestic government securities market. Securities in the amount of only 0.9 million lats (the allotment amount being 8.0 million lats) at the weighted average discount rate of 3.842% (0.553 basis point higher than at the previous auction held in February) were sold at a competitive multi-price auction on the primary market.

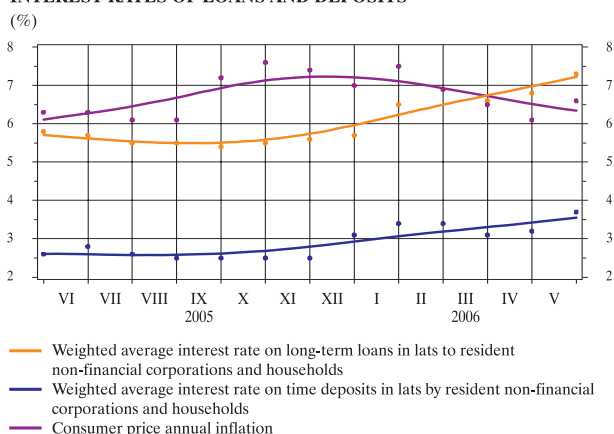
In May, money supply edged up slightly. Currency outside banks increased by 10.4 million lats or 1.3%. Overnight deposits grew by 26.4 million lats, and the monetary aggregate M1 expanded by 36.9 million lats or 1.2% (by 3.4% in the previous month). The growth of the monetary aggregate M2 also moderated (by 44.2 million lats or 1.0%; by 3.0% in April), since deposits with agreed maturity of up to two years posted only a slight increase. Broad money M3 grew by 40.9 million lats or 0.9% (by 2.8% in April). Hence, the annual growth rates of all monetary aggregates decreased in May (M1 – to 41.9%, M2 – to 41.1% and M3 – to 41.8%).

Deposits of resident financial institutions, non-financial corporations and households expanded by 25.7 million lats in May, with the annual growth rate decreasing to 44.9%. As regards breakdown by currency, only the deposits in euro increased

DEPOSITS OF HOUSEHOLDS WITH MFIs
(in millions of lats)



CONSUMER PRICE ANNUAL INFLATION AND WEIGHTED AVERAGE INTEREST RATES OF LOANS AND DEPOSITS



(by 34.8 million lats) while those made in lats and other currencies diminished somewhat. Household deposits continued to grow (a pickup of 73.5 million lats) whereas those made by financial institutions and non-financial corporations diminished.

The increase in loans granted to resident financial institutions, non-financial corporations and households was record high (340.5 million lats) in May; however, their annual growth rate remained the same (61.7%). The increase of 240.0 million lats in mortgage loans was the major contributor to the overall loan expansion, including a rise of lending to households for house purchase (118.7 million lats). Commercial credit and consumer credit to households grew by 53.6 million lats and 24.7 million lats, whereas industrial credit contracted. Loans granted in euro still reported the highest growth (331.3 million lats), although loans granted in lats also continued to increase slightly (by 44.8 million lats). Loans granted in other currencies continued on their downward trend (by 35.6 million lats). Loans granted to households and financial institutions and non-financial corporations posted similar expansion (159.1 million lats and 181.4 million lats, respectively). The annual growth rate of loans granted to households declined somewhat (to 81.7%) while that of loans granted to financial institutions and non-financial corporations edged up (to 49.9%).

To fund credit expansion and ensure compliance with the reserve requirement, banks raised additional funds from abroad as well as reduced foreign assets. As a result negative net foreign assets of MFIs (excluding the Bank of Latvia) grew by 290.1 million lats in May. With the surplus of general government consolidated budget growing, net credit of MFIs to the general government shrank by 92.1 million lats.

As a result of expanding the reserve base, the amount of funds required for compliance with the reserve requirement increased considerably, and bank demand deposits with the central bank grew by 234.2 million lats. As the demand for cash also rose, the monetary base M0 increased by 240.7 million lats. The central bank's money supply mostly increased on account of foreign currency purchase from banks (resumed currency swaps also contributed somewhat), resulting in the Bank of Latvia's net foreign asset increase (227.7 million lats). At the end of May, the backing of the national currency with the Bank of Latvia's net foreign assets was 103.8%. The increase in the repo loans (45.1 million lats) granted to banks also contributed to the monetary base growth. In May, repo loans granted by the Bank of Latvia accounted for 79.4 million lats (2.0 times higher than in April), and currency swaps amounted to 3.5 million lats. The amount of time deposits with the central bank (mostly at the beginning of the month) was 50.3 million lats.

Overnight RIGIBOR rose from 2.4%–2.7% at the beginning of the month to 4.9% at the beginning of the new reserve maintenance period. RIGIBOR for loans with a 6- and 12-month maturity also grew, reaching 4.71% and 4.59% at the end of May, respectively. At the same time, interest rates on loans to non-MFIs in lats expanded substantially. Interest rates on loans granted to households and non-financial corporations increased by 1.3 percentage points (to 9.3%) and 0.5 percentage point (to 7.0%), respectively. Interest rates on loans granted in foreign currencies remained broadly unchanged.

In May, with the euro appreciating on the global currency markets, the US dollar and the Japanese yen continued to depreciate against the lats by 2.8% and 0.4%, respectively, whereas the British pound sterling appreciated by 1.8%.

MACROECONOMIC INDICATORS	2006	
	IV	V
Changes in the volume index of industrial output (year-on-year basis; %)	4.3	*
Changes in the CPI		
Month-on-month basis (%)	0.6	1.2
Year-on-year basis (%)	6.1	6.6
Annual rate of core inflation ¹ (%)	5.0	4.9
Number of registered unemployed persons (at end of period)	77 151	74 789
Unemployment rate (%)	7.3	7.0
General government consolidated budget financial deficit/surplus (in millions of lats)	150.0	230.6
Foreign trade (in millions of lats)		
Exports	258.4	*
Imports	458.7	*
Balance	-200.3	*

¹ 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)	2006	
	IV	V
MFIs¹		
M3	4 316.9	4 357.8
Repurchase agreements	0	0
Money market fund shares and units	39.9	36.6
Debt securities issued with maturity of up to 2 years	2.6	2.6
M2	4 274.4	4 318.6
Deposits with agreed maturity of up to 2 years	1 031.8	1 039.7
Deposits redeemable at notice of up to 3 months	121.7	121.3
M1	3 120.8	3 157.7
Currency outside MFIs	796.6	807.0
Overnight deposits	2 324.2	2 350.6
Net external assets	-1 419.7	-1 482.1
Credit to resident financial institutions, non-financial corporations and households	6 929.9	7 270.5
Credit to general government	373.9	373.0
Deposits of central government	219.3	301.3
Longer-term financial liabilities	1 384.5	1 541.6
Bank of Latvia		
M0	1 501.2	1 741.9
Currency in circulation	885.7	892.2
Deposits with the Bank of Latvia in lats	615.4	849.7
Deposits with the Bank of Latvia in foreign currencies	0	0
Net foreign assets	1 579.6	1 807.3
Net domestic assets	-78.4	-65.4
Credit	-24.4	-7.7
To MFIs	1.2	46.3
To central government (net)	-25.6	-54.0
Other items (net)	-53.9	-57.7
International reserves (at end of period; in millions of US dollars)	2 776.69	3 266.23
Gold	158.14	161.88
Special Drawing Rights	0.15	0.15
Reserve position in the IMF	0.08	0.08
Foreign convertible currencies	2 618.32	3 104.12

¹In accordance with the methodology of the European Central Bank.

EXCHANGE RATES SET BY THE BANK OF LATVIA AND INTEREST RATES	2006	
	IV	V
Weighted average interest rate on domestic interbank loans in lats	3.2	3.0
Interest rates on loans to resident non-financial corporations and households		
Loans to non-financial corporations (in lats)	6.5	7.0
Loans to households (in lats)	8.0	9.3
incl. for house purchase	6.0	6.1
Loans to non-financial corporations (in foreign currencies)	5.0	5.1
Loans to households (in foreign currencies)	4.9 ¹	4.9
incl. for house purchase	4.8	4.6
Interest rates on deposits of non-financial corporations and households		
Time deposits of non-financial corporations (in lats)	3.2	4.0
Demand deposits of non-financial corporations (in lats)	0.8	1.2
Time deposits of households (in lats)	3.1	3.3
Demand deposits of households (in lats)	0.5	0.5
Time deposits of non-financial corporations (in foreign currencies)	2.6	3.1
Demand deposits of non-financial corporations (in foreign currencies)	1.3	1.4
Time deposits of households (in foreign currencies)	3.3	3.0
Demand deposits of households (in foreign currencies)	1.2	1.2
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	0.5640	0.5480
LVL/GBP	1.0070	1.0250
LVL/100 JPY	0.4920	0.4900
LVL/EUR	0.7028	0.7028

¹Data have been revised.

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

	2006	
	IV	V
MFI reserves	698.5	928.5
Vault cash in national currency	89.1	85.1
Deposits with the Bank of Latvia	609.4	843.4
Foreign assets	3 467.8	3 411.2
Vault cash in foreign currencies	57.1	58.4
Claims on MFIs	2 111.3	2 021.3
Claims on non-MFIs	1 252.8	1 292.0
Other assets	46.5	39.5
Claims on central government	226.8	226.6
Claims on local government	88.5	88.7
Claims on public non-financial corporations	118.2	115.9
Claims on financial institutions and private non-financial corporations	3 972.3	4 158.2
Claims on households	2 876.8	3 035.9
Unclassified assets	700.4	757.1
Fixed assets	142.0	142.6
Items in transit	19.7	16.5
Other assets	82.9	80.8
Claims on resident MFIs (incl. investments)	455.8	517.3
Total assets	12 149.2	12 722.1
<i>Memo item: Trust assets</i>	425.6	430.5
Overnight deposits in lats	1 255.4	1 278.4
Public non-financial corporations	61.4	50.3
Financial institutions and private non-financial corporations	519.2	526.7
Households	674.7	701.4
Time deposits and deposits redeemable at notice in lats	751.0	726.1
Public non-financial corporations	94.0	102.0
Financial institutions and private non-financial corporations	218.6	177.7
Households	438.4	446.3
Foreign currency deposits of residents	1 500.5	1 528.2
Public non-financial corporations	20.8	18.4
Financial institutions and private non-financial corporations	481.6	472.7
Households	998.2	1 037.2
Deposits of central government	135.0	189.5
Deposits of local government	116.6	125.9
Transit funds	4.9	4.7
Foreign liabilities	6 467.1	6 700.6
Liabilities to MFIs	3 442.6	3 584.5
Liabilities to non-MFIs	2 779.0	2 871.7
Other liabilities (incl. subordinated liabilities)	245.4	244.4
Liabilities to the Bank of Latvia	1.2	46.3
Debt securities issued	162.8	304.5
Money market fund shares and units	39.9	36.6
Capital and reserves	986.4	997.4
Residents	574.3	584.1
Non-residents	412.1	413.3
Provisions	82.8	83.2
Unclassified liabilities	645.5	700.7
Items in transit	138.4	139.0
Other liabilities (incl. subordinated liabilities)	81.3	79.4
Liabilities to resident MFIs	425.7	482.4
Total liabilities	12 149.2	12 722.1
<i>Memo item: Trust liabilities</i>	425.6	430.5

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>).