

# MONETARY BULLETIN 2010

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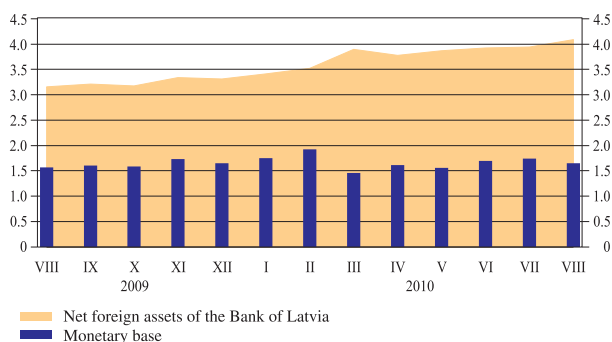
The macroeconomic indicators increasingly pointed to the strengthening of economic activity. Data on GDP for the second quarter confirmed more rapid than previously forecasted growth quarter-on-quarter (0.8%). Although uncertainty was observed in several export markets, exports continued to grow considerably with the annual growth rates of exports reaching 41.9% in July and suggesting that the economic recovery is determined by export opportunities. The dynamics of price and cost competitiveness remained favourable. Registered unemployment continued to decrease for the fifth consecutive month, to stand at 15.0% of the economically active population at the end of August. The tax revenue dynamics of the government budget was stable, providing for a more than two times lower budget deficit level than in the corresponding period of the previous year.

The positive contribution of external demand in July supported the expansion of manufacturing. The seasonally adjusted industrial output in manufacturing grew by 2.7% month-on-month, with the annual increase (working day unadjusted) amounting to 18.7%. As domestic demand remained unstable, retail trade did not record any significant changes. Retail trade turnover (including sales of motor vehicles) went up by 0.1% month-on-month according to seasonally adjusted data, while the year-on-year increase was 2.8%. However, retail trade turnover (excluding sales of motor vehicles) slightly contracted. With transit cargo traffic shrinking, overall freight turnover at Latvian ports decreased by 11.5% year-on-year in August, and the volume of freight transportation by rail dropped by 15.9%.

In August, consumer prices fell by 0.7% quarter-on-quarter. The prices of vegetables and clothing usually decrease in August due to seasonal factors; moreover, given the persistently weak demand, a downside of several other commodity group prices also accounted for the seasonal drop. The monthly prices were pushed down by falling oil prices as well, reflecting the stabilisation trends of the global oil prices. However, annual deflation continued to ease due to the base effect, and the consumer price level was only 0.3% lower year-on-year. At the same time, the average inflation of the last 12 months was -1.8%, whereas the 12-month average harmonised index of consumer prices (HICP) used for the Maastricht criterion decreased by 2.0%.

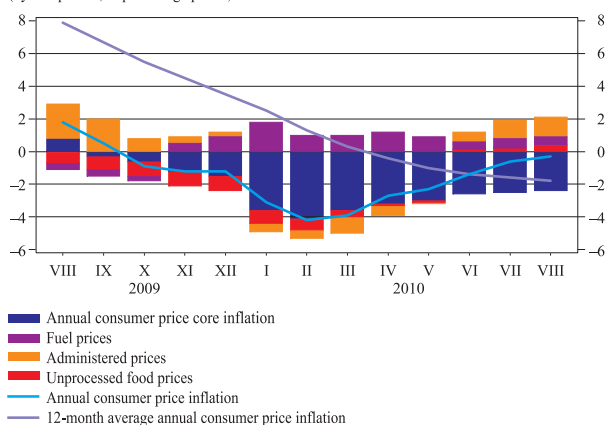
The consolidated general government budget ran a 9.3 million lats deficit in August. Consequently, the deficit accumulated from the beginning of the year grew to 195.9 million lats (in the eight months of the previous year the deficit of the consolidated general government budget amounted to 416.7 million lats). Only central government social security budget recorded a deficit in August, while the central government basic budget and the consolidated local government budget were in surplus. As inflows of foreign financial assistance funding diminished, the consolidated general government budget revenue decreased by 6.5% year-on-year in August, while tax revenue increased by 1.1%, with revenues from personal income tax and value added tax posting a more rapid increase. In August, the central government budget expenditure declined by 1.2% year-on-year, mainly on account of the reduction in the expenditure for compensation to employees (16.9%). The general government debt increased to 4 878.0 million lats in August.

**BACKING OF THE NATIONAL CURRENCY**  
(at end of period; in billions of lats)



## ANNUAL CONSUMER PRICE INFLATION

(by component; in percentage points)



MACROECONOMIC INDICATORS	2010	
	VII	VIII
Volume index of industrial output (working-day adjusted annual rate of change; %)	18.0	*
Changes in the CPI		
Month-on-month basis (%)	0.2	-0.7
Average annual inflation rate (HCPI) of last 12 months (%)	-1.6	-1.8
Year-on-year basis (%)	-0.6	-0.3
Annual rate of core inflation <sup>1</sup> (%)	-3.5	-3.3
Number of registered unemployed persons (at end of period)	173 301	169 676
Unemployment rate (%)	15.3	15.0
General government consolidated budget financial deficit/surplus (in millions of lats)	-186.5	-195.9
Foreign trade (in millions of lats)		
Exports	388.1	*
Imports	486.7	*
Balance	-98.6	*

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

\* Figure available at a later date.

Source: Central Statistical Bureau of Latvia and Ministry of Finance.

With economic recovery trends gradually strengthening, money supply continued to expand. In August, M1, M2 and M3 increased at a more rapid pace than in the previous month, with the annual growth rate reaching 16.2%, 9.7% and 10.6% respectively.

Money supply in August was determined by the growing demand for cash (currency outside MFIs expanded by 1.0%), and a rise in deposits attracted by banks. With overnight deposits and deposits with an agreed maturity of up to two years attracted by banks increasing, the aggregate deposits by resident financial institutions, non-financial corporations and households grew by 1.0% in August and was 9.1% higher year-on-year.

In contrast to the steep fall observed in the previous months, loans to resident financial institutions, non-financial corporations and households remained broadly unchanged in August (a fall of 0.1%). Moreover, after a period of protracted slowdown loans to non-financial corporations increased somewhat for the first time. The decline in lending to households (both the loans for house purchase and consumer credits) remained moderate. Thus, the annual rate of decrease of loans decelerated to 7.4% in August.

Although liabilities to foreign banks shrank somewhat, foreign funding to the banking sector expanded by 124.2 million lats in August. Foreign liabilities increased on account of a pronounced rise in non-resident non-MFI deposits (171.8 million lats). As the increase in banks' foreign assets was more rapid, the negative net foreign assets of MFIs (except the Bank of Latvia) continued to shrink.

In August, the monetary base M0 decreased by 88.5 million lats. The central bank's money supply shrank due to banks increasingly resorting to the deposit facility with the Bank of Latvia in the context of the ample liquidity (the monthly growth of 187.7 million lats), while the bank demand deposits contracted simultaneously. Thus, the annual rate of change in M0 and demand deposits with the Bank of Latvia decelerated. At the same time, the annual rate of change of currency in circulation continued to increase (to 14.2%; a high since May 2007). A decrease in the government deposit in lats with the Bank of Latvia, by contrast, had an insignificant upward effect on the money supply of the central bank.

In August, net foreign assets of the Bank of Latvia grew by 148.6 million lats or 3.8%, exceeding the level of 4 billion lats, and the backing of the national currency with the Bank of Latvia net foreign assets was 247.3% at the month-end. The increase in net reserves was mainly on account of the pick-up in government deposit in foreign currency following receipt of the current installment of the foreign loan and EU funds.

Interbank market interest rates continued to decrease in August: the weighted average rate on overnight loans edged down to 0.51% as compared to 0.87% in July, while the average RIGIBOR on overnight loans was 0.68% during the month (1.02% in July). 3-month, 6-month and 12-month RIGIBOR went on decreasing by 13, 29 and 28 basis points, to 1.25%, 2.02% and 3.60% respectively.

Interest rates on loans granted in lats to households and non-financial corporations (except loans for house purchase) and interest rates on loans granted in foreign currency to non-financial corporations increased in August, whereas those on loans granted in foreign currency to households decreased. Interest rates on some types of deposits also shrank.

In August, the exchange rates of the US dollar, British pound sterling, and Japanese yen set by the Bank of Latvia against the lats depreciated by 2.2%, 1.5%, and 4.4% respectively.

MONETARY INDICATORS (at end of period; in millions of lats)	2010	
	VII	VIII
<b>MFI<sup>1</sup></b>		
M3	6 173.7	6 252.0
Repurchase agreements	0	0
Money market fund shares and units	97.5	103.2
Debt securities issued with maturity of up to 2 years	20.6	20.6
M2	6 055.6	6 128.1
Deposits with agreed maturity of up to 2 years	2 496.4	2 532.7
Deposits redeemable at notice of up to 3 months	233.1	231.5
M1	3 326.1	3 364.0
Currency outside MFIs	750.8	758.5
Overnight deposits	2 575.3	2 605.5
Net external assets	-1 658.0	-1 470.6
Credit to resident financial institutions, non-financial corporations and households	12 893.7	12 885.2
Credit to general government	543.1	516.7
Deposits of central government	2 046.2	2 094.5
Longer-term financial liabilities	2 197.6	2 315.2
<b>Bank of Latvia</b>		
M0	1 741.2	1 652.7
Currency in circulation	856.4	864.5
Deposits with the Bank of Latvia in lats	869.9	773.5
Deposits with the Bank of Latvia in foreign currencies	14.9	14.8
Net foreign assets	3 939.4	4 088.0
Net domestic assets	-2 198.2	-2 435.3
Credit	-1 347.0	-1 372.3
To MFIs	0	0
To central government (net)	-1 347.0	-1 372.3
Other items (net)	-851.2	-1 063.0
International reserves (at end of period; in millions of euro)	5 582.63	5 849.73
Gold	222.83	241.40
Special Drawing Rights	141.80	144.15
Reserve position in the IMF	0.06	0.07
Foreign convertible currencies	5 217.94	5 464.11
International reserves (at end of period; in millions of US dollars)	7 265.74	7 447.84
Gold	290.01	307.35
Special Drawing Rights	184.55	183.53
Reserve position in the IMF	0.08	0.08
Foreign convertible currencies	6 791.10	6 956.88

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

<sup>2</sup> Data have been revised.

EXCHANGE RATES SET BY THE BANK OF LATVIA AND INTEREST RATES	2010	
	VII	VIII
Weighted average interest rate on domestic interbank loans in lats	0.9	0.5
Interest rates on loans to resident non-financial corporations and households		
Loans to non-financial corporations (in lats)	3.5	6.1
Loans to households (in lats)	16.0	18.9
incl. for house purchase	10.1	7.4
Loans to non-financial corporations (in foreign currencies)	4.6	5.8
Loans to households (in foreign currencies)	5.4	5.0
incl. for house purchase	4.3	3.7
Interest rates on deposits of non-financial corporations and households		
Time deposits of non-financial corporations (in lats)	0.7	0.9
Demand deposits of non-financial corporations (in lats)	0.3	0.2
Time deposits of households (in lats)	3.2	3.2
Demand deposits of households (in lats)	0.8	0.7
Time deposits of non-financial corporations (in foreign currencies)	0.8	0.6
Demand deposits of non-financial corporations (in foreign currencies)	0.2	0.2
Time deposits of households (in foreign currencies)	2.0	2.0
Demand deposits of households (in foreign currencies)	0.5	0.5
The Bank of Latvia's refinancing rate (at end of period; %)	3.5	3.5
Exchange rates of foreign currencies (at end of period)		
LVL/USD	0.5400	0.5520
LVL/GBP	0.8440	0.8570
LVL/100 JPY	0.6200	0.6470
LVL/EUR	0.7028	0.7028

AGGREGATED BALANCE SHEET OF MFIs (EXCLUDING THE BANK OF LATVIA) (at end of period; in millions of lats)	2010	
	VII	VIII
MFI reserves	1 567.7	1 664.9
Vault cash in national currency	105.7	106.0
Deposits with the Bank of Latvia	1 462.0	1 558.9
Foreign assets	4 742.8	4 905.8
Vault cash in foreign currencies	70.0	81.6
Claims on MFIs	2 579.2	2 662.2
Claims on non-MFIs	1 998.0	2 050.2
Other assets	95.6	111.7
Claims on central government	479.9	454.0
Claims on local government	63.2	62.6
Claims on public non-financial corporations	410.8	414.4
Claims on financial institutions and private non-financial corporations	6 776.1	6 789.2
Claims on households	5 914.5	5 893.0
Unclassified assets	806.6	832.9
Fixed assets	92.8	91.4
Items in transit	14.5	18.6
Other assets	479.7	506.1
Claims on resident MFIs (incl. investments)	219.6	216.8
<b>Total assets</b>	<b>20 761.6</b>	<b>21 016.9</b>
<i>Memo item: Trust assets</i>	<i>414.5</i>	<i>424.0</i>
Overnight deposits in lats	1 389.6	1 409.4
Public non-financial corporations	93.5	84.2
Financial institutions and private non-financial corporations	613.5	655.4
Households	682.5	669.7
Time deposits and deposits redeemable at notice in lats	1 235.8	1 222.5
Public non-financial corporations	207.7	219.7
Financial institutions and private non-financial corporations	485.8	460.8
Households	542.4	542.0
Foreign currency deposits of residents	2 685.0	2 729.7
Public non-financial corporations	43.5	52.1
Financial institutions and private non-financial corporations	952.3	996.2
Households	1 689.2	1 681.5
Deposits of central government	699.2	722.2
Deposits of local government	186.7	201.0
Foreign liabilities	10 340.2	10 464.4
Liabilities to MFIs	6 629.1	6 551.1
Liabilities to non-MFIs	3 588.4	3 760.2
Other liabilities (incl. subordinated liabilities)	122.7	153.1
Liabilities to the Bank of Latvia	0	0
Debt securities issued	191.8	189.2
Money market fund shares and units	97.9	103.6
Capital and reserves	1 536.9	1 634.6
Residents	272.1	356.8
Non-residents	1 264.9	1 277.8
Provisions	1 852.9	1 827.4
Unclassified liabilities	545.7	513.0
Items in transit	69.9	111.3
Other liabilities (incl. subordinated liabilities)	181.1	205.9
Liabilities to resident MFIs	294.7	195.8
<b>Total liabilities</b>	<b>20 761.6</b>	<b>21 016.9</b>
<i>Memo item: Trust liabilities</i>	<i>414.5</i>	<i>424.0</i>

<sup>2</sup> Data have been revised.

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>).