

# MONETARY BULLETIN 2006

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The published data on the GDP growth in the fourth quarter (10.5%) and overall in 2005 (10.2%) suggested that the highest contribution was made by sectors dependent on domestic demand. The year-on-year pickup in value added in trade, construction and finances reached 17.4%, 15.5% and 10.3%, respectively. The transport, storage and communication sector demonstrated strong growth (16.2%) while that of manufacturing was considerably lower (6.3%).

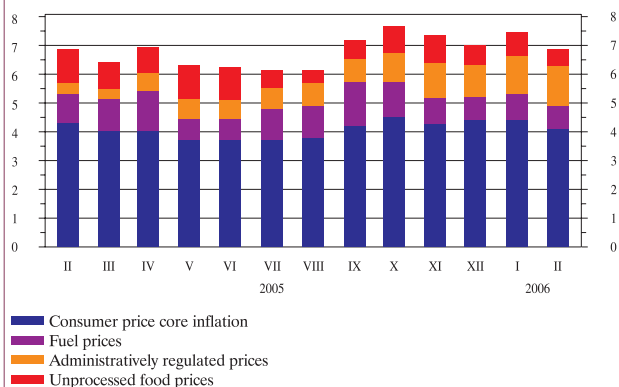
Similar economic development was also observed in the first months of 2006. In January, the working-day-adjusted retail trade turnover at constant prices improved by 18.6% year-on-year. The seasonally adjusted volume index of industrial output in manufacturing rose by 5.8% and total industrial output expanded by 8.6%. In February, cargo turnover at Latvian ports and the volume of rail freight decreased (by 10.4% and 10.6%, respectively). Unemployment rate remained unchanged (7.5%).

In comparison with January, consumer prices rose by 0.4%, whereas the annual inflation rate dropped to 6.9%, a low since August 2005. Price changes in February were mostly driven by a 1.5% rise in food prices, including an increase in vegetable and milk and dairy product prices of 17.6% and 1.9%, respectively. As in January, a 2.9% decline in the prices of clothing and footwear as a result of seasonal sales exerted a dampening effect on inflation.

In February 2006, the financial deficit of the general government consolidated budget was 2.1 million lats (a financial surplus of 2.8 million lats in February 2005). The central government basic budget deficit of 20.6 million lats was almost offset by the surplus in the social insurance fund and local government consolidated budget (7.3 million lats and 11.4 million lats, respectively). Tax revenue posted a buoyant growth of 25.6%. Foreign financial assistance inflows contracted by 6.7%. The growth of budgetary expenditure outpaced that of revenue (21.4% and 19.0%, respectively). The boost in tax revenue was driven by a rise in value added tax collections as well as personal income tax revenue and social insurance contributions (28.0% and 26.5%, respectively). Despite the increase in the monthly untaxed minimum of personal income tax payers and the tax relief for a dependent person for the second consecutive year, the growth rate of personal income tax revenue also remained high. Raising the public sector wages and salaries, pensions and social benefits in early 2006 resulted in an increase in the general government consolidated budget expenditure.

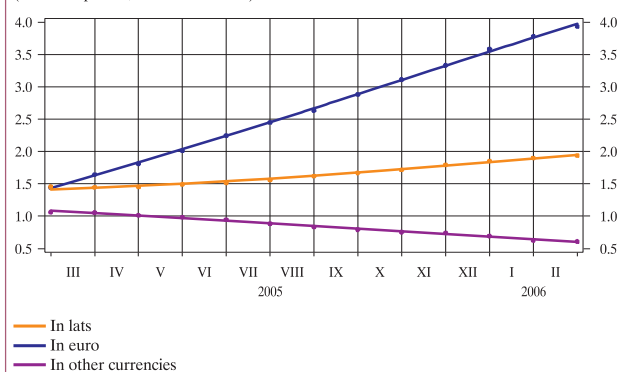
In February, the central government and local government debt grew by 94.7 million lats totalling 1 131.5 million lats at the end of the month. The external debt increased on account of the borrowing from the European Investment Bank in the amount of 52.7 million lats for the purpose of co-financing projects funded from the Cohesion Fund and EU Structural Funds. The auction of 12-month Treasury bills held in the domestic government securities market contributed to the growth of the domestic debt. Securities in the amount of 8.4 million lats (52.5% of the amount supplied) at the weighted average discount rate of 3.289% (67.9 basis points higher than at the previous auction held in December 2005) were sold at a competitive multi-price auction on the primary market.

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



### LOANS TO RESIDENT FINANCIAL INSTITUTIONS, NON-FINANCIAL CORPORATIONS AND HOUSEHOLDS

(at end of period; in billions of lats)



MACROECONOMIC INDICATORS	2006	
	I	II
Changes in the volume index of industrial output (year-on-year basis; %)	8.6	*
Changes in the CPI		
Month-on-month basis (%)	1.1	0.4
Year-on-year basis (%)	7.5	6.9
Annual rate of core inflation <sup>1</sup> (%)	5.8 <sup>2</sup>	5.4
Number of registered unemployed persons (at end of period)	79 368	79 625
Unemployment rate (%)	7.5	7.5
General government consolidated budget financial deficit/surplus (in millions of lats)	64.4	62.3
Foreign trade (in millions of lats)		
Exports	217.7	*
Imports	375.2	*
Balance	-157.5	*

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

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

\* Figure available at a later date.

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

Currency outside MFIs resumed a rising course in February. Overnight deposits expanded and money supply M1 increased by 39.6 million lats or 1.4%. M2 reported a slightly higher growth (67.8 million lats or 1.7%), with both deposits with agreed maturity of up to two years and deposits redeemable at notice of up to 3 months expanding. Broad money M3 rose by 71.1 million lats or 1.8%. Thus, the annual growth rate of M1 remained unchanged in February (43.0%), whereas that of M2 and M3 decreased (to 38.4% and 40.0%, respectively).

The deposits of resident financial institutions, non-financial corporations and households grew by 46.6 million lats, with euro and lats deposits expanding. For the second consecutive month, the pickup in deposits only resulted from deposits of households.

The loans granted to resident financial institutions, non-financial corporations and households rose by 185.3 million lats or 2.9%. The annual growth rate of lending accelerated to 63.7%. Albeit slightly exceeding that of January, in absolute terms monthly increase remained substantially lower than the average in the last four months of 2005. An upsurge in mortgage loans (113.2 million lats) contributed to the growth of lending, with loans granted to households for house purchase expanding by 71.2 million lats. A rise in euro loans (159.2 million lats) continued to account for the pickup. An increase in loans granted in lats was also retained (42.5 million lats), with those granted in other currencies shrinking. Household lending grew by 100.8 million lats and loans granted to financial institutions and non-financial corporations – by 84.5 million lats.

The negative net foreign assets of MFIs rose by 50.1 million lats in February. MFI (excluding the Bank of Latvia) assets expanded by 217.1 million lats in February, with profit reaching 32.5 million lats in the first two months of 2006 (26.5% higher than in the respective period of the previous year).

With repo loans granted to banks shrinking, banks' deposits with the Bank of Latvia declined, hence the monetary base M0 decreased by 21.6 million lats month-on-month. The central bank's money supply was affected by resumed foreign currency purchase transactions, resulting in an increase in the Bank of Latvia's net foreign assets (66.7 million lats). At the end of February, the backing of the national currency with the Bank of Latvia's net foreign assets was 102.8%. The impact of foreign currency purchase was offset by a decline in repo loans (72.0 million lats) granted to banks and expansion of the Government deposits with the Bank of Latvia (15.7 million lats). Repo loans granted by the Bank of Latvia accounted for 44.2 million lats (7 times lower than in January) and time deposits attracted by the Bank of Latvia amounted to 12.9 million lats (3.6 times higher).

RIGIBOR on overnight loans stood at 4.1%–4.3% throughout the month, shrinking only temporarily on the last days of the reserve maintenance period. RIGIBOR for loans with a 6- and 12-month maturity remained broadly unchanged in February (at the end of the period, 3.82% and 3.70%, respectively). Interest rates on loans granted to households continued to grow: interest rates on loans granted in lats rose by 0.9 percentage point (including loans granted to households for house purchase – by 0.3 percentage point), whereas those on loans granted in foreign currency expanded by 0.2 percentage point.

In February, the US dollar, the Japanese yen and the British pound sterling appreciated against the lats by 2.1%, 3.0% and 0.6%, respectively.

**MONETARY INDICATORS** (at end of period; in millions of lats)

	2006	
	I	II
<b>MFIs<sup>1</sup></b>		
<b>M3</b>	3 957.6	4 028.7
Repurchase agreements	0	0
Money market fund shares and units	38.1	41.4
Debt securities issued with maturity of up to 2 years	3.6	3.6
<b>M2</b>	3 915.9	3 983.7
Deposits with agreed maturity of up to 2 years	937.4	958.0
Deposits redeemable at notice of up to 3 months	109.5	117.0
<b>M1</b>	2 869.1	2 908.7
Currency outside MFIs	768.2	775.5
Overnight deposits	2 100.9	2 133.2
Net external assets	-1 410.5	-1 460.6
Credit to resident financial institutions, non-financial corporations and households	6 315.9	6 501.2
Credit to general government	407.1	391.7
Deposits of central government	131.5	160.6
Longer-term financial liabilities	1 252.9	1 275.8
<b>Bank of Latvia</b>		
<b>M0</b>	1 454.9	1 433.3
Currency in circulation	853.9	862.1
Deposits with the Bank of Latvia in lats	601.0	571.2
Deposits with the Bank of Latvia in foreign currencies	0	0
Net foreign assets	1 406.8	1 473.5
Net domestic assets	48.1	-40.2
Credit	111.0	21.8
To MFIs	74.0	2.0
To central government (net)	37.0	19.8
Other items (net)	-62.9	-62.0
International reserves (at end of period; in millions of US dollars)	2 420.53	2 504.56
Gold	139.83	138.27
Special Drawing Rights	0.14	0.15
Reserve position in the IMF	0.08	0.08
Foreign convertible currencies	2 280.48	2 366.06

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

**EXCHANGE RATES SET BY THE BANK OF LATVIA AND INTEREST RATES**

	2006	
	I	II
Weighted average interest rate on domestic interbank loans in lats	4.0	3.7
Interest rates on loans to resident non-financial corporations and households		
Loans to non-financial corporations (in lats)	6.4	6.5
Loans to households (in lats)	7.2	8.1
incl. for house purchase	5.8	6.1
Loans to non-financial corporations (in foreign currencies)	5.3	5.1
Loans to households (in foreign currencies)	4.7	4.9
incl. for house purchase	4.4	4.6
Interest rates on deposits of non-financial corporations and households		
Time deposits of non-financial corporations (in lats)	3.6	3.5
Demand deposits of non-financial corporations (in lats)	1.1	1.0
Time deposits of households (in lats)	3.1	3.1
Demand deposits of households (in lats)	0.5	0.5
Time deposits of non-financial corporations (in foreign currencies)	2.8	2.4
Demand deposits of non-financial corporations (in foreign currencies)	1.2	1.1
Time deposits of households (in foreign currencies)	3.0	3.0
Demand deposits of households (in foreign currencies)	1.1	1.1
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	0.5810	0.5930
LVL/GBP	1.0270	1.0330
LVL/100 JPY	0.4950	0.5100
LVL/EUR	0.7028	0.7028

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

	2006	
	I	II
MFI reserves	685.6	656.1
Vault cash in national currency	85.7	86.5
Deposits with the Bank of Latvia	599.9	569.5
Foreign assets	3 389.3	3 443.0
Vault cash in foreign currencies	59.5	59.7
Claims on MFIs	2 152.0	2 144.1
Claims on non-MFIs	1 146.3	1 200.4
Other assets	31.5	38.7
Claims on central government	255.0	241.1
Claims on local government	89.3	89.3
Claims on public non-financial corporations	114.3	109.4
Claims on financial institutions and private non-financial corporations	3 712.1	3 801.8
Claims on households	2 525.1	2 625.9
Unclassified assets	468.9	490.1
Fixed assets	137.6	140.3
Items in transit	14.6	13.1
Other assets	72.0	73.4
Claims on resident MFIs (incl. investments)	244.7	263.3
<b>Total assets</b>	<b>11 239.5</b>	<b>11 456.6</b>
<i>Memo item: Trust assets</i>	381.2	391.7
Overnight deposits in lats	1 208.3	1 219.6
Public non-financial corporations	56.0	53.5
Financial institutions and private non-financial corporations	543.0	540.3
Households	609.4	625.8
Time deposits and deposits redeemable at notice in lats	671.9	686.1
Public non-financial corporations	55.2	61.4
Financial institutions and private non-financial corporations	205.5	200.9
Households	411.2	423.8
Foreign currency deposits of residents	1 336.0	1 357.1
Public non-financial corporations	19.5	14.5
Financial institutions and private non-financial corporations	443.7	444.6
Households	872.8	898.0
Deposits of central government	105.6	119.1
Deposits of local government	82.0	93.9
Transit funds	4.9	4.9
Foreign liabilities	6 206.6	6 377.1
Liabilities to MFIs	2 955.4	3 125.4
Liabilities to non-MFIs	2 966.4	3 054.7
Other liabilities (incl. subordinated liabilities)	284.9	197.1
Liabilities to the Bank of Latvia	74.0	2.0
Debt securities issued	162.5	162.8
Money market fund shares and units	38.1	41.4
Capital and reserves	854.7	880.8
Residents	527.7	552.1
Non-residents	327.0	328.7
Provisions	88.0	90.6
Unclassified liabilities	407.0	421.2
Items in transit	105.0	113.5
Other liabilities (incl. subordinated liabilities)	84.6	72.4
Liabilities to resident MFIs	217.4	235.3
<b>Total liabilities</b>	<b>11 239.5</b>	<b>11 456.6</b>
<i>Memo item: Trust liabilities</i>	381.2	391.7

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>).