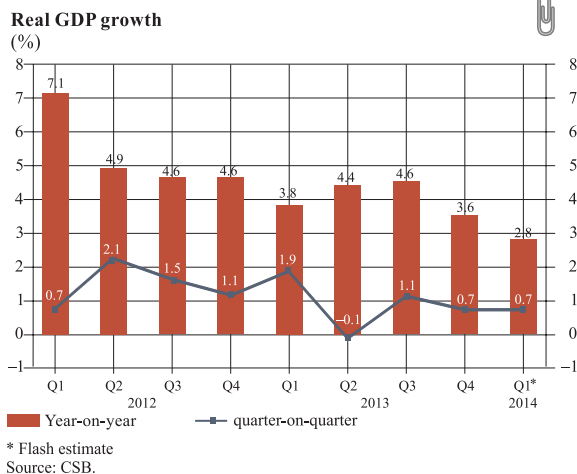




LATVIJAS BANKA
MONTHLY NEWSLETTER

MAY 2014

Latvian economy growing at a stable rate

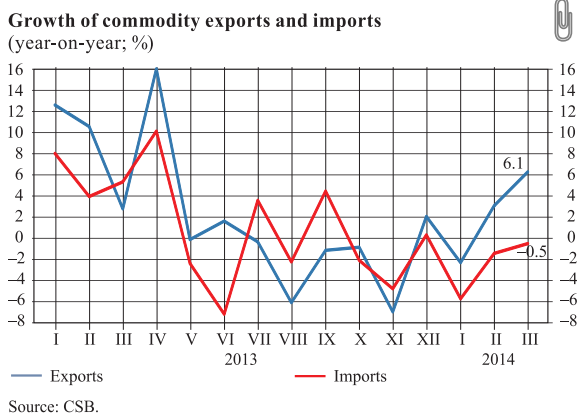


According to the flash estimate, GDP grew by 0.7% quarter-on-quarter (seasonally adjusted data) and by 2.8% year-on-year in the first quarter of 2014.

There were some positive surprises in the first quarter, supporting the GDP growth. Firstly, because of the warm weather conditions activity in construction was stronger than usually in the winter months. Thus, in all likelihood, we can expect a substantial rise in the construction sector in the first quarter. Secondly, the transport sector (particularly transportation through ports) has performed especially well during the first three months of the year. Moreover, other services sub-sectors, including utilities, have posted stable growth in recent quarters. The continued recovery of the EU economies will allow Latvian manufacturers to raise their export volumes, yet currently the main uncertainty is related to the tensions between Ukraine and Russia. At the moment, there are no macroeconomic signs

that would indicate that the Latvian economy is already suffering from the effects of the above-mentioned geopolitical situation. However, new tensions could weigh on economic activity by hurting business and consumers confidence.

Latest export data confirm the flexibility of Latvian exporters to adapt to changes in external demand



In March 2014, the turnover of external trade in Latvian goods grew by 11.2%. Despite the deterioration of the political and economic situation concerning its eastern neighbours, the exports of Latvian goods increased by 7.3% month-on-month. The annual rise in the exports of goods reached 6.1%, whereas the respective imports decreased by a mere 0.5%.

Compared to February, the fastest growth was reported for the exports of products of chemical and allied industries (exports of medical products to Uzbekistan and Finland), mineral products, wood products, electrical and optical equipment, furniture and transport vehicles. According to the preliminary data of the World Trade Organization, the Latvian export market shares in the world's imports continued to expand in the first two months of this year.

The structural changes in manufacturing, i.e. gradual re-focussing on the production of higher value added goods, together with cost competitiveness will pave the road for further growth in commodity exports this year. Yet this might be dampened by weaker external demand.

Annual inflation was 0.7% in April



In April, the annual inflation rose to 0.7%. One of the reasons for this rise was the gradual shrinking of the negative contribution of supply-side factors to inflation. For example, in the case of thermal energy and fuel it was explained by the base effect. Compared to March, the negative contribution from prices of unprocessed food also diminished, while the prices of processed food rose.

Reflecting the economic growth with a slight lag, core inflation is higher this year than the average for 2013. At the same time, the consumer survey conducted by the European Commission in April points to further decreasing of the inflation expectations in Latvia, i.e. the percentage of respondents believing that the prices will rise rapidly in the course of the next year is declining. In the coming periods, domestic factors are not

expected to cause substantial inflationary pressure, while the main risks are related to the global food and energy price developments.

	Reporting period	Data (%)
Gross Domestic Product (GDP)		
Real GDP (year-on-year growth)	2014 Q1 <i>(flash estimate)</i>	2.8
Real GDP (quarter-on-quarter growth; seasonally adjusted) 09.05.2014 Despite weaker retail trade and industry growth, the economy growing at a stable rate 	2014 Q1 <i>(flash estimate)</i>	0.7
Public Finances		
Tax revenue (since the beginning of the year; year-on-year growth)	2014 IV	3.4
General government budget expenditure (since the beginning of the year, year-on-year growth)	2014 IV	4.1
Consumer price changes		
Consumer Price Index CPI (year-on-year growth)	2014 IV	0.7
Consumer Price Index HICP (year-on-year growth)	2014 IV	0.8
12-month average inflation (HICP) 12.05.2014 The annual inflation level characterizes a moderately growing economy 	2014 IV	0.1
Foreign trade		
Exports (year-on-year growth)	2014 III	6.1
Imports (year-on-year growth) 12.05.2014 Latest export data support the ability of Latvian exporters to quickly adapt to changes in external demand 	2014 III	-0.5
Balance of payments		
Current account balance (ratio to GDP)	2013 Q4	0.8
Foreign direct investment in Latvia (net flows; ratio to GDP)	2013 Q4	3.5
Industrial output		
Working day-adjusted manufacturing output index (year-on-year growth) 06.05.2014 Manufacturing output on the rise 	2014 III	3.9
Retail trade turnover		
Retail trade turnover at constant prices (year-on-year growth) 30.04.2014 After euro introduction, retail trade volumes in Latvia more stable than in Estonia 	2014 III	3.8
Labour market		
Registered unemployment (share in working age population)	2014 IV	9.6
Job seekers rate (share in working age population) 15.05.2014 Labour market improvement is slow, but it should not be speeded up artificially 	2014 Q1	11.9
Monetary indicators		
Resident deposits (year-on-year growth) 30.04.2014 No substantial change in deposit and loan level in March 	2014 III	11.4

Source: Treasury, Central Statistical Bureau of the Republic of Latvia, and Latvijas Banka data.

Growing use of non-cash payments in the light of the euro changeover

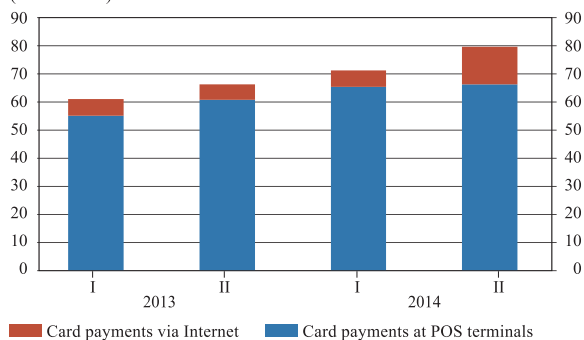


Anda Zalmane
Payment systems
analyst
Latvijas Banka

According to statistical data compiled by Latvijas Banka, in 2013 **the total volume and value of non-cash payments used in Latvia expanded by 12.8% (to 297.7 million) and 17.8% (to 579.2 billion euro) respectively**. The value increase exceeded the growth of GDP several times. In the second half of the year, this increase was even higher and was inter alia attributable to the growing household deposits before the introduction of euro.

The highest year-on-year growth in volume, at 18.5%, was recorded for card payments. As a result, card payments became the most frequently used non-cash payment instrument in Latvia for the first time ever. Card payments were mostly used as an alternative for cash when shopping; however, the expansion in card payments was mainly attributable to a rise in the card payments initiated via Internet, since online shopping in euro became easier as currency conversion became unnecessary.

The number of card payments
(in millions)

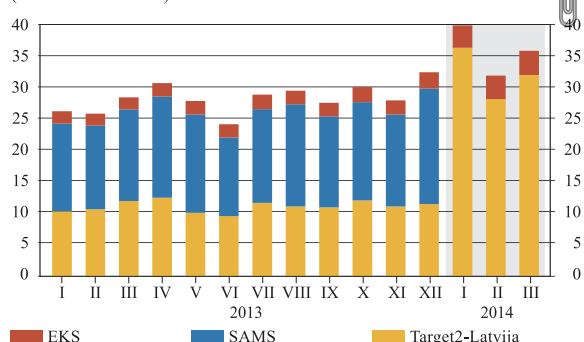


Credit transfers, e.g. payments initiated in internet-banking applications, were the second most popular non-cash payment instrument in 2013. Credit transfers are predominately used by businesses as well as in transfers between private individuals. The volume of those particular payments grew by 7.3% year-on-year. With the euro changeover, national credit transfers were substituted by SEPA credit transfers and similar terms for all SEPA credit transfers in Latvia were provided. This means that the fees for cross-border payments with Europe were aligned with the fees for domestic payments in Latvia. As a result, the fees for cross-border payments dropped about ten times.

The main precondition for providing non-cash payment services to the public is a safe and reliable functioning of the payment systems. In Latvia, the card processing infrastructure is provided by the private company First Data Latvia as well as by the international card companies VISA and MasterCard, whereas the payment systems for the processing of credit transfers and large-value interbank transfers are operated by Latvijas Banka.

In 2013, Latvijas Banka ensured the operation of the payment systems for settlements in lats and euro. Following the euro changeover, the operation of the payment systems in lats was discontinued. In 2014, Latvijas Banka operates two systems: TARGET2-Latvija and the Electronic Clearing System (EKS). The daily average of payments processed by Latvijas Banka continued to grow and in the first quarter of 2014 totalling 143.3 thousand payments with a daily value of 1.7 billion euro, representing an increase of 2.4% in terms of volume and 30.8 % in terms of value over 2013. For comparison, the amount equal to Latvia's GDP is processed via Latvijas Banka's payment systems in less than 20 days.

Value of payments processed by Latvijas Banka payment systems
(in billions of euro)



TARGET2-Latvija is the national component of TARGET2, the Trans-European Automated Real-time Gross settlement Express Transfer system operated by the Eurosystem's central banks. TARGET2 is one of the largest payment systems in the world. TARGET2 settles the Eurosystem monetary policy operations, large value financial market transactions as well as final positions coming from other payment and financial instrument settlement systems.

The EKS, Latvijas Banka's retail payment system, is used for the processing of credit transfers initiated by bank customers. The EKS is a SEPA compliant system interlinked with other European retail payment systems and thus providing cheap and reliable means for making

payments from Latvia to all over Europe. The EKS provides the possibility for banks to execute their customer payments on the same day or at least next day following payment initiation.

Therefore, by ensuring a smooth functioning of the two payment systems, Latvijas Banka provides the financial sector with a safe and reliable infrastructure for financial market transactions, thus contributing to the overall economic growth and financial stability. Moreover, Latvijas Banka provides the general public with reliable means to make retail payments safely, in a timely manner and at low risks, promoting quick money circulation in the economy.