

# MACROECONOMIC AND BUDGETARY REVIEW

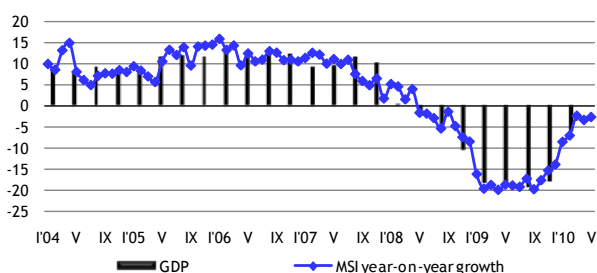


MINISTRY OF FINANCE  
REPUBLIC OF LATVIA

May, 2010

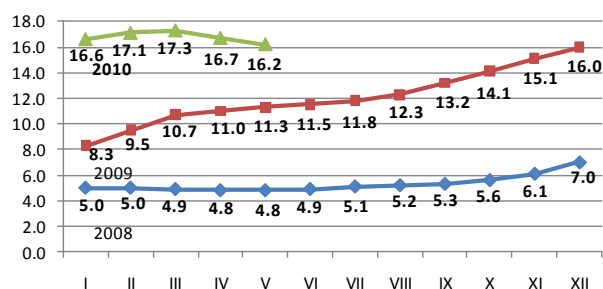
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According to the estimations of the Ministry of Finance, the **Composite Index of Macroeconomic Indicators** (index is calculated using operative data on economy, in order to get a view of possible GDP growth) in May 2010 shrunk by 2.6% at constant prices. The decrease of index was caused by a slowdown in retail trade turnover, reduction of the amount of loaded/unloaded cargoes and decrease of the employment level.



Composite Index of Macroeconomic Indicators

There was an improvement in unemployment indicators due to seasonal factors already for the second months. Officially registered **unemployment rate** in May compared to the previous month decreased by 0.5 percentage points and amounted to 16.2% of the economically active population at the end of the month. The number of the registered unemployed fell by 6.4 thsd people from the previous month and amounted to 183.5 thsd people at the end of May. During this period status of unemployed was assigned to 1.8 thsd less people than in April an amounted to 10.3 thsd. The number of registered vacancies in the State Employment Agency in May increased as rapidly as in April - by 23.8% compared to April and reached 2.6 thsd.

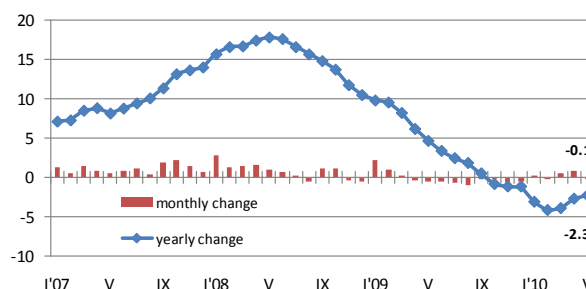


Officially registered unemployment rate, %

In May 2010 unemployment rate has decreased in all region of Latvia compared to April 2010. The highest unemployment rate in May 2010 was still registered in the region of Latgale, 22.8% (15.2% in May 2009); in the region of Vidzeme, 17.9% (12.0%); in the region of Zemgale, 17.8% (12.3%); and in the region of Kurzeme, 17.1% (12.4%). The lowest unemployment rate was registered in the region of Riga, 13.2% (9.5%).

**Consumer Price Index (CPI)** in May 2010, compared with April 2010, decreased by 0.1%. Average price levels for both goods and

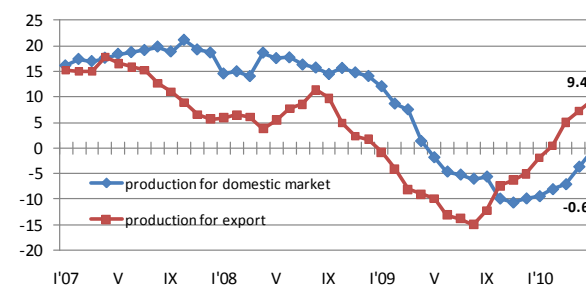
services declined by 0.1%. Compared to the corresponding month of the previous year, consumer prices decreased by 2.3%, average prices for goods fell by 1.0%, for services – by 5.6%.



Consumer price index, %

Consumer price changes in May 2010 for the most part were influenced by increase in heating and vegetable prices and decrease in meat product and disposable household ware prices. The ongoing rise of heating tariffs increased their price during the month by 3.2%. Fluctuations of prices were mostly driven by price reduction campaigns held by large retail sellers. Also the seasonal price increase took place for various vegetables.

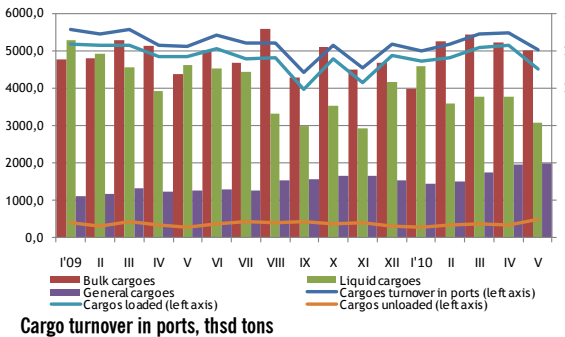
In May 2010 **producer prices** increased by 1.8% compared to April 2010. In May 2010 compared to May 2009 producer prices increased by 3.3%. Substantial contribution to the price changes came from manufacturing of basic metals that showed a rise by 25.1%, wood and wood product (except furniture) prices gained 14.2%. There was also a decrease in producer prices for mining industry – by 4.6%, furniture production – by 4.2% and food product manufacturing – by 0.8%. Producer prices for exports are growing faster than prices for local market (yearly change accordingly 9.4% increase and 0.6% decrease, monthly change is 3.1% and 0.9% growth accordingly). The reason is that external market demand is recovering faster than internal market demand.



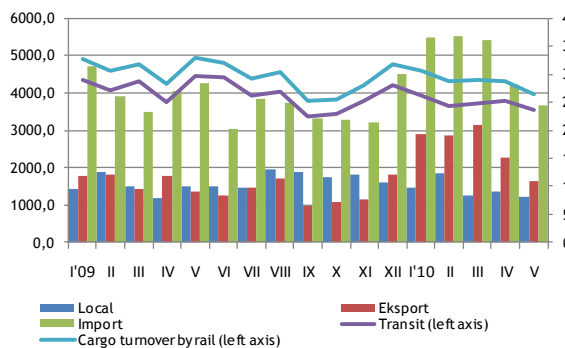
Producer price index, %

The volume of **cargo transhipped in Latvian ports** in May amounted to 5.0 mln t, down by 2.1% from the corresponding month of 2009. May data show that the cargo turnover at ports, compared with the previous month has decreased. A loaded cargoes turnover dropped, but cargoes unloaded turnover increased. Positive that ports cargo turnover has increased for goods with greater added value – general cargoes. In May

2010 freight carried by rail was 4.0 mln tons, a decrease of 19.4% compared to the same period of the previous year. The big drop in the May 2010 is partly due to high freight turnover growth by railway in May 2009. Compared with April of this year turnover of freight by rail has dropped by 7.9%.



Cargo turnover in ports, thsd tons

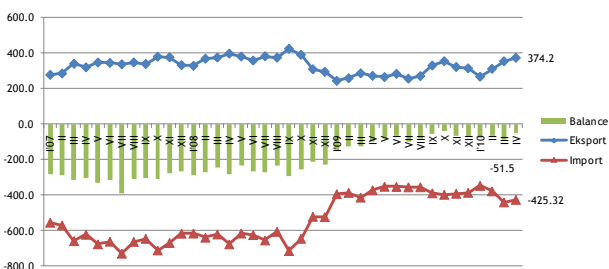


Cargo turnover by rail, thsd tons

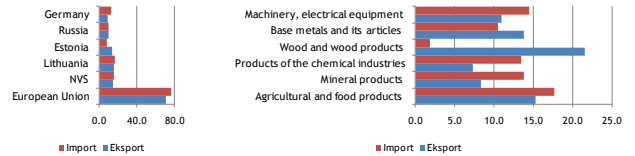
In April 2010 the total foreign trade turnover at current prices reached 799.5 mln lats – more by 4.8 mln lats or 0.6% than a month before and more by 139.6 mln lats or 21.2% than in April 2009, according to provisional data of Central Statistical Bureau.

In January - April 2010 total volume of goods in foreign trade of Latvia at current prices reached 2896.4 mln lats – an increase of 211.7 mln lats or 7.9%, if compared to January – April 2009. Of which exports volume grew by 209.7 mln lats or 19.1% and was 1309,6 mln lats, but imports volume – increased by 2.0 mln lats or 0.1% and was 1586,8 mln lats.

In April 2010, compared to the previous month, rise in export and decline in import improved trade balance. In April 2010, as compared to the April 2009, the trade balance deficit decreased by 47.6 mln lats and amounted to 51.1 mln lats.

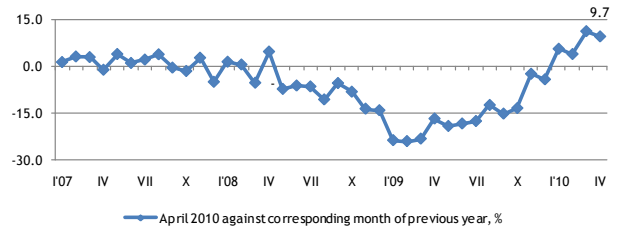


Foreign trade balance, mln lats

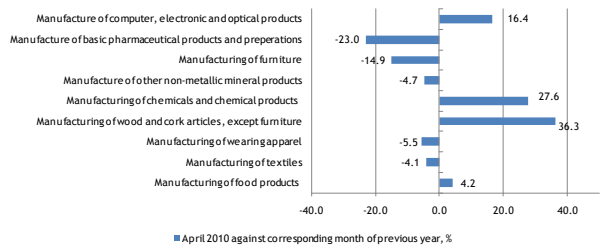


Main trading partners and commodities in Latvia's foreign trade, in April

Compared to April of previous year industrial production output in April 2010 has increased by 9.7%, according to working day adjusted data at constant prices. The growth was influenced by the production increase in electricity and gas supply by 20.2%, in manufacturing – by 8.0%, in mining and quarrying – by 1.9%. Over the past four months industrial output is positive, after more than a year and a half drop.

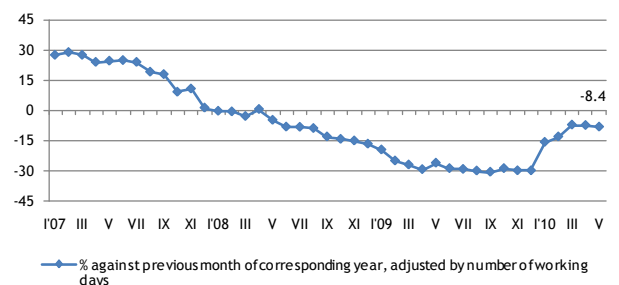


Industrial production index (seasonally adjusted data)

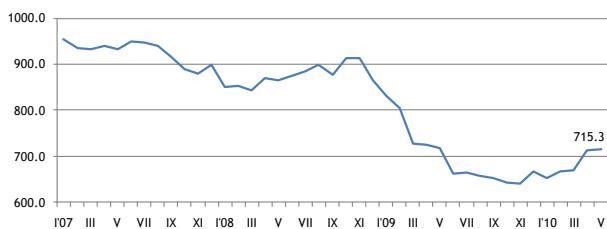


Most important changes in volume indices of industrial production (seasonally adjusted data)

According to working (trade) day adjusted data, retail trade turnover in constant prices in May 2010, compared to May 2009, has reduced by 8.4%. Most notable decrease was recorded in food product group – by 10.5%. Slightly smaller reduction was recorded in companies selling non-food products – by 7.2%. Compared to April 2010, retail trade decrease by 0.4%, but a slight decrease in May doesn't indicate a drop in retail activity. At the end of last year, when was observed the lowest point of the retail turnover, now it is on much higher level.



Turnover indices of retail trade (at constant prices)



Cash in circulation, mln lats

	XII	10'1	II	III	IV	V
RIGIBOR (3month)	7.46	4.00	2.81	2.25	2.08	2.27
EURIBOR (3month)	0.71	0.67	0.66	0.64	0.65	0.697

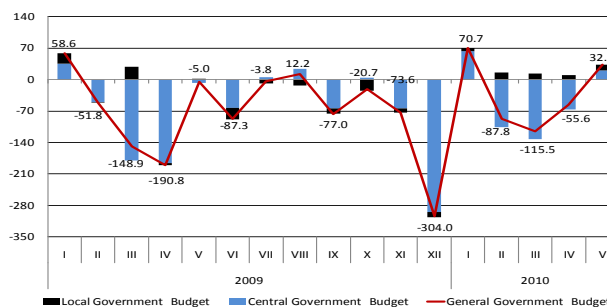
Money Market Indexes RIGIBID and EURIBOR for last 6 month on 25th date of each month

In the first five months of 2010 economic recession continued to negatively influence budget revenue in comparison with the same period of 2009, as a result amount of money received in the budget declined both in tax revenue and non-tax revenue.

	I-V 2010 execution, mln lats	I-IV 2010 execution changes against I-V of 2009, %
<b>GENERAL GOVERNMENT BUDGET</b>		
Revenue	1939.62	-5.8
Expenditure	2094.90	-12.6
Financial Balance	<b>-155.28</b>	
<b>CENTRAL GOVERNMENT BUDGET</b>		
Revenue	1602.29	-4.6
Expenditure	1822.86	-11.8
Financial Balance	<b>-220.57</b>	
<b>Central government basic budget</b>		
Revenue	1135.65	-2.8
Expenditure	1145.40	-23.2
Financial Balance	<b>-9.75</b>	
<b>Central government special budget</b>		
Revenue	464.69	-13.1
Expenditure	680.75	12.3
Financial Balance	<b>-216.06</b>	
<b>LOCAL GOVERNMENT BUDGET</b>		
Revenue	503.46	-17.3
Expenditure	444.77	-20.8
Financial Balance	<b>58.69</b>	

Budget revenue and expenditure

In accordance with the State Treasury's official monthly report's data for the period of January - May 2010 (I-V), **general government consolidated budget** revenue in the first five months of 2010 was 1 939.62 mln lats, which was by 5.8% less than in the same period of 2009. Expenditure declined more rapidly than revenue. General government consolidated budget expenditure in the first five months of 2010 was 2 094.90 mln lats, which is by 12.6% less than in the same period of 2009. In the first five months of 2010 general government consolidated budget financial deficit was in amount of 155.3 mln lats, which was determined by high level of deficit in the central government special budget.



General government budget balance, mln lats

**Central government consolidated budget** revenue (including grants, donations and derived public persons) in the first months of 2010 composed 39.9% of planned annual revenue amount while still maintaining revenue decrease observed in the previous months compared with the same period of 2009. Revenue decrease was 78.0 mln lats or 4.6%, which, mainly, was due to the tax revenue decrease by 11.6%. In comparison with the first five months of 2009 was observed increase in non-tax revenue (an increase of 48.8 mln lats), donations and grants (an increase of 1.6 mln lats) and foreign financial assistance (an increase of 28.5 mln lats).

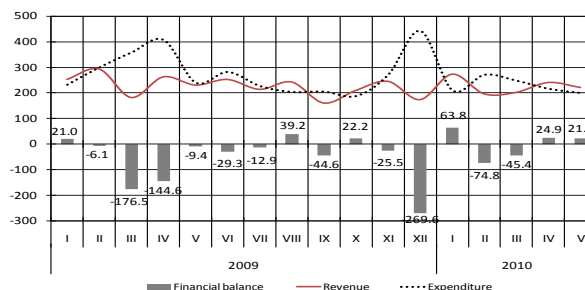
In the first five months of 2010 central government consolidated budget expenditure was 39.3% of planned annual expenditure amount, but, in comparison with the same period of 2009, expenditure decreased by 244.8 mln lats or by 11.8%.

In the first five months of 2010 central government consolidated budget financial deficit was 220.6 mln lats.

**Central government basic budget** revenue reduction in the first five months of 2010 was influenced by tax revenue decrease by 13.3% and revenue decline from the paid services and self-earned revenue - by 21.5%. In the first five months of 2010 total revenue was 42.1% of the planned central government basic budget annual revenue.

Central government basic budget expenditure reduction by 346.0 mln lats, mainly was influenced by cost decline in maintenance expenditure in amount of 296.1 mln lats (including cost reduction of current expenditure, subsidy and grant distribution) and for capital expenditure in amount of 49.9 mln lats (including a reduction in expenditure for capital formation, total transfers decline). The total expenditure was 36.9% of planned annual amount.

Central government basic budget financial deficit in the first five months of 2010 was 9.8 mln lats.



Central government basic budget, mln lats

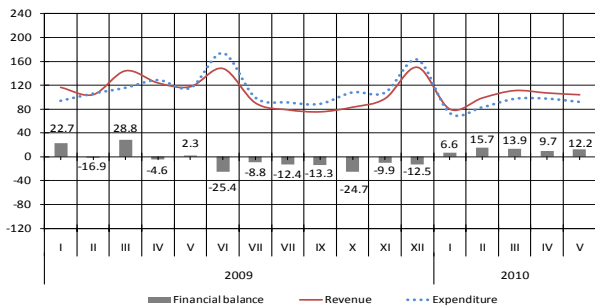
Unlike central government basic budget, local government basic budget and special budget expenditure decline, the **central government special budget** expenditure continued to grow and in the first five months of 2010 increased by 74.3 mln lats or 12.3% compared with

the same period of 2009. Expenditure increase was defined by increase in unemployment rate compared with the same period of 2009 and pension detention reimbursement in April of 2010. As a result social benefits and public pensions total costs increased by 79.1 mln lats and in the first five months of 2010 expenditure for social benefits was 44.4% of planned annual expenditure amount.

In the first five months of 2010 **local government consolidated budget** revenue decreased compared with the same period of 2009, mainly due to personal income tax revenue decrease by 6.2% and goods and services tax revenue decrease by 29.7%. Also local government basic budget revenue reduction was influenced by basic budget transfers amount - by 45.3% less in comparison with the first five months of 2009. Local government consolidated budget in the first five months of 2010 received 44.1% of expected annual revenue.

The decrease of local government consolidated budget expenditure mainly was due to the local government basic budget maintenance expenditure reduction by 25.4%, which included wage reduction by 31.7%, goods and services expenditure reduction by 9.9%. By contrast, the local government basic budget expenditure on social benefits, in comparison with the first five months of 2009, was by 50.7% more. The total amount of local government budget expenditure was 35.1% of planned annual expenditure amount.

In first five months of 2010 the local government consolidated budget financial surplus was in amount of 58.7 mln lats.



Local government consolidated budget, mln lats

According to information of State Revenue Service in the first five months of 2010 **tax revenue** exceeded the projected amount by 3.0%, because the corporate income tax, value added tax and lottery and gambling tax revenue was higher than expected.

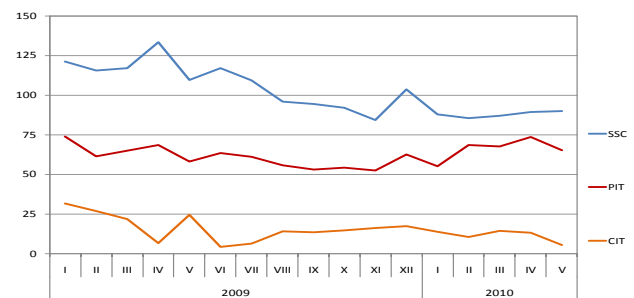
	I-V 2010 execution, mln lats	I-V 2010 execution of the same period plan, %	V 2010 execution of V 2010 plan, %	I-V 2010 execution changes against I-V 2009, %
Personal income tax	316.5	98.2	96.0	-3.2
Social security contributions	460.7	99.0	99.0	-22.9
Corporate income tax	57.0	107.6	49.5	-48.8
Value added tax	336.0	122.0	118.8	-5.2
Excise tax	179.9	92.9	89.7	-13.1
Lottery and gambling tax	7.2	106.8	142.6	-36.4
Customs tax	6.1	97.5	112.8	-24.3
Natural resources tax	3.6	94.6	72.1	-4.6
Total	1 367.1	103.0	99.3	-15.6

**Major tax revenue**

**Social security contributions (SSC)** (including contributions into the State Funded Pension Scheme) and **personal income tax (PIT)** revenue in first five months of 2010 continued to decline, although decrease of unemployment rate in May of 2010 was just 0.5 percentage point

compared with data in April of 2010. In the first five months of 2010 social security contributions revenue was 99,0% of the planned annual revenue. There was a lack of 5.7 mln lats to implement annual plan of personal income tax revenue.

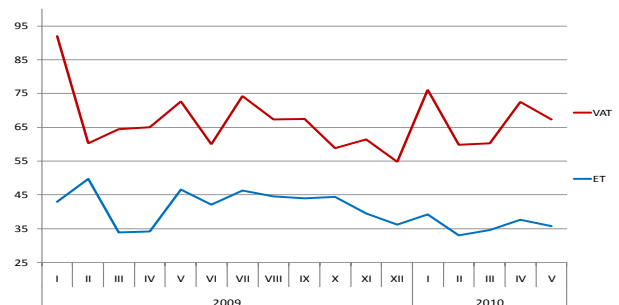
In first five months of 2010 **corporate income tax (CIN)** plan was exceeded by 7.6%, but total revenue in the same period of 2010 decreased by 48.8% compared with the first five months of 2009. According to State Revenue Service information revenue reduction was influenced by increased tax repayments in May of 2010 and by decline of corporate income tax contributions. From total corporate income tax revenue change, decrease of 57.0% was in the financial services industry, 41.7% in services and 40.1% - in wholesale industry. It should be noted that biggest part of corporate income tax revenue was made by taxpayers of post and telecommunications industry and building industry.



Direct tax revenue, mln lats

**Value added tax (VAT)** revenue in first five months of 2010 exceeded the projected revenue amount by 60.6 mln lats, but, in comparison with the same period of 2009, total value added tax revenue was by 18.3 mln lats or 5.2% less. These changes were due to the decrease of the total transaction value by 13.4%, also the decline of consumer prices.

The decrease of **excise tax (ET)** in the first five months of 2010 was still affected by the excise tax rate increase for practically all excise duties at the beginning of 2009 and also the decline of excise goods sale caused by the economic downturn. The excise tax revenue showed the reduction in such excise commodity groups as tobacco (revenue decreases by 34.4%), alcoholic beverages (revenue decreased by 13.3%) and oil products (revenue decreased by 6.6%). but the excise tax revenue increased by 55.0% of beer products sale.



Indirect tax revenue, mln lats

In first five months of 2010 general government budget **non-tax revenue** showed increase of 24.8 mln lats or 12.4%, in comparison with the same period of 2009. This mainly was due to revenue from dividends on the state capital and the Latvia Bank payment.

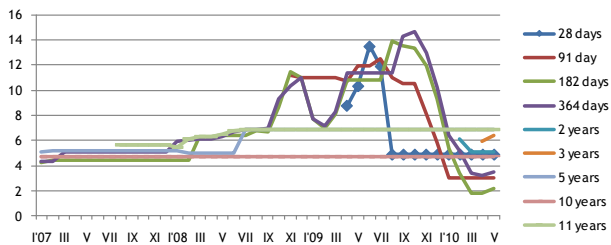
In first five months of 2010, revenue from the paid services and self-earned revenue was 89.7 mln lats, which is by 22.6% less than in first

five months of 2009. Foreign financial assistance revenue was 284.5 mln lats, which is by 2.5% less than in first five months of 2009.

In the end of May 2010 **public debt** was 4 728.8 mln lats and in first five months of 2010 increased by 589.4 mln lats. Domestic public debt was 39.1 mln lats less than in the end of December 2009 and was 847.5 mln lats in the end of May 2010. In the end of May 2010 external public debt total sum was 3 881.3 mln lats and since the beginning of this year was increased by 628.5 mln lats.

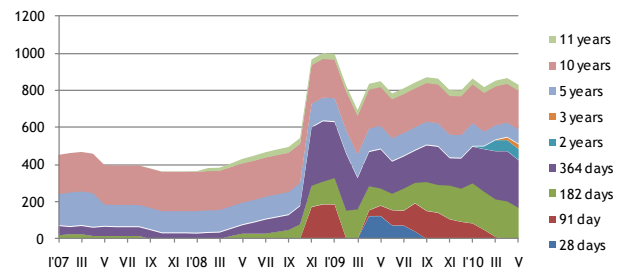
The Treasury in May sold **treasury bills** for a total amount of 23.0 mln lats. Overall investor demand for bonds in this period reached 56.6 mln lats in a nominal value. The six-month bills average weighted interest rate in last auction was 2.151%, 12-month bills average weighted interest rate was - 3.528%.

The Treasury in May sold **three-year bonds** for a total amount of 11,8 mln lats. Overall investor demand for bonds in this period reached 15.8 mln lats in a nominal value. The weighted average interest rate for 3-year bonds was 6.395%.



The average interest rate of government internal borrowing securities, %

In May 2010 government medium and long term bond weight in the domestic debt portfolio amounted to 48.0% (45.0% in May 2009), but short-term government bond proportion reached 52.0% (55.0%).



Structure of government internal borrowing securities turnover in May 2010, mln lats