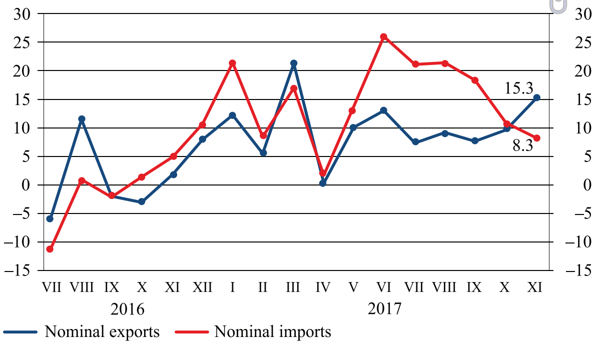
LATVIJAS BANKA
EIROSISTĒMA

LATVIJAS BANKA MONTHLY NEWSLETTER

JANUARY 2018

Successful year for Latvian exporters

Annual growth of total merchandise exports and imports
(%)



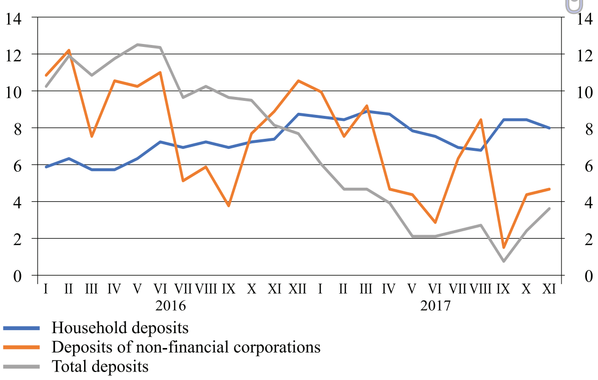
Source: CSB.

In November 2017, Latvia exported goods worth EUR 1.1 billion, which is the largest exported volume per month so far. Latvia's foreign trade balance slightly improved. Latvian producers are still taking advantage of the improved global economic situation. The resumption of demand in the main trading partners and a rise in export prices have helped exports to return as a determinant engine of Latvian economic growth. The first eleven months of the year saw a 10.2% year-on-year rise in the value of exports of goods. Positive export growth is ensured by practically all groups of goods. The most important contribution to 2017's export growth was made by food products, articles of base metals, machinery and electrical equipment, products of wood, animal products and products of the chemical industry.

In 2017, exports of goods have posted an increase both in real and nominal terms. Moreover, export growth was mainly ensured by exports manufactured domestically rather than by re-exports.

Corporate and household deposits up

Domestic deposits
(year-on-year; %)



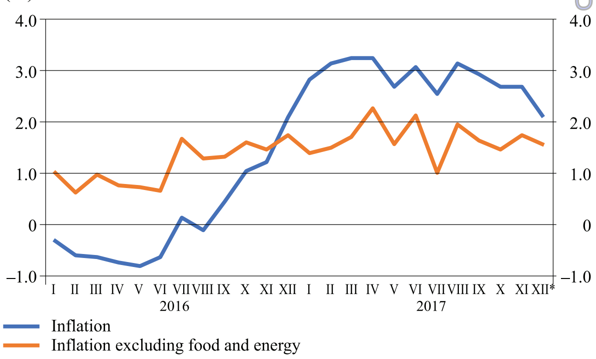
Source: Latvijas Banka.

In anticipation of the approaching year-end spending spree, notable increases in corporate and household savings were recorded in bank accounts in November. Domestic deposits with banks expanded, including increases in corporate and household deposits. Meanwhile, deposit dynamics by maturity remained unchanged: overnight deposits and deposits redeemable at notice expanded, while deposits with an agreed maturity shrank. The strengthening of the economy is likely to stimulate accumulation of savings also in 2018 and this is a positive factor both supporting financial sector stability and developing economic growth potential.

As regards lending growth, despite favourable financing conditions provided by the central bank, it still remained weak overall, with merely a slight increase in loans to non-financial corporations and those for house purchase. In 2018, lending will continue to develop on a very moderate path and will not be among the main drivers of economic growth; nevertheless, some growth is expected both in corporate lending (in the real estate and construction sectors in particular) and loans to households for house purchase and consumer credit.

Inflation growth moderates at the close of the year

Annual HICP inflation and core inflation
(%)



Source: CSB.
* Based on CPI data.

According to the Central Statistical Bureau data, the annual inflation rate in December stood at 2.2%, down from 2.7% in November. Annual inflation declined on account of the base effect of the fuel and food price rises observed at the end of 2016. In month-on-month terms, prices of non-food goods posted a minor drop, while those of service increased; therefore the average price level remained the same as in November. Although prices for some groups of food products still remain high in annual terms (milk, butter), last few months have seen more moderate price rises or even a fall in them. This can be explained by both global changes in food prices and the impact of the domestic market factors. Meanwhile, the rise in service prices could be seen as a signal suggesting higher demand driven by the rapid increase in wages.

Based on the official statistics for December 2017, the average annual inflation rate is also available: it is 2.9% and corresponds to the forecast released by Latvijas Banka already in June. Latvijas Banka's inflation projection for 2018 is 2.9% as well. Meanwhile, the oil price stabilisation at levels above 60 US dollars per barrel is seen as the main upward risk on inflation.

	Reporting period	Data (%)
Gross domestic product (GDP)		
Real GDP (year-on-year growth)	2017 Q3	**6.2**
Real GDP (quarter-on-quarter growth; seasonally adjusted)	2017 Q3	**1.5**
Public finances		
General government budget expenditure (since the beginning of the year; year-on-year growth)	2017 XII	**7.4**
Tax revenue (since the beginning of the year; year-on-year growth)	2017 XII	**8.0**
Consumer price changes		
Consumer Price Index (CPI; year-on-year growth)	2017 XII	**2.2**
Harmonised Index of Consumer Prices (HICP; year-on-year growth)	2017 XII	**1.4**
12-month average inflation (HICP)	2017 XII	**2.9**
12.01.2018 Inflation growth moderates at the close of the year		
Foreign trade		
Exports (year-on-year growth)	2017 XI	**15.3**
Imports (year-on-year growth)	2017 XI	**8.3**
Balance of payments		
Current account balance (ratio to GDP)	2017 Q3	**5.5**
Foreign direct investment in Latvia (net flows; ratio to GDP)	2017 Q3	**5.5**
Industrial output		
Working day-adjusted manufacturing output index (year-on-year growth)	2017 XI	**9.1**
Retail trade turnover		
Retail trade turnover at constant prices (year-on-year growth)	2017 XI	**4.7**
Labour market		
Registered unemployment (share in working age population)	2016 XII	**6.8**
Jobseekers rate (share in working age population)	2017 Q3	**8.5**
Monetary indicators		
Resident deposits (year-on-year growth)	2017 XI	**3.7**
29.12.2017 Corporate and household deposits up		

Sources: Treasury, CSB and Latvijas Banka.

What will the second Payment Services Directive bring about?

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So far, the payment market of the European Union (EU) has been governed by the first Payment Services Directive adopted in 2007. As of 13 January 2018, however, all payment service providers within the EU countries are subject to a new procedure and provisions stipulated by the second Payment Services Directive (PSD2).

The first Payment Services Directive (PSD) was approved in 2007 with a view to create a single European payment market. The Directive laid down uniform provisions for electronic payments in all EU Member States. 10 years have passed since then, and the digitalisation of the European economy has made significant progress. Technologies have evolved considerably during this time, and new participants offering a range of innovative services have entered the market, with many of them currently subject to no regulation whatsoever.

One purpose of the Directive is to open up the payments market for new entrants, in other words, ensuring equal conditions for all payment market participants, including the new participants entering the payment market with innovative solutions. In addition it enables bank customers to use the solutions of innovative service providers, as well as it secures safer payments, improves consumer protection and facilitates innovation and competition.

The second Payment Services Directive (PSD2) lays down that strong customer authentication shall be ensured in all electronic transactions. This means that two or more independent security elements shall be applied when using payment services, inter alia, when confirming payment transactions. Moreover, one of these elements should be non-reusable and non-replicable.

The Directive defines new payment service providers who will have to receive a licence in order to be allowed to work in the entire EU.

PSD2 will establish two types of new services in the financial sector: payment initiation service and account information service.

The payment initiation service is a service whereby an institution not holding a customer's account obtains access, with the customer's permission, to the customer's payment account opened with a bank to make transfers on the customer's behalf. For example, when making purchases online, the customer will no longer have to use the internet banking services of the respective bank, since e-merchants will be able to receive payments via the new service provider directly from the customer's account opened with any bank. This service will make online shopping easier both for customers and businesses who will now be able to conclude only one contract with a payment initiation service provider, ensuring payments by customers of any EU bank. The account information service will allow users to promptly receive consolidated information on all their accounts and balances, thereby providing better means of financial planning. Accessing a customer's accounts, the service providers will be able to provide consolidated information on all of the customer's accounts opened with different institutions.

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