



The following is a brief summary of the IMF-Latvian Republic Stand-By Arrangement. It is based on an IMF Staff report and includes excerpts from the © 2009 International Monetary Fund January 2009, IMF Country Report No. 09/3.

INTERNATIONAL MONETARY FUND REPUBLIC OF LATVIA Request for Stand-By Arrangement

SUMMARY:

IMF PROGRAM'S MAIN OBJECTIVE:

1. Arrest immediate liquidity crisis;
2. Ensure long-term stability;
3. Maintain the exchange rate peg.

WHAT THE LATVIAN GOVERNMENT IS DOING:

Taking measures to stabilize the financial sector and restore depositor confidence:

1. Launching a decisive economic reform program;
2. Tightening fiscal policies to reduce financing needs and foster real depreciation;
3. Undertaking structural reforms and income policies to improve competitiveness and facilitate external adjustment;
4. Seeking international financial assistance.

A COORDINATED INTERNATIONAL EFFORT:

1. The IMF, European Commission, ECB, Sweden and other Nordic countries are involved;
2. Expertise from World Bank and EBRD.

KEY ELEMENTS OF THE PROGRAM:

1. Measures undertaken to stem loss of bank deposits and international reserves;
2. Restoration of confidence in the banking system;
3. Fiscal measures to reduce budget deficit;
4. Structural reforms to rebuild competitiveness under the fixed rate regime.

The following are excerpts from the IMF Staff Report.

The program's main objectives are to arrest the immediate liquidity crisis and then to ensure long-term external stability, while maintaining the exchange rate peg. The program includes measures to stabilize the financial sector and restore depositor confidence. It also includes substantial fiscal policy tightening to reduce financing needs and foster real depreciation. Structural reforms and incomes policies will be developed to improve competitiveness and facilitate external adjustment.

1. YEARS OF UNSUSTAINABLY HIGH GROWTH AND LARGE CURRENT ACCOUNT DEFICITS HAVE COALESCED INTO A FINANCIAL AND BALANCE OF PAYMENTS CRISIS. Since end-August, private sector deposits have fallen by 10 percent, led by a run on Parex Bank (the second largest bank, and largest domestically owned) which encountered severe liquidity problems after it lost more than a quarter of its deposits. Attempts by the government to negotiate a partial take over of this bank, while allowing the main shareholders to retain significant influence, failed to restore confidence. Concerns over the financial system and external debt sustainability increased, and the exchange rate peg came under threat.

2. THE LATVIAN AUTHORITIES ARE LAUNCHING A DECISIVE ECONOMIC REFORM PROGRAM AND ARE SEEKING SUBSTANTIAL INTERNATIONAL FINANCIAL ASSISTANCE TO QUELL THIS CRISIS. The global liquidity crisis has prevented the government from accessing outside private capital markets and obtaining the foreign currency needed to bolster the banking system and to re-establish confidence. With international reserves falling precipitously and reserves barely covering base money, the authorities are now seeking Fund assistance under the emergency financing procedures. The authorities are also requesting support from the European Union's balance of payments facility partner countries and other international organizations.

3. THE PROPOSED FUND-SUPPORTED PROGRAM IS PART OF A COORDINATED INTERNATIONAL EFFORT. The European Commission has participated fully in the Fund mission, along with representatives from the ECB, Sweden and other Nordic countries. Financial assistance and expertise from the World Bank and EBRD are other key components of the international response.

4. THE PROGRAM IS CENTERED ON MAINTAINING LATVIA'S EXCHANGE RATE PEG THROUGH STRONG DOMESTIC POLICIES AND SUBSTANTIAL INTERNATIONAL FINANCIAL ASSISTANCE. Key elements include: (i) immediate measures to stem the loss of bank deposits and international reserves; (ii) steps to restore confidence in the banking system in the medium-term; (iii) fiscal measures to limit the substantial widening in the budget deficit, and prepare for early fulfilment of the Maastricht criteria; and (iv) incomes policies and structural reforms that will rebuild competitiveness under the fixed exchange rate regime. With substantial international support, these policies should allow the economy eventually to emerge from a period of slow growth, with fewer strains on corporate and household balance sheets.

THE LATVIAN INSTITUTE

The Latvian Institute (Latvijas institūts) was established by the Latvian state to provide a wide range of information about Latvia, its society, culture and history.

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