



Cabinet of Ministers
Republic of Latvia

Latvian Financial Sector Update

No. 3 11 September 2018

Message from the Supervisory Authority



Substantial work has been undertaken in the Latvian financial sector to reduce risk and improve business practice. Over the past three years, under the supervision of the Financial and Capital Markets Commission (FCMC), we have successfully seen a significant reduction in risky segments and foreign deposits. Today, domestic and European deposits account for 90% of the deposit base in Latvian banks, a radical change in the customer structure that had existed for the previous 25 years. We have a completely different risk model that has been adopted into the business strategies of our banks, taking a significant step to cutting risky money flows in Latvia. There is still work to do, but under the supervision of the FCMC the financial reforms will continue apace.

Pēteris Putniņš,
The Chairman of the FCMC

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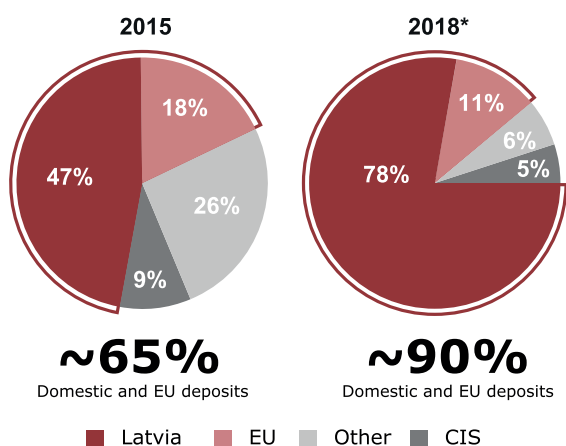
Financial Sector Transformation

Change management in the banking sector

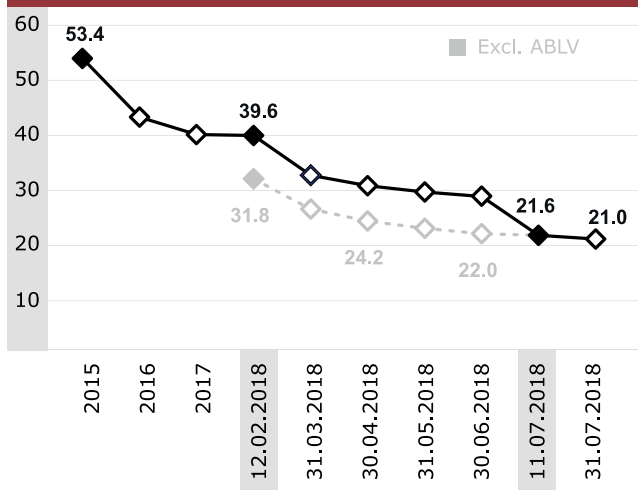
This year, Latvian banks have recorded a historical low level of foreign deposits at 20%. A risk reduction approach, carried out in accordance with guidelines set out by the FCMC, is being undertaken by Latvian banks that specialize in servicing foreign customers. The process has been planned in a controlled manner and with full transparency to prevent any unnecessary shocks.

Since 2011 the FCMC mandated higher stability indicators for banks servicing foreign customers, annually reviewing and adjusting the demands. As a result, banks are fulfilling their obligations to customers while radically changing their business models to mitigate risk posed by high foreign deposit levels.

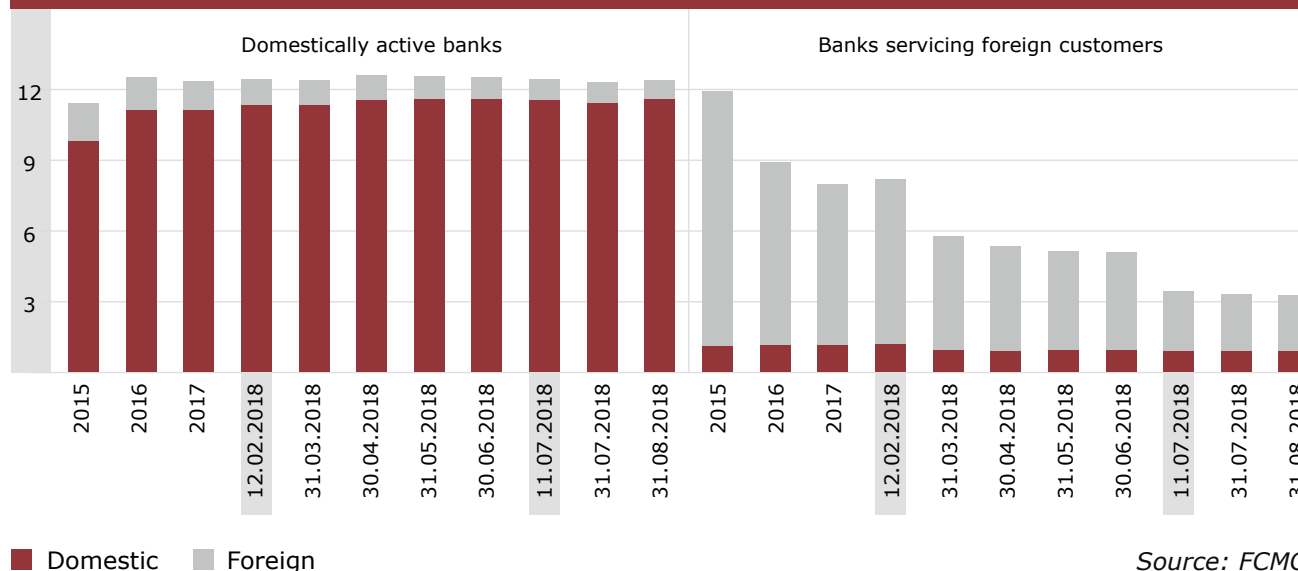
Strong move to the dominance of EU and domestic deposits



Share of foreign deposits in the Latvian banking system, %



Deposits, bln. EUR



Source: FCMC

Q2 2018: Operating results of Latvian banks

Finance Latvia Association has published its Q2 statistics. The Association is seeing a combined impact of significantly tighter AML/CFT standards in Latvia and further tightening of international sanctions policy, a serious EU focus on AML/CFT issues, and "know your customer" principles.

Banks' equity has stabilized in the 2nd quarter of 2018. Total capital of the Latvian banking sector reached EUR 3.1 billion as of June 30, 2018, it did not change significantly compared to Q1 2018. Total equity has increased in the past 12 months period by EUR 0.2 billion or 6%. Average return on equity (ROE) in the banking sector of Eurozone was 3.8% in 2017. Based on Q2 results, ten Latvian banks exceed the average ROE for Eurozone banks.

During Q2 Deposits declined by EUR 0.5 billion or 3% comparing to Q1 2018, the decrease was mainly observed in foreign deposits. Net profit of Latvian banking sector in H1 of 2018 reached EUR 133 million, EUR 32 million or 19% lower compared to the results of the H1 of 2017. Read more on [Finance Latvia Association website](#).

FCMC meets with ECB Supervisory Board

The Chair of the Supervisory Board of the European Central Bank (ECB) Danièle Nouy arrived for a working visit in Latvia on 27 August. In this visit she met with managerial staff of the FCMC and its Chairman Pēteris Putniņš, who is also a member of the ECB Supervisory Board. Particular attention was being paid to

supervisory matters: bank management mechanisms, new business lines and strategies, as well as risk management in the context of future challenges in the Eurozone.

Latvia has been part of the Single Supervisory Mechanism (SSM) since 2014. This is a key pillar of the European banking union and the three largest banks in Latvia (Swedbank, Luminor Bank and SEB Banka) have been supervised within this single mechanism for the Eurozone countries. Read more on the [FCMC website](#).

In an interview with LETA, Nouy said: "I personally think that combating money laundering requires a common European framework, hence a regulation rather than a directive. I also think that it would be better to address the money laundering issue through a European institution. I am sure that my colleagues are doing the best they can. But in this relatively small country, compared with the rest of the euro area, which has correspondingly small supervisory institutions, it is difficult to obtain enough staff with the required expertise and experience to focus on this issue. This is all the more critical since the geopolitical risks in this region, in the Baltic and Scandinavian region, I would say, are not negligible. I would reiterate that this is not a matter that can be addressed exclusively at the national level; the discussions should take place at the European level." Read the full interview [here](#).

AML Risk Management & Compliance

Moneyval

On 11 September, the Financial Sector Development Board approved the Action Plan addressing all the recommendations outlined in the Moneyval Assessment report published on 23 August. The Plan consists of action items in eleven areas related to Moneyval report to be completed by the end of 2019. Within this timeline all the responsible institutions will have to demonstrate progress in areas starting from AML/CTF policy elaboration and coordination up to CTF prevention, investigation, law enforcement, as well as proliferation related sanctions. The government is expected to approve the plan within upcoming weeks.

Effective implementation of the Sanctions Law in Latvia

From 12 to 28 September 2018, the Ministry of Foreign Affairs in association with the Ministry of Finance, The FCMC, The Procurement Monitoring Bureau, The Consumer Rights Protection Centre, and the State Revenue Service is organizing a series of lectures on "Effective implementation of the Sanctions Law in Latvia".

The lectures have been designed for representatives from supervisory and law enforcement institutions, as well as financial and other sectors to provide an insight into the international context of sanctions and their current legal framework. Read more on the [Ministry of Foreign Affairs website](#).

Controlled liquidation of ABLV Bank

ABLV Bank is going through a controlled liquidation process under the supervision of the FCMC. The latest updates include:

- Assets of the to-be-liquidated ABLV Bank in the first six months of this year were EUR 2.37 billion, down EUR 1.3 billion from the respective period last year, according to the bank's unaudited consolidated report.
- Liquidator Arvids Kostomarovs forecasts that by the end of 2018 ABLV Bank will make 5% to 7% of its employees redundant, with further job losses to follow in 2019. Currently there are 370 people working at the bank, while ABLV Group employs approximately 500 people.
- The liquidator also said that options are currently being assessed for the future of ABLV Bank Luxembourg. These options include a potential sale or liquidation, depending on the regulator's approval and shareholder value from a potential sale.

- ABLV Bank liquidators have signed an advisory agreement with Superia to assess strategic options for the potential sale of ABLV's mortgage loans portfolio. Various strategic options will be evaluated with a view to maximizing the value of proceeds for creditors. As of 30 June 2018, the mortgage loans portfolio of ABLV Bank amounted to EUR 292 million.

More information on the liquidation of ABLV Bank and control mechanism set up by the FCMC is available on the [FCMC website](#).

Financial Sector Development

European Parliament TAX3 Committee mission to Latvia

A delegation of the Special Committee on Financial Crimes, Tax Evasion and Tax Avoidance (TAX3) of the European Parliament conducted a mission to Latvia on 30 and 31 August.

The head of delegation Petr Ježek acknowledged that Latvia is aware of the challenges associated with its banking sector and that some steps have been taken to address them, singling out efforts to reduce foreign deposits for particular praise. He was, however, clear that further action is required.

TAX3 recommended that improvements are required in the Latvian judicial system to ensure that financial crime cases lead to convictions. In this regard, the head of the TAX3 delegation came to a similar conclusion as the Council of Europe's Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism (Moneyval).

TAX3 met with a range of representatives from the public and private sectors including Finance Minister Dana Reizniece-Ozola, the State Revenue Service, Financial Intelligence Unit, The FCMC, The Corruption Prevention and Combating Bureau, as well as members of the Latvian Parliament, The Freeport of Riga, liquidators of ABLV Bank, and Finance Latvia Association. Read more on what was discussed during meetings on the websites of [the FCMC](#) and [Finance Latvia Association](#).

Latvia's customer payment statistics in the first half of 2018

Overall, 235.5 million non-cash payments totalling EUR 104.7 billion were executed in the first half of 2018. This represents a 3% rise in volume compared with the second half of 2017, but an 18.2% fall in value.

This trend is a result of amendments to the Law on the Prevention of Money Laundering and Terrorism Financing that were adopted by the Latvian parliament on 8 May 2018. These provisions required credit institutions to review their customer base, leading to a decrease in the number of customer accounts, and consequently the fall in the volume and value of credit transfers and card payments. Read more [on the website of Latvijas Banka](#).

A year of instant payments: achievements and ambitious plans

The 28 August 2018 marks one year since Latvijas Banka became the first euro area central bank to introduce the instant payments between commercial banks. Commercial banks have been rolling out this benefit to their customers, and since November 2017 Citadele and SEB Banka account holders have benefitted from the advantages of instant payments by making both mutual transfers and transfers to more than 1000 euro area banks.

Over the past nine months, more than 1.2 million instant payments were processed in Latvijas Banka's system, with positive feedback received from both technology experts and bank customers. In the coming months, the number of the commercial banks providing the instant payment settlement service to their customers is expected to rise and the vast majority of the mutual payments between individuals and companies in Latvia will be made instantly thanks to this infrastructure. Read more on [www.macroeconomics.lv](#).

SEB opens its Innovations Centre

SEB bank opened its Innovations Centre in Riga on 4 September to encourage domestic entrepreneurial growth. Ieva Tetere, CEO of SEB in Latvia, said: "We have opened Innovation Centres already in Estonia and Lithuania. SEB bank has a common goal in the Baltics – Innovation Centres as a place for the growth of entrepreneurs and their employees. This growth will be driven by various events, including the launch of our Growth Program, where we have invested € 60,000 this year for 27 companies during 2 batches to help them reach rapid growth."

Blockchain in the financial industry – future perspectives in EU and Baltics

In August, the Finance Latvia Association together with the European Commission Representation in Latvia and Eversheds Sutherland Bitāns Law Office organized a working discussion on the future of blockchain in the financial industry. The goal of the workshop was to lay the groundwork for a joint Baltic proposal and position on the future use of blockchain technology in the EU. Read more and watch speaker presentations [on the website of Finance Association Latvia](#).

Contributing Institutions



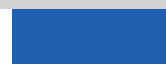
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Foreign Affairs
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Financial and Capital
Market Commission



Office for Prevention
of Laundering of Proceeds
Derived from Criminal Activity

