CHAPTER 8

Latvia: The Domino That Did Not Fall

Latvia went through the most extreme boom-bust cycle in all of emerging Europe. The liquidity freeze following the Lehman Brothers collapse hit very hard an economy that was already slowing after many years of unsustainably rapid growth. Economic activity fell by a quarter and a banking crisis claimed Latvia's second-largest bank. Latvia designed its adjustment program around its fixed exchange rate, made possible by massive financial support from the international community, with an eye on the exit strategy of euro adoption. The peg held, external imbalances corrected quickly, and by the end of 2009 the economy had returned to growth. Unprecedented fiscal austerity measures, wage cuts, and structural reforms were key to keeping the fiscal deficit from spiraling out of control and improving competitiveness without recourse to a nominal devaluation of the currency. Despite these achievements, the fall in output has been substantial. Reducing the high level of unemployment and strengthening the social safety net, redirecting output toward exports and the tradable sector, and continuing with structural reform remain important challenges.

BACKGROUND

Following independence from the Soviet Union in 1991, Latvia's economy faced multiple challenges: output initially collapsed; the subsequent recovery gave way to a recession in 1995 and a systemic banking crisis; and the Russian financial crisis in 1998 was another setback. It was not until the 2000s that growth became established, but Latvia's industrial base had become rather narrow, relying on the wood and furniture sector as well as food processing. The banking crisis had been overcome, but credit-to-GDP ratios were low. Foreign banks, mainly from Sweden and other Nordic countries, began buying up local banks and started to dominate the financial system. One major financial institution, Parex Bank, remained in local hands. However, just as the foreign banks relied on parent financing rather than local deposits, Parex's financing relied increasingly on the wholesale market and non-resident deposits. Inflation was brought down to single digits in the late 1990s under a fixed exchange rate regime, which pegged the lat against the SDR, and later the euro, and which was supposed to operate like a currency board.

The main author of this chapter is Mark Griffiths, helped by James John and the IMF's Latvia team. Material is drawn from the IMF Staff Reports for the initial stand-by arrangement, the first through fifth reviews, and especially the 2010 Article IV Consultation. These documents provide more detail and are available at http://www.imf.org/external/country/lva/index.htm.

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THE RUN-UP TO THE GLOBAL FINANCIAL CRISIS

Latvia had accumulated substantial and unsustainable economic imbalances long before the crisis. From 2000 to 2004, annual GDP growth had averaged an already very high 7.5 percent, but following EU membership in 2004 growth accelerated to double digits. Low interest rates under the peg and large inflows from Nordic banks fueled rapid credit expansion, largely foreign currency-denominated. Investment in the nontradable sector took off, together with a bubble in real estate prices. Current account deficits exceeded 20 percent of GDP in 2006 and 2007, as Latvia's private sector credit rose rapidly from 40 percent of GDP in 2003 to 90 percent in 2007. With tax revenues growing rapidly, rather than saving these and running surpluses, the government decided to put its "pedal to the metal" and was able to double public spending in real terms during 2001–07 without causing sizable fiscal deficits.

The boom ran out of steam in late 2007. Worried about the rise of inflation, the Bank of Latvia had tightened its regulatory policy at the beginning of the year by restricting mortgage lending and increasing reserve requirements. Foreign parent banks started reducing lending to their Latvian subsidiaries in the summer, amid signs of overheating. The credit boom had peaked, hitting the housing and construction sector. Real estate prices fell from the second quarter of 2007 and real GDP followed suit from the first quarter of 2008.

IMPACT OF THE GLOBAL FINANCIAL CRISIS

The collapse of Lehman Brothers and the subsequent international liquidity freeze catalyzed and compounded the crisis in Latvia. Doubts over the health of Swedish parent banks surfaced, but the Swedish government's September support package restored confidence. Speculation soon turned to Parex Bank and whether it would be able to repay its short-term syndicated loans. In the resulting panic, the bank lost 25 percent of its deposits. To provide liquidity to banks under pressure, the Bank of Latvia cut reserve requirements, but depositors continued to withdraw funds and convert them to foreign exchange. Initial half-hearted attempts to stabilize Parex Bank through partial nationalization proved insufficient, and the authorities had to impose a partial deposit freeze on Parex to stabilize its deposits and conserve liquidity.

Latvia had reached a crossroads. Private sector deposits in the banking system had fallen almost 10 percent between end-August and end-November 2008, with much of the decline due to nonresident accounts. Rumors of imminent lat devaluation were widespread. With banks' loan-to-deposit ratios at 150 percent (and 280 percent if less stable nonresilient deposits are excluded), reserves covering less than a third of short-term external debt, and the future of the quasi-currency board coming into doubt as the reserve cover of base money dropped towards 100 percent, the situation became precarious.

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POLICY RESPONSES

In November 2008, the Latvian authorities decided to seek outside financial assistance, primarily from the IMF and the European Union. However, not all of the authorities were fully prepared to recognize the enormity of the challenge, as evidenced by the now famous words of the then finance minister that Latvia's problems were "nothing special." Time was running short. The IMF mission was only invited to Latvia in mid-November when the financial and exchange rate panic was already well underway. Given the depth of the problem, the response needed to be not only quick but also substantial, requiring the pooling of resources from the IMF, the European Union, bilaterals, and other international financial institutions. In any event, as an EU member Latvia had to approach the EU balance of payments facility before seeking IMF support. This in turn required coordination of the various assistance programs, an extra step. However, unless it were resolved quickly and decisively, Latvia's crisis risked spilling over to other European countries with fixed exchange rates, from neighboring Estonia and Lithuania to the currency board in Bulgaria.

A €7.5 billion program was announced on December 19, 2008, with financing from the European Union (€3.1 billion), IMF (€1.7 billion), Nordic countries (€1.8 billion, though as a second line of defense and ultimately not utilized), and the World Bank (€0.4 billion), with the EBRD and other bilateral lenders providing the remainder. An emergency swap line from the central banks of Sweden and Denmark that was already in place provided a bridge to the first disbursement from the IMF. The IMF arrangement was approved by the IMF Board on December 23, under emergency financing procedures. Total program financing corresponded to over 30 percent of Latvia's GDP—a relative size never reached in any previous IMF-supported program.

The program's strategy was centered on maintaining Latvia's exchange rate peg. In light of Latvia's large current account deficit, estimates of overvaluation, and the difficulties in defending an exchange rate peg under an open capital account in the middle of a financial panic, exchange rate policy was hotly debated in the program discussions. The IMF wanted to make sure that all options were considered, including the possibilities of a widening of the exchange rate band to ±15 percent or some form of accelerated euro adoption, potentially at a depreciated rate.[1] However, the EU authorities firmly ruled out immediate euro adoption as inconsistent with the Maastricht Treaty. The Latvian authorities were unequivocally committed to keeping the exchange rate peg, since it had been the linchpin of economic stability since the early days of transition. Moreover, devaluation would have had severe balance sheet effects, since most private sector debt was denominated in euros and rollover of external debt might have become even more difficult. However, the decision to leave the exchange rate unchanged increased demands on the rest of the program.

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[1] See Request for Stand-By Arrangement, paragraphs 19–20 and Box 1; 2010 Article IV Consultation Staff Report, paragraphs 4–5.

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With the exchange rate peg maintained, domestic policies needed to be radically strengthened to generate the needed real depreciation. In essence, real exchange rate overvaluation would need to be addressed through price and wage adjustment, along with productivity-boosting structural reforms—a process referred to as "internal devaluation." This price adjustment in turn required tight wage policies and, most likely, a short period of economic recession would be unavoidable. This would be a painful process, and there were doubts whether it would be possible to generate sufficient competitiveness gains this way.

Fiscal policy needed to be tightened for two reasons. First, the worsening recession led to a deep slump in revenues which threatened to raise the fiscal deficit into double digits as a share of GDP. While Latvia's public debt was extremely low at the outset, such large deficits would have been difficult to finance, would have left no room to support the shaky financial sector, and would not have inspired confidence. Second, given the choice of the fixed exchange rate, fiscal policy needed to contribute to internal devaluation by restraining domestic demand and lowering wages to improve competitiveness. The government would end up implementing measures of some 15 percent of GDP over the next three years—much more than initially envisaged, as the recession proved substantially deeper than expected at the outset. Measures included across-the-board cuts in salaries and bonuses for civil servants.

The program emphasized the need for social safety net protection to cushion the recession's impact, with an adjuster allowing new safety net spending of up to 1 percent of GDP. Safety net measures, designed with the World Bank, included jobs programs for the unemployed, increases in guaranteed minimum income support, and coverage of health copayments for the poor.[2]

The program's immediate task was to restore confidence in the financial system and the exchange rate to contain outflows of deposits and reserves. To this end, the government took full control of Parex Bank by increasing its stake to 85 percent and by installing new management in mid-December. In the event, the bank received government capital injections in March and September 2009, the EBRD provided it with loans and acquired a 25 percent stake in September 2009, and the bank was split into a good and bad bank in August 2010, with the former retaining the performing assets and carrying out all regular banking functions and the latter receiving the problem loans for workout. Financial sector reform under the program also involved a focused examination of the banking system and encouragement for recapitalization, monitoring of foreign banks to ensure that they maintained credit lines, and legal changes providing the authorities with better tools to resolve banks. Program funding was calibrated so as to be able to accommodate financial restructuring costs as high as 15–20 percent of GDP—much more than would eventually be needed, but signaling to markets and depositors that the program was well financed. The announcement of substantial assistance was followed by the actual disbursement of €0.6 billion from the IMF

[2] See First Review Letter of Intent, paragraph 14.

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in late December and €1 billion from the European Union in early 2009, increasing confidence in the peg by substantially strengthening the outlook for reserves.

Implementing the program proved challenging, especially for the budget. In the program's first months, the economic slump in Latvia intensified as the world economy too fell into recession. The fiscal deficit rose sharply, well beyond program forecasts, and the government's initial program commitment to reduce it to 5 percent of GDP in 2009 became harder to deliver. Demonstrations and protests became more numerous, though largely without violence, and it was unclear whether the Latvian people could tolerate the coming severe recession. Unable to pass a supplementary budget that would include structural reforms to underpin the budget cuts agreed in December, only two months into the program, in February 2009, the government fell.

A new coalition government formed in March. Deepening recession and failure to implement the adjustment agreed to in December threatened to increase the deficit to around 15 percent of GDP unless measures were taken. Without the IMF/EU-supported program, the deficit could not be financed. The new government submitted a supplementary budget, but the first draft included only token measures that were clearly insufficient.

A revised supplementary budget for 2009 was finally passed on June 16, once local elections had been held and following consultations with social partners and with the president's involvement. The supplementary budget included 3.5 percent of GDP in consolidation measures for the remainder of the year (6.5 percent of GDP on a full-year basis).

While the authorities deserve considerable credit for delivering an adjustment of this magnitude, the last-minute rush to pass the budget meant there were many problems with its quality.[3] However, the authorities were not willing to amend the budget to address these issues, lest the agreement with social partners unravel. Given the sheer magnitude of the government's effort (and promises of further adjustment in the future), the European Commission quickly completed its first review of the program. Despite concerns with the quality of the adjustment, the IMF followed soon after.

Preparation and passage of the 2010 budget proved the next major challenge. After much wrangling, and helped both by the interventions of European Commissioner Joaquin Almunia and Swedish Finance Minister Anders Borg and by long negotiations with the IMF and the Commission teams, the government in the end delivered on its First Review Letter of Intent commitment to a further L500 million (4.2 percent of GDP) of adjustment. Increases in personal income tax, real estate tax, car tax, and excises were expected to raise 2.3 percent of GDP, with spending cuts providing the remainder.[4] However, the adjustment was partially unwound, first by December's Constitutional Court ruling reversing the

[3] These included reducing teacher salaries to close to minimum wage, excessive use of across-the-board spending cuts, tax increases that were regressive, and uniform cuts in pensions without protecting the poor (and which were later ruled unconstitutional). See Box 4 of the First Review Staff Report.
[4] Staff Report for the Second Review, paragraphs 25–30.

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pension cuts passed in June (1 percent of GDP) and then, with the government falling into minority, by ad hoc spending increases and tax cuts throughout 2010, ahead of October's parliamentary elections.

ECONOMIC OUTCOMES IN 2010–11

Passage of the supplementary budget in June 2009 and completion of the first program review marked the turning point. Disbursements of €1.2 billion from the European Union and €0.2 billion from the IMF increased international reserves to €4.5 billion, or roughly 200 percent of base money, and more than 55 percent of broad money, by end-August 2009. As a result, confidence in the exchange rate gradually returned, overnight interbank interest rates fell from more than 30 percent in June 2009, when the exchange rate was under attack, to the low single digits, and the central bank's foreign exchange sales fell off. Deposit withdrawal restrictions on Parex Bank could largely be lifted in October 2009, as nonresident and resident depositors returned to the banking system.

Contagious currency devaluations and financial meltdown had been successfully averted. The exchange rate peg held, and currency boards elsewhere in emerging Europe also endured. Foreign banks stood by their local subsidiaries, recapitalizing them as needed. The banking crisis was largely contained to Parex Bank, and the fiscal cost of bank restructuring would turn out to be much lower than initially allowed for. Latvia's banking system returned to profitability in 2011. Large-scale international financial support had proved effective, even if it could not convince syndicated lenders to roll over their exposures initially, though only because the Latvian authorities used the time to deliver on substantial fiscal adjustment. The Latvian government returned to the Eurobond market in June 2011 with a US$500 million 10-year issue, the country's first international issue since 2008. In February 2012 a successful US$1 billion issuance followed.

The large precrisis current account deficit corrected much more swiftly than expected. Indeed, external surpluses were recorded in 2009 and 2010. While this reflected the exceptionally deep recession, it also meant that official financing—together with the restoration of confidence, the return of deposits, and the authorities' fiscal adjustment—proved larger than needed. Arresting a capital account crisis and bank run tends to require larger upfront international support packages to restore confidence. If successful in restoring confidence, then these amounts may not actually need to be drawn down, provided program implementation is strong. Accordingly, the Latvian authorities have treated official funding that became available with the fourth and fifth program reviews in May and December 2011 as precautionary. The program ended on December 22, 2011, with €4.1 billion drawn from the financing package of €7.5 billion.

Public finances are improving. Although fiscal policy during the boom had been procyclical, Latvia entered the crisis with public debt of only around 10 percent of GDP. Given this favorable starting point, and with strong fiscal consolidation measures to keep public finances under control, Latvia's fiscal

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solvency was never really an issue, despite high fiscal deficits in the crisis years. The 2010 deficit (ESA basis, including bank restructuring costs) fell to 8.2 percent of GDP (from 9.7 percent in 2009), below the 8.5 percent revised program target. A huge fiscal effort of some 15 percent of GDP over the program period is likely to have reduced the deficit to less than 4 percent of GDP in 2011. With the government determined to bring the deficit below the Maastricht threshold, euro entry is coming within reach and would mark a major success for the program. And despite having overseen a tough adjustment program, following elections in October 2010 and again in September 2011, Prime Minister Valdis Dombrovskis has kept his office, heading governments committed to implementing the program.

While the program delivered economic and financial stability, it could not prevent a severe recession. Output fell by 18 percent in 2009. The peak-to-trough decline came to a cumulative 25 percent—more than in any other country in emerging Europe. Unemployment increased to 20 percent and, despite the recession in Europe, outward migration increased too. With exchange rate depreciation ruled out, it was difficult to generate sufficient expenditure switching to offset the collapse in domestic demand. Though the output collapse was much worse than initial program projections, these developments also reflected the unanticipated world recession, the collapse in world trade, and the end of Latvia's real estate and financial sector bubble: precrisis output levels were not sustainable.

Latvia's economy has returned to growth. Output started to expand again at the end of 2009 on a quarter-over-quarter basis. The recovery was initially driven by exports, but domestic demand followed suit, with GDP growing by more than 5 percent in 2011.

The experience shows that internal devaluation can work, although it has its limits, even in Latvia where labor markets are considered relatively flexible. Between December 2008, when the program was launched, and December 2010, wages fell by around 8 percent and unit labor costs by much more (around 20 percent), reflecting the effect of labor shedding on productivity. However, prices fell only around 4 percent from the peak in the first quarter of 2009 to the trough in February 2010, and since then both wages and prices have started to increase despite the sizable output gap and high unemployment. Thus, while competitiveness has improved, there are limits to downward wage and (especially) price flexibility.

CHALLENGES AHEAD

The next challenges are to maintain Latvia's stabilization, boost growth, and reduce unemployment.

Macroeconomic stability would be best secured if Latvia could qualify for euro adoption—the exit strategy envisaged under the program. For a small open economy like Latvia, fixed exchange rates have numerous benefits. Euro adoption would not remove all vulnerabilities, but it would have the major advantages of removing currency risk, ending speculative attacks on the exchange rate, and

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ensuring sufficient international reserves so that the central bank (in this case, the ECB) could act as an effective lender of last resort. With strong fiscal, structural, and financial regulatory policies in place, joining the euro would also reduce the risk of recurrence of financial crisis.

Meeting the Maastricht criteria for euro adoption in the fiscal area will require a final push. The general government deficit needs to be lowered to no more than 3 percent of GDP on a sustainable basis. Much of the adjustment will need to come from spending: spending ratios have increased massively, in part because of the fall in GDP but primarily because government spending increased too rapidly during the precrisis years, on the erroneous assumption that rapid growth was permanent. Across-the-board cuts have been relatively simple to implement but may be difficult to sustain. Durable cuts depend on finding functions that are duplicated or unnecessary or which can be shifted to the private sector. The government's functional analysis working group has made suggestions (although savings are limited), as have IMF technical assistance missions and the World Bank's public expenditure review.

Political decisions to protect pensions have forced a disproportionate adjustment burden on other spending. Pensions make up roughly 20 percent of government spending and increased almost 30 percent between 2005 and 2008. Before the crisis, supplementary pensions, initially awarded only to poor pensioners, were extended to all; price indexation was supplemented with partial indexation to wage growth; and retirees received supernormal pension increases since under the notional defined contribution system their rates of return were linked to (rapid) wage growth, which proved unsustainable. As a result, from 2005 to 2010 pension spending rose from 6 percent to 10 percent of GDP. Although it would be difficult politically, it seems that a case could be made for finding savings in pensions to share the adjustment burden in a way that was fair and which protected the poor. Failure to do this meant that greater spending cuts had to be imposed elsewhere or that social contributions had to rise, which increases the labor tax wedge, raises unemployment, and encourages migration, further undermining the adjustment.

On the surface, tax increases are easier and more tempting to implement, but they do not solve the underlying problem, namely that during boom years a government may have grown ahead of the economy. In Latvia, tax increases in 2012 would also be inconsistent with the authorities' aim of meeting the Maastricht inflation criteria. However, introduction of a progressive personal income tax would have helped share the burden of fiscal adjustment, and increases in residential real estate taxes might have raised revenue in a less distortionary manner. These options remain available for the future.

Sustaining growth will depend on structural reforms and creating a business environment that encourages investment, since Latvia's fixed exchange rate regime prevents competitiveness gains through currency depreciation.[5] These reforms are difficult and will take time. But without growth, the European

[5] Staff Report for the 2010 Article IV Consultation, paragraphs 46–49.

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Union's single labor market (and labor mobility facilitated by the Schengen zone) and the gap in living standards between Latvia and the rest of the European Union could lead to renewed emigration. Euro adoption could also help promote growth, by increasing confidence in the exchange rate, reducing interest rates, and encouraging credit growth. To prevent growth from leading to new current account deficits, the economy's structure needs to be redirected away from real estate, construction, and financial services and toward traded goods. This may require new skills and retraining. And boosting demand for Latvian tradable goods may require further improvements in competitiveness. Finally, given the risk that higher unemployment rates are likely to persist, strengthening the social safety net—in a way that does not penalize Latvians for taking job offers—will be an important challenge.

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Latvia: Principal Economic and Financial Indicators, 2003–11

	2003	2004	2005	2006	2007	2008	2009	2010	2011
Real Sector Indicators									
GDP (real growth in percent)	7.2	8.7	10.6	10.5	9.6	–3.3	–17.7	–0.3	5.5
Domestic demand (real growth in percent)	10.7	12.1	9.3	16.6	12.9	–9.1	–27.4	0.1	10.2
Net exports (real growth contribution in percent)	–4.5	–5.1	0.1	–8.9	–6.2	7.6	12.9	–0.2	–4.7
Exports of goods and services (real growth in percent)	5.2	9.4	20.2	6.5	10.0	2.0	–14.1	11.5	12.6
CPI (end-of-period change in percent)	3.5	7.4	7.1	6.8	14.0	10.4	–1.4	2.4	3.9
Employment (growth in percent)	2.0	0.7	1.6	4.4	2.7	0.1	–11.4	–3.6	3.3
Unemployment rate (percent)	10.7	10.6	8.8	7.0	6.2	7.8	17.3	19.0	15.6
Public Finances									
Fiscal balance (percent of GDP)	–1.7	–1.2	–1.3	–0.5	0.6	–7.5	–7.8	–7.2	–3.4
Government revenue (percent of GDP)	32.9	33.9	35.3	36.2	36.3	35.6	36.2	36.2	35.9
Government expenditure (percent of GDP)	34.6	35.2	36.6	36.7	35.7	43.1	44.1	43.4	39.3
Government primary expenditure (percent of GDP)	33.8	34.4	36.0	36.1	35.3	42.8	42.9	42.0	37.9
Government primary expenditure (real growth in percent)	5.6	10.7	15.6	11.0	7.2	17.0	–17.4	–2.5	–4.8
Public debt (percent of GDP)	14.6	14.4	11.8	9.9	7.8	17.2	32.9	39.9	37.8
Of which foreign held	7.6	8.3	6.0	5.8	5.3	5.8	21.5	25.9	23.8
External Sector									
Current account balance (percent of GDP)	–8.1	–12.9	–12.5	–22.6	–22.4	–13.2	8.7	3.0	–1.2
Net capital inflows (percent of GDP)[1]	8.2	14.9	16.8	30.3	23.9	9.4	–21.9	–6.2	–5.3
FDI	2.3	3.8	3.6	7.5	6.8	3.0	0.6	1.5	5.1
Portfolio	–2.0	1.6	–0.8	0.2	–2.4	1.1	0.7	–0.9	–2.3
Other investment	7.9	9.5	14.0	22.7	19.4	5.2	–23.2	–6.8	–8.1
Exports (percent of GDP)	41.8	43.6	47.0	44.2	41.6	42.3	43.3	53.4	58.3
Exports (€, growth in percent)	3.2	16.7	25.5	15.3	24.5	10.6	–16.4	20.3	22.5
Global export market share (basis points)	3.8	4.4	4.9	5.1	6.0	6.3	6.2	6.3	...
Remittances (percent of GDP)	0.01	0.01	0.01	0.01	0.01	0.01	0.01	0.00	0.00
Imports (percent of GDP)	54.4	59.5	62.2	66.5	62.2	56.2	44.4	54.3	61.6
Imports (€, growth in percent)	8.0	22.2	21.6	31.3	23.5	–1.7	–35.5	19.4	27.2
External debt (percent of GDP)	76.3	89.2	99.5	120.6	136.5	121.2	164.3	165.0	137.2
Gross international reserves (€ billions)	1.1	1.4	1.9	3.3	3.8	3.6	4.6	5.7	4.9
Gross international reserves (percent of GDP)	12.9	14.0	14.0	22.0	19.4	15.1	25.7	31.7	22.5
Reserve coverage (GIR in percent of short-term debt)	22.9	19.3	22.8	33.4	24.0	29.2	48.6	42.2	35.5

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Latvia: Principal Economic and Financial Indicators, 2003–11 (*continued*)

	2003	2004	2005	2006	2007	2008	2009	2010	2011
					Monetary Sector				
Broad money (end of period, growth in percent)	21.1	27.0	38.9	37.5	12.6	–3.9	–1.9	9.8	1.5
Monetary base (end of period, growth in percent)	6.3	18.4	44.4	65.8	7.4	–15.2	–22.2	10.1	13.2
Private sector credit (end of period, percent of GDP)	41.3	51.7	69.2	88.5	89.5	98.4	109.2	103.7	86.1
Of which foreign currency denominated	22.3	30.9	48.1	68.2	77.6	87.5	100.8	95.8	77.2
Of which foreign currency indexed	...	...	...	...	...	...	...	...	...
Cross-border loans to nonbanks (Q4, percent of GDP)	4.3	5.3	6.1	8.6	15.3	14.4	18.5	15.2	10.8
Private sector credit (end of period, real growth in percent)	33.0	35.6	52.3	47.3	17.3	8.8	–8.6	–9.6	–11.1
					Financial Sector				
Assets (percent of GDP)	83.0	99.3	115.1	134.9	138.5	136.1	155.0	160.6	136.9
ROA (percent)	1.4	1.7	2.1	2.1	2.0	0.3	–3.5	–1.6	–0.9
ROE (percent)	...	...	27.1	25.6	24.3	4.6	–41.6	–20.4	–11.2
CAR (percent of risk-weighted assets)	11.7	11.7	10.1	10.2	11.1	11.8	14.6	14.6	17.4
NPLs (percent of total loans)	...	...	0.7	0.5	0.8	3.6	16.4	19.0	17.5
Loan-to-deposit ratio	...	...	...	1.2	1.3	1.6	1.6	1.2	1.1
Cross-border claims by foreign banks (all sectors, percent of GDP)	16.7	21.8	35.6	58.4	71.6	68.1	77.1	65.2	48.7
					Financial Markets				
Interest rates (end of period, one-year government bond, percent)	...	...	...	...	...	...	...	...	...
CDS spreads (sovereign, end of period, basis points)	...	...	...	7	138	833	551	265	365
EMBIG spread (sovereign, end of period, basis points)	...	...	...	...	...	...	...	...	...
Exchange rate (end of period, domestic currency/€)	0.67	0.70	0.70	0.70	0.70	0.71	0.71	0.71	0.70
NEER (index, 2003 = 100)	100.0	97.9	92.9	92.4	93.8	95.0	98.7	95.4	97.1
REER (CPI-based, 2003 = 100)	100.0	100.9	98.9	102.0	110.1	122.0	128.9	120.4	122.7
REER (ULC-based, 2003 = 100)	100.0	102.3	110.4	126.1	156.2	180.6	164.2	144.9	...
					Memorandum Items				
GDP (nominal, in billions of domestic currency)	6.4	7.4	9.1	11.1	14.7	16.1	13.1	12.7	14.2
GDP (nominal, in billions of €)	9.9	11.1	12.9	15.8	20.9	22.7	18.6	18.1	21.3

Source: IMF staff.

Note: CAR = capital adequacy ratio; CDS = credit default swap; CPI = consumer price index; EMBIG = Emerging Markets Bond Index Global; FDI = foreign direct investment; GIR = gross international reserves; NEER = nominal effective exchange rate; NPLs = nonperforming loans; REER = real effective exchange rate; ROA = return on assets; ROE = return on equity; ULC = unit labor cost.

[1] Financial and capital account balances excluding EU balance-of-payments support, use of IMF resources, and SDR allocations.

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