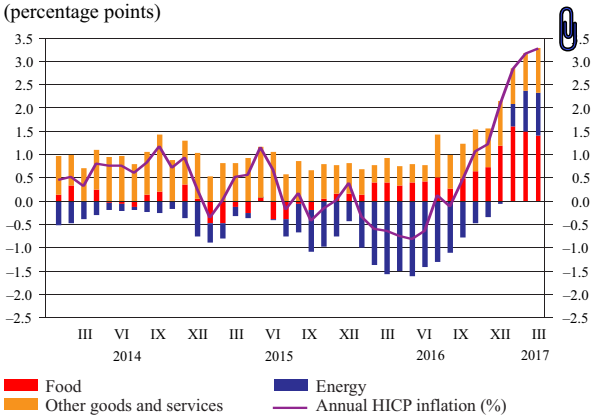
Inflation stabilises, main risk stems from oil price fluctuations

Contributions to annual HICP inflation
(percentage points)

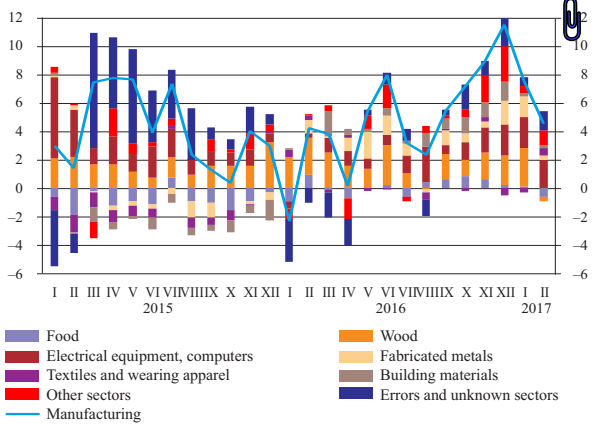


Sources: CSB, Bank of Latvia staff calculations.

Consumer prices (HICP) posted a 3.3% year-on-year rise in March. This outcome is in line with Latvijas Banka's expectations and has hardly changed since February (3.2%). In the coming months, the year-on-year inflation will hover around the 3% mark, with main risks stemming from oil price fluctuations. After losing one tenth of its worth in the world's market in mid-March, the price of *Brent* oil returned to 55 US dollars per barrel, reacting to decreased supplies in Libya and increased tensions in Syria. Since the oil price transmission to natural gas and heating prices takes a few months, any oil price hike would slow the decline of annual inflation only at the end of 2017. In turn, the global food price transmission to food retail prices is much faster. Month-on-month, global food prices declined in March, and so did wholesale and retail prices in Latvia.

Manufacturing retains high growth momentum

Contribution to manufacturing annual growth
(percentage points)

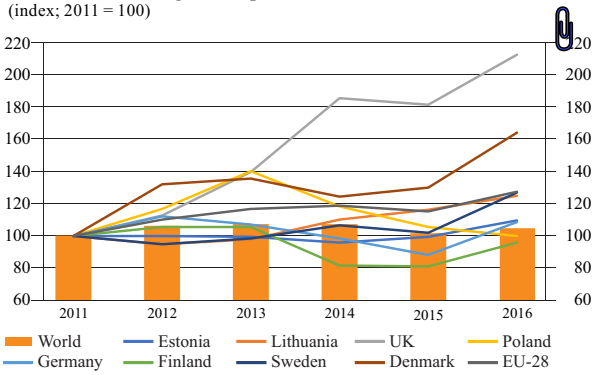


Sources: CSB, Bank of Latvia staff calculations.

After posting robust growth in 2016, manufacturing output continues to expand, increasing by 4.6% year-on-year in February 2017. The structure of manufacturing is gradually shifting towards high-value-added goods, with the highest year-on-year growth rates recorded in the production of computers and electrical and optical equipment (+34.8%), chemical industry (+24.7%), production of motor vehicles and trailers (+17.4%) as well as equipment and mechanisms (+15.7%). The demand-side factors look hopeful for manufacturing, with confidence indicators (both in Latvia and foreign trade partners) being at a high level. Moreover, the expected rebound in domestic construction is likely to boost the production of building materials and metalworking. Although capacity utilisation in manufacturing is close to its historically high level, there is still room for increase towards the EU peers.

Exports of goods increase volume and diversity

Shares of Latvia's goods exports
(index; 2011 = 100)



Sources: Eurostat data; Bank of Latvia staff calculations.

Year-on-year, exports of goods rose by 9.3% in nominal terms during the first two months of 2017. The export rise was broadly based both in terms of products and countries. The structure of Latvian exports has improved over the recent years, with exports of goods becoming more varied and increasingly new, innovative and niche products being generated. Export diversification is also going on: in each group of goods exports, the dominance of a single kind of goods is weakening. Although unit labour costs increased moderately during the recent years (i.e. wages rose faster than labour productivity), Latvia's export share in world imports is still growing, possibly pointing to increasing non-cost competitiveness.