



Republic of Latvia

Entering A New Phase of Reforms

September 2018

Disclaimer

This presentation and its contents are confidential and may not be reproduced, redistributed, published or passed on to any other person, directly or indirectly, in whole or in part, for any purpose and should not be treated as offering material of any sort. If this presentation has been received in error it must be returned immediately to the Ministry of Finance of the Republic of Latvia ("Latvia"). This presentation is not directed at, or intended for distribution to or use by, any person or entity that is a citizen or resident of, or located in, any locality, state, country or other jurisdiction where such distribution or use would be contrary to law or regulation or which would require any registration, licensing or other action to be taken within such jurisdiction.

THIS PRESENTATION IS NOT FOR PUBLICATION, RELEASE OR DISTRIBUTION, DIRECTLY OR INDIRECTLY, INTO THE UNITED STATES, AUSTRALIA, CANADA OR JAPAN OR ANY OTHER JURISDICTION IN WHICH SUCH PUBLICATION, RELEASE OR DISTRIBUTION WOULD BE UNLAWFUL. This presentation and the information contained herein are not an offer of securities for sale in the United States or any other jurisdiction. No action has been or will be taken by Latvia in any country or jurisdiction that would, or is intended to, permit a public offering of securities in any country or jurisdiction where action for that purpose is required. In particular, no securities have been or will be registered under the U.S. Securities Act of 1933, as amended (the "Securities Act") or with any securities regulatory authority of any state or other jurisdiction of the United States and securities may not be offered, sold or delivered within the United States except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act and applicable state securities laws and may only be sold outside of the United States in reliance on Regulation S under the Securities Act and otherwise in compliance with all applicable laws and regulations in each country or jurisdiction in which any such offer, sale or delivery of securities is made. Latvia does not intend to register or to conduct a public offering of any securities in the United States or any other jurisdiction. This presentation and its contents may not be viewed by persons within the United States (within the meaning of Regulation S under the Securities Act).

This presentation is directed solely at (i) persons who are outside the United Kingdom, (ii) persons in the United Kingdom who have professional experience in matters relating to investments falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 as amended (the "Order"), (iii) high net worth entities, and other persons in the United Kingdom to whom it may lawfully be communicated, falling within Article 49(2)(a) to (d) of the Order and (iv) persons in the United Kingdom to whom an invitation or inducement to engage in investment activity within the meaning of section 21 of the Financial Services and Markets Act 2000 in connection with the issue or sale of any securities of Latvia may otherwise lawfully be communicated or caused to be communicated (all such persons in (i)-(iv) above being referred to as "relevant persons"). In the United Kingdom, this presentation is directed only at relevant persons and persons who are not relevant persons should not in any way act or rely on this presentation. Any investment activity to which this presentation relates will only be available to and will only be engaged with relevant persons.

This presentation does not constitute or form part of, and should not be construed as, an offer or invitation to sell securities of Latvia, or the solicitation of an offer to subscribe for or purchase securities of Latvia, and nothing contained herein shall form the basis of or be relied on in connection with any contract or commitment whatsoever. Any decision to purchase any securities of Latvia should be made solely on the basis of the conditions of the securities and the information contained in the offering circular, information statement or equivalent disclosure document prepared in connection with the offering of such securities. Prospective investors are required to make their own independent investigations and appraisals of the business and financial condition of Latvia and the nature of any securities before taking any investment decision with respect to securities of Latvia.

By accessing this presentation the recipient will be deemed to represent that they possess, either individually or through their advisers, sufficient investment expertise to understand the risks involved in any purchase or sale of any financial instrument or any other information contained herein. The information in this presentation has not been independently verified. No representation or warranty, express or implied, is made as to the accuracy, completeness or fairness of the presentation and the information contained herein and no reliance should be placed on such information. None of Latvia, their advisers, connected persons or any other person accepts any liability for any loss howsoever arising, directly or indirectly, from this presentation or its contents. This presentation should not be construed as legal, tax, investment or other advice and any recipient is strongly advised to seek their own independent advice in respect of any related investment, financial, legal, tax, accounting or regulatory considerations. There is no obligation to update, modify or amend this presentation or to otherwise notify any recipient if any information, opinion, projection, forecast or estimate set forth herein changes or subsequently becomes inaccurate or in light of any new information or future events.

This presentation contains forward-looking statements, which include all statements other than statements of historical facts, including, without limitation, any statements preceded by, followed by or including the words "anticipates," "estimates," "expects," "believes," "intends," "plans," "aims," "seeks," "may," "will," "should" or similar expressions or the negative thereof. Such forward-looking statements involve known and unknown risks, uncertainties and other important factors beyond Latvia's control that could cause Latvia's actual results, performance or achievements to be materially different from future results, performance or achievements expressed or implied by such forward-looking statements. These forward-looking statements speak only as at the date of this presentation. Latvia expressly disclaims any obligation or undertaking to disseminate any updates or revisions to any forward-looking statements contained herein to reflect any change in its expectations with regard thereto or any new information or change in events, conditions or circumstances on which any of such statements are based.



Five Points Underpinning Latvia's Credit Profile



1

Flexible, resilient economy, among fastest growing in the Eurozone

2

Broadly-diversified exports, important factor underpinning the stable current account balance

3

Fiscal discipline, deeply embedded, reflected in low, and still declining, government debt

4

New era of reforms launched in 2017, focused on improving productivity and more inclusive growth

5

Well-capitalized and profitable banking sector, supporting moderate expansion of credit, with tighter AML/anti-terrorism funding regime





1. Overview

Portrait of an Improving Sovereign Credit

Presentation Outline

- 1) Overview: Portrait of an Improving Sovereign Credit 4
- 2) The Economy: Strong, Sustainable Growth 8
- 3) Banking Sector: Well-Capitalized, Profitable, and Beginning to Lend Again 13
- 4) Banking Sector Reforms: Strengthening AML/Anti-Terrorism Funding Controls 18
- 5) Fiscal Policy: Disciplined Approach Supports Improved Credit Profile 21
- 6) New Reform Push: Targets Productivity and More Inclusive Growth 24
- 7) Government Debt and Funding Strategy 29
- 8) Conclusion 35

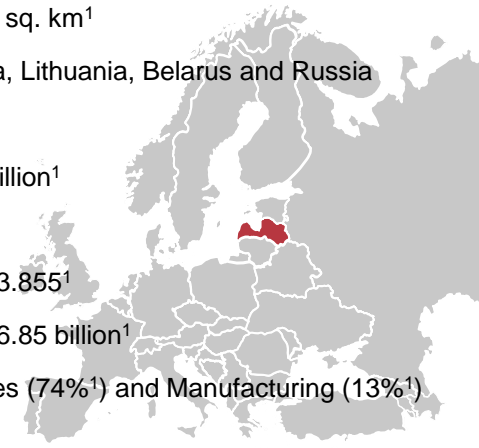


Latvia Belongs to Core Europe

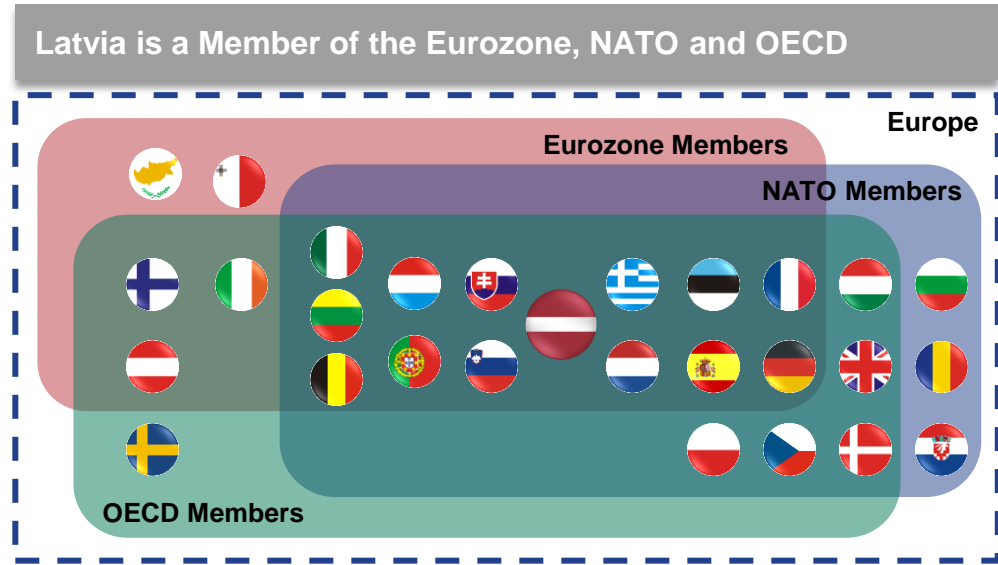
Latvia belongs to core Europe. Latvia is deeply integrated in the international community and committed to high standards in terms of economic policies and governance.

Key Facts

Territory	64,573 sq. km ¹
Borders	Estonia, Lithuania, Belarus and Russia
Capital	Riga
Population₂₀₁₇	1.93 million ¹
Currency	Euro
GDP per capita₂₀₁₇	EUR 13.855 ¹
Nominal GDP₂₀₁₇	EUR 26.85 billion ¹
Main economic sectors₂₀₁₇	Services (74% ¹) and Manufacturing (13% ¹)



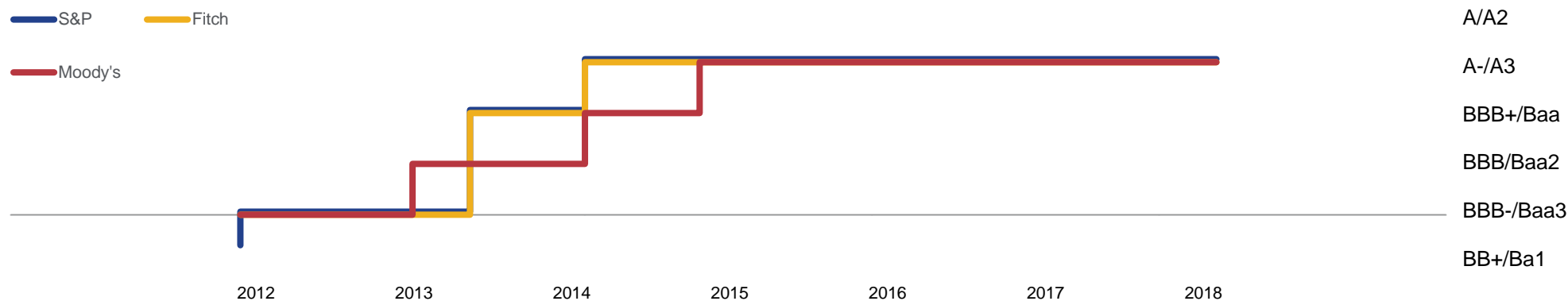
Source: Central Statistical Bureau of Latvia



Latvia's Credit Ratings are on an Improving Trend

Rating agencies acknowledged Latvia's low general government debt, small fiscal deficit and institutional strength

Long-term Foreign Currency Rating Development



Key Strengths of Latvia's Sovereign Credit Rating

- **Rapid growth** without worries about overheating
- **Eurozone membership enhances Latvia's creditworthiness:**
 - underpins economic policy coherence and credibility
 - improves fiscal and external financing flexibility
 - reduces foreign-currency risks on balance sheets
 - gives Latvian banks access to European Central Bank liquidity facilities
- **Membership in the OECD with its accompanying commitments to structural reforms and economic liberalization**
- **Sound banking sector** – dominated by foreign Scandinavian banks

Key Risk Factors Affecting Latvia's Sovereign Credit Rating

- **Social expenditures and defence spending could be higher** than anticipated
- **External financing risks and geo-political tensions with Russia** continue to constrain the ratings
- Latvia is a small and highly open economy, making it **vulnerable to external shocks**





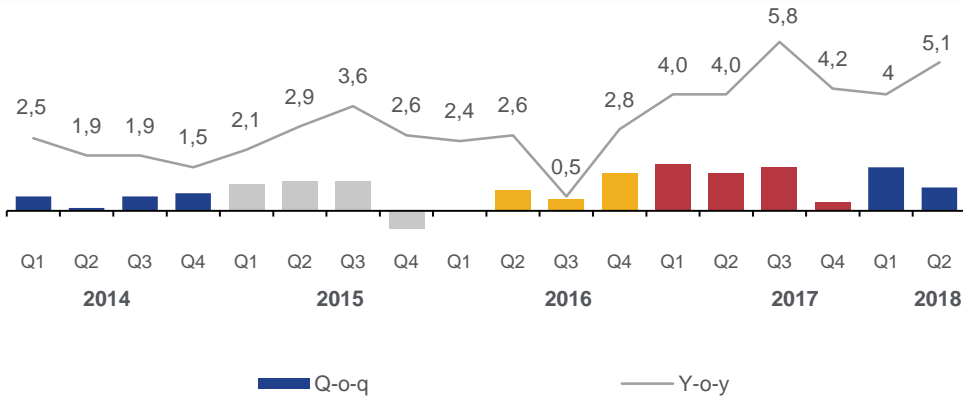
2. The Economy

Strong, Sustainable Growth

Growth Accelerated in 2017 and expected to remain solid in 2018

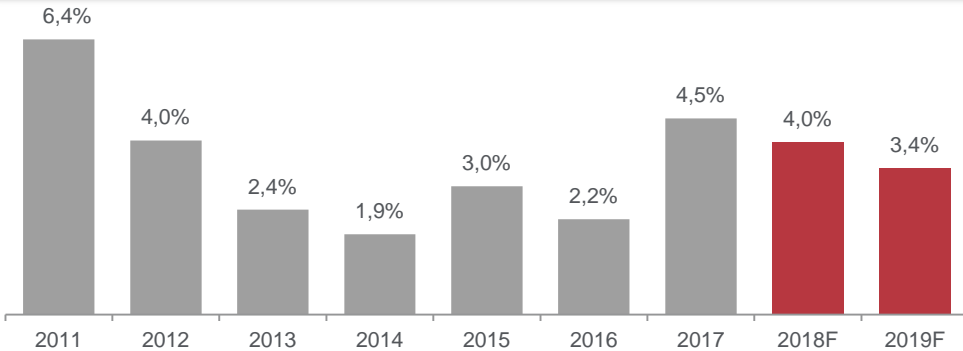
Latvia is among the top 5 fastest growing countries in the EU with a 3.0% average growth in the last 6 years. Robust growth is currently supported by strong consumption, private investment inflows, the EU funding cycle and favourable foreign trade conditions.

Real GDP Growth (%)



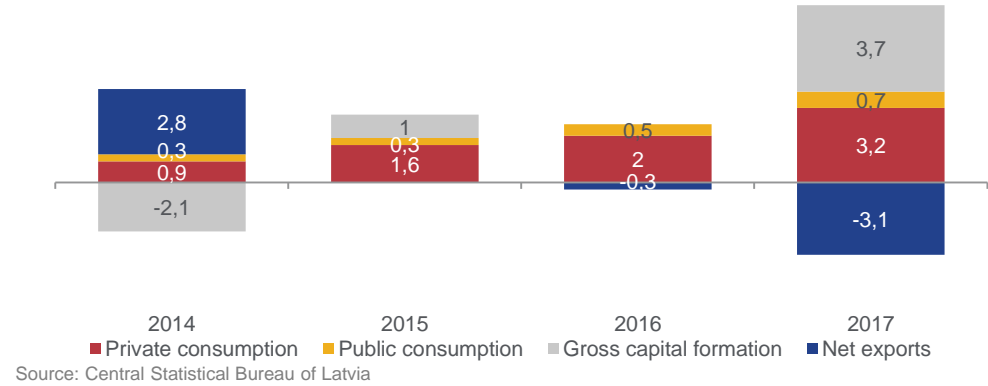
Source: Central Statistical Bureau of Latvia

Real GDP Growth (%)



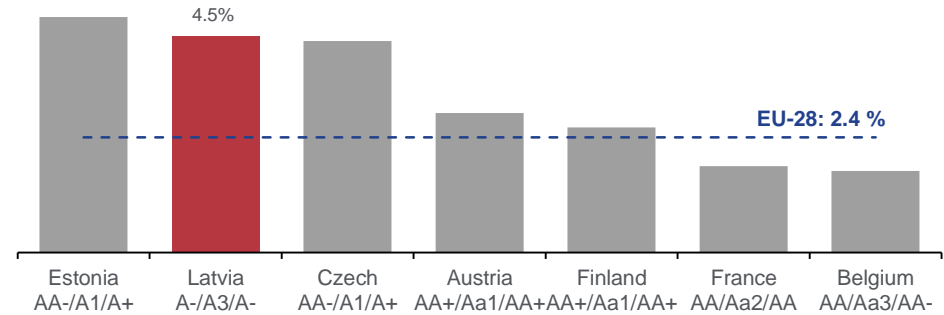
Source: Central Statistical Bureau of Latvia, Ministry of Finance

GDP Growth Composition (%)



Source: Central Statistical Bureau of Latvia

GDP Growth (2017, %)



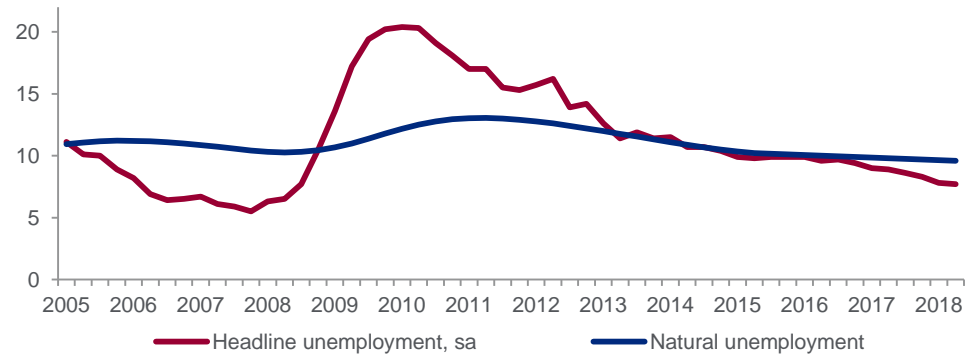
Source: Eurostat



Wage and Employment Growth Boosts Domestic Demand

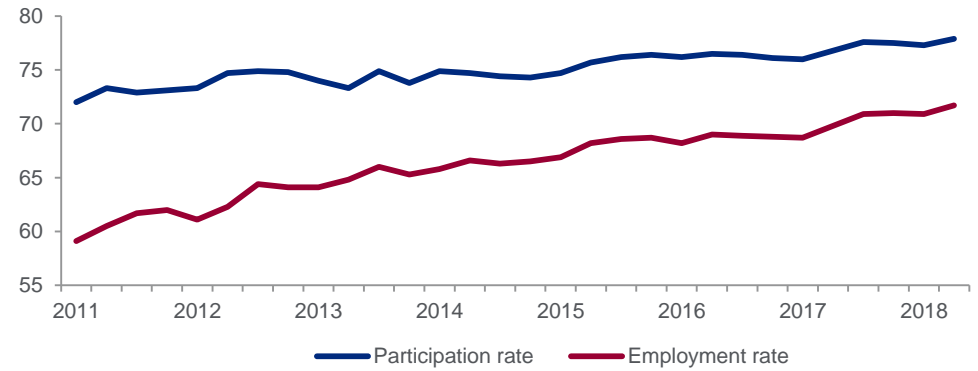
Unemployment is slightly below the natural rate; productivity growth is on the rise

Unemployment: Headline and Natural Rates



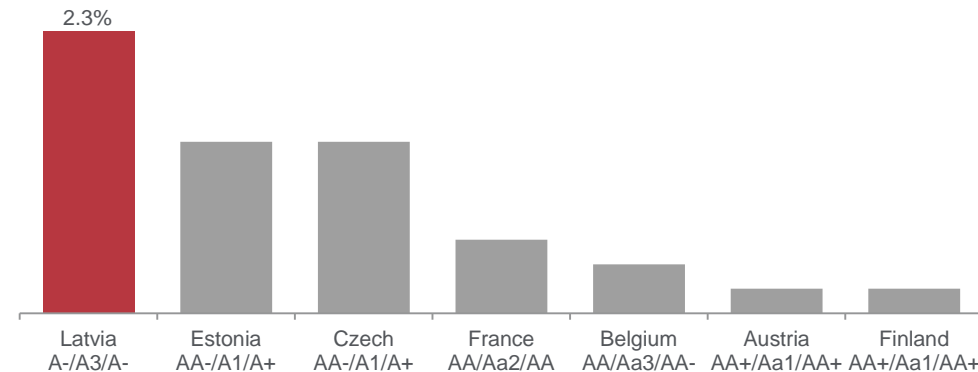
Source: Eurostat, Bank of Latvia

Participation and Employment Rates (age 15-64, %)



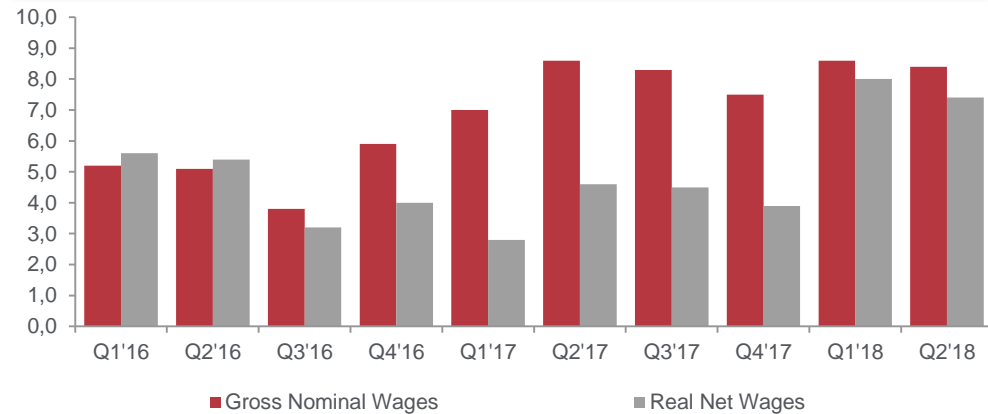
Source: Central Statistical Bureau of Latvia data

Real Productivity Growth Per Worker (2012-2017 average, %)



Source: Eurostat

Average Monthly Wage For Full-time Job (Y-o-y, %)



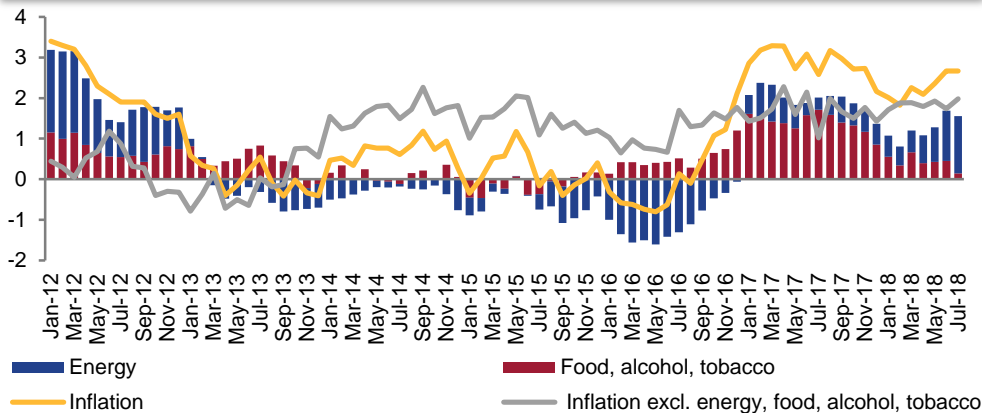
Source: Central Statistical Bureau of Latvia data



Inflation increased to slightly above 2%

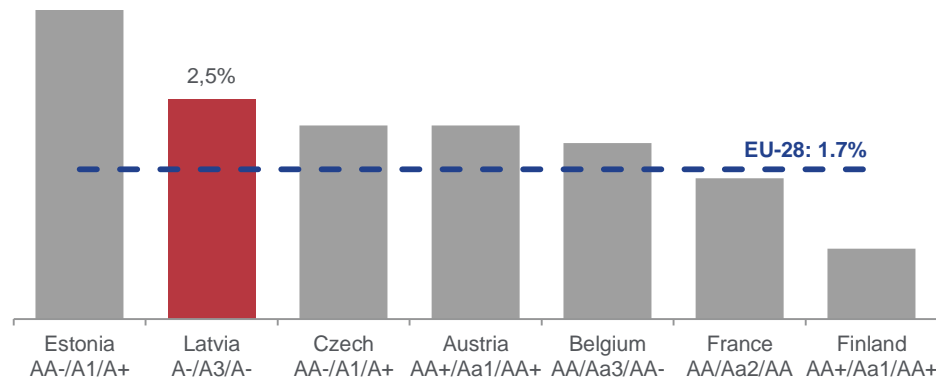
Latvia has maintained moderate and predictable inflation for years. Core inflation is moderate and stable

Inflation (HICP, %)



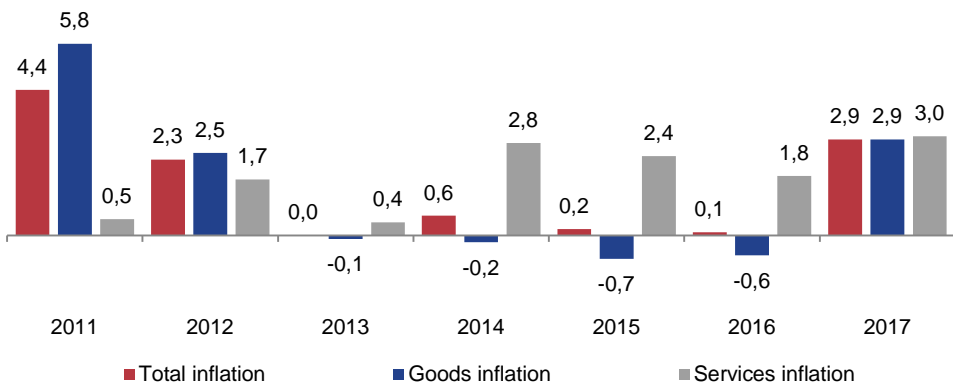
Source: Central Statistical Bureau of Latvia data, Bank of Latvia calculations

Harmonised Index of Consumer Prices (HICP) (July 2018, 12 month average rate of change; %)



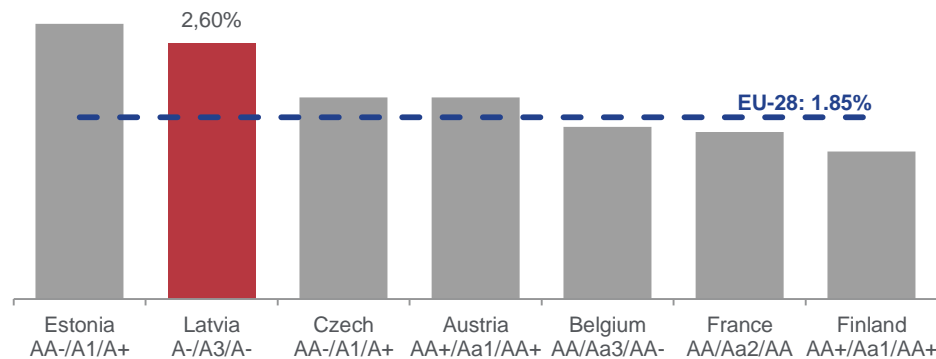
Source: Eurostat

Inflation in Latvia (HICP, %)



Source: Central Statistical Bureau of Latvia data

HICP Projection (2018-2019, %)



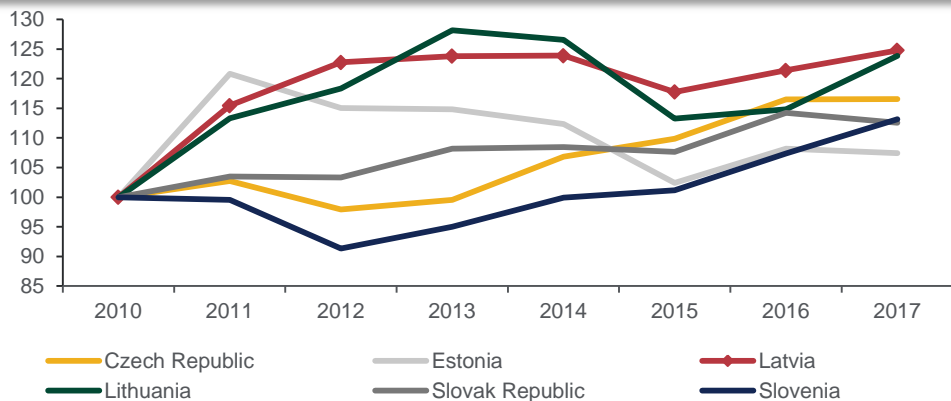
Source: European Commission, Summer projection, 2018



Improved Competitiveness and Value-Added Products Drive Exports

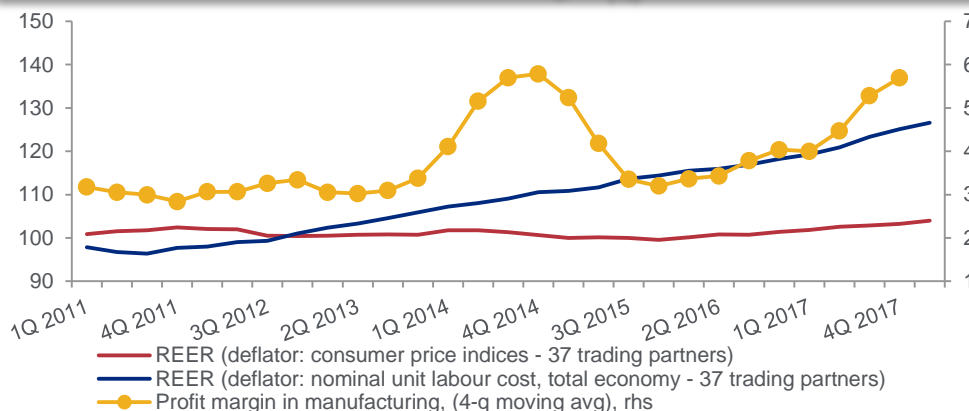
Favourable position in both price and quality competitiveness

Export Market Shares (2010=100)



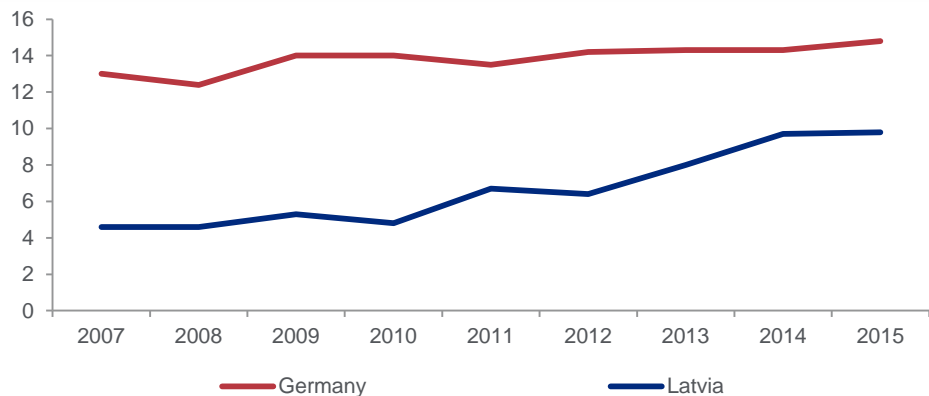
Source: World Trade Organization

Real Effective Exchange Rate (REER) Index (2005 = 100) and Profit Margin (%)



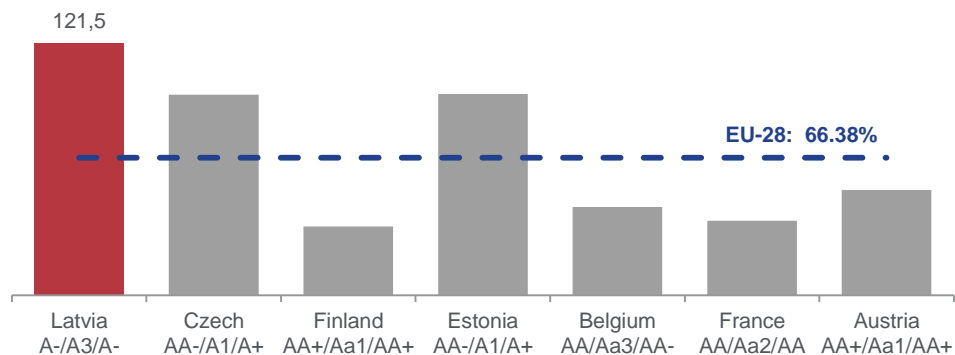
Source: Eurostat

High - Tech Exports (% Of Total Exports)



Source: Eurostat

Goods Exports Growth (2009-2017, %)



Source: Eurostat





3. Banking Sector

Well-Capitalized, Profitable, and Beginning to Lend Again

Sound, Well Capitalised and Liquid Banking Sector

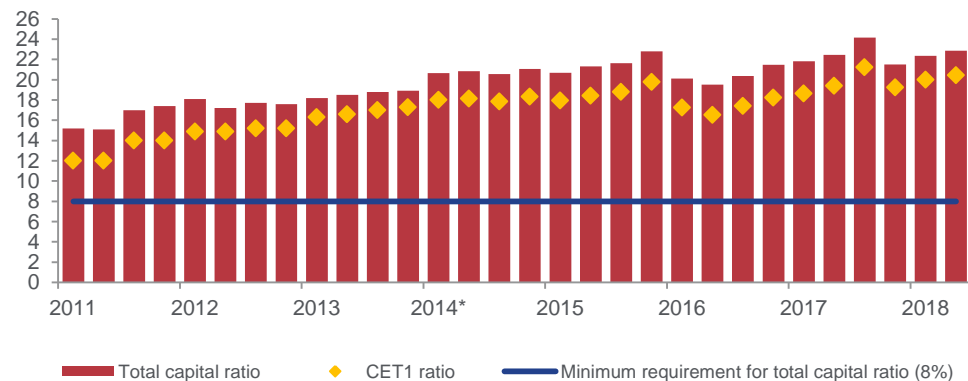
Latvia's outstanding growth engine has been supported by well capitalized banking sector, majority of which is owned by large Nordic banking groups.

Key Highlights

- The Latvian banking sector is dominated by subsidiaries and branches of banks from the European Economic Area, mostly Nordic countries¹ (54% of the banking sector capital, 67% of assets, 85% of domestic loans and 81% of domestic deposits)
- Capitalisation and liquidity ratios are well above minimum requirements. The banking sector's capital is mostly made of CET1 capital:
 - CET1 ratio $_{2Q\ 2018} = 20.5\%$ vs. EU average $_{1Q\ 2018} = 14.2\%$ ²
 - LCR $_{2Q\ 2018} = 251\%$
- The three largest banks are directly supervised by the ECB. Four banks fall under the remit of the Single Resolution Mechanism (12.07.2018. licence of ABLV Bank AS was withdrawn)

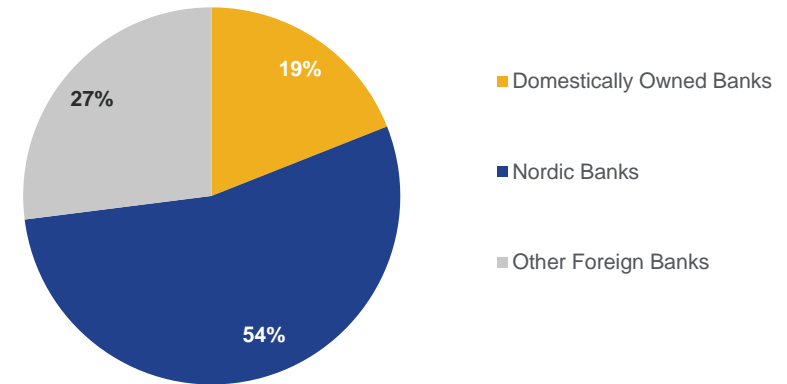
Source: ¹FCMC, ²EBA risk dashboard, fully loaded ratio

Capital Adequacy (%)



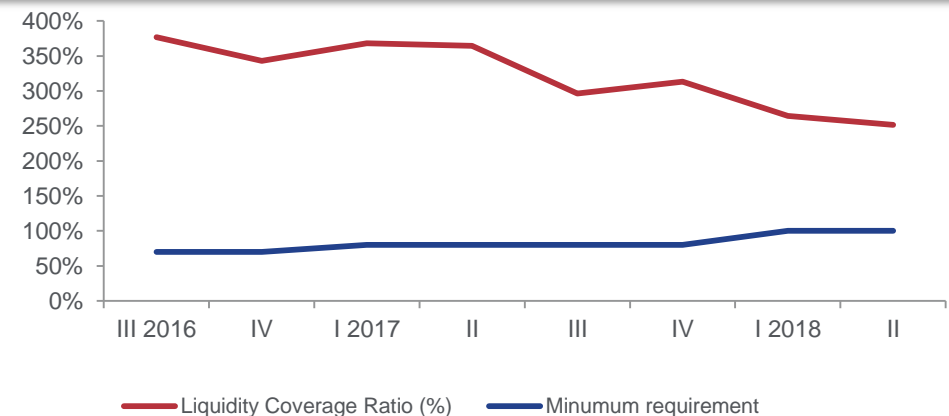
Source: FCMF | Note: As of Q1 2014 capital adequacy is calculated according to the CRDIV/CRR requirements and is not directly comparable with the data until Q1 2014 due to differences in methodology. Tier 1 ratio matches CET 1 ratio. The regulatory minimum capital adequacy requirement is 8%. Since 28 May 2014 the FCMC also applies a 2.5% capital conservation buffer.

Capital Ownership of the Banking System (2Q 2018)



Source: Bank of Latvia

Liquidity Coverage Ratio



Source: FCMF



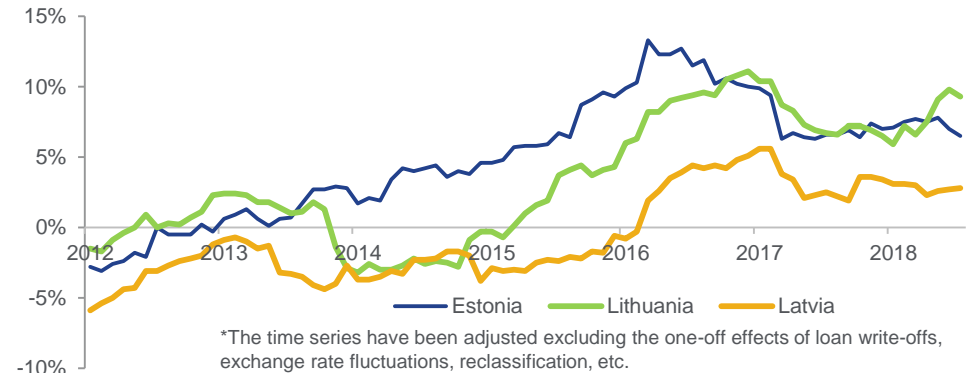
Bank Lending Recovers and Supports Growth

Domestic lending recovers and loan portfolio quality is above EU average

Key Highlights

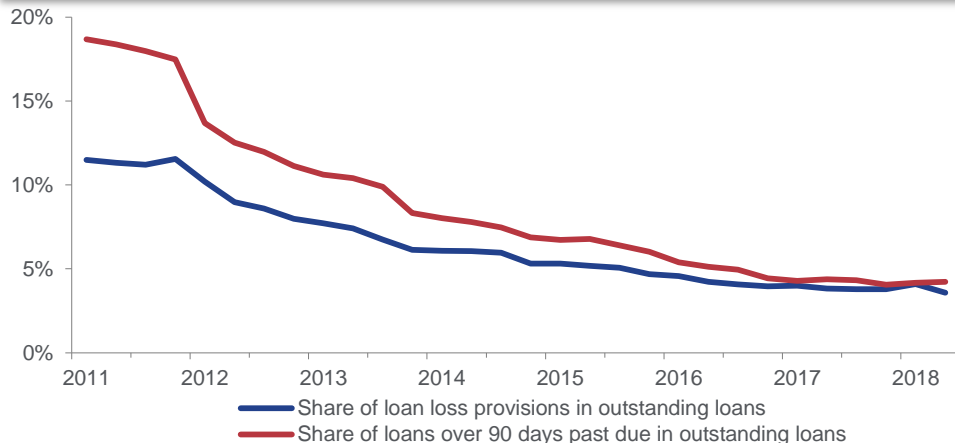
- After prolonged period of deleveraging, lending growth turned positive in April 2016
 - Loans to domestic households and NFCs stand at 39% of GDP in June 2018, down from almost 100% at the outset of the crisis
 - Loan-to-deposit ratio has fallen substantially leading to more balanced and sustainable domestic funding for loans
- The quality of loan portfolio is above EU average and continues improving further. The coverage ratio of overdue loans remains high
- The ECB bank lending survey indicates gradual increase in demand for loans in Latvia. Lending standards remain stable, however, banks plan to ease them. Expansionary monetary policy of the ECB is a supportive factor for lending

Loans to Domestic Clients excluding Government (yoy)



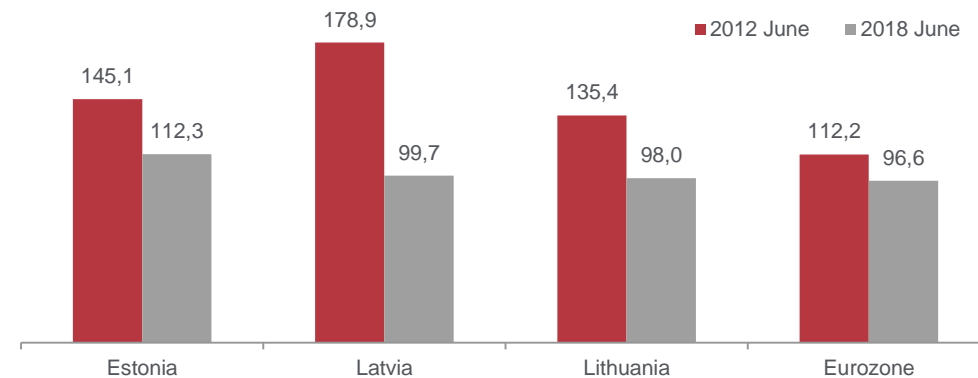
Source: ECB

Total Loan Portfolio Quality



Source: FCMF

Domestic Loan-to-Deposit Ratio (%)



Source: ECB



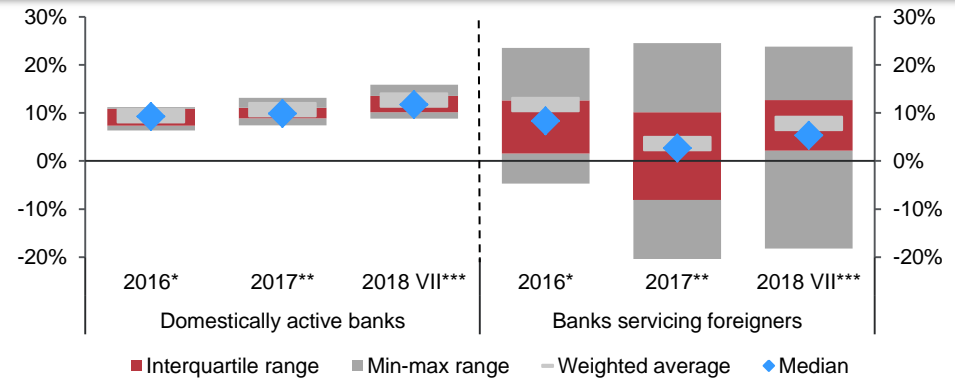
Banking Sector Profitability Remains Healthy

Banking sector profitability is supported by stable interest spread and economic growth

Key Highlights

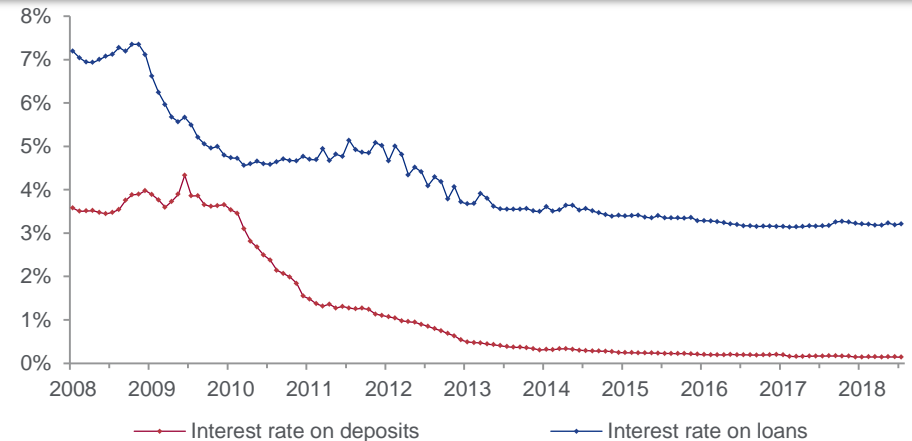
- In 2017, profitability of domestically active banks gradually increases as a result of favorable macrofinancial conditions.
- The profit of banks servicing foreigners continues to decrease due to decline in business volume and increased administrative expenses, which were largely caused by implementing enhanced AML/CFT requirements. In the light of recent events, a further deterioration of their profitability is expected. In 2017, severe losses of one credit institution (RoE < -50%; not shown on chart) were caused by a sale of a subsidiary.
- RoE and RoA of the Latvian credit institutions are relatively high, and still exceeds the EU average. In 2017, average RoE was 9.1% (when adjusted for the one-off write-off of DTAs and creation of the Luminor Group); EU average – 6.1% (EBA Risk Dashboard Q4 2017).
- In 2018, domestically active banks' returns remain more stable, less dispersed, while returns of banks servicing foreigners remain quite volatile. Average RoE stayed at 11.1% at the end of July 2018.
- With record-low loan and deposit rates, interest rate spread on outstanding amounts remains stable at around 3%

ROE Dispersion



Source: Bank of Latvia | Noted: *One-off adjusted data – VISA transaction in 2016, **One-off adjusted data – write-off of DTAs of Citadele Banka and Signet Bank, and creation of Luminor Bank. *** Annualized data

Interest Spread on Outstanding Loan Amounts



Source: Bank of Latvia | Note: * Banks which grant more than 50% of loans domestically and receive more than 50% of deposits from domestic clients ** Other banks



Parent Banks are Stable, Financially Sound and Profitable

Banks have high credit ratings, good profits, and on average they outperform their European peers on stock exchanges (compared to Eurostoxx Bank index)

Key Highlights

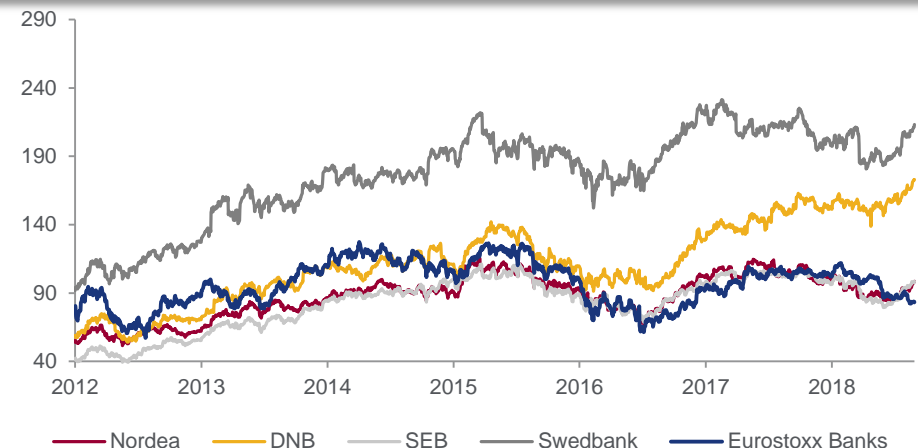
- Financial performance and capitalization level of the parent banks are strong
- Nordic banking groups' profitability is higher than the average in Europe
- Banks continue to invest in IT related projects to increase their operational efficiency and lower administrative expenses
- Since October 1, 2017, Nordea Bank AB Latvia branch and DNB Bank have merged their operations in the Baltic States. The newly-established Luminor Bank. Q2 2018, Luminor Bank is:
 - The second largest bank in Latvia by assets (4.8 billion EUR, 19% market share)
 - The second largest bank by equity (509 million EUR) and deposits value (2.9 billion EUR, 16% market share)
 - The first largest bank by the issued loans value (3.5 billion EUR, 25% market share)

Banks Financial Information

	Swedbank	SEB	Luminor*	
			DNB	Nordea
Assets (EUR mil)*	5,530	3,589	4 803	
CET1 ratio (%)*	25.57	22.49	17.35	
ROE (%)*	17.75	12.64	4.82	
S&P Global long term rating	AA-	A+	*	
Moody's long term rating	Aa3	Aa3	*	
Fitch long term rating	AA-	AA-	*	

Source: Association of Latvian Commercial Banks – financial reports, 1st quarter 2018 | *October 2017 Nordea group and DNB entities merged in the Baltics into one financial institution Luminor. Data on Luminor credit rating to be assigned.

Banking Groups' Equity Prices (01.01.2016 = 100, local currency)





4. Banking Sector Reforms

Strengthening AML/Anti-Terrorism Funding Controls

Tougher AML and CFT requirements are on the way

The events leading to the liquidation of ABLV Bank triggered regulatory efforts to significantly reduce high risk transactions by Latvian banks. New business models are being implemented in targeted banks as part of this initiative.

Key Highlights

- All credit institutions in Latvia specialising in foreign customer service have been provided with initial information about the necessity to ensure faster changes in the business model of the bank, in order to prevent and decrease the share of high risk transactions and in doing, non-residents servicing banks had to submit the FCMC plans for restructuring their business by April.
- FCMC is supervising the change of the business models of the credit institutions, by reducing the share of large exposure customers and achieving the target variables set by the FCMC for the sector as a whole.
- On April 10 the Government approved the amendments to the Law on the Prevention of Money Laundering and Terrorism Financing banning cooperation between banks and shell companies in Latvia which have no real economic activity, thus even more strengthening the AML/CFT requirements.
- In addition Law plans to establish Financial Crime Investigation Special Task force, enabling effective cooperation of private and public sector in financial intelligence and investigation of financial crimes.
- Respective amendments were adopted by the Parliament on April 26 and the amended Law on the Prevention of Money Laundering and Terrorism Financing is fully effective from May 9, 2018
- The Law would prescribe that within 14 days after the date when the Law is effected, banks shall notify their high-risk clients of closing their accounts and within 60 days banks no longer can perform any operations with the accounts.

Timeline for the enforcement of the amendments to the Law on the Prevention of Money Laundering and Terrorism Financing

April 10th

- Government approves the amendments to the Law on the Prevention of Money Laundering and Terrorism Financing

April 26th

- The amended Law approved by the Parliament (Saeima)

May 9th

- The amended Law is fully effected

May 22nd

- The deadline of 2-week notice by Banks to their clients in question

July 8th

- Banks no longer can perform any operations with the high risk clients accounts.

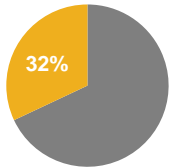


The Economic Impact of Tighter AML CFT is Minimal

Latvia's banking system is dominated by banks owned by strong Nordic parents, funded through domestic deposits, lending to Latvia-based clients. Banks funded through foreign currency deposits play a small role in Latvia's economy

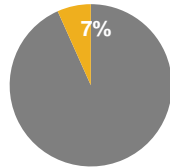
The Role of Foreign Clients Banks in Latvia (without ABLV Bank)

Total Banking Assets

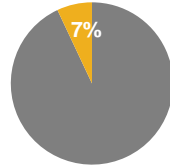


■ Banks servicing Foreign Clients (FC)

Total Domestic Lending

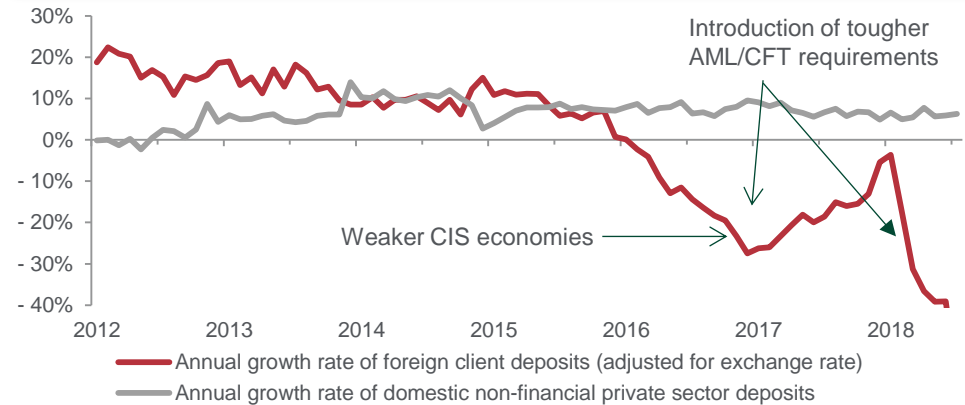


Total Domestic Deposits



Source: Bank of Latvia, data 2Q 2018

Growth Rates of Domestic and Foreign Client Deposits (%)



Source: Bank of Latvia

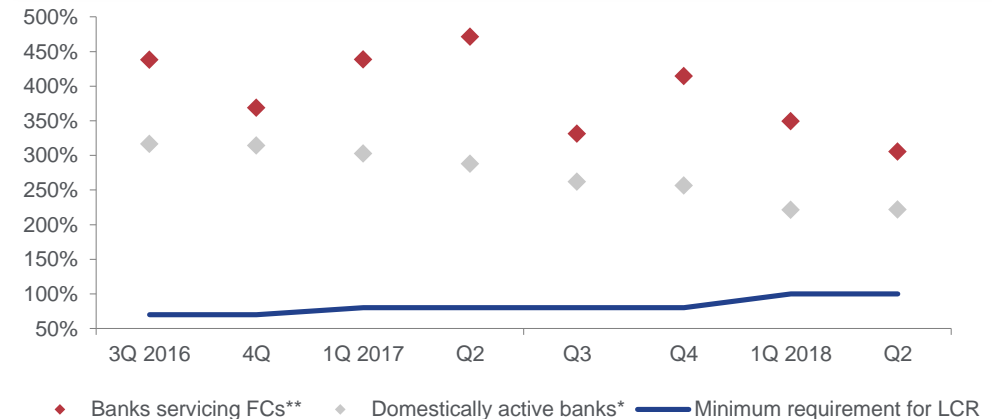
Economic Impact of ABLV Bank Liquidation

- The liquidation of ABLV has had little impact on the Latvian economy
 - Government revenues from ABLV were 0.06 % from GDP in 2017, with 0.3 % from GDP generated overall from NRD sector.*
 - Funds covering guaranteed deposits were transferred from ABLV
 - ABLV has already repaid the emergency liquidity assistance extended to it earlier by the Bank of Latvia.
 - Deposit flight has not spread to other banks whose business models are based primarily on domestic funding and lending.

Source: Bank of Latvia,

*Fitch (Latvia sovereign risk from ABLV Bank failure appears limited, 27.02.2018.)

Bank Liquidity Ratios Well Above FCMC Requirement



Source: FCMC



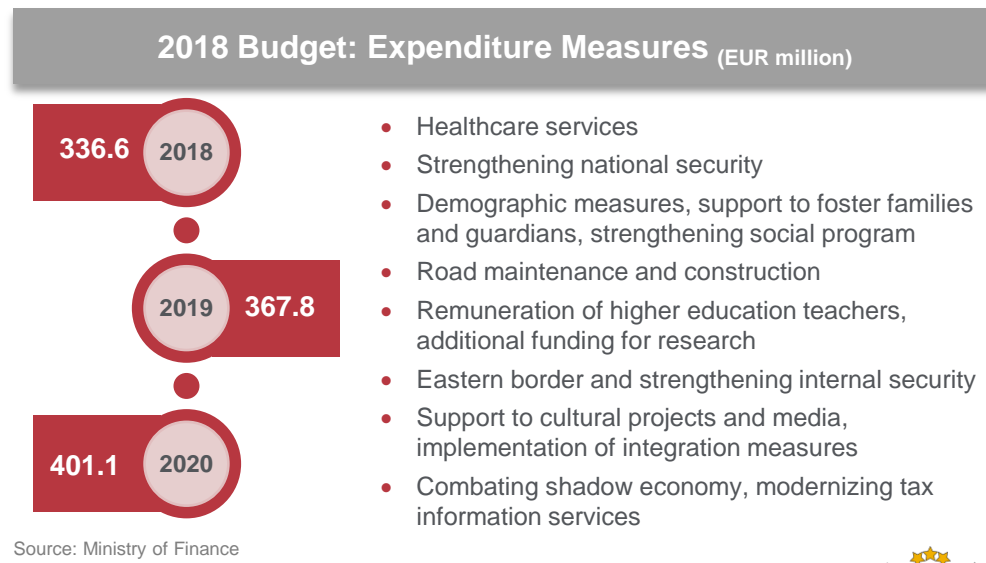
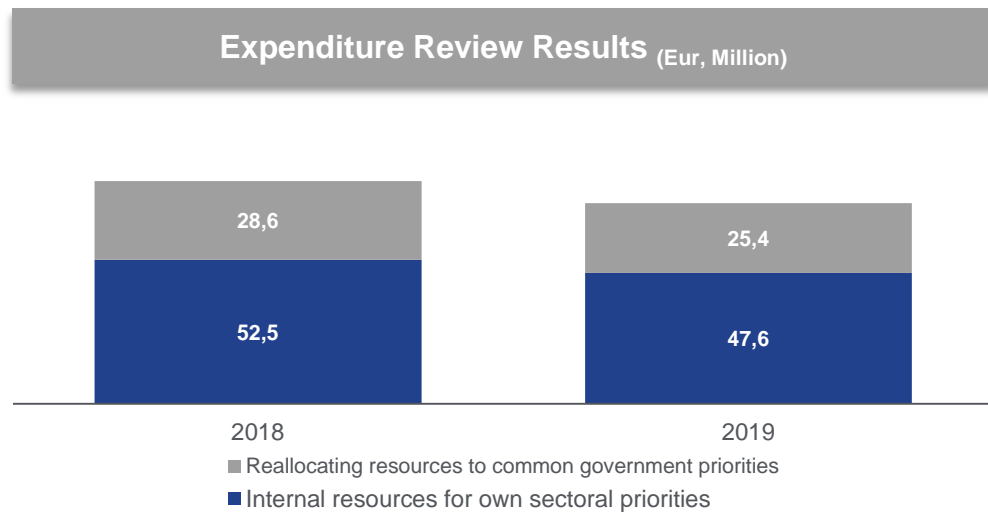
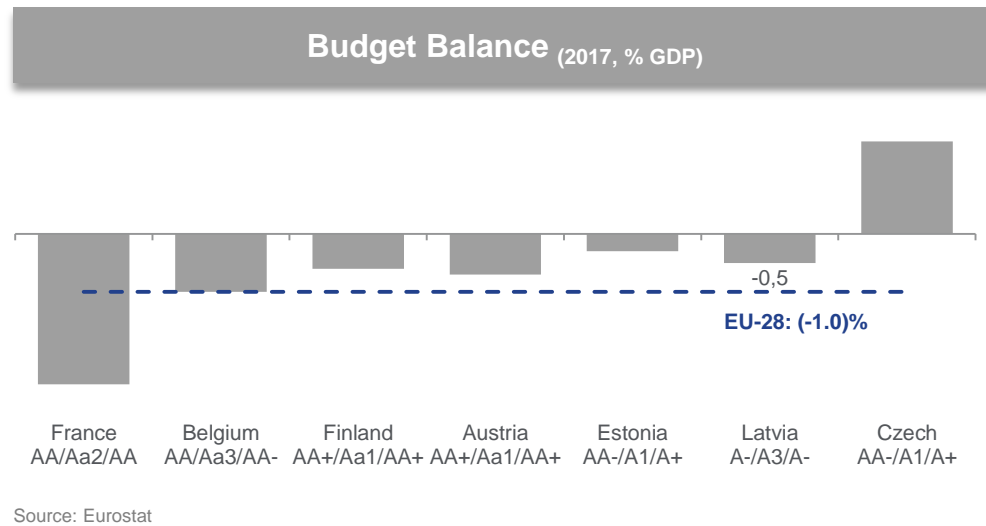
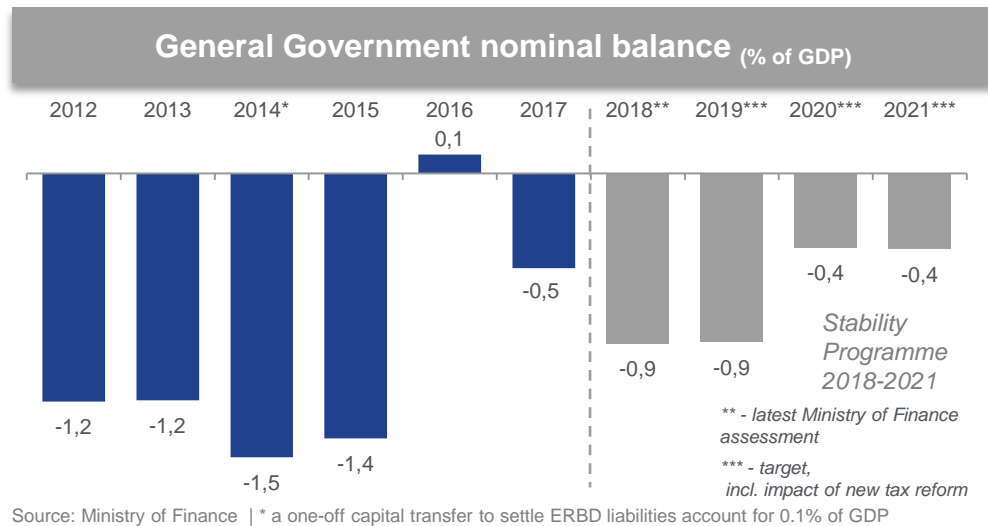


5. Fiscal Policy

Disciplined Approach Supports Improved Credit Profile

Fiscal Sustainability Remains Top Priority

Prudent fiscal management and fiscal discipline regulation ensures public deficits to be at low and sustainable level.



Pension Reform Underpins Stability of Public Finances

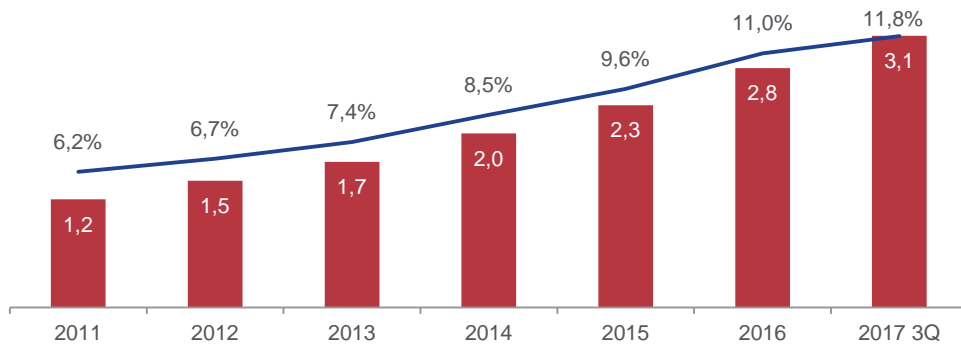
Latvia is well positioned to withstand fiscal challenges arising from an aging population.

Latvia's Pension System And Recent Reforms

- Latvia's reformed pension system consists of three tiers:
 - state compulsory unfunded pension scheme (the 1st tier)
 - state funded pension scheme (the 2nd tier)
 - private voluntary pension scheme (the 3rd tier)
- In 2012, measures were introduced to address long-term sustainability:
 - starting with 2014 retirement age is gradually increased by 3 months each year until it reaches 65 years in 2025
 - minimum contribution period to secure full pension was increased from 10 to 15 years starting from 2014 and up to 20 years starting from 2025
 - contributions to the funded, e.g. 2nd tier, pension scheme increased from 2% to 4% in 2013, to 5% in 2015, and to 6% in 2016

Source: The State Social Insurance Agency

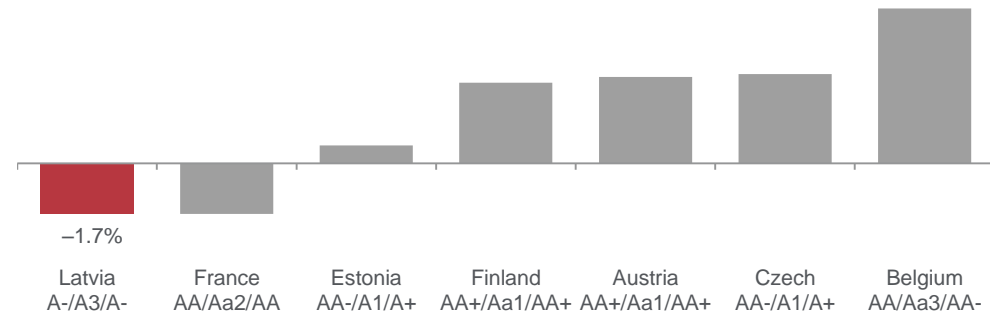
The 2nd Tier Pension Net AUM (EUR billion, % GDP)



■ 2nd tier pension net assets (EUR billion) — 2nd tier pension net assets (% of GDP)

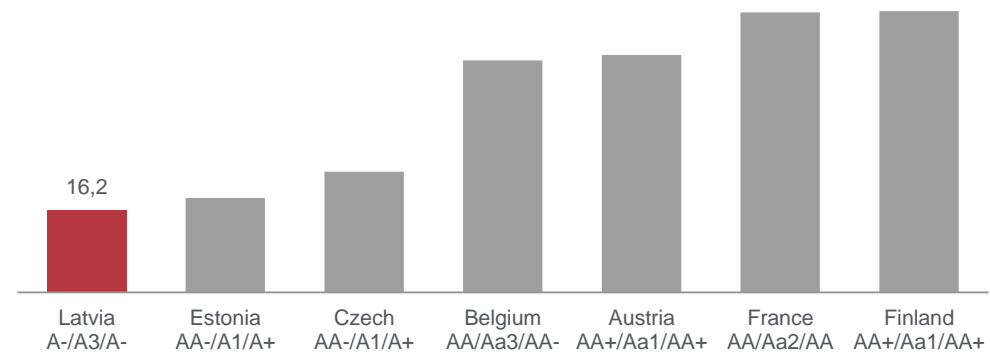
Source: Financial and Capital Markets Commission, Central Statistical Bureau of Latvia

Age-related Spending, Projected Change (2013-2060, % GDP)



Source: European Commission Ageing Report, May 2015

Latvia's age-related spending is one the lowest in EU (2013, % GDP)



Source: European Commission Ageing Report, May 2015





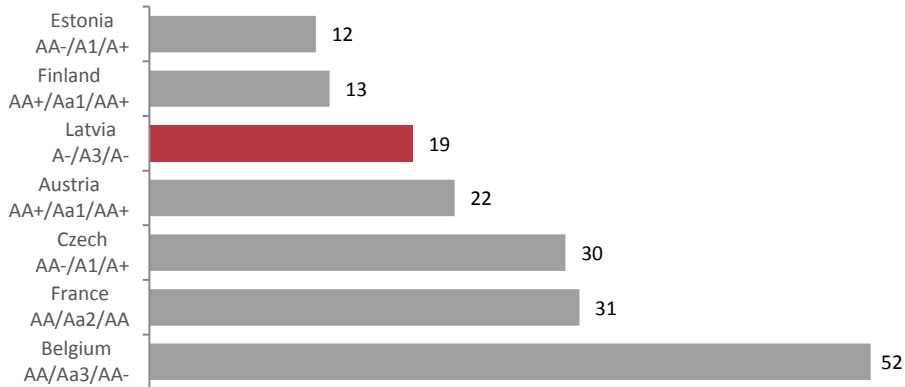
6. New Reform Push

Targets Productivity and More Inclusive Growth

Latvia's Advanced Country Status Reflected in "Soft" Metrics

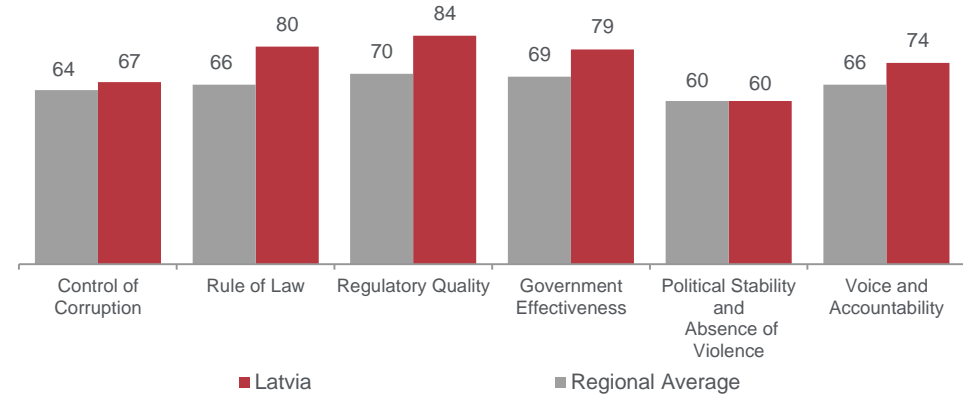
Expanded Structural reforms to build on existing high institutional strength and favourable business environment.

World Bank "Ease of Doing Business" Ranking



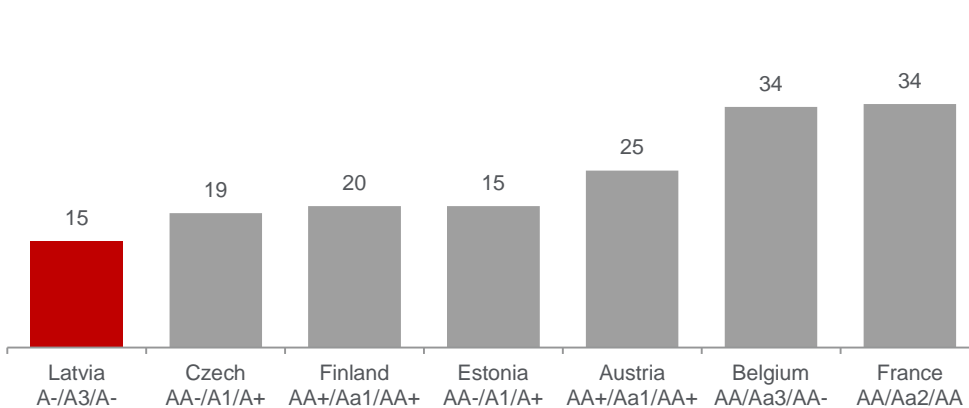
Source: World Bank, Doing Business 2017

World Bank Worldwide Governance Rankings



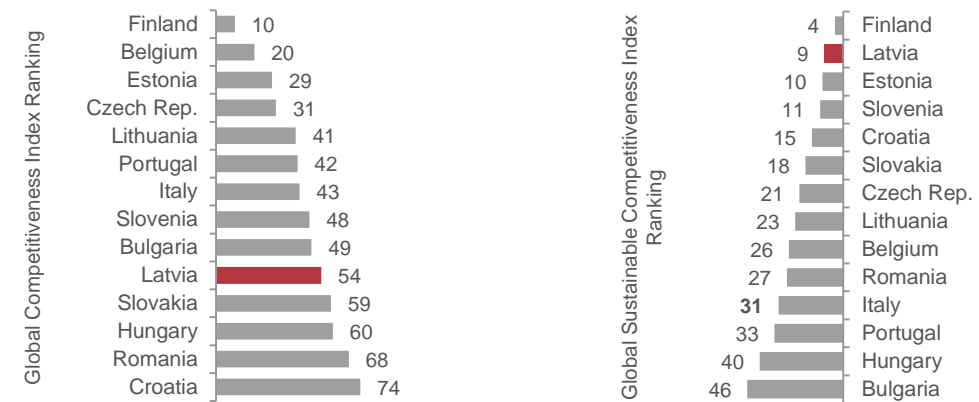
Source: World Bank, 2016 Rankings

Adjusted Top Statutory Tax Rate on Corporate Income (2017, %)



Source: Financial and Capital Markets Commission, Central Statistical Bureau of Latvia

The Global Competitiveness Index Rankings



Source: Klaus Schwab, World Economic Forum, The Global Competitiveness Report 2017–2018, The Global Sustainable Competitiveness Index 2017



Reform Policies Laying Foundation for New Growth Model

Structural reforms in education, employment and judicial environment help improving labour market and business conditions



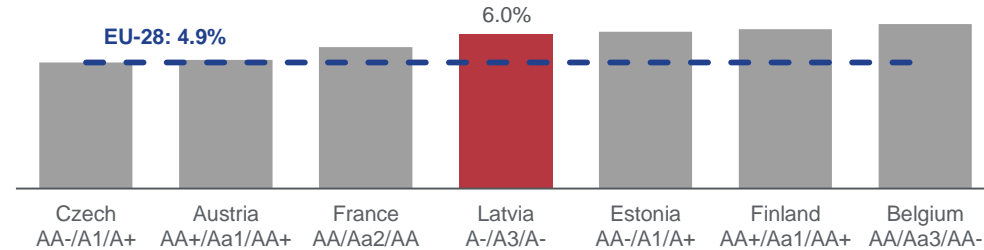
Source: National Reform Programme 2016; European Commission, Country Report Latvia 2016; EU Council's recommendations 2016; OECD Economic Survey on Latvia 2015

Healthcare Reform

- Aimed to improve governance, clearer principles of resource allocation and more efficient use of funds
- Implementation of Public Health Guidelines 2014 - 2020 to encourage the health care system availability, quality and cost-effectiveness
- Healthcare long term funding reform
- **Stability and Growth Pact deficit derogation for 2017 - 2019 was granted for healthcare reform** (e.g., reducing waiting line; detection of cancer and improving access to treatment; reform of reimbursable drugs for patients of the Chronic hepatitis C).

Education Reform (2015, % GDP)

- Funding for education is adequate, but the network of education system and number of pupils per teacher are not optimal.
- Teacher remuneration reform starting from September, 2016: (i) fixed minimum salary for teacher; (ii) school network rearrangement; (iii) increase in funding for teachers' salaries.



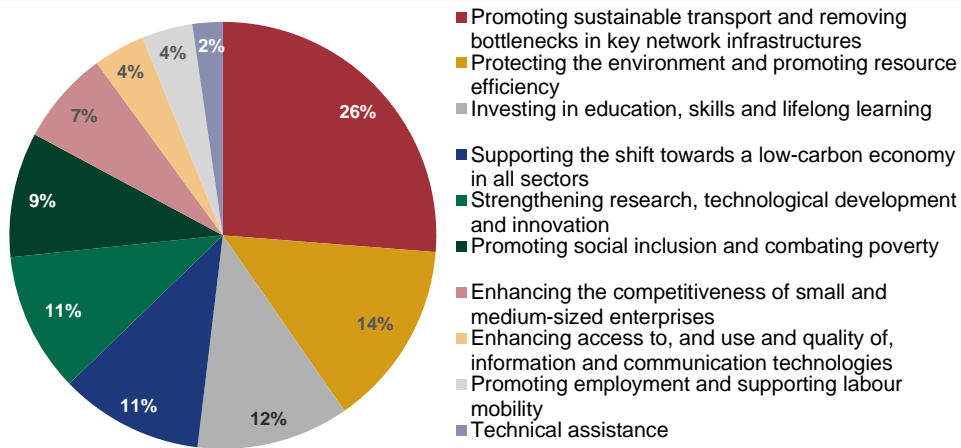
Source: Eurostat



EU Playing Key Role in Funding Structural Change in Latvia

Efficient and well targeted absorption and use of EU funds will promote competitiveness and stimulate economic growth as well as support necessary structural reforms

Allocation Of EU Funds For 2014-2020 By Priority Axes



Source: Ministry of Finance

EU Cohesion Policy Accompanies Structural Reforms

- Latvian economy and the goals envisaged by the National Development Plan are strongly supported by well targeted and smart EU cohesion policy funds (EU funds like Structural funds and Cohesion Fund) investments.
- EUR 4.4 billion EU funds are available for targeted and smart investments in Latvia within 2014 - 2020 programming period across major nine priority areas with general aim to enhance competitiveness of Latvia's economy and build foundation for the sustained and smart growth.
- EUR 2.9 billion EU funds are already contracted for investment projects.
- During 2007 - 2013 period Latvia has successfully completed the investment programme supported by EUR 4.5 billion Cohesion Policy EU funds (100% of EU funds «envelope» for Latvia).
- EU funds investment progress is transparent and can be followed: www.esfondi.lv

Source: Ministry of Finance

EU Funds After 2020 and Government's Support

- The European Commission has published a proposal for the new multiannual financial framework after 2020 in May 2018. In optimistic scenario European Commission expects to reach agreement on budget in first half of 2019.
- After the European Commission published legislative sectoral proposal for Cohesion policy the overall impact on the Latvia's envelope is -13% comparing to the envelope of the MFF 2014-2020. Final allocation from Cohesion policy will be set in the result of negotiations between EU Member States, Commission and European Parliament.
- Initial European Commission proposal for Latvia's Cohesion policy allocation is 4.3 billion EUR. Allocation will be a subject of negotiations and Latvia will insist on bigger allocation.
- Latvia will remain eligible to receive support from all three Cohesion policy funds (Cohesion Fund, European Regional and Development Fund, European Social Fund).



Pro-growth Tax Reform in Line with Balanced Budget Mandate

Key goals: improve competitiveness, promote exports, reduce inequality and raise revenue to one-third of GDP

Strategy framework

- Tax structures and rates review
- Improving tax administration
- The fight against the shadow economy

Principles

- Predictability and a long-term vision
- Regional competitiveness, at least in the Baltic region
- Tax motivation for improvement
- A similar tax burden on similar types of revenue
- Lending and capitalization improvement
- Reducing the cost of tax administration

Positive impact on economy

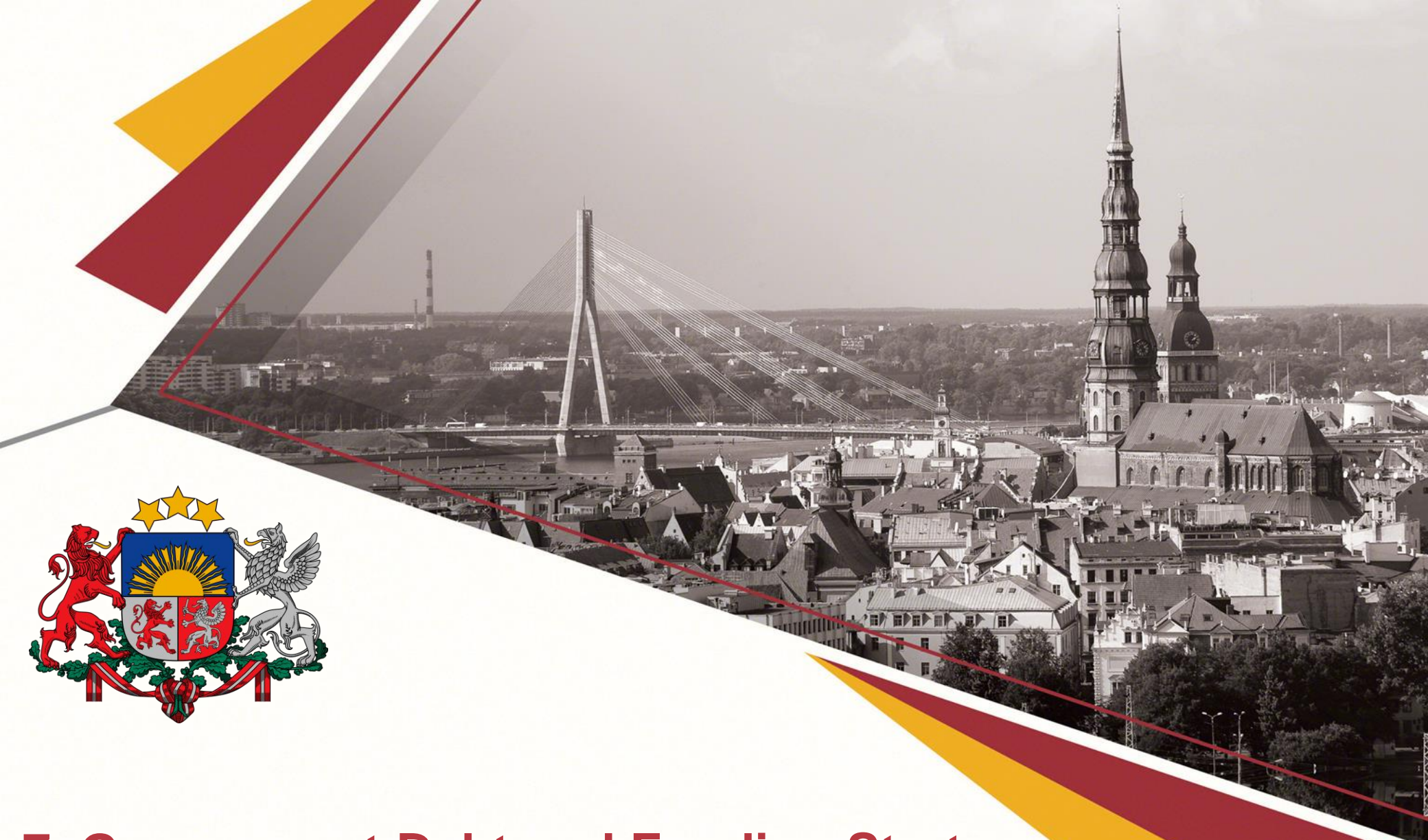
- Raise of disposable income of employees inducing private consumption;
- More competitive entrepreneurs on regional and global scene as well as stimulation of own investment;
- Better capitalized businesses, more opportunities to raise additional funds for development;
- Increased prospects to raise production capacity of goods and services, more effective and efficient production process;
- More equality between different income groups and types of income;
- Higher tax revenue resulting from increased economic activity and less tax avoidance.

Source: Ministry of Finance

Main changes

- ✓ **Non-taxable minimum – EUR 250**
Differenced depending on income level from EUR 0 / month to EUR 250 per month (2020)
- ✓ **Allowance for dependents**
EUR 250 per month (2020)
- ✓ **Minimum salary**
from EUR 380 to EUR 430
- ✓ **Social contribution**
increase by 1% directed to health care
- ✓ **Reform of Solidarity tax**
- ✓ **PIT rate smoothing**
- ✓ **Progressive Personal Income Tax**
Decrease from 23% to 20% for year's salary up to EUR 20,004, 23% for EUR 20,004 – 55,000, 31,4% for above EUR 55,000
- ✓ **Corporate Income Tax**
20% on distributed profit; no CIT is payable on undistributed profits





7. Government Debt and Funding Strategy

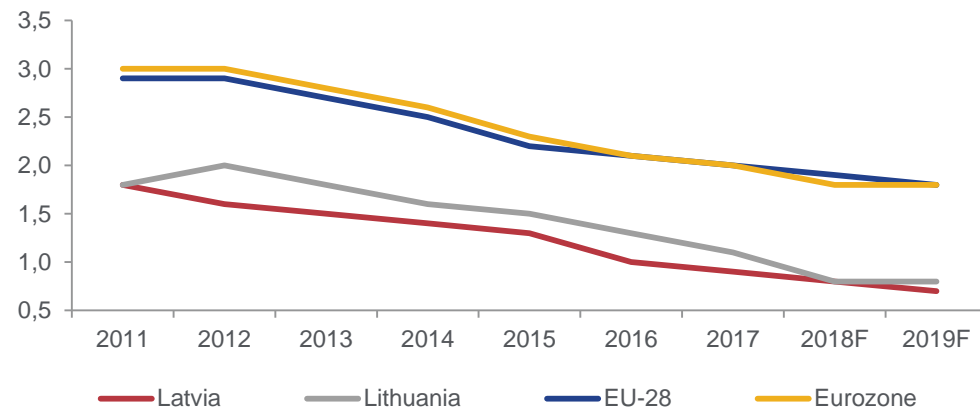
Public Debt on Declining Trend

Latvia remains committed to keeping government debt at moderate levels

Key Characteristics of Latvia's Government Debt

- Fiscal consolidation and reduction of the deficit along with economic growth has helped stabilise levels of government debt
- General government debt is amongst the lowest in the EU at 40% of GDP at the end of 2017. It is the 4th lowest in the Eurozone and the 8th lowest in the EU
- Latvia enjoys one of the lowest debt servicing costs across the region, significantly lower than the EU and Eurozone averages
- Since March 2014 Latvia participates in the European Stability Mechanism, which provides additional financial stability to its members

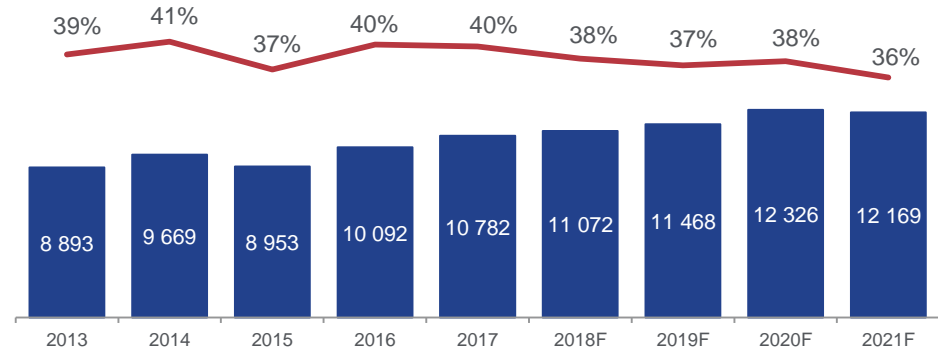
Debt Servicing Costs (% GDP)



Source: European Economic Forecast, Spring 2018, European Commission

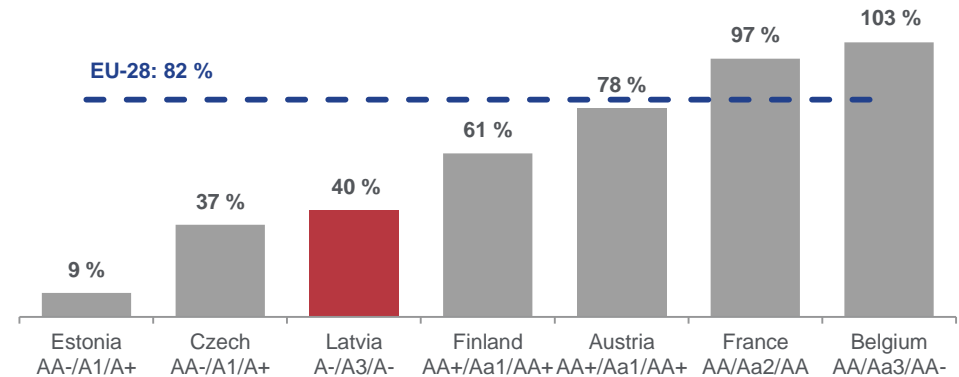
General Government Debt Year End

(EUR million, % GDP, ESA methodology)



Source: Eurostat, The Treasury

General Government Debt (2017, % GDP)



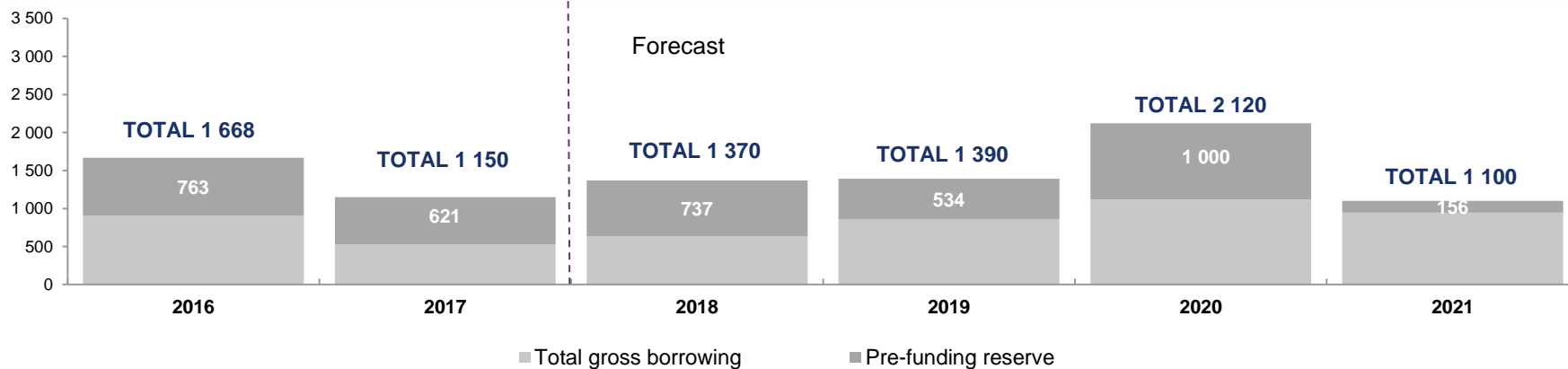
Source: Eurostat



Conservative Borrowing Based on Pre-funding

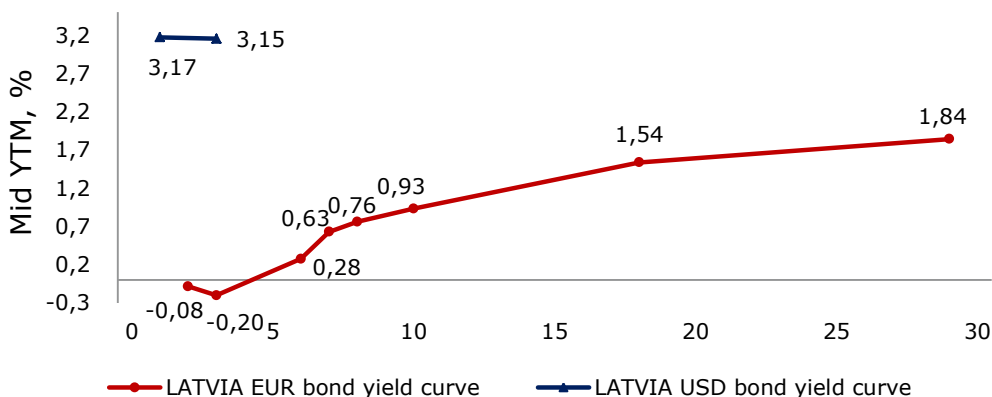
Latvia is conducting a prudent and efficient debt management strategy

Government Gross Borrowing (nominal, EUR million)



Source: The Treasury

Latvia Secondary Eurobond Market (mid yield to maturity, %)



Source: Data as of 12th September 2018, Bloomberg

Borrowing activities in international capital markets in 2017

- Latvia tapped the market twice with dual tranche Eurobond issues.
- For the first time 30-year Eurobonds were issued as the longest tenor so far, setting a coupon at 2.250% (yield 2.330%), providing a benchmark issue size of EUR 500 million.
- In order to increase liquidity, Latvia also reopened two of its Eurobonds in 2017:
 - maturing October 7, 2026 increasing the outstanding amount by EUR 300 million in two transactions;
 - maturing May 16, 2036 increasing the outstanding amount by EUR 200 million in two transaction.

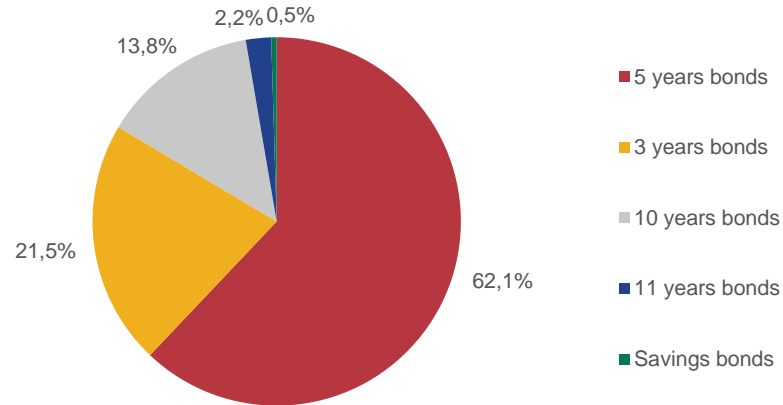


Domestic Market Continues to Perform Strongly

Demand is steady and average yields remain low

Domestic Securities Outstanding by Original Maturity

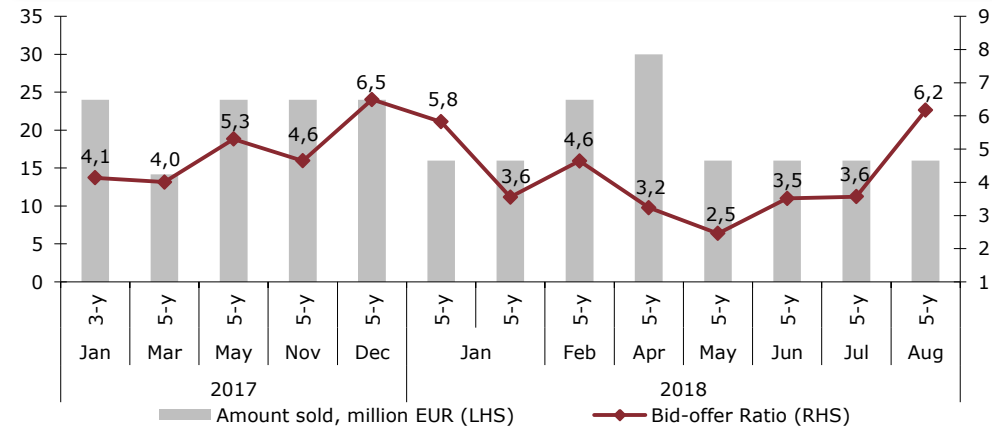
(end of the June 2018, %)



Source: The Treasury

- Primary dealer system operates since 11 February 2013. Domestic debt securities outstanding constituted EUR 1.117 billion as of 29th August 2018.
- The Treasury maintains regular domestic debt securities auctions offering medium term T-bonds. Long term segment is covered by international issues.
- For several years Latvia has concentrated domestic supply mainly in 5-year segment and focuses on increasing the liquidity.
- Last 5 year T-bond program (via 6 auctions) reached of 150 million EUR outstanding.
- A new 5-long T-bond program was opened in the beginning of 2018. Coupon was fixed at the 0,250%. Currently amount outstanding is 190 million EUR. In order to maintain liquidity it is expected to continue regular auctions and gradually increase on-the-run 5-long T-bond program.

Domestic T-Bond Competitive Multi-Price Auctions



Source: The Treasury | Note: Bid-to-Cover ratio: Bid Amount to State Treasury offered amount, * Since 2015 6m T-Bills benchmarks are tap issues of original 12m T-Bills in maturity brackets from 4.5 to 9 months.

Last 5 year T-Bond auction results

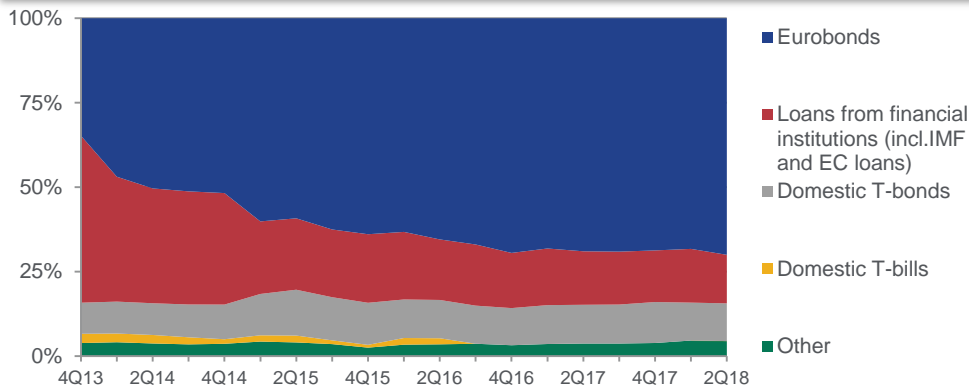
- On 29th of August Latvia had last T-bond auction
- Nominal value of 16 million EUR were sold in a competitive multi-price auction with total demand of 57.1 million EUR (bid-offer ratio of 6.17).
- In addition 4 million EUR were sold in non-competitive (fixed price) auction.
- The weighted average yield rate was 0,459%.



Central Government Debt Profile

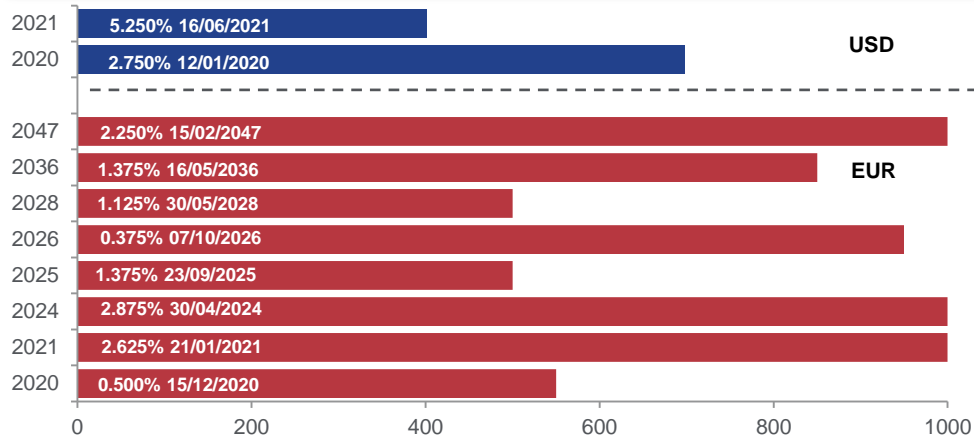
International Loan Programme has been largely refinanced in international capital markets, while government debt redemptions remain moderate

Debt structure by Instruments (%)



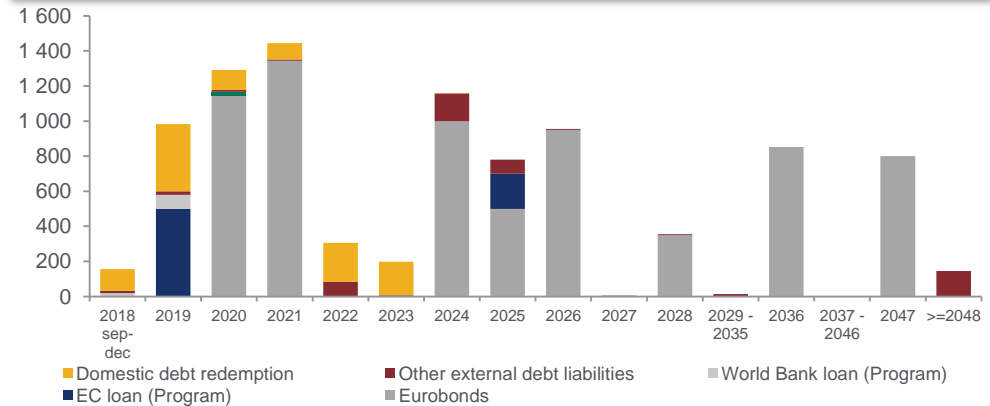
Source: The Treasury

Outstanding Bonds in the International Markets (nominal amount, million)



Source: The Treasury

Debt Redemption Profile (EUR million)



Source: The Treasury

Debt Portfolio Management

Parameters	Strategy	31/03/2017	30/06/2018
Maturity profile (%)			
• up to 1 year	≤ 25%	10.2%	14.6%
• up to 3 year	≤ 50%	43.8%	44.1%
Share of fixed rate ⁽¹⁾	≥ 60%	93.8%	89.1%
Macaulay duration (years)	5.00 – 9.00	6.05	6.47
Net debt ⁽²⁾ currency composition	100% EUR with a deviation of +/- 5%	99.96%	99.97%

Source: The Treasury | ⁽¹⁾Fixed rate central government debt with a maturity over one year; ⁽²⁾Central government debt at the end of the period less the amount of loans and receivables, where impairment loss of guarantees are not taken in account (including Treasury's cash accounts, investments in deposits and fixed income securities, loans, receivables (including receivables of derivative financial instruments which are not classified as risky from credit risk perspective)), and increased by provisions of guarantees as well as liabilities of derivative financial instruments which are not classified as risky from credit risk perspective.



Medium Term Funding Requirement and Borrowing Strategy 2018-2020

External borrowing instruments will represent the most significant share of the overall borrowing volume

Medium Term Borrowing Strategy

Goal

Ensure timely and full availability of financial resources for covering the financing requirement, by maintaining continuous borrowing opportunities in the international and domestic financial markets on optimal terms and conditions.

Principles

- Flexibility (towards timing, maturities and currencies)
- Achieve balance between risks and costs
- Consistency and transparency to markets

General Financing Requirement

Central Government Budget Balance

Net Lending

Other Flows
at the Treasury's Accounts

Outstanding Central Government Debt
Redemptions
(domestic and external)

Pre-funding
Strategy For
Refinancing
Debt

Borrowing Instruments (BASE scenario)

- Benchmark issuances in global capital markets
- Continuing issuances in domestic market

Alternative Instruments

- Niche capital market instruments (JPY, CHF, etc.)
- Private placements (reverse enquiries)
- Loans from international financial institutions (EIB, CEB, etc.)

Central Government financing estimation

(2018-2020, EUR million)

31-August-2018	2018		2019	2020
	Jan - Aug	Sep - Dec		
Central government budget balance, net lending and other flows	659	-1 186	-510	-446
Outstanding central government debt redemption	-720	-156	-982	-1 284
<i>Of which:</i>				
Domestic debt repayment	-240	-124	-383	-114
External debt repayment	-480	-32	-599	-1 170
Total	-61	-1 342	-1 492	-1 731
Gross borrowing	840	530	1 390	2 120
<i>Of which:</i>				
International issuance	650	350	1 000	2 000

Note: Indicative in the planned period

The borrowing volume could be increased in case of:

Liability management activities

Possible restructuring of the government guaranteed commitments (loans) of several hospitals by refinancing / early repayment





8. Conclusion

Building on Past Success, Facing Future Challenges

Latvia has fully recovered from the economic recession and has built-up an outstanding fiscal position, returning to its previous standards of fiscal prudence. The economy is on a sustainable, robust growth path, characterized by improved competitiveness, solid domestic demand, and a flexible business sector able to adjust to external shocks

Flexible and Resilient Economy

→ Decreasing Unemployment

Sustainable Debt Levels and Prudent Fiscal Management

→ Investor attractiveness

Resilient towards external shocks

→ Proven track record in overcoming economic crisis in the past

Belongs to the Core of Europe

→ EZ membership
→ The member of all the important international organizations



Predictable public policies and outstanding track record of successful structural reforms

→ Long term growth reinforced

Well Capitalised Banking Sector

→ Credit Growth is being restored
→ Economic Development promoted

Credit rating gains

→ Investors confidence boosted due to reforms and sound macroeconomic fundamentals

Solid Export Growth

→ Balance of Payments improvement
→ Sustainable Current Account Balance

