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THE FOLLOWING OFFERING CIRCULAR MAY NOT BE FORWARDED OR DISTRIBUTED OTHER THAN AS PROVIDED BELOW AND MAY NOT BE REPRODUCED IN ANY MANNER WHATSOEVER. THIS OFFERING CIRCULAR MAY ONLY BE DISTRIBUTED OUTSIDE THE UNITED STATES TO PERSONS THAT ARE NOT U.S. PERSONS AS DEFINED IN REGULATION S UNDER THE U.S. SECURITIES ACT OF 1933, AS AMENDED (THE "**SECURITIES ACT**") AND WITHIN THE UNITED STATES TO "QUALIFIED INSTITUTIONAL BUYERS" ("**QIBs**") AS DEFINED IN AND PURSUANT TO RULE 144A OF THE SECURITIES ACT ("**RULE 144A**"). ANY FORWARDING, DISTRIBUTION OR REPRODUCTION OF THIS DOCUMENT IN WHOLE OR IN PART IS UNAUTHORISED. FAILURE TO COMPLY WITH THIS DIRECTIVE MAY RESULT IN A VIOLATION OF THE SECURITIES ACT OR THE APPLICABLE LAWS OF OTHER JURISDICTIONS.

NOTHING IN THIS ELECTRONIC TRANSMISSION CONSTITUTES AN OFFER TO SELL OR THE SOLICITATION OF AN OFFER TO BUY ANY SECURITIES IN ANY JURISDICTION. THE SECURITIES HAVE NOT BEEN AND WILL NOT BE REGISTERED UNDER THE SECURITIES ACT OR WITH ANY SECURITIES REGULATORY AUTHORITY OF ANY STATE OR OTHER JURISDICTION OF THE UNITED STATES AND MAY NOT BE OFFERED OR SOLD WITHIN THE UNITED STATES EXCEPT TO QIBs PURSUANT TO RULE 144A.

Confirmation of your Representation: In order to be eligible to view this Offering Circular or make an investment decision with respect to the securities, you must be a person other than a U.S. person (within the meaning of Regulation S under the Securities Act) who is outside the United States unless you are a QIB in the United States. By accepting the email and accessing this Offering Circular, you shall be deemed to have represented to us that you and any customers you represent are not a U.S. person unless you are a QIB in the United States; the electronic mail address that you have given to us and to which this e-mail has been delivered is not located in the U.S., its territories and possessions (including Puerto Rico, the U.S. Virgin Islands, Guam, American Samoa, Wake Island and the Northern Mariana Islands), any State of the United States or the District of Columbia unless you are a QIB in the United States; and that you consent to delivery of such Offering Circular by electronic transmission.

You are reminded that this Offering Circular has been delivered to you on the basis that you are a person into whose possession this Offering Circular may be lawfully delivered in accordance with the laws of the jurisdiction in which you are located and you may not, nor are you authorised to, deliver this Offering Circular to any other person.

Any materials relating to the potential offering do not constitute, and may not be used in connection with, an offer or solicitation in any place where offers or solicitations are not permitted by law. If a jurisdiction requires that the potential offering be made by a licensed broker or dealer and any underwriter or any affiliate of any underwriter is a licensed broker or dealer in that jurisdiction, any offering shall be deemed to be made by the underwriter or such affiliate on behalf of the Issuer in such jurisdiction.

Under no circumstances shall this Offering Circular constitute an offer to sell or the solicitation of an offer to buy any securities in any jurisdiction. Recipients of this Offering Circular who intend to subscribe for or purchase the securities are reminded that any subscription or purchase may only be made on the basis of the information contained in the final Offering Circular. This Offering Circular may only be communicated to persons in the United Kingdom in circumstances where section 21(1) of the Financial Services and Markets Act 2000 does not apply.

This Offering Circular has been sent to you in an electronic form. You are reminded that documents transmitted via this medium may be altered or changed during the process of electronic transmission and consequently none of the Republic of Latvia, acting through the Treasury, Citigroup Global Markets Limited, Credit Suisse Securities (Europe) Limited, any person who controls any such persons, or any of their respective directors, officers, employees, agents or affiliates accepts any liability or responsibility whatsoever in respect of any difference between the Offering Circular distributed to you in electronic format and the hard copy version available to you on request from Citigroup Global Markets Limited or Credit Suisse Securities (Europe) Limited.

NOT FOR GENERAL CIRCULATION IN THE UNITED STATES OF AMERICA
OFFERING CIRCULAR DATED 13 JUNE 2011

REPUBLIC OF LATVIA,
ACTING THROUGH THE TREASURY

U.S.$500,000,000

5.25 PER CENT. NOTES DUE 2021

The issue price of the U.S.$500,000,000 5.25 per cent. Notes due 2021 (the "**Notes**") of the Republic of Latvia, acting through the Treasury ("**Latvia**" or the "**Republic**") is 98.164 per cent. of their principal amount.

Unless previously redeemed or cancelled, the Notes will be redeemed at their principal amount on 16 June 2021. See "*Terms and Conditions of the Notes – Redemption and Purchase*".

The Notes will bear interest from and including 16 June 2011 (the "**Issue Date**") at the rate of 5.25 per cent. per annum payable semi-annually in arrear on 16 June and 16 December each year, commencing on 16 December 2011. Payments on the Notes will be made in U.S. dollars without deduction for or on account of any Latvian withholding taxes and the Republic will pay additional amounts if any such taxes are imposed, as described under "*Terms and Conditions of the Notes – Taxation*".

Application has been made to list the Notes on the Official List of the Luxembourg Stock Exchange and to admit the Notes to trading on the Luxembourg Stock Exchange's regulated market pursuant to the rules and regulations of the Luxembourg Stock Exchange.

This Offering Circular neither constitutes an offering circular pursuant to Part II of the Luxembourg law on prospectuses for securities (*loi relative aux prospectus pour valeurs mobilières*) dated 10 July 2005 (the "**Luxembourg Prospectus Law**") which implements Directive 2003/71/EC (the "**Prospectus Directive**") nor a simplified offering circular pursuant to Part III of the Luxembourg Prospectus Law. Accordingly, this Offering Circular does not purport to meet the format and the disclosure requirements of the Prospectus Directive and Commission Regulation (EC) No. 809/2004 implementing the Prospectus Directive, and it has not been, and will not be, submitted for approval to any competent authority within the meaning of the Prospectus Directive and in particular the Supervisory Commission of the Financial Sector (*Commission de Surveillance du Secteur Financier*), in its capacity as competent authority under the Luxembourg Prospectus Law. The Notes, issued pursuant to this Offering Circular, will therefore not qualify for the benefit of the single European passport pursuant to the Prospectus Directive.

The Notes are expected to be rated BBB- by Fitch Ratings Limited ("**Fitch**"), Baa3 by Moody's Investors Service, Inc. ("**Moody's**") and BB+ by Standard & Poor's Ratings Services, a division of The McGraw-Hill Companies, Inc. ("**S&P**"). A rating is not a recommendation to buy, sell or hold securities and may be subject to revision, suspension or withdrawal at any time by the assigning rating organisation.

Fitch, Moody's and S&P are established in the European Union and have applied for registration under Regulation (EU) No 1060/2009, although notification of the corresponding registration decision has not yet been provided by the relevant competent authority. In general, European regulated investors are restricted from using a rating for regulatory purposes if such rating is not issued by a credit rating agency established in the European Union and registered under the Regulation (EU) No 1060/2009 ("**CRA Regulation**") unless the rating is provided by a credit rating agency operating in the European Union before 7 June 2010 which has submitted an application for registration in accordance with the CRA Regulation and such registration is not refused.

The Notes have not been and will not be registered under the United States 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 may not be offered, sold or delivered within the United States or to, or for the account or benefit of, U.S. persons 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. Accordingly, the Notes are being offered, sold or delivered: (a) in the United States only to qualified institutional buyers ("QIBs") (as defined in Rule 144A ("Rule 144A") under the Securities Act) in reliance on, and in compliance with, Rule 144A; and (b) to Persons (other than U.S. Persons) (each as defined in Regulation S) outside the United States in reliance on Regulation S ("Regulation S") under the Securities Act. Each purchaser of the Notes will be deemed to have made the representations described in "*Subscription and Sale*" and is hereby notified that the offer and sale of Notes to it is being made in reliance on the exemption from the registration requirements of the Securities Act provided by Rule 144A. In addition, until 40 days after the commencement of the offering, an offer or sale of any of the Notes within the United States by any dealer (whether or not participating in the offering) may violate the registration requirements of the Securities Act if the offer or sale is made otherwise than in accordance with Rule 144A.

The Notes will initially be represented by two global certificates in registered form (the "**Global Certificates**"), one of which will be issued in respect of the Notes offered and sold in reliance on Rule 144A (the "**Restricted Global Certificate**") and will be registered in the name of Cede & Co., as nominee for The Depository Trust Company ("**DTC**") and the other of which will be issued in respect of the Notes offered and sold in reliance on Regulation S (the "**Unrestricted Global Certificate**") and will be registered in the name of a nominee of a common depositary for Euroclear Bank SA/NV ("**Euroclear**") and Clearstream Banking, société anonyme ("**Clearstream, Luxembourg**"). It is expected that delivery of the Global Certificates will be made on 16 June 2011 or such later date as may be agreed (the "**Closing Date**") by the Republic and the Joint Lead Managers (as defined under "*Subscription and Sale*").

JOINT LEAD MANAGERS

CITI **CREDIT SUISSE**

CO-MANAGERS

SEB **SWEDBANK**

13 June 2011

The Republic has confirmed to the Managers named under "*Subscription and Sale*" that all information regarding the Republic and the Notes contained in this Offering Circular is true and accurate in all material respects and is not misleading in any material respect; this Offering Circular does not omit to state any material fact necessary to make such information not misleading in any material respect; and all proper enquiries have been made to ascertain and to verify the foregoing. The Republic accepts responsibility for the information contained in this document accordingly.

The Republic has not authorised the making or provision of any representation or information regarding the Republic or the Notes other than as contained in this Offering Circular or as approved for such purpose by the Republic. Any such representation or information should not be relied upon as having been authorised by the Republic or the Managers.

Neither the delivery of this Offering Circular or the offering, sale or delivery of any Note shall in any circumstances create any implication that there has been no adverse change, or any event reasonably likely to involve any adverse change, in the condition (financial, economic or otherwise) of the Republic since the date of this Offering Circular.

This Offering Circular does not constitute an offer of, or an invitation to subscribe for or purchase, any Notes. Each investor contemplating purchasing any Notes should make its own independent investigation of the financial condition and affairs, and its own appraisal of the creditworthiness, of the Republic.

The distribution of this Offering Circular and the offering, sale and delivery of Notes in certain jurisdictions may be restricted by law. Persons into whose possession this Offering Circular comes are required by the Republic and the Managers to inform themselves about and to observe any such restrictions. For a description of certain restrictions on offers, sales and deliveries of Notes and on distribution of this Offering Circular and other offering material relating to the Notes, see "*Subscription and Sale*".

In this Offering Circular, unless otherwise specified, references to "**U.S.$**", "**U.S. dollars**" and "**dollars**" are to the lawful currency for the time being of the United States of America, references to "**LVL**", "**Lats**" and "**Ls**" are to the lawful currency for the time being of the Republic of Latvia and references to "**Euro**", "**euro**" and "**€**" are to the single currency introduced at the start of the third stage of European economic and monetary union, and as defined in Article 2 of Council Regulation (EC) No. 974/98 of 3 May 1998 on the introduction of the euro, as amended. Translations of amounts from Lats to U.S. dollars are solely for the convenience of the reader and, unless otherwise stated, are made at year end exchange rates. No representation is made that Lats or dollar amounts referred to herein could have been or could be converted into dollars or Lats, as the case may be, at any particular rate at all. The Bank of Latvia's foreign exchange rate for U.S. dollars on 27 May 2011 was LVL 0.496 = U.S.$1.00, whilst the Bank of Latvia's foreign exchange rate for Euro since 1 January 2005 has been fixed at LVL 0.702804 = €1.00.

Unless otherwise stated, all annual information, including budgetary information, is based on calendar years. Government budget execution is compiled on a cash flow basis. Statistical data appearing in this Offering Circular has, unless otherwise stated, been obtained from the Central Statistical Bureau of Latvia (the "**Central Statistical Bureau**"), the Ministry of Finance, the Bank of Latvia, the Financial and Capital Market Commission and the Treasury. Similar statistics may be obtainable from other sources, although the underlying assumptions and methodology, and consequently the resulting data, may vary from source to source. Certain statistical information relating to 2011 should be treated as preliminary and statistical information for this and prior years may be subject to future adjustment.

Certain figures including in this Offering Circular have been subject to rounding adjustments; accordingly, figures shown for the same category presented in different tables may vary slightly and figures shown as totals in certain tables may not be an arithmetic aggregation of the figures which precede them.

In connection with the issue of Notes, Credit Suisse Securities (Europe) Limited (the "Stabilising Manager") (or persons acting on behalf of any Stabilising Manager) may over allot Notes or effect transactions with a view to supporting the price of the Notes at a level higher than that which might otherwise prevail. However, there is no assurance that the Stabilising Manager (or persons acting on behalf of a Stabilising Manager) will undertake stabilisation action. Any stabilisation action may begin on or after the date on which adequate public disclosure of the terms of the offer of the Notes is made and, if begun, may be ended at any time, but it must end no later than the earlier of 30 days after the issue date of the Notes and 60 days after the date of the allotment of the Notes. Any stabilisation action

or over-allotment must be conducted by the Stabilising Manager (or person(s) acting on behalf of any Stabilising Manager) in accordance with all applicable laws and rules.

The Notes have not been approved or disapproved by the United States Securities and Exchange Commission or any other securities commission or other regulatory authority in the United States, nor have the foregoing authorities reviewed or passed upon the accuracy or adequacy of this Offering Circular. Any representation to the contrary is a criminal offence.

This Offering Circular is being submitted on a confidential basis in the United States to a limited number of QIBs for informational use solely in connection with the consideration of the purchase of the Notes. It may not be copied or reproduced in whole or in part nor may it be distributed or any of its contents disclosed to anyone other than the prospective investors to whom it is originally submitted.

Each purchaser or holder of interests in the Notes will be deemed, by its acceptance or purchase of any such Notes, to have made certain representations and agreements as set out in "*Subscription and Sale*".

NOTICE TO NEW HAMPSHIRE RESIDENTS

NEITHER THE FACT THAT A REGISTRATION STATEMENT OR AN APPLICATION FOR A LICENSE HAS BEEN FILED UNDER CHAPTER 421-B OF THE NEW HAMPSHIRE REVISED STATUTES WITH THE STATE OF NEW HAMPSHIRE NOR THE FACT THAT A SECURITY IS EFFECTIVELY REGISTERED OR A PERSON IS LICENSED IN THE STATE OF NEW HAMPSHIRE CONSTITUTES A FINDING BY THE SECRETARY OF STATE OF NEW HAMPSHIRE THAT ANY DOCUMENT FILED UNDER CHAPTER 421-B IS TRUE, COMPLETE AND NOT MISLEADING. NEITHER ANY SUCH FACT NOR THE FACT THAT AN EXEMPTION OR EXCEPTION IS AVAILABLE FOR A SECURITY OR A TRANSACTION MEANS THAT THE SECRETARY OF STATE HAS PASSED IN ANY WAY UPON THE MERITS OR QUALIFICATIONS OF, OR RECOMMENDED OR GIVEN APPROVAL TO, ANY PERSON, SECURITY OR TRANSACTION. IT IS UNLAWFUL TO MAKE, OR CAUSE TO BE MADE, TO ANY PROSPECTIVE PURCHASER, CUSTOMER OR CLIENT ANY REPRESENTATION INCONSISTENT WITH THE PROVISIONS OF THIS PARAGRAPH.

CAUTIONARY STATEMENT REGARDING FORWARD-LOOKING STATEMENTS

Some of the statements contained in this Offering Circular, as well as written and oral statements that Republic and its representatives make from time to time in reports, filings, news releases, conferences, teleconferences, web postings or otherwise, are or may be deemed to be forward-looking statements. Statements that are not historical facts, including, without limitation, statements about the Republic's beliefs and expectations, are forward-looking statements. These statements are based on current plans, objectives, assumptions, estimates and projections. When used in this Offering Circular, the words "anticipates", "estimates", "expects", "believes", "intends", "plans", "aims", "seeks", "may", "will", "should" and any similar expressions generally identify forward-looking statements. Therefore, undue reliance should not be placed on them. The Republic has based these forward-looking statements on its current view with respect to future events and financial results.

Forward-looking statements speak only as of the date on which they are made and the Republic undertakes no obligation to update publicly any of them in light of new information or future events. Forward-looking statements involve inherent risks and uncertainties. the Republic cautions that a number of important factors could cause actual results to differ materially from those contained in any forward-looking statement. Forward-looking statements include, but are not limited to: (i) plans with respect to the implementation of economic policy, including privatisations, and the pace of economic and legal reforms; (ii) expectations about the behaviour of the economy if certain economic policies are implemented; (iii) the outlook for gross domestic product, inflation, exchange rates, interest rates, foreign investment, trade and fiscal accounts; and (iv) estimates of external debt repayment and debt service.

CONTENTS

SUMMARY

This Summary does not purport to be complete and must be read as an introduction to this Offering Circular and any decision to invest in the Notes should be based on a consideration of this Offering Circular as a whole.

Words and expressions defined in "*Terms and Conditions of the Notes*" shall have the same meanings in this Summary.

THE REPUBLIC OF LATVIA

Geography and Population

Latvia is located in the Baltic region of northern Europe and is bordered by Estonia to the north, Russia to the east, Lithuania to the south and Belarus to the south-east. The western border of the country is the Baltic Sea, along which the country has a 498 kilometre ("**km**") coastline. Latvia is divided into four historical districts: Kurzeme (western Latvia), Zemgale (southern Latvia), Vidzeme (northern Latvia) and Latgale (eastern Latvia). Latvia covers an area of approximately 64,559 square kilometres. The capital city is Riga.

Government Structure

In accordance with the Constitution of the Republic of Latvia (the "**Constitution**"), the Saeima is the highest legislative body. The Saeima is a unicameral parliament consisting of 100 members, elected in general, equal, direct, secret and proportional elections for a four-year term. All Latvian citizens who are 18 years of age and over are entitled to vote. The next Saeima elections will be held in October 2014.

The Saeima is entitled to elect, appoint, approve or dismiss a range of state officials and also elects the president of Latvia (the "**President**") for a term of four years. The current President is Valdis Zatlers who will be in office until 7 July 2011. On 2 June 2011, Andris Bērziņš was elected as the new President and will assume office on 8 July 2011.

International Relations

Latvia became a member state of the United Nations ("**UN**") in 1991, of the International Monetary Fund (the "**IMF**") in 1992, of the World Trade Organization (the "**WTO**") in 1998 and of the European Union (the "**EU**") and the North Atlantic Treaty Organization ("**NATO**") in 2004. Latvia's relations with Russia are based on pragmatic foundations and co-operation and Latvia regards the United States of America as a strategic partner and ally.

GDP

During 2006 and 2007, Latvia experienced rapid growth with real GDP growing by 12.2 per cent. in 2006 and 10.0 per cent. in 2007. These growth rates were principally driven by private consumption and investment, which was largely based on a substantial inflow of foreign capital. In 2008 and 2009, Latvia's economy was significantly adversely affected by the global economic crisis which commenced at the end of 2007, with real GDP falling by 4.2 per cent. in 2008 and by 18.0 per cent. in 2009.

Since 2009, Latvia's economy has begun to recover, with real GDP growing in each quarter since the last quarter of 2009, although on an annual basis and reflecting the steep decline in 2009 Latvia's real GDP for 2010 was 0.3 per cent. lower than it was for 2009. Latvia's real GDP grew by 0.3 per cent. in the first quarter of 2011 compared to the fourth quarter of 2010.

Inflation

Inflation (measured in terms of changes in the consumer price index) fell from a peak of 17.9 per cent. in May 2008 to a low of minus 4.2 per cent. in February 2009 (in each case when compared with the corresponding period of the previous year). The decrease in consumer prices principally reflected reduced private consumption (as a result of increased unemployment, wage reductions and other factors) and falling global energy and food prices. Since the end of 2009, inflation has increased gradually as a result of increasing world energy and food prices and domestic indirect tax rate increases and was 4.5 per cent. in April 2011.

Financial Assistance

Deteriorating economic conditions in Latvia in 2008 and a banking crisis at the end of that year significantly adversely affected State budget revenues and, as a result, Latvia sought financial assistance from the IMF and other international bodies towards the end of 2008. As at 30 April 2011, €4.4 billion in financial assistance (out of a total agreed package of €7.5 billion) had been disbursed to Latvia. No further borrowings within the programme are planned in 2011, except that a €100 million loan from the International Bank for Reconstruction and Development (the "**World Bank**") may be drawn.

On 25 May 2011, the Executive Board of the IMF completed its fourth review of Latvia's performance in connection with the provision of the financial assistance package and confirmed that funds would continue to made available to Latvia under the package. On 7 June 2011, the EU and Latvia entered into a supplemental memorandum of understanding in relation to the financial assistance provided by the EU and following completion of its fourth review of Latvia's performance in connection with the provision of the financial assistance package. The EU also confirmed that funds would continue to be made available to Latvia under the package.

Issuer:	The Republic of Latvia, acting through the Treasury
Risk Factors:	There are certain factors that may affect the issuer's ability to fulfil its obligations under the Notes. These are set out under "*Risk Factors*" below and include, among other risks, certain potential factors which could adversely affect Latvia's economy and banking sector in the future and risks relating to the strength and sustainability of Latvia's economic recovery. In addition, there are certain factors which are material for the purpose of assessing the market risks associated with the Notes. These are set out under "*Risk Factors*" and include the fact that the Notes may not be a suitable investment for all investors.
Description of Notes:	U.S.$500,000,000 5.25 per cent. Notes due 2021, to be issued by the Republic on the Issue Date.
Joint Lead Managers:	Citigroup Global Markets Limited Credit Suisse Securities (Europe) Limited
Co-Managers:	Skandinaviska Enskilda Banken AB (publ) Swedbank AB (publ)
Interest:	5.25 per cent. per annum payable semi-annually in arrear on 16 June and 16 December in each year.
Events of Default:	Events of default under the Notes include the non-payment of any interest due in respect of the notes or any of them for a period of 14 days from the due date for payment thereof, breach of other obligations under the Notes (which breach is not remedied within 30 days) and certain events related to the Republic. Notes may only be declared due and payable, upon an Event of Default, if holders of at least 25 per cent. in aggregate principal amount of the outstanding Notes give notice in writing to the Republic. Furthermore if the Republic receives notice in writing from holders of at least 50 per cent. in aggregate principal amount of the outstanding Notes to the effect that the event of default giving rise to a declaration of acceleration is cured and that such holders wish the relevant declaration to be withdrawn, the relevant declaration shall be withdrawn and shall have no further effect.
Negative Pledge:	The terms of the Notes contain a negative pledge provision given by the Republic in respect of Public External Indebtedness as described in Condition 4 (*Negative Pledge*).
Status of the Notes:	The Notes will constitute direct, general, (subject to the provisions of Condition 3 (*Status*)) unsecured and unconditional obligations of the Republic and will rank *pari passu* and without any preference

	among themselves and at least (save for certain obligations required to be preferred by law) equally with all other present and future unsecured obligations of the Republic.
Meetings of Noteholders:	The Conditions of the Notes contain provisions for calling meetings of Noteholders to consider matters affecting their interests generally (see Condition 13 (*Meetings of Noteholders; Written Resolutions*)). These provisions permit defined majorities to bind all Noteholders including Noteholders who did not attend and vote at the relevant meeting and Noteholders who voted in a manner contrary to the majority. The Conditions also contain provisions for the appointment of a Noteholders' representative committee (see Condition 14 (*Noteholders' Representative Committee*)).
Modification:	The Conditions of the Notes contain a provision permitting the Notes and the Conditions of the Notes to be amended without the consent of the Noteholders to correct a manifest error.
Taxation:	All payments in respect of the Notes by or on behalf of the Republic shall be made without withholding or deduction for, or on account of any Taxes as provided in Condition 8 (*Taxation*).
Listing and admission to trading:	Application has been made to list the Notes on the Official List of the Luxembourg Stock Exchange and to admit the Notes to trading on the Luxembourg Stock Exchange's regulated market.
Governing Law:	The Notes and any non-contractual obligations arising out of or in connection with the Notes are governed by and shall be construed in accordance with, English law, provided, however, that the due authorisation and execution of the Notes by and on behalf of the Republic shall be governed by the laws of the Republic.
Form and Denomination:	The Notes will be issued in registered form in denominations of U.S.$200,000 and integral multiples of U.S.$1,000 in excess thereof.
Credit Ratings:	The Notes are expected to be assigned on issue a rating of BBB- by Fitch Ratings Limited, Baa3 by Moody's Investors Service, Inc. and BB+ by Standard & Poor's Rating Services, a division of The McGraw-Hill Companies, Inc. Fitch, Moody's and S&P are established in the European Union and have applied for registration under the CRA Regulation (EU) No 1060/2009, although notification of the corresponding registration decision has not yet been provided by the relevant competent authority. A credit rating is not a recommendation to buy, sell or hold securities and may be subject to revision, suspension or withdrawal at any time by the assigning rating organisation.
Selling Restrictions:	The Notes have not been and will not be registered under the Securities Act and are subject to certain restrictions on transfers. See "*Subscription and Sale*" below.
Use of Proceeds:	The net proceeds of the issue of the Notes will be applied by the Republic for the refinancing of indebtedness and general budgetary purposes of the Republic.

RISK FACTORS

Investment in the Notes involves risk. Prospective investors should carefully consider the following risk factors, together with the other information set out in this Offering Circular, before making a decision to invest in the Notes and should understand that the risks set forth below could, individually or in the aggregate, have a material adverse effect on Latvia's capacity to repay principal and make payments of interest on the Notes or otherwise fulfil its obligations under the Notes. Most of these factors are contingencies which may or may not occur and the Republic is not in a position to express a view on the likelihood of any such contingency occurring. Additional risks and uncertainties not currently known to the Republic or that the Republic currently deems to be immaterial may also materially affect the Republic's economy and its ability to fulfil its obligations under the Notes. In any such case, investors may lose all or part of their investment in the Notes. Words and expressions defined in "Terms and Conditions of the Notes" or elsewhere in this Offering Circular have the same meanings in this section.

Risk Factors Relating to Latvia

Latvia's economy and banking sector were significantly adversely affected by the global financial crisis and any similar future global economic downturns, or difficulties experienced by its major regional trading partners or by more general "contagion" effects, could have a material adverse effect on Latvia's economic growth and banking sector

Latvia experienced adverse economic and financial effects as a result of the global financial crisis. For example, Latvia's nominal gross domestic product ("**GDP**") declined by 18.0 per cent. in real terms in 2009 compared to 2008 and by 0.3 per cent. in 2010 compared to 2009. Although certain sectors of the economy have recovered, including manufacturing (which increased by 15.4 per cent. primarily due to exports to recovering EU countries), others including, in particular, construction (which decreased by 24.2 per cent. in 2010) and public services (which decreased by 7.8 per cent. in 2010 due to government spending cuts), have not. Austerity measures taken in response to the recession have slowed growth in domestic consumption, which is reflected in the 1.4 per cent. decline in services in 2010 compared to 2009. The downturn has caused the registered unemployment rate in Latvia to increase from 7.0 per cent. at 31 December 2008 to 16.0 per cent. at 31 December 2009 and although this decreased in 2010, to 14.3 per cent. at 31 December 2010, the registered unemployment rate remains well above the pre-recession level. Latvia also recorded consolidated general government budget deficits of 3.3 per cent. of nominal GDP in 2008, 6.8 per cent. in 2009 and 6.3 per cent. in 2010. The consolidated general government budget deficit is currently budgeted to be around 4.1 per cent. of assumed nominal GDP for 2011. See "*Public Finance – Consolidated General Government Budget*".

In addition, Latvia's banking sector was significantly adversely affected by the global financial crisis. Parex Bank, the largest Latvian-owned bank, was nationalised in November 2008 and subsequently restructured into Citadele Banka during 2010 with the troubled assets remaining in the former Parex Bank. The recession in Latvia also adversely affected the financial position of both corporate and retail borrowers resulting in a deterioration of loan quality and an increase in provisions in Latvian banks, with the share of non-performing Latvian bank loans (being loans with payments overdue more than 90 days) ("**NPLs**") in the total Latvian bank loan portfolio being 16.4 per cent. and 19.0 per cent., respectively, at 31 December 2009 and 2010, compared to 3.6 per cent. at 31 December 2008. Reflecting adverse economic conditions, the total amount of bank loans outstanding fell by 7.0 per cent. during 2009 and by 7.1 per cent. in 2010.

Instability in the financial markets and the recession in Latvia also adversely affected the profits of Latvian banks. The profit of the Latvian banking sector for the years ended 31 December 2006, 2007 and 2008 was LVL 265.9 million, LVL 371.3 million and LVL 60.1 million, respectively. In 2009 and 2010, the losses of the Latvian bank sector were LVL 773.4 million and LVL 360.7 million, respectively. These losses mainly reflected increased provisions for loan losses.

Latvia's economy and banking sector may be vulnerable to further significant external shocks. As noted above, the recovery of several of Latvia's trading partners contributed significantly to certain sectors of the economy that exhibited growth in 2010. A significant decline in the economic growth of any of Latvia's major trading partners, such as the EU countries and the Russian Federation, could, among other effects, have a material adverse impact on Latvia's balance of trade and adversely affect Latvia's economic growth and its banking sector.

In addition, because international investors' reactions to the events occurring in one market sometimes appear to demonstrate a "contagion" effect, in which an entire region or class of investment ceases to be favoured by international investors, Latvia could be adversely affected by negative economic or financial developments in neighbouring countries (including, among others, Lithuania and Estonia). Latvia has been adversely affected by such contagion effects on a number of occasions, including following the 1998 Russian financial crisis and the global financial crisis. Similar developments can be expected to affect the Latvian economy and banking sector in the future.

There can be no assurance that any crises such as those described above or similar events will not negatively affect investor confidence in markets such as Latvia. In addition, there can be no assurance that these events will not adversely affect Latvia's economy, its banking sector or its ability to raise capital in the external debt markets in the future. See "*Cautionary Statement Regarding Forward-Looking Statements*" in this Offering Circular.

Although Latvia's economy has emerged from recession, no assurance can be given as to the strength of the recovery or that it will be sustained

Latvia's economy has emerged from recession, having grown on a quarterly basis since the last quarter of 2009. The quarterly growth rates remain low and, reflecting the depth of the recession in 2009, real GDP for 2010 was still 0.3 per cent. lower than that for 2009. A significant contributor to Latvia's emergence from recession has been the economic reforms implemented, including those required under the conditions of the financial assistance package (the "**financial assistance package**") agreed with the EU, the IMF, the World Bank , the European Bank for Reconstruction and Development (the "**EBRD**") and a number of Nordic and other EU countries. The principal aims of this economic reform programme were to arrest the liquidity crisis prevailing in late 2008, to stabilise the financial sector and to make structural adjustments with a view to ensuring economic recovery, while maintaining the exchange rate peg. As at 30 April 2011, €4.4 billion in financial assistance had been disbursed to Latvia. Although (excluding the Loan Agreement with the Nordic countries which remains undrawn) €1.2 billion remains available under the programme funds, no further borrowings within the programme are planned in 2011, except that the remaining €100 million of the loan from the World Bank may be drawn. To date, the economic policy criteria set out as conditions to the disbursement of funds under the financial assistance package have been sufficiently achieved to permit all disbursements requested by Latvia. Except as described above, Latvia does not expect to make further drawings and is now reorienting its borrowing strategy towards market funding. This does not, however, affect Latvia's commitment to comply with any further criteria to be achieved under the financial assistance package.

Notwithstanding these achievements, a number of risks remain, including:

- *Political factors*: the political landscape in Latvia has historically been fragmented, with multiple parties represented in parliament, and collaborations among different parties required in order to form a governing coalition. The governing coalition can change, and has also changed, in between elections. There were three separate governing coalitions between the prior two elections in October 2006 and October 2010. The current coalition remained intact before and after the October 2010 general election and has been in place since 3 November 2010. However, on 28 May 2011, the then President, in accordance with Article 48 of the Latvian Constitution, announced a proposal for a referendum on the dissolution of the tenth Saeima which will be held on 23 July 2011. If the referendum results in a decision to dissolve the current Saeima, then a new general election will be required. The dissolution, referendum and possible general election create political uncertainty and may exert pressure on the current coalition. Any significant change in, or in the policies of, the current administration might cause a shift in economic policy or a reversal (in whole or in part) of the economic and other reform measures undertaken to mitigate the impact of the global financial crisis on Latvia's economy or might lead to Latvia not achieving the remaining targets included in the financial assistance package, either of which could give rise to a decrease in the confidence of external lenders in the Latvian economy and/or the administration;

- *Internal economic factors*: decreasing disposable income and reduced confidence levels among individuals could lead to reduced spending by them which in turn could negatively influence economic performance and structural reforms which have been, or may in the future be, implemented could prove to be less efficient than anticipated;

- *External factors*: external factors such as a failure of the economies of Latvia's main trading partners to return to, or to sustain, growth as anticipated or other global financial shocks or significant commodity price movements could adversely affect Latvia's economy; and

- *Growth in shadow economy*: higher tax rates may increase the share of the shadow economy in the total economy of Latvia and exert pressure on public finances.

The occurrence of any one or more of these factors could adversely affect the Latvian economy, increase Latvia's cost of funding in the capital markets and affect Latvia's capacity to repay principal and make payments of interest on the Notes.

Any depreciation of the lat could adversely affect Latvia's economy

Latvia's central government debt at 30 April 2011 amounted to LVL 4,950.4 million, equal to 36.9 per cent. of assumed nominal GDP for 2011, of which LVL 4,066.7 million (or 82.1 per cent.) was denominated in foreign currencies, principally the euro, see "*Indebtedness*". As a result, Latvia is vulnerable to currency risk. Since 2005, the lat has been pegged to the euro and maintaining the peg has been a key governmental policy, including throughout the global financial crisis when it came under sustained market pressure to devalue, as well as a condition in the financial assistance package Latvia obtained in 2008. Thus Latvia considers a devaluation of the lat (whether pursuant to a "re-pegging" or otherwise) to be unlikely. Nevertheless, in the event of a significant devaluation of the lat, the negative impact on Latvia's service obligations in respect of its central government debt denominated in foreign currencies could be significant and would not be significantly offset by the positive impact on its service obligations in respect of central government debt denominated in Lats. Any significant devaluation of the lat may have an adverse effect on the Republic's ability to repay its central government debt denominated in foreign currencies, including the amounts due under the Notes.

In addition, at 31 December 2010 approximately LVL 11.4 billion of private sector credit and approximately LVL 2.5 billion of private sector deposits were foreign currency-denominated. Any devaluation of the lat against foreign currencies would also therefore be likely to affect negatively the capacity of private sector borrowers to repay their debt and, as a result, adversely affect the financial and economic condition of Latvia.

Further, a devaluation of the lat would not necessarily have a material positive effect on Latvia's current account, as a significant portion of the value of goods and services exported by Latvia reflects the cost of raw materials imported by Latvia which are denominated in other currencies, primarily the euro. Consequently, a devaluation may not result in a significant decrease in the costs of Latvia's exports.

Any deterioration in Latvia's relations with its major energy suppliers may adversely affect the supply of energy resources and therefore have a negative effect on the Latvian economy

In 2009, Latvia was 35.9 per cent. self-sufficient in its energy requirements. As a result, Latvia imports a large percentage of its energy requirements, including all of its natural gas requirements, from Russia. Any significant increases in the prices of its major energy imports or adverse changes in relations with its major energy suppliers could have an adverse effect on certain sectors of Latvia's economy.

Official economic data may not be directly comparable with data produced by other sources

Although a range of government ministries, including the Ministry of Finance, along with the Bank of Latvia and the Central Statistical Bureau, produce statistics on Latvia and its economy, there can be no assurance that these statistics are comparable with those compiled by other bodies, or in other countries, which use different methodologies. Prospective investors in the Notes should be aware that figures relating to Latvia's GDP and many other aggregate figures cited in this Offering Circular have been prepared in accordance with EU standards and may differ from figures prepared by international bodies, such as the IMF, which use a different methodology. The existence of an unofficial or unobserved economy may affect the accuracy and reliability of statistical information. Prospective investors should be aware that none of the statistical information in this Offering Circular has been independently verified.

Risk Factors Relating to an Investment in the Notes

The Notes may not be a suitable investment for all investors

Each potential investor in the Notes must determine the suitability of that investment in light of its own circumstances. In particular, each potential investor should:

- have sufficient knowledge and experience to make a meaningful evaluation of the Notes, the merits and risks of investing in the Notes and the information contained in this Offering Circular;
- have access to, and knowledge of, appropriate analytical tools to evaluate, in the context of its particular financial situation, an investment in the Notes and the impact the Notes will have on its overall investment portfolio;
- have sufficient financial resources and liquidity to bear all of the risks of an investment in the Notes, including where the currency for principal or interest payments is different from the potential investor's currency;
- understand thoroughly the terms of the Notes and be familiar with the behaviour of any relevant financial markets; and
- be able to evaluate (either alone or with the help of a financial adviser) possible scenarios for economic, interest rate and other factors that may affect its investment and its ability to bear the applicable risks.

The conditions of the Notes may be modified, waived or substituted without the consent of all the Noteholders

The conditions of the Notes contain provisions for calling meetings of Noteholders to consider matters affecting their interests generally and for the passing of written resolutions of Noteholders without the need for a meeting. These provisions permit defined majorities to bind all Noteholders including Noteholders who did not attend and vote at the relevant meeting or sign the relevant written resolution and Noteholders who voted in a manner contrary to the majority. Any such change in the conditions of the Notes may adversely affect the trading price of the Notes.

The conditions of the Notes contain a provision permitting the Notes and the conditions of the Notes to be amended without the consent of the Noteholders to correct a manifest error or where the amendment is of a formal, minor or technical nature or is not materially prejudicial to the interests of the Noteholders.

The conditions of the Notes restrict the ability of an individual holder to declare a default and permit a majority of holders to rescind a declaration of default

The conditions of the Notes contain a provision which, if an Event of Default occurs, allows the holders of at least 25 per cent. in aggregate principal amount of the outstanding Notes to declare all the Notes to be immediately due and payable by providing notice in writing to the Republic, whereupon the Notes shall become immediately due and payable, at their principal amount with accrued interest, without further action or formality.

The conditions of the Notes also contain a provision permitting the holders of at least 50 per cent. in aggregate principal amount of the outstanding Notes to notify the Republic to the effect that the Event of Default or Events of Default giving rise to any above-mentioned declaration is or are cured following any such declaration and that such holders wish the relevant declaration to be withdrawn. The Republic shall give notice thereof to the Noteholders, whereupon the relevant declaration shall be withdrawn and shall have no further effect.

The EU Savings Directive may result in certain holders not receiving the full amount of interest

Under EC Council Directive 2003/48/EC (the "**EU Savings Directive**") on the taxation of savings income, each Member State is required to provide to the tax authorities of another Member State details of payments of interest or other similar income (within the meaning of the EU Savings Directive) paid by a paying agent in the meaning of the EU Savings Directive within its jurisdiction to, or collected by such a paying agent for, an individual resident or certain limited types of entity established in that other Member State; however, for a transitional period, Austria and Luxembourg may instead apply a withholding system in relation to such payments, deducting tax at rates rising over time to 35 per cent., unless in the case of Luxembourg the beneficial owner of the interest payments opts for one of the two information exchange procedures available. The transitional period is to terminate at the end of the first full fiscal year following agreement by certain non-EU countries to the exchange of information relating to such payments.

A number of non-EU countries and certain dependent or associated territories of certain Member States, have adopted similar measures (either provision of information or transitional withholding) in relation to payments made by a paying agent within its jurisdiction to, or collected by such a paying agent for, an individual resident in a Member State. In addition, the Member States have entered into provision of information or transitional withholding arrangements with certain of those dependent or associated territories in relation to payments made by a person in a Member State to, or collected by such a person for, an individual resident or certain limited types of entity established in one of those territories.

The European Commission has proposed certain amendments to the EU Savings Directive, which may, if implemented, amend or broaden the scope of the requirements described above. Investors who are in any doubt as to their position should consult their professional advisers.

If a payment were to be made or collected through a Member State which has opted for a withholding system and an amount of, or in respect of, tax were to be withheld from that payment, neither the Republic nor any Paying Agent nor any other person would be obliged to pay additional amounts with respect to any Note as a result of the imposition of such withholding tax. The Republic is required to maintain a Paying Agent in a Member State that is not obliged to withhold or deduct tax pursuant to the EU Savings Directive.

The law governing the conditions of the Notes may change

The conditions of the Notes are based on English law in effect as at the date of this Offering Circular. No assurance can be given as to the impact of any possible judicial decision or change to English law or administrative practice after the date of this Offering Circular.

There may be no active trading market for the Notes

Although an application has been made to list on the Official List of the Luxembourg Stock Exchange and to trade the Notes on the Luxembourg Stock Exchange's regulated market, there is no assurance that such application will be accepted or that an active trading market for the Notes will develop or, if one does develop, that it will be liquid or maintained. If an active trading market in the Notes does not develop or is not maintained, the market price and liquidity of the Notes may be adversely affected.

The market for securities issued by the Republic is influenced by economic and market conditions in Latvia and, to a varying degree, economic conditions in other Eastern European markets as well as global, emerging and developed markets generally. There can be no assurance that events which would cause volatility of the sort that occurred in worldwide financial markets in 1998 and 2008 will not occur again, or that any such volatility will not adversely affect the price or liquidity of the Notes.

In addition, if the Notes are traded after their initial issuance, they may trade at a discount to their initial offering price, depending upon prevailing interest rates, the market for similar securities, general economic conditions and the financial condition of the Republic. As a result of the above factors, investors may not be able to sell their Notes easily or at prices that will provide them with a yield comparable to similar investments that have a developed secondary market.

A claimant may not be able to enforce a court judgment against certain assets of the Republic in certain jurisdictions

Latvia is a sovereign state. Consequently, it may be difficult for investors to obtain judgments of courts in countries outside Latvia against the Republic. Enforcement of such judgments in Latvia may be refused in certain circumstances in the absence of an applicable treaty facilitating such enforcement. There is also a risk that, notwithstanding the waiver of sovereign immunity by the Republic, a claimant will not be able to enforce a court judgment against certain assets of the Republic in certain jurisdictions (including the imposition of any arrest order or attachment or seizure of such assets and their subsequent sale) without the Republic having specifically consented to such enforcement at the time when the enforcement is sought.

The foreign exchange reserves of Latvia are controlled and administered by the Bank of Latvia, which is an independent central bank legally distinct from the government. Accordingly, such reserves would not be available to satisfy any claim or judgment in respect of the Notes.

Fluctuations in exchange rates and interest rates may adversely affect the value of the Notes

The Republic will pay principal and interest on the Notes in U.S. dollars. This presents certain risks relating to currency conversions if an investor's financial activities are denominated principally in a currency or currency unit (the "**Investor's Currency**") other than U.S. dollars. These include the risk that exchange rates may significantly change (including changes due to devaluation of the U.S. dollar or revaluation of the Investor's Currency) and the risk that authorities with jurisdiction over the

Investor's Currency may impose or modify exchange controls. An appreciation in the value of the Investor's Currency relative to the U.S. dollar would decrease (1) the Investor's Currency-equivalent yield on the Notes, (2) the Investor's Currency-equivalent value of the principal payable on the Notes and (3) the Investor's Currency-equivalent market value of the Notes.

Government and monetary authorities may impose (as some have done in the past) exchange controls that could adversely affect an applicable exchange rate. As a result, investors may receive less interest or principal than expected, or no interest or principal. In addition, investment in the Notes involves the risk that subsequent changes in market interest rates may adversely affect the value of the Notes.

Legal investment considerations may restrict certain investments

The investment activities of certain investors are subject to legal investment laws and regulations, or review or regulation by certain authorities. Each potential investor should consult its legal advisers to determine whether and to what extent (1) the Notes are legal investments for it, (2) the Notes can be used as collateral for various types of borrowing and (3) other restrictions apply to its purchase or pledge of the Notes. Financial institutions should consult their legal advisers or the appropriate regulators to determine the appropriate treatment of the Notes under any applicable risk-based capital or similar rules.

Credit ratings may not reflect all risks

Moody's, Standard & Poor's and Fitch have assigned credit ratings to the Notes. The ratings may not reflect the potential impact of all risks related to structure, market, additional factors discussed above, and other factors that may affect the value of the Notes. A credit rating is not a recommendation to buy, sell or hold securities and may be revised or withdrawn by the rating agency at any time.

In general, European regulated investors are restricted under the CRA Regulation from using credit ratings for regulatory purposes, unless such ratings are issued by a credit rating agency established in the EU and registered under the CRA Regulation (and such registration has not been withdrawn or suspended), subject to transitional provisions that apply in certain circumstances whilst the registration application is pending. Such general restriction will also apply in the case of credit ratings issued by non-EU credit rating agencies, unless the relevant credit ratings are endorsed by an EU-registered credit rating agency or the relevant non-EU rating agency is certified in accordance with the CRA Regulation (and such endorsement action or certification, as the case may be, has not been withdrawn or suspended).

TERMS AND CONDITIONS OF THE NOTES

The following is the text of the Terms and Conditions of the Notes which (subject to completion and amendment) will be endorsed on the Certificates issued in respect of the Notes:

The U.S.$500,000,000 5.25 per cent. Notes due 2021 (the "**Notes**", which expressions includes any further notes issued pursuant to Condition 15 (*Further Issues*) and forming a single series therewith) of the Republic of Latvia, acting through the Treasury (the "**Republic**") are the subject of a fiscal agency agreement dated 16 June 2011 (as amended or supplemented from time to time, the "**Fiscal Agency Agreement**") between the Republic, Citibank, N.A., London Branch as fiscal agent (the "**Fiscal Agent**", which expression includes any successor fiscal agent appointed from time to time in connection with the Notes) and the paying agents named therein (together with the Fiscal Agent, the "**Paying Agents**", which expression includes any successor or additional paying agents appointed from time to time in connection with the Notes). Certain provisions of these Conditions are summaries of the Fiscal Agency Agreement and subject to its detailed provisions. The holders of the Notes (the "**Noteholders**") are entitled to the benefit of a deed of covenant dated 16 June 2011 (the "**Deed of Covenant**") and made by the Republic. The original of the Deed of Covenant is held by the Fiscal Agent on behalf of the Noteholders at its specified office. The holders of the Notes (the "**Noteholders**") are bound by, and are deemed to have notice of, all the provisions of the Fiscal Agency Agreement and the Deed of Covenant applicable to them. Copies of the Fiscal Agency Agreement are available for inspection during normal business hours at the Specified Offices (as defined in the Fiscal Agency Agreement) of each of the Paying Agents, the initial Specified Offices of which are set out below. References in these Conditions to the Fiscal Agent, the Registrar, the Paying Agents and the Agents shall include any successor appointed under the Fiscal Agency Agreement.

*The owners shown in the records of Euroclear Bank SA/NV ("**Euroclear**"), Clearstream Banking, société anonyme ("**Clearstream, Luxembourg**") and the Depository Trust Company ("**DTC**") of book-entry interests in Notes are entitled to the benefit of, are bound by, and are deemed to have notice of, all the provisions of the Fiscal Agency Agreement applicable to them.*

1. Form, Denomination and Title

(a) *Form and denomination*

The Notes are issued in registered form in amounts of U.S.$200,000 and integral multiples of U.S.$1,000 in excess thereof (referred to as the "**principal amount**" of a Note). A note certificate (each a "**Certificate**") will be issued to each Noteholder in respect of its registered holding of Notes. Each Certificate will be numbered serially with an identifying number which will be recorded on the relevant Certificate and in the Register (as defined below) which the Republic will procure to be kept by the Registrar.

The Notes are not issuable in bearer form.

(b) *Title*

The Registrar will maintain a register (the "**Register**") in respect of the Notes in accordance with the provisions of the Fiscal Agency Agreement. Title to the Notes passes only by registration in the Register. The holder of any Note will (except as otherwise required by law) be treated as its absolute owner for all purposes (whether or not it is overdue and regardless of any notice of ownership, trust or any interest or any writing on, or the theft or loss of, the Certificate issued in respect of it) and no person will be liable for so treating the holder. In these Conditions Noteholder and (in relation to a Note) holder means the person in whose name a Note is registered in the Register.

For a description of the procedures for transferring title to book-entry interests in the Notes, see the Fiscal Agency Agreement and Condition 2.

2. Transfers of Notes and Issue of Certificates

(a) *Transfers*

A Note may be transferred by depositing the Certificate issued in respect of that Note, with the form of transfer on the back duly completed and signed, at the specified office of the Registrar or any of the Agents.

For a description of certain restrictions on transfers of interests in the Notes, see "Transfer Restrictions" and the Fiscal Agency Agreement.

(b) ***Delivery of new Certificates***

Each new Certificate to be issued upon transfer of Notes will, within five business days of receipt by the Registrar or the relevant Agent of the duly completed form of transfer endorsed on the relevant Certificate, be mailed by uninsured mail at the risk of the holder entitled to the Note to the address specified in the form of transfer. For the purposes of this Condition, "**business day**" shall mean a day on which commercial banks and foreign exchange markets are open for business in the city in which the specified office of the Agent with whom a Certificate is deposited in connection with a transfer is located.

Except in the limited circumstances described herein (see "The Global Certificates – Registration of Title" and "The Global Certificates – Exchange For Certificates"), owners of interests in the Notes will not be entitled to receive physical delivery of Certificates. Issues of Certificates upon transfer of Notes are subject to compliance by the transferor and transferee with the certification procedures described above and in the Fiscal Agency Agreement and, in the case of Restricted Notes, compliance with the Securities Act legend as set out under "Subscription and Sale".

Where some but not all of the Notes in respect of which a Certificate is issued are to be transferred a new Certificate in respect of the Notes not so transferred will, within five business days of receipt by the Registrar or the relevant Agent of the original Certificate, be mailed by uninsured mail at the risk of the holder of the Notes not so transferred to the address of such holder appearing on the Register or as specified in the form of transfer.

(c) ***Formalities free of charge***

Registration of transfer of Notes will be effected without charge by or on behalf of the Republic or any Agent but upon payment (or the giving of such indemnity as the Republic or any Agent may reasonably require) in respect of any tax or other governmental charges which may be imposed in relation to such transfer.

(d) ***Closed periods***

No Noteholder may require the transfer of a Note to be registered during the period of 15 days ending on the due date for any payment of principal, premium or interest on that Note.

(e) ***Regulations***

All transfers of Notes and entries on the Register will be made subject to the detailed regulations concerning transfer of Notes scheduled to the Fiscal Agency Agreement. The regulations may be changed by the Republic with the prior written approval of the Registrar. A copy of the current regulations will be mailed (free of charge) by the Registrar to any Noteholder who requests one.

3. Status

The Notes constitute direct, general, (subject to the provisions of Condition 4 (*Negative Pledge*) unsecured and unconditional obligations of the Republic and will at all times rank *pari passu* and without any preference among themselves. The full faith and credit of the Republic is pledged for the due and punctual payment of the principal of, and interest on, the Notes and the performance of all the Republic's other obligations under the Notes. The payment obligations of the Republic under the Notes will at all times rank at least equally with all the other present and future unsecured and unsubordinated indebtedness of the Republic.

4. Negative Pledge

So long as any of the Notes remains outstanding the Republic will not grant or permit to be outstanding, and will procure that there is not granted or permitted to be outstanding, any mortgage, charge, lien, pledge or other security interest over any of its present or future assets or revenues or upon the official external reserves of the Republic (which expression includes the gold and the reserves of the Republic by whomsoever and in whatever form owned or held or customarily regarded and held out as the official external reserves thereof) or any part thereof, to secure any Relevant Indebtedness or any guarantee thereof unless the Republic shall, in the case of the granting of the security, before or at the same time, and in any other case, promptly, procure that all amounts payable in respect of the Notes are secured equally and rateably, or such other security or other arrangement is provided as shall be approved by an Extraordinary Resolution (as defined in the Fiscal Agency Agreement) of the Noteholders.

For this purpose, "**Relevant Indebtedness**" means any indebtedness, present or future, (A) evidenced by notes, bonds or other similar instruments which are or may be quoted, listed or ordinarily purchased and sold on any stock exchange and (B) which is not listed on the Riga Stock Exchange and issued in dematerialised form into the Latvian Central Depositary system.

5. Interest

(a) ***Interest rate and Interest Payment Dates***

The Notes bear interest on their outstanding principal amount from, and including, 16 June 2011 (the "**Issue Date**") at the rate of 5.25 per cent. per annum, payable in arrear on 16 June and 16 December in each year (each, an "**Interest Payment Date**"), subject as provided in Condition 7 (*Payments*).

(b) ***Interest accrual***

Each Note will cease to bear interest from and including its due date for redemption unless, upon due presentation, payment of the principal in respect of the Note is improperly withheld or refused or unless default is otherwise made in respect of payment. In such event, interest will continue to accrue until whichever is the earlier of:

(i) the date on which all amounts due in respect of such Note have been paid; and

(ii) the day on which notice has been given to the Noteholders that the Fiscal Agent or the Registrar has received all sums due in respect of the Notes up to such day (except, in the case of payment to the Fiscal Agent or the Registrar to the extent that there is any subsequent default in payment in accordance with these Conditions).

(c) ***Calculation of broken interest***

When interest is required to be calculated in respect of a period of less than a half-year, it shall be calculated on the basis of a 360-day year consisting of 12 months of 30 days each and, in the case of an incomplete month, the number of days elapsed on the basis of a month of 30 days.

6. Redemption Purchase

(a) ***Scheduled redemption***

Unless previously redeemed, repaid or purchased and cancelled, the Republic will redeem the Notes at their principal amount on 16 June 2021, subject as provided in Condition 7 (*Payments*).

(b) ***Purchase and cancellation***

The Republic and its Agencies may at any time purchase Notes in the open market or otherwise and at any price. Any Notes so purchased, while held by or on behalf of the Republic or any Agency, shall not entitle the holder to vote at any meeting of Noteholders and shall not be deemed to be outstanding for the purposes of calculating quorums at meetings of Noteholders. Any Notes so purchased may be cancelled or held and resold by the Republic. Any Notes so cancelled will not be reissued or resold.

In this Condition 6(b), "**Agency**" means any political sub-division, regional government, ministry, department, authority or statutory corporation of the Republic and the government thereof (whether or not such statutory corporation is autonomous) and "**Agencies**" shall be construed accordingly.

7. Payments

(a) ***Payments in respect of Notes***

Payment of principal and interest will be made by transfer to the registered account of the Noteholder or by U.S.$ cheque drawn on a bank that processes payments in U.S.$ mailed to the registered address of the Noteholder if it does not have a registered account. Payments of principal and payments of interest due otherwise than on an Interest Payment Date will only be made against surrender of the relevant Certificate at the specified office of any of the Agents. Interest on Notes due on an Interest Payment Date will be paid to the holder shown on the Register at the close of business on the date (the "**record date**") being the fifteenth day before the due date for the payment of interest.

For the purposes of this Condition 7(a), a Noteholder's registered account means the U.S.$ account maintained by or on behalf of it with a bank that processes payments in U.S.$, details of which appear on the Register at the close of business, in the case of principal, on the second Business Day (as defined below) before the due date for payment and, in the case of interest, on the relevant record date, and a Noteholder's registered address means its address appearing on the Register at that time.

(b) ***Payments subject to applicable laws***

Payments in respect of principal and interest on Notes are subject in all cases to any fiscal or other laws and regulations applicable in the place of payment, but without prejudice to the provisions of Condition 8 (*Taxation*).

(c) ***Payment on Business Days***

Where payment is to be made by transfer to a registered account, payment instructions (for value the due date or, if that is not a Business Day (as defined below), for value the first following day which is a Business Day) will be initiated and, where payment is to be made by cheque, the cheque will be mailed, on the Business Day preceding the due date for payment or, in the case of a payment of principal or a payment of interest due otherwise than on an Interest Payment Date, if later, on the Business Day on which the relevant Certificate is surrendered at the specified office of an Agent.

Noteholders will not be entitled to any interest or other payment for any delay after the due date in receiving the amount due if the due date is not a Business Day, if the Noteholder is late in surrendering its Certificate (if required to do so) or if a cheque mailed in accordance with this Condition arrives after the due date for payment.

In this Condition 7 (*Payments*) "**Business Day**" means a day (other than a Saturday or Sunday) on which commercial banks are open for business in London, New York City and, in the case of presentation of a Note Certificate, in the place in which the Note Certificate is presented.

(d) ***Partial Payments***

If the amount of principal or interest which is due on the Notes is not paid in full, the Registrar will annotate the Register with a record of the amount of principal, premium (if any) or interest in fact paid.

8. Taxation

All payments of principal and interest in respect of the Notes shall be made free and clear of, and without withholding or deduction for, any taxes, duties, assessments or governmental charges of whatsoever nature imposed, levied, collected, withheld or assessed by the Republic of Latvia or any political sub-division or any authority thereof or therein having power to tax (together, "**Taxes**"), unless such withholding or deduction is required by law. In that event, the Republic shall pay such additional amounts as will result in the receipt by the Noteholders of such amounts as would have been received by them if no such withholding or deduction had been required, except that no such additional amounts shall be payable in respect of any Note:

(a) presented for payment by a holder which is liable to such Taxes in respect of such Note by reason of its having some connection with the Republic of Latvia other than the mere holding of such Note; or

(b) where such withholding or deduction is imposed on a payment to an individual and is required to be made pursuant to European Council Directive 2003/48/EC or any other Directive implementing the conclusions of the ECOFIN Council meeting of 26-27 November 2000 on the taxation of savings income or any law implementing or complying with, or introduced in order to conform to, such Directive; or

(c) presented for payment by or on behalf of a holder who would not be liable for or subject to such withholding or deduction (A) by making a declaration of non-residence or other similar claim for exemption to the relevant tax authority if, after having been requested to make such a declaration or claim, such holder fails to do so, or (B) by presenting the relevant Note to another Paying Agent in a member state of the European Union; or

(d) presented for payment more than 30 days after the Relevant Date except to the extent that the relevant holder would have been entitled to such additional amounts if it had presented such Note on the last day of such period of 30 days.

In these Conditions, "**Relevant Date**" means whichever is the later of (i) the date on which the payment in question first becomes due and (ii) if the full amount payable has not been received by the Fiscal Agent as provided in the Fiscal Agency Agreement on or prior to such due date, the date on which (the full amount having been so received) notice to that effect has been given to the Noteholders.

Any reference in these Conditions to principal or interest shall be deemed to include any additional amounts in respect of principal or interest (as the case may be) which may be payable under this Condition.

9. Events of Default

(a) ***Declaration of acceleration***

If either of the following events (each an "**Event of Default**") occurs and is continuing:

(i) *Non-payment*

Any default is made in the payment of any interest due in respect of the Notes or any of them when due and the default continues for a period of 14 days; or

(ii) *Breach of other obligations or undertakings*

The Republic fails to perform or observe any of its other obligations under these Conditions and (except in any case where the failure is incapable of remedy when no continuation or notice as is hereinafter mentioned will be required) the failure continues for the period of 30 days next following the service by any Noteholder on the Republic of notice requiring the same to be remedied,

then the holders of at least 25 per cent. in aggregate principal amount of the outstanding Notes may, by notice in writing to the Republic (with a copy to the Fiscal Agent), declare all the Notes to be immediately due and payable, whereupon they shall become immediately due and payable at their principal amount together with accrued interest without further action or formality. Notice of any such declaration shall promptly be given to all other Noteholders by the Republic.

(b) ***Rescission of declaration of acceleration***

If the Republic receives notice in writing from holders of at least 50 per cent. in aggregate principal amount of the outstanding Notes to the effect that the Event of Default or Events of Default giving rise to the above mentioned declaration of acceleration is or are cured following any such declaration, the Republic shall give notice thereof in writing to the Noteholders (with a copy to the Fiscal Agent), the Notes shall cease to be due and payable. No such rescission shall affect any other or any subsequent Event of Default or any right of any Noteholder in relation thereto.

10. Prescription

Claims for principal shall become void unless the relevant Notes are presented for payment within ten years of the appropriate Relevant Date. Claims for interest shall become void unless the relevant Notes are presented for payment within five years of the appropriate Relevant Date.

11. Replacement of Certificates

If any Note is lost, stolen, mutilated, defaced or destroyed, it may be replaced at the Specified Office of the Fiscal Agent, subject to all applicable laws and stock exchange requirements, upon payment by the claimant of the expenses incurred in connection with such replacement and on such terms as to evidence, security, indemnity and otherwise as the Republic and the Fiscal Agent may require. Mutilated or defaced Notes must be surrendered before replacements will be issued.

12. Paying Agents

In acting under the Fiscal Agency Agreement and in connection with the Notes, the Paying Agents act solely as agents of the Republic and do not assume any obligations towards or relationship of agency or trust for or with any of the Noteholders.

The initial Paying Agents and their initial Specified Offices are listed below. The Republic reserves the right at any time to vary or terminate the appointment of any Paying Agent and to appoint a successor fiscal agent and additional or successor paying agents; provided, however, that the Republic shall at all times maintain (a) a fiscal agent and (b) a paying agent in a member state (if any) of the

European Union that will not be obliged to withhold or deduct tax pursuant to European Council Directive 2003/48/EC.

Notice of any change in any of the Paying Agents or in their Specified Offices shall promptly be given to the Noteholders in accordance with Condition 16 (*Notices*) below.

13. Meetings of Noteholders; Written Resolutions

(a) ***Convening meetings of Noteholders***

The Fiscal Agency Agreement contains provisions for convening meetings of Noteholders to consider matters relating to the Notes, including the modification of any provision of these Conditions or the provisions of the Fiscal Agency Agreement. Such a meeting may be convened by the Republic and shall be convened by the Republic at any time upon the request in writing of holders of at least 10 per cent. of the aggregate principal amount of the outstanding Notes.

(b) ***Quorum***

The quorum at any meeting of Noteholders convened to vote on an Extraordinary Resolution (as defined below) will be:

(i) one or more persons present and holding or representing at least 50 per cent. of the aggregate principal amount of the outstanding Notes; or

(ii) where a meeting is adjourned and rescheduled owing to a lack of quorum, at any rescheduled meeting of Noteholders, one or more persons present and holding or representing at least 25 per cent. of the aggregate principal amount of the outstanding Notes;

provided, however, that any proposals relating to a Reserved Matter (as defined below) may only be approved by an Extraordinary Resolution passed at a meeting of Noteholders at which one or more persons present and holding or representing at least 75 per cent. of the aggregate principal amount of the outstanding Notes form a quorum.

(c) ***Reserved Matters***

In these Conditions, "**Reserved Matter**" means any proposal:

(i) to change the date, or the method of determining the date, for payment of principal, interest or any other amount in respect of the Notes, to reduce or cancel the amount of principal, interest or any other amount payable on any date in respect of the Notes or to change the method of calculating the amount of principal, interest or any other amount payable in respect of the Notes on any date;

(ii) to change the currency in which any amount due in respect of the Notes is payable;

(iii) to change the quorum required at any meeting of Noteholders or the majority required to pass an Extraordinary Resolution, Written Resolution or any other resolution of Noteholders or the number or percentage of votes required to be cast, or the number or percentage of Notes required to be held, in connection with the taking of any decision or action by or on behalf of the Noteholders or any of them;

(iv) to change this definition, the definition of "**Extraordinary Resolution**", the definition of "**outstanding**" or the definition of "**Written Resolution**" in these Conditions or in the Fiscal Agency Agreement;

(v) to change or waive the provisions of the Notes set out in Condition 3 (*Status*);

(vi) to change the law governing the Notes, the courts to the jurisdiction of which the Republic has submitted in the Notes, the Republic's obligation to maintain an agent for service of process in England or the Republic's waiver of immunity, in respect of actions or proceedings brought by any Noteholder, set out in Condition 17 (*Governing Law and Jurisdiction*);

(vii) to approve any exchange or substitution of the Notes for, or the conversion of the Notes into, any other obligations or securities of the Republic or any other person; or

(viii) in connection with any proposed exchange, substitution or conversion of the type referred to in paragraph (vii) to amend any of the provisions of the Notes describing circumstances in which Notes may be redeemed or declared due and payable prior to their scheduled maturity date.

(d) ***Modifications***

Any modification of any provision of these Conditions may be made if approved by an Extraordinary Resolution or a Written Resolution (as defined below). In these Conditions, "**Extraordinary Resolution**" means a resolution passed at a meeting of Noteholders duly convened and held in accordance with the Fiscal Agency Agreement by a majority of at least:

(i) in the case of a Reserved Matter, 75 per cent. of the aggregate principal amount of the outstanding Notes; or

(ii) in the case of a matter other than a Reserved Matter, $66^2/3$ per cent. of the aggregate principal amount of the outstanding Notes which are represented at that meeting. Any Extraordinary Resolution duly passed at any such meeting shall be binding on all the Noteholders, whether present or not and whether they voted in favour or not.

(e) ***Written Resolutions***

In addition, the Fiscal Agency Agreement contains provisions relating to Written Resolutions. A "**Written Resolution**" is a resolution in writing signed by or on behalf of the holders of at least 75 per cent. of the principal amount of the outstanding Notes, in the case of a Reserved Matter, or $66^2/_3$ per cent. of the principal amount of the outstanding Notes, in the case of a matter other than a Reserved Matter. Any Written Resolution may be contained in one document or several documents in the same form, each signed by or on behalf of one or more Noteholders. Any Written Resolution shall be binding on all of the Noteholders, whether or not signed by them.

(f) ***Manifest error, etc.***

The Notes, these Conditions and the provisions of the Fiscal Agency Agreement may be amended without the consent of the Noteholders to correct a manifest error. In addition, the parties to the Fiscal Agency Agreement may agree to modify any provision thereof, but the Republic shall not agree, without the consent of the Noteholders, to any such modification unless it is of a formal, minor or technical nature or it is not materially prejudicial to the interests of the Noteholders.

(g) ***Outstanding Notes***

For the purposes of (i) ascertaining the right to attend and vote at any meeting of Noteholders, (ii) this Condition 13 (*Meetings of Noteholders; Written Resolutions*) and Schedule 5 to the Fiscal Agency Agreement, (iii) Condition 14 (*Noteholders' Representative Committee*) and (iv) Condition 9 (*Events of Default*), those Notes (if any) which are for the time being held by or on behalf of the Republic or by any person owned or controlled directly or indirectly by the Republic, or by any public sector instrumentality of the Republic shall (unless and until ceasing to be so held) be disregarded and be deemed not to remain outstanding. "**Public sector instrumentality**" means the Republic of Latvia, any department, ministry or agency of the government of the Republic of Latvia or any corporation, trust, financial institution or other entity owned or controlled by the government of the Republic of Latvia. "**Control**" means the power, directly or indirectly, through the ownership of voting securities or other ownership interests or otherwise, to direct the management of or elect or appoint a majority of the board of directors or other persons performing similar functions in lieu of, or in addition to, the board of directors of a corporation, trust, financial institution or other entity.

(h) ***Written requests etc.***

Before any request is made or notice is delivered or Written Resolution is signed by any Noteholder in accordance with the provisions of this Condition or Conditions 14 (*Noteholders' Representative Committee*) or 9 (*Events of Default*), the relevant Noteholder must deposit its Notes with any Paying Agent and obtain two copies of an acknowledgment of receipt (an "**Acknowledgment**") signed and dated by the relevant Paying Agent and certifying the principal amount of Notes so deposited. Any request so made, notice so given or Written Resolution so signed by any Noteholder must be accompanied by an Acknowledgment issued to the Noteholder. Notes so deposited will not be released until the earlier of (i) the thirtieth day after the date of deposit and (ii) the request, notice or Written Resolution becoming effective in accordance with these Conditions and will only be released against surrender of a relevant Acknowledgment.

14. Noteholders' Representative Committee

(a) ***Appointment***

The Noteholders may, by a resolution passed at a meeting of Noteholders duly convened and held in accordance with the Fiscal Agency Agreement by a majority of at least 50 per cent. in aggregate principal amount of the Notes then outstanding, or by notice in writing to the Republic (with a copy to the Fiscal Agent) signed by or on behalf of the holders of at least 50 per cent. in aggregate principal amount of the Notes then outstanding, appoint any person or persons as a committee to represent the interests of the Noteholders if any of the following events has occurred:

(i) an Event of Default;

(ii) any event or circumstance which could, with the giving of notice, lapse of time, the issuing of a certificate and/or fulfilment of any other requirement provided for in Condition 9 (*Events of Default*) become an Event of Default; or

(iii) any official public announcement by the Republic to the effect that the Republic is seeking or intends to seek a restructuring of the Notes (whether by amendment, exchange offer or otherwise),

provided, however, that no such appointment shall be effective if the holders of more than 25 per cent. of the principal amount of the outstanding Notes have either (A) objected to such appointment by notice in writing to the Republic (with a copy to the Fiscal Agent) during a specified period following notice of the appointment being given (if such notice of appointment is made by notice in writing to the Republic) where such specified period shall be either 30 days or such other longer or shorter period as the committee may, acting in good faith, determine to be appropriate in the circumstances, or (B) voted against such resolution at a meeting of Noteholders duly convened and held in accordance with the Fiscal Agency Agreement.

(b) ***Powers***

Such committee shall, if appointed by notice in writing to the Republic, give notice of its appointment to all Noteholders in accordance with Condition 16 (*Notices*) as soon as practicable after the notice is delivered to the Republic. Such committee in its discretion may, among other things, (i) engage legal advisers and financial advisers to assist it in representing the interests of the Noteholders, (ii) adopt such rules as it considers appropriate regarding its proceedings and (iii) enter into discussions with the Republic and/or other creditors of the Republic. The Republic shall pay any fees and expenses of any such committee (including, without limitation, the costs of giving notices to Noteholders and the reasonable fees and expenses of the committee's legal advisers and financial advisers, if any) within 30 days of the delivery to the Republic of a reasonably detailed invoice and supporting documentation.

15. Further Issues

The Republic may from time to time, without the consent of the Noteholders, create and issue further notes having the same terms and conditions as the Notes in all respects (or in all respects except for the amount and date of the first payment of interest) so as to form a single series with the Notes provided, however, that the Notes are either (i) not issued with original issue discount, (ii) issued with less than a *de minimis* amount of original issue discount, or (iii) issued in a "qualified reopening" for U.S. federal income tax purposes.

16. Notices

Notices to the Noteholders shall be valid if published (i) in a leading newspaper having general circulation in Luxembourg (which is expected to be the *Luxemburger Wort* or the *Tageblatt*) or, if such publication is not practicable, in a leading English language daily newspaper having general circulation in Europe or (ii) to the extent and in the manner permitted by the rules and regulations of the Luxembourg Stock Exchange, by posting such notices on the official website of the Luxembourg Stock Exchange (www.bourse.lu). Any such notice shall be deemed to have been given on the date of first publication or, if so published more than once on different dates, on the date of the first publication.

All notices to the Republic will be valid if sent to the Republic at the Treasury of the Republic of Latvia, Riga or such other address as may be notified by the Republic to the Noteholders in accordance with the above paragraph of this Condition.

17. Governing Law and Jurisdiction

(a) ***Governing law***

The Notes and any non-contractual obligations arising out of or in connection with them are governed by English law.

(b) ***Jurisdiction***

The Republic agrees for the benefit of the Noteholders that the courts of England shall have jurisdiction to hear and determine any suit, action or proceedings, and to settle any disputes, which may arise out of or in connection with the Notes (respectively, "**Proceedings**" and "**Disputes**") and, for such purposes, irrevocably submits to the jurisdiction of such courts.

(c) ***Appropriate forum***

The Republic irrevocably waives any objection which it might now or hereafter have to the courts of England being nominated as the forum to hear and determine any Proceedings and to settle any Disputes, and agrees not to claim that any such court is not a convenient or appropriate forum.

(d) ***Service of process***

The Republic irrevocably appoints the Ambassador of the Republic of Latvia to the Court of St. James's as its authorised agent for the service of process in England in respect of any Proceedings or Disputes. Nothing in this paragraph shall affect the right of any Noteholder to serve process in any other manner permitted by law.

(e) ***Non-exclusivity***

The submission to the jurisdiction of the courts of England shall not (and shall not be construed so as to) limit the right of any Noteholder to take Proceedings in any other court of competent jurisdiction, nor shall the taking of Proceedings in any one or more jurisdictions preclude the taking of Proceedings in any other jurisdiction (whether concurrently or not) if and to the extent permitted by law.

(f) ***Consent to enforcement etc***

For the purposes of the State Immunity Act 1978, the Republic consents generally in respect of any Proceedings to the giving of any relief or the issue of any process in connection with such Proceedings including (without limitation) the making, enforcement or execution against any property whatsoever (irrespective of its use or intended use) of any order or judgment which may be made or given in such Proceedings.

(g) ***Waiver of immunity***

To the extent that the Republic may in any jurisdiction claim for itself or its assets or revenues immunity from suit, execution, attachment (whether in aid of execution, before judgment or otherwise and whether or not on the grounds of sovereignty or otherwise) or other legal process and to the extent that such immunity (whether or not claimed) may be attributed in any such jurisdiction to the Republic or its assets or revenues, the Republic agrees not to claim and irrevocably waives such immunity to the full extent permitted by the laws of such jurisdiction provided, however, that immunity is not waived in respect of present or future "**premises of the mission**" as defined in the Vienna Convention on Diplomatic Relations signed in 1961, "**consular premises**" as defined in the Vienna Convention on Consular Relations signed in 1963 or military property or military assets or property or assets of the Republic related thereto.

There will appear at the foot of the Conditions endorsed on each Note in definitive form the names and Specified Offices of the Paying Agents as set out at the end of this Offering Circular.

THE GLOBAL CERTIFICATES

The Global Certificates contain the following provisions which apply to the Notes in respect of which they are issued whilst they are represented by the Global Certificates, some of which modify the effect of the Conditions. Terms defined in the Conditions have the same meaning in paragraphs 1 to 7 below.

1. FORM OF THE NOTES

The Notes sold in reliance on Regulation S under the Securities Act will be represented on issue by the Unrestricted Global Certificate, which will be deposited with, and registered in the name of a nominee for the common depositary for, Euroclear and Clearstream, Luxembourg. Beneficial interests in an Unrestricted Global Certificate may be held only through Euroclear or Clearstream, Luxembourg or their participants at any time. By acquisition of a beneficial interest in the Unrestricted Global Certificate, the purchaser thereof will be deemed to represent, among other things, that it acquired such beneficial interest in accordance with Regulation S and that it will only offer, sell, pledge or otherwise transfer such beneficial interest in an offshore transaction in accordance with Rule 903 or Rule 904 of Regulation S. See "*Subscription and Sale*" and "*Transfer Restrictions*".

The Notes sold in reliance on Rule 144A will be represented on issue by the Restricted Global Certificate, which will be deposited with a custodian for, and registered in the name of a nominee of, DTC. Beneficial interests in a Restricted Global Certificate may only be held through DTC or its participants at any time. Beneficial interests in a Restricted Global Certificate may only be held by persons who are QIBs, holding their interests for their own account or for the account of one or more QIBs. By acquisition of a beneficial interest in a Restricted Global Certificate, the purchaser thereof will be deemed to represent, among other things, that it is a QIB and that, if in the future it determines to transfer such beneficial interest, it will transfer such interest in accordance with the procedures and restrictions contained in the Restricted Global Certificate. See "*Subscription and Sale*".

Beneficial interests in Global Certificates will be subject to certain restrictions on transfer set out therein and under "*Transfer Restrictions*" and in the Agency Agreement and such Global Certificates will bear a legend as set out under "*Subscription and Sale*". On or prior to the 40th day after the later of the commencement of the offering and the Issue Date, ownership of interests in an Unrestricted Global Certificate will be limited to persons who have accounts with Euroclear or Clearstream, Luxembourg, or persons who hold interests through Euroclear or Clearstream, Luxembourg, and any sale or transfer of such interests to U.S. persons shall not be permitted during such period unless such resale or transfer is made pursuant to Rule 144A as provided below.

No beneficial interest in an Unrestricted Global Certificate may be transferred to a person who takes delivery in the form of a beneficial interest in a Restricted Global Certificate unless (i) the transfer is to a person that is a QIB, (ii) such transfer is made in reliance on Rule 144A, and (iii) the transferor provides the Registrar with a written certification substantially in the form set out in the Agency Agreement to the effect that the transferor reasonably believes that the transferee is a QIB, that the transfer is being made in a transaction meeting the requirements of Rule 144A and that such transaction is in accordance with any applicable securities laws of any state of the United States or any other jurisdiction. No beneficial interest in the Restricted Global Certificate may be transferred to a person who takes delivery in the form of a beneficial interest in an Unrestricted Global Certificate unless the transfer is to a non-U.S. person in an offshore transaction in reliance on Regulation S and the transferor provides the Registrar with a written certification substantially in the form set out in the Agency Agreement to the effect that the transfer is being made to a person who is a non-U.S. person in accordance with Regulation S.

Any beneficial interest in an Unrestricted Global Certificate that is transferred to a person who takes delivery in the form of an interest in a Restricted Global Certificate will, upon transfer, cease to be an interest in such Unrestricted Global Certificate and become an interest in the Restricted Global Certificate, and, accordingly, will thereafter be subject to all transfer restrictions and other procedures applicable to beneficial interests in a Restricted Global Certificate for as long as it remains such an interest. Any beneficial interest in a Restricted Global Certificate that is transferred to a person who takes delivery in the form of an interest in an Unrestricted Global Certificate will, upon transfer, cease to be an interest in each Restricted Global Certificate and become an interest in the Unrestricted Global Certificate and, accordingly, will thereafter be subject to all transfer restrictions and other procedures applicable to beneficial interests in an Unrestricted Global Certificate for so long as it remains such an interest. No service charge will be made for any registration of transfer or exchange of Notes, but the Republic may require payment of a sum sufficient to cover any tax or other governmental charge payable in connection therewith.

Except in the limited circumstances described below, owners of beneficial interests in the Global Certificates will not be entitled to receive physical delivery of Notes.

2. ACCOUNTHOLDERS

For so long as any of the Notes are represented by the Global Certificates, each person (other than another clearing system) who is for the time being shown in the records of DTC or Euroclear or Clearstream, Luxembourg (as the case may be) as the holder of a particular aggregate principal amount of such Notes (each an "**Accountholder**") (in which regard any certificate or other document issued by DTC or Euroclear or Clearstream, Luxembourg (as the case may be) as to the aggregate principal amount of such Notes standing to the account of any person shall be conclusive and binding for all purposes) shall be treated as the holder of such aggregate principal amount of such Notes (and the expression "Noteholders" and references to "holding of Notes" and to "holder of Notes" shall be construed accordingly) for all purposes other than with respect to payments on such Notes, the right to which shall be vested, as against the Republic, solely in the nominee for the relevant clearing system (the "**Relevant Nominee**") in accordance with and subject to the terms of the Global Certificates. Each Accountholder must look solely to DTC or Euroclear or Clearstream, Luxembourg, as the case may be, for its share of each payment made to the Relevant Nominee.

3. CANCELLATION

Cancellation of any Note following its redemption or purchase by the Republic will be effected by reduction in the aggregate principal amount of the Notes in the Register and by the annotation of the appropriate schedule to the relevant Global Certificate.

4. PAYMENTS

Payments of principal and interest in respect of Notes represented by a Global Certificate will be made upon presentation or, if no further payment falls to be made in respect of the Notes, against presentation and surrender of such Global Certificate to or to the order of the Fiscal Agent or such other Agent as shall have been notified to the holders of the Global Certificates for such purpose.

Distributions of amounts with respect to book-entry interests in the Unrestricted Notes held through Euroclear or Clearstream, Luxembourg will be credited, to the extent received by the Fiscal Agent, to the cash accounts of Euroclear or Clearstream, Luxembourg participants in accordance with the relevant system's rules and procedures.

Holders of book-entry interests in the Restricted Notes holding through DTC will receive, to the extent received by the Fiscal Agent, all distribution of amounts with respect to book-entry interests in such Notes from the Fiscal Agent through DTC. Distributions in the United States will be subject to relevant U.S. tax laws and regulations.

A record of each payment made will be endorsed on the appropriate schedule to the relevant Global Certificate by or on behalf of the Fiscal Agent and shall be *prima facie* evidence that payment has been made.

5. NOTICES

So long as the Notes are represented by a Global Certificate and such Global Certificate is held on behalf of a clearing system, notices to Noteholders may be given by delivery of the relevant notice to that clearing system for communication by it to entitled Accountholders in substitution for notification as required by Condition 16 (*Notices*) except that, so long as the Notes are listed on the Luxembourg Stock Exchange and the rules of that Exchange so require, notices shall also be published in a daily newspaper having general circulation in Luxembourg (which is expected to be the *Luxemburger Wort* or the *Tageblatt*). Any such notice shall be deemed to have been given to the Noteholders on the second day after the day on which such notice is delivered to Euroclear and/or Clearstream, Luxembourg (as the case may be) as aforesaid.

Whilst any of the Notes held by a Noteholder are represented by a Global Certificate, notices to be given by such Noteholder may be given by such Noteholder (where applicable) through Euroclear and/or Clearstream, Luxembourg and otherwise in such manner as the Fiscal Agent and Euroclear and Clearstream, Luxembourg may approve for this purpose.

6. REGISTRATION OF TITLE

The Registrar will not register title to the Notes in a name other than that of the Relevant Nominee for a period of 15 calendar days preceding the due date for any payment of principal, or interest in respect of the Notes.

7. EXCHANGE FOR CERTIFICATES

(a) ***Exchange***

Each Restricted Global Certificate will be exchangeable, free of charge to the holder, in whole but not in part, for Restricted Certificates and each Unrestricted Global Certificate will be exchangeable, free of charge to the holder, in whole but not in part, for Unrestricted Certificates upon the occurrence of an Exchange Event.

For these purposes an "**Exchange Event**" means that:

(i) circumstances described in Condition 9 (*Events of Default*) have occurred;

(ii) in the case of an Unrestricted Global Certificate only, if Euroclear and/or Clearstream, Luxembourg is closed for business for a continuous period of 14 days (other than by reason of holiday, statutory or otherwise) or announces that it is permanently to cease business or does in fact do so and no successor or alternative clearing system is available; or

(iii) in the case of a Restricted Global Certificate only, if DTC notifies the Republic that it is no longer willing or able to discharge properly its responsibilities as depositary with respect to the relevant Global Certificate or DTC ceases to be a "clearing agency" registered under the U.S. Securities Exchange Act of 1934, as amended (the "**Exchange Act**") or is at any time no longer eligible to act as such and no qualified successor clearing system has been identified within 90 days of receipt of such notice from DTC,

provided that, in the case of any exchange pursuant to (b) or (c) above, the holder has given the Registrar not less than 30 days' notice at its specified office of such holder's intention to effect such exchange.

In exchange for the relevant Global Certificate, as provided in the Agency Agreement, the Registrar will deliver or procure the delivery of an equal aggregate principal amount of duly executed Certificates in or substantially in the form set out in the Agency Agreement.

(b) ***Delivery***

In such circumstances, the relevant Global Certificate shall be exchanged in full for Certificates and the Republic will, at the cost of the Republic (but against such indemnity as the Registrar or Transfer Agent may require in respect of any tax or other duty of whatever nature which may be levied or imposed in connection with such exchange), cause sufficient Certificates to be executed and delivered to the Registrar for completion and dispatch to the relevant Noteholders. A person having an interest in a Global Certificate must provide the Registrar with (a) a written order containing instructions and such other information as the Republic and the Registrar may require to complete, execute and deliver such Certificates and (b) in the case of the Restricted Global Certificate only, a fully completed, signed certification substantially to the effect that the exchanging holder is not transferring its interest at the time of such exchange or, in the case of simultaneous sale pursuant to Rule 144A, a certification that the transfer is being made in compliance with the provisions of Rule 144A to a purchaser that the transferor reasonably believes to be a QIB. Certificates issued in exchange for a beneficial interest in the Restricted Global Certificate shall bear the legend applicable to transfers pursuant to Rule 144A, as set out under "*Subscription and Sale*".

(c) ***Legends and transfers***

The holder of a Certificate may transfer the Notes represented thereby in whole or in part in the applicable denomination by surrendering it at the specified office of any Transfer Agent, together with the completed form of transfer thereon. Upon the transfer, exchange or replacement of a Certificate bearing the legend referred to under "*Subscription and Sale*", or upon specific request for removal of the legend on a Certificate, the Republic will deliver only Certificates that bear such legend, or will refuse to remove such legend, as the case may be, unless there is delivered to the Republic and the Registrar such satisfactory evidence, which may include an opinion of counsel, as may reasonably be required by the Republic that neither the legend nor the restrictions on transfer set out therein are required to ensure compliance with the provisions of the Securities Act. Restricted Certificates will bear the same legend as the legend for the Restricted Global Certificates set out under "*Subscription and Sale*". The Restricted Certificates may not at any time be held by or on behalf of U.S. persons that are not QIBs. Before any Unrestricted Certificate may be offered, resold, pledged or otherwise transferred to a person who takes delivery in the form of a Restricted Certificate, the transferor and/or transferee, as applicable, will be required to provide the Registrar with a written certification substantially in the form set out in the Agency Agreement to the effect that the transferor reasonably believes that the transfer is (i) to a person that is a QIB and (ii) such transfer is made in reliance on Rule 144A. Unrestricted Certificates will bear the same legend as the legend for the Unrestricted Global Certificates set out under "*Subscription and Sale*". Before any Restricted Certificates may be offered, resold, pledged or otherwise transferred to a person who takes delivery in the form of an Unrestricted Certificate, the transferor and/or transferee, as applicable, will be required to provide the relevant Registrar with a written certification substantially in the form set out in the Agency Agreement to the effect that the transfer is being made to a person who is a non-U.S. person in accordance with Regulation S.

USE OF PROCEEDS

The net proceeds of the issue of the Notes, expected to amount to U.S.$489,820,000, will be used for the refinancing of indebtedness and general funding purposes of the Republic.

DESCRIPTION OF THE REPUBLIC OF LATVIA

Geography and Population

Latvia is located in the Baltic region of northern Europe and is bordered by Estonia to the north, Russia to the east, Lithuania to the south and Belarus to the south-east. The western border of the country is the Baltic Sea, along which the country has a 498 kilometre coastline. Latvia is divided into four historical districts: Kurzeme (western Latvia), Zemgale (southern Latvia), Vidzeme (northern Latvia) and Latgale (eastern Latvia). Latvia covers an area of approximately 64,559 square kilometres. The capital city is Riga.

The country is low lying and generally flat, rising steadily from west to east, reaching its highest point of 312 metres above sea level at Gaizina Kalns. Latvia shares its longest border with Lithuania (588 km), followed by Estonia (343 km), Russia (276 km) and Belarus (161 km).

As of 1 January 2011, the total population of Latvia was approximately 2,229,600. Since early 2000, the total population has decreased by approximately 152,100 persons, or 6.4 per cent. of the population in early 2000, principally as a result of ageing, low birth rate and emigration. In terms of age profile, 20.1 per cent. of the population was under 20 at 1 January 2010, 57.3 per cent. was between 20 and 59 and 22.6 per cent. was aged 60 and over. The equivalent proportions at 1 January 2005 were 22.8 per cent., 55.0 per cent. and 22.2 per cent., respectively.

The urban/rural ratio of the total population has remained constant since 2000 with 68 per cent. of the total population living in urban areas as of 1 January 2010 and 32 per cent. in rural areas. The population density is 34.8 persons per square kilometre as of 1 January 2010.

The highest population concentration is in the capital city, Riga. As of 1 January 2010, the population in Riga was 706,413, which is equal to 31.4 per cent. of the total population. Since 2000, the population in Riga has decreased by 59,968, or 7.8 per cent.

At 1 January 2010, 66.0 per cent. of the Latvian population was of working age, 59.4 per cent. of the population were Latvian, 27.6 per cent. were Russian and no other ethnic group exceeded 4 per cent. of the total population.

The average life expectancy of those born in 2009 is 73.4 years (68.3 years for males and 78.1 years for females), weighted for gender balance.

Historical Background

Latvia's origins lie in the 12th century with the arrival of western Europeans, mainly German crusaders spreading the Catholic faith, although records of inhabitants date back to the ancestors of Baltic Finns in around 3,000 BC and the formation of the Baltic and Finno-Ugrian tribes in 2,000 BC.

The crusaders had established the state of Livonia as a political union of territories belonging to the Livonian Order of Knights and to the Catholic church by the 1270s. Riga, the capital city of Latvia, was founded in 1201. In 1285, Riga was admitted into the Hanseatic League of northern Germany, thereby assuming a central mediating role in east-west trade.

The territory of Latvia, through its access to the Baltic Sea trade routes, is strategically positioned. As a result, throughout the middle ages, Latvia (or parts of it) was controlled by other states, including Denmark, Poland-Lithuania, Sweden and Russia. From the middle of the 16th century until the end of the 18th century, part of Latvia was known as the Duchy of Courland, a semi-independent state paying tribute to Poland.

In 1721, Russia took control of the Latvian territories as a result of its victory over Sweden in the Great Northern War. In the 1860s, the Young Latvian Movement was formed in order to promote the indigenous language against Russification policies and to publicise and counteract the socioeconomic oppression of Latvians. In 1903, the Latvian Social Democratic Union was formed, which continued to champion national interests and Latvia's national self-determination, particularly during the failed 1905 revolution in Russia.

As a consequence of the First World War, Latvia's independence from Russia was declared on 18 November 1918. In 1922, the Constitutional Assembly (*Satversmes Sapulce*, a special meeting convened to approve a constitution) adopted a constitution (*Satversme*) which proclaimed the country to be a democratic republic. In May 1934, the parliament was dismissed and the activities of the political parties were suspended following a coup d'etat engineered by the then prime minister. With the outbreak of the Second World War, Latvia was annexed by the Soviet Union in 1940 and was invaded and occupied by Germany between 1941 and 1944. The Soviet Union reacquired control of Latvia in 1944 although its annexation of Latvia in 1940 was never recognised by most western democracies, including the United States.

After rapid political change in Eastern Europe and the Soviet Union in the late 1980s, the Supreme Council of Latvia re-established legal independence with the Declaration of the Renewal of the Independence of the Republic of Latvia on 4 May 1990. On 6 September 1991, the independence of the Baltic Republics (including Latvia) was recognised by the Soviet Union.

In September 1991, following the collapse of the Soviet Union, Latvia was admitted to the UN. On 29 March 2004, Latvia joined NATO and, on 1 May 2004, it became a Member State of the EU.

On 27 March 2007, a border treaty between Latvia and Russia was signed. The treaty was ratified by the Saeima (the Latvian Parliament) on 17 May 2007, by the State Duma of the Russian Parliament on 5 September 2007, and by the Russian Parliament Federation Council on 19 September 2007. The ratification procedure was finalised on 3 October 2007 when the President of Russia, Vladimir Putin, signed the agreement.

Political System and Developments

In accordance with the Constitution, the Saeima is the highest legislative body. The Saeima is a unicameral parliament consisting of 100 members, elected in general, equal, direct, secret and proportional elections for a four-year term. All Latvian citizens who are 18 years of age and over are entitled to vote.

The main function of the Saeima is to pass legislation. In addition, the Saeima approves the national budget, determines the size of the armed forces and oversees the work of the government. International agreements, which include matters that are decided by a legislative process, require ratification by the Saeima.

The Saeima is entitled to elect, appoint, approve or dismiss a range of state officials and also elects the President for a term of four years. According to the Constitution, any person who enjoys full rights of citizenship and who has attained the age of 40 years may be elected President. A person with dual citizenship is not eligible. The same person may not hold office as President for more than eight consecutive years.

One of the President's main functions is to represent Latvia internationally. The President nominates the prime minister and, if necessary, may initiate a referendum to approve the dissolution of the Saeima. The Cabinet of Ministers, which consists of ministers appointed by the prime minister, is the highest executive power in Latvia.

On 2 June 2011, the Saeima elected Andris Bērziņš as the President. Mr. Bērziņš will be the fourth President to be appointed since the Constitution was re-instituted in 1993.

The elections for the tenth Saeima were held in October 2010 with an election turnout of 944,841 (or 63.1 per cent. of eligible voters). The following political parties or party alliances were elected to the tenth Saeima:

Name of party	Number of seats
Alliance of political parties: Unity	33
Alliance of political organisations: Concord Centre	29
Union of Greens and Farmers	22
National alliance of: All for Latvia and Union For Fatherland and Freedom/LNNK(1)	8
Political alliance: For a Good Latvia	8
Total	**100**

Source: the Saeima
Note:
(1) Subsequently, one member has left the alliance and is now an unaffiliated member.

Five parliamentary groups have been established in the tenth Saeima. The Presidium of the Saeima consists of the Speaker, two Deputy Speakers, the Secretary and a Deputy Secretary. There are 16 standing committees in the Saeima. In addition, groups of members of Parliament and permanent delegations to international organisations have been established to promote cooperation with parliaments of other countries.

On 28 May 2011, the then President, in accordance with Article 48 of the Latvian Constitution, announced a proposal for a referendum on the dissolution of the tenth Saeima which will be held on 23 July 2011. The President declared that he was taking this step on the basis of a lack of trust between the people of Latvia and the Saeima after a majority of deputies in the Saeima blocked an anti-corruption investigation.

Local Governments

Following reform of local government and the local elections held in June 2009, there is now a single tier of 118 local government bodies in Latvia, comprising nine cities (*republikas pilsēta*) and 109 municipalities (*novads*). Previously there were two tiers of local government, comprising 548 local government bodies. The purpose of the reform of the local government system was to improve the efficiency and effectiveness of local government. Local government bodies are elected for four years by direct universal suffrage, under proportional representation on the basis of a list system.

Local government bodies in Latvia are responsible for a wide range of functions, including organising utility services, providing some education and health facilities, social assistance and social care for residents and maintaining cultural activities. See "*Public Finance – Relationship between Central Government and Local Government Budgets*" and "*Indebtedness – Local Government Debt*" for a discussion on local government funding.

Prevention and Combating of Corruption

In 2002, a single independent institution aimed at the prevention and combating of corruption and the monitoring of political parties' financing was established. This institution, known as the Bureau for the Prevention and Combating of Corruption (the "**Bureau**") currently employs approximately 140 people. The Bureau is an independent public administration institution supervised by the Cabinet of Ministers.

The Bureau develops and coordinates implementation of Latvia's mid-term anti-corruption policy (which is defined in two documents, the National Strategy and the National Programme for Prevention and Combating of Corruption (the "**Anti-corruption Programme**"), both for 2009-2013), monitors observance of the law "On Prevention of Conflict of Interest in Activities of Public Officials", controls party financing and screens draft legislation in order to identify any corruption risk. The Bureau reports on a regular basis to the Government and the Parliament with its results.

The Bureau also has full capacity to initiate enforcement proceedings in corruption-related crimes in public service. Between 2003 and 2010, the Bureau initiated 275 criminal cases, of which 167 criminal cases against 376 persons resulted in criminal prosecutions. From the time the Bureau started to control party financing up to 31 December 2010, LVL 2.0 million of illegal funding has been reimbursed to the State budget as a result of Bureau investigations.

The Bureau has investigated a number of cases of aggravated corruption as a result of which several high ranking officials (including a local government head, board members of one of the largest state companies and a former head of the Customs Criminal Board) have been detained. In order to decrease the influence of specific individuals or groups, the Bureau has initiated state funding for political parties and is responsible for administering this funding. The Bureau has also ensured that protection for whistle blowers has been introduced in Latvia. Looking ahead, the Bureau intends to focus on increasing the awareness of, and providing guidance in relation to preventing, conflicts of interest and on strengthening internal control measures in line with the stated policy in the Anti-corruption Programme.

According to the annual Transparency International Corruption Perception Index, an index published by Transparency International (a global civil society organisation), Latvia ranked 59th out of 180 countries in 2010 in terms of its perceived level of corruption, as determined by expert assessments and opinion surveys. For these purposes, corruption is defined as the abuse of entrusted power for private gain. Since 2006, when Latvia's score on the index was 4.7 out of 10, the scores have been 4.8 in 2007, 5.0 in 2008, 4.5 in 2009 and 4.3 in 2010, principally reflecting the fact that although the number of persons involved in criminal offences in Latvia has increased in recent years, the number of criminal proceedings investigated by the Bureau has decreased. See also "– *Political System and Developments*".

Combating Terrorism

In April 2003, a Government Action Plan for fighting terrorism was prepared and introduced. The plan aims to improve co-operation between state institutions in measures for the prevention and combating of terrorism. In particular, the plan aims to prevent terrorists from using the territory of Latvia or its banking system to achieve their goals. All the measures identified in the plan have been implemented and completed.

In particular, a counter-terrorism centre has been established which started operations on 1 February 2005. The centre seeks to co-ordinate the actions of institutions fighting terrorism, ensuring the timely exchange of information, and the compilation and analysis of information on counter-terrorist activities. In order to improve the efficiency of the national counter-terrorism system, the Ministry of Interior and the counter-terrorism centre have prepared a conceptual rating scale of levels of terrorism threat.

Latvia also participates in the efforts of international organisations, including the UN, NATO, the EU, the Organisation for Security and Co-operation in Europe and the Council of Europe, to combat global terrorism. Latvia has ratified and introduced all 13 UN Conventions and Protocols which form the basis of international legislation on issues of counter-terrorism, including most recently, the International Convention for the Suppression of Acts of Nuclear Terrorism.

Within the EU, Latvia has become involved in a range of practical counter-terrorism initiatives which provide for an increased level of cooperation between investigatory and security services, as well as in judicial matters. According to the EU Declaration on Combating Terrorism (adopted 25 March 2004) and the EU Plan of Action on Combating Terrorism (passed by the European Council on 17-18 June 2004), Latvia has introduced a number of provisions in its legislation aimed at promoting practical cooperation among EU Member States in combating terrorism and is participating in the preparation of other EU regulations relating to the exchange of information, witness protection and funding for the fight against terrorism.

The Judicial System

Latvia's three-tier judicial system is independent. The first level comprises 35 district (city) courts as the courts of first instance, with six regional courts acting as courts of appeal and courts of first instance for certain civil, criminal cases and administrative cases comprising the second level and the Supreme Court comprising the third level. The administrative courts were introduced to the Latvian judicial system in 2004. They consider cases relating to the exercise of executive power by state, municipal and other public institutions which relate to the rule of law and public law issues.

The highest court in Latvia is the Republic of Latvia's Supreme Court (the "**Supreme Court**"). The Supreme Court comprises two separate judicial bodies: the Senate, which has authority to accept cassation appeals in all types of cases and is the final and supreme judicial body in Latvia, and the

Supreme Court Chambers. The total number of Supreme Court justices is established by Saeima, upon the recommendation of the Board of Justice. The total number of justices in the Senate and the Supreme Court Chambers is determined by the Board of Justice, upon the recommendation of the Chief Justice. The Chief Justice is selected from among the justices for confirmation by the Saeima and serves a seven-year term. The current Chief Justice has been in office since 2008.

In addition, the Constitutional Court of Latvia consists of seven justices who are elected by the Saeima for a 10-year term. This court is authorised to hear cases involving legislative acts and international agreements, including cases relating to the compliance of such acts and agreements with law and the Constitution. The Constitutional Court hears cases following the filing of a petition by an eligible party in accordance with the Constitution. Members of the Constitutional Court elect a Chairman for a three-year term who presides at sessions of the Constitutional Court, organises the work of the Court and represents the Court.

International Relations

Participation in global and regional organisations, especially membership of the EU, NATO, the IMF and other European organisations (such as the Council of Europe and the Organisation for Security and Co-operation in Europe) is becoming increasingly important in terms of meeting new challenges and is advantageous for Latvia, allowing Latvia to contribute to the resolution of specific problems while also representing its national interests in global politics.

Latvia became a member state of the UN in 1991, thus creating a global dimension for Latvian foreign policy. By acceding to international declarations such as the Millennium Development Declaration and the UN Cairo Declaration, Latvia has demonstrated its readiness to become involved in the resolution of global problems.

In October 2010, Latvia was elected to the United Nations Economic and Social Council ("**ECOSOC**") for the period 2011 to 2013. As an ECOSOC member, Latvia will be expected to participate in the decision-making process relating to current international matters, including the implementation of the Millennium Development Goals.

Membership of the WTO, which was achieved in 1998, has contributed to the development of Latvia's economy. Latvia continues to cooperate actively with the Organisation for Economic Co-operation and Development (the "**OECD**") with a view to eventual accession to the OECD.

By joining NATO and the EU in 2004, Latvia achieved its strategic goals in terms of international institutional membership. Ensuring and developing relations with EU Member States and institutions plays a major role in Latvia's foreign policy; see "– *EU Membership*".

Latvia has participated in the UN-mandated and NATO-led International Security Assistance Force ("**ISAF**") mission in Afghanistan and Latvia has also contributed to NATO training programmes in Iraq.

Latvia has been a member of the Schengen Area since 21 December 2007. This allows the free movement of people and goods within the Schengen zone, comprising 25 European countries, without any passport controls or customs formalities.

Latvia seeks good relations with its neighbouring countries, both at a bilateral level and through membership of regional organisations such as the Council of Baltic Sea States. Other institutions that have been jointly established by Latvia, Lithuania and Estonia, such as the Baltic Assembly and the Baltic Council of Ministers, have also contributed to harmonising the foreign policies of these Baltic States and to promoting practical cooperation between them.

Active bilateral and multilateral dialogue with the Nordic countries is also important to Latvia as a means of enhancing long-term cooperation among the Baltic and Nordic countries, sharing participation in the implementation of regional programmes, projects and initiatives and strengthening the region's influence at a global level. The EU Strategy for the Baltic Sea region provides another opportunity to increase regional competitiveness and sustainable growth.

At the bilateral level, relations between Latvia and Russia are based on pragmatic foundations and cooperation, with particular emphasis on the need to resolve issues which affect both countries (for instance, the border demarcation), and to strengthen the role of the Baltic Sea region. In December 2010, the President of Latvia paid the first official visit to Russia by a Latvian President since 1994. Latvia also promotes its interests with regard to Russia within the framework of EU-Russia relations, by participating actively in the work of the relevant EU institutions, dealing with specific issues and developing a joint strategy of relations.

Latvia regards the United States of America as a strategic partner and ally and believes that it is important to maintain an ongoing dialogue with the United States on both traditional and new security challenges, including energy security and areas such as money laundering and international terrorism.

EU Membership

As a Member State of the EU, Latvia actively participates in the EU decision-making process at meetings of the European Council and the Council of Ministers and in working groups of the European Commission, the Council of Ministers and the Committee of Permanent Representatives. Latvia is also represented in the European Parliament, the Committee of Regions and the European Economic and Social Committee. On 8 May 2008, Latvia became the 12th EU Member State to ratify the Treaty of Lisbon. Latvia will assume the rotating presidency of the Council of Ministers during the first half of 2015.

After the European Parliamentary elections of 2009, Latvia has eight parliamentary seats in the European Parliament. The Group of the European People's Party (Christian Democrats) holds the largest number of the Latvian seats in the European Parliament with three seats. The Group of the Alliance of Liberals and Democrats for Europe, the Group of the Progressive Alliance of Socialists and Democrats in the European Parliament, the Confederal Group of the European United Left – Nordic Green Left, the Group of the Greens/European Free Alliance and the European Conservatives and Reformists each hold one seat.

As membership in the European Economic and Monetary Union and the adoption of the single currency are both required by the terms of Latvia's accession to the EU and have been set as objectives by the Latvian government, Latvia is in a continuing dialogue with the EU on these matters. As a Member State, Latvia is subject to multilateral surveillance by the Council of Ministers. Latvia is obliged to prepare an annual Convergence Programme covering fiscal policy, Latvia's main assumptions underlying its economic outlook and an assessment of economic policy measures and their budgetary impact. This information must cover the current and previous year and include forecasts for at least the next three years.

Latvia's membership in the EU has resulted in a major inflow of EU funds. The total amount of financing allocated to Latvia for the period between 2007 and 2013 equals €6.6 billion, of which €4.6 billion is intended for cohesion and structural funds, and €2.0 billion is intended for agricultural development.

The table below sets out the inflow of EU funds to Latvia for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006	2007	2008	2009	2010
			(LVL)		
Pre-accession funds[1]	21,766,013	368,715	226,631	15,094	0
Structural funds[2]	44,836,650	214,537,225	143,115,312	245,437,315	208,333,548
Cohesion policy[3]	73,410,700	123,117,324	113,613,189	97,186,884	143,565,547
Common agricultural policy[4]	95,964,070	106,042,840	161,052,090	165,037,291	198,920,370
Transition policy	20,469,710	4,594,649	1,748,517	557,639	0
Other funds	7,871,610	9,309,363	7,865,347	13,874,782	27,233,896
Non-EU facilities	—	858,524	3,659,623	8,647,226	22,113,430
Repaid to EU	—	—	(4,219,000)	(6,244,316)	(1,640,003)
Total	**264,318,753**	**458,828,640**	**427,061,709**	**524,511,915**	**598,526,788**

Source: The Treasury

Notes:

(1) Pre-accession funds help to finance a Member State's expenditure on conforming its laws to the existing body of European Community law and on development in general.

(2) Structural funds allow the EU to grant financial assistance to help resolve a Member State's structural economic and social problems.

(3) Cohesion policy funds are designed to offset the burden of the single market for the less-favoured Member States or regions of Member States.

(4) Common agricultural policy funds represent agricultural subsidies paid to a Member State.

The table below sets out the use of EU funds by Latvia for the period between 1 January 2006 and 31 December 2010.

	(LVL)
Current expenditure	1,975,479,621
Capital expenditure	468,634,173
Funds received but not yet spent	170,865,989
Total	**2,273,247,805**

Source: The Treasury

The table below summarises Latvia's own resource payments to the EU for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010 and for the period from 1 January 2011 to 31 March 2011.

	2006	2007	2008	2009	2010	2011[1]
			(LVL millions)			
GNI[2]	70.4	82.4	94.8	107.7	90.7	32.8
VAT[3]	17.6	24.6	24.8	15.8	9.7	5.1
UK correction[4]	8.1	10.5	13.6	10.8	7.6	2.0
Traditional own resources[5]	15.6	21.6	20.4	13.1	11.9	3.9
Agricultural levies	0.7	1.0	1.1	0.5	—	—
Customs duties	14.7	19.4	18.7	12.0	11.9	3.9
Sugar levies	0.2	1.2	0.6	0.6	—	—
Total	**111.7**	**139.1**	**153.5**	**147.4**	**119.9**	**43.8**

Source: Ministry of Finance

Notes:

(1) From 1 January 2011 to 31 March 2011.

(2) Gross National Income, charged at a uniform rate of 0.73 per cent. of each Member State's gross national income.

(3) Charged at 0.3 per cent. of Latvia's VAT revenue (harmonised to reflect VAT rate differences between Member States).

(4) Reflecting Latvia's contribution to the EU compensation paid to the UK in respect of its lower agricultural fund receipts.

(5) This represents duties that are charged on imports of relevant products into Latvia from a non-EU state.

ECONOMY OF LATVIA

Background

During 2006 and 2007, Latvia experienced rapid growth with real GDP growing by 12.2 per cent. in 2006 and 10.0 per cent. in 2007. These growth rates were principally driven by private consumption and investment, which was largely based on a substantial inflow of foreign capital. In 2008 and 2009, Latvia's economy was significantly adversely affected by the global economic crisis which commenced at the end of 2007, with real GDP falling by 4.2 per cent. in 2008 and by 18.0 per cent. in 2009. Since 2009, Latvia's economy has begun to recover, with real GDP growing in each quarter since the last quarter of 2009, although on an annual basis and reflecting the steep decline in 2009 Latvia's real GDP for 2010 was 0.3 per cent. lower than it was for 2009.

Impact of the Global Economic Crisis and Resolution

The global economic crisis significantly adversely impacted Latvia's economy. Comparing the last quarter of negative real growth (the fourth quarter of 2009) with the last quarter of positive real growth (the fourth quarter of 2007), real GDP decreased by 23.8 per cent., with the steepest period of decline being the first six months of 2009. Although the economic downturn continued in the second six months of 2009, the rate of negative real growth slowed significantly and slight increases in both exports and manufacturing output became apparent.

Positive growth on a quarter-on-quarter basis began in the last quarter of 2009, with real GDP growing by 0.1 per cent. In 2010, real GDP grew by 0.2 per cent., 0.6 per cent., 1.6 per cent. and 1.1 per cent., respectively, in the four quarters of the year, in each case compared to the previous quarter, although, on an annual basis, in 2010, real GDP decreased by 0.3 per cent. in comparison to 2009. Latvia's real GDP grew by 0.3 per cent. in the first quarter of 2011 compared to the fourth quarter of 2010.

Economic sentiment and confidence in Latvia were both adversely affected by developments commencing in early 2007. The general economic sentiment indicator in Latvia showed a declining trend on a quarter-by-quarter basis since March 2007 (when it stood at a positive 15 per cent., indicating that 15 per cent. more respondents had a positive outlook than a negative outlook) to March 2009 (when it stood at a negative 48 per cent.). Since March 2009, economic sentiment in Latvia has steadily improved and, at December 2010, it stood at a negative 9 per cent. Confidence indicators in the industry, retail trade, services, construction and consumer sectors have all shown similar trends; see "*Recent Economic Developments*".

The economic downturn also significantly adversely affected the labour market. By the end of 2009, the registered unemployment rate (being the number of unemployed non-working persons aged 15 to 62 actively seeking a job who are registered with the State Employment Agency expressed as a percentage of the active population (which in turn is defined as employed persons and persons actively seeking a job)) had increased from 4.9 per cent. in 2007 to 16.0 per cent. and the employment rate (defined as the number of employed persons in the 15 to 64 years age group expressed as a percentage of the total population) had fallen from 68.4 per cent. in 2007 to 61.1 per cent. In 2010, the registered unemployment rate fell to 14.3 per cent. although the employment rate also fell, to 59.4 per cent. The 2010 information is estimated.

The global financial crisis did, however, positively affect Latvia's foreign trade balance and its current account balance of payments. In 2009, Latvia's imports fell by 37.7 per cent. compared to 2008. Latvia's exports fell by 19.2 per cent. in 2009 compared to 2008. As a result, Latvia's negative foreign trade balance fell significantly, from LVL 2,862.4 million in 2008 to LVL 931.6 million in 2009, and represented 7.1 per cent. of GDP in 2009. The foreign trade balance continued to improve in 2010 as exports increased faster than imports, with the deficit being 6.5 per cent. of GDP in that year. Latvia's current account balance of payments was additionally significantly affected by a slowdown in the inflow of foreign investments from the second half of 2007 due to the global crisis and, as a result, the current account balance moved from a deficit equal to 24.8 per cent. of GDP in the third quarter of 2007 to a surplus equal to 10.7 per cent. of GDP in the fourth quarter of 2009. In 2010, the current account balance showed a surplus equal to 3.6 per cent. of GDP.

In addition, inflation (measured in terms of changes in the CPI) fell from a peak of 17.9 per cent. in May 2008 to a low of minus 4.2 per cent. in February 2009 (in each case when compared with the corresponding period of the previous year). The decrease in consumer prices principally reflected reduced private consumption (as a result of increased unemployment, wage reductions and other factors) and falling global energy and food prices. Since the end of 2009, inflation began to increase gradually as a result of increasing world energy and food prices and domestic indirect tax rate increases.

Financial Assistance

Deteriorating economic conditions in Latvia in 2008 and a banking crisis at the end of that year significantly adversely affected State budget revenues and, as a result, Latvia sought financial assistance from the IMF and other international bodies towards the end of 2008. The IMF Standby Arrangement which Latvia entered into in December 2008 was part of the wider financial assistance package agreed with the EU, the World Bank, the EBRD and a number of Nordic and other EU countries. In addition to the IMF Standby Arrangement of up to SDR1.5 billion, the EU agreed to provide a loan of up to €3.1 billion, five Nordic countries (Sweden, Denmark, Finland, Norway and Estonia) agreed to provide a loan of up to €1.9 billion, the World Bank agreed to provide a loan of up to about €400 million, the Czech Republic and Poland agreed to provide a loan of up to €300 million and the EBRD agreed to provide financial assistance in the amount of around €100 million, bringing the total financial assistance package to approximately €7.5 billion (equal to approximately U.S.$10.5 billion). As at 30 April 2011, €4.4 billion in financial assistance had been disbursed to Latvia. Although (excluding the Loan Agreement with the Nordic countries which remains undrawn) €1.2 billion remains available under the programme funds, no further borrowings within the programme are planned in 2011, except that the remaining €100 million of the loan from the World Bank may be drawn. See "*Indebtedness – Financial Assistance from International Lenders*".

Economic Reform Programme

As part of the financial assistance package, Latvia agreed to implement an economic reform programme whose principal objectives were to arrest the immediate liquidity crisis and then to restructure Latvia's economy and improve its competitiveness to reach sustainable GDP growth and a balanced budget as soon as practicable, while maintaining the exchange rate peg which is a key policy of both the Latvian government and the Bank of Latvia. The programme included a range of measures to stabilise and strengthen the financial sector as well as substantial fiscal tightening to reduce financing needs and foster real depreciation.

The economic reform programme also aimed to develop structural reforms and other policies to increase competitiveness and facilitate external adjustment, through tax incentives as well as improved property registration, construction approval and insolvency and liquidation processes.

Recent Economic Developments

Economic sentiment and confidence in Latvia fell significantly during the financial crisis and as a result of the early stages of the economic reform programme in Latvia that followed. The low point for general economic sentiment in Latvia was March 2009 (when 48 per cent. more respondents had a negative outlook than a positive outlook). Since March 2009, general economic sentiment in Latvia has improved with confidence indicators in the industry, construction, retail trade, services and consumer sectors showing similar trends.

The table below shows economic sentiment and confidence indicators (seasonally adjusted) by sector in the period March 2007 to December 2010.

	2007				2008			
	March	June	September	December	March	June	September	December
				(per cent.)[(1)]				
Economic sentiment	**15**	13	11	7	(1)	(10)	(15)	(32)
Industry	**9**	6	2	0	(8)	(13)	(18)	(29)
Construction	**17**	12	11	0	(14)	(31)	(46)	(59)
Retail trade	**23**	19	19	11	5	(1)	(8)	(27)
Services	**18**	16	17	14	6	(3)	(6)	(22)
Consumers	**(5)**	(4)	(9)	(14)	(18)	(27)	(31)	(48)

	2009				2010			
	March	June	September	December	March	June	September	December
	(per cent.)[(1)]							
Economic sentiment	(48)	(42)	(39)	(31)	(19)	(12)	(10)	(9)
Industry[(2)]	(36)	(28)	(26)	(19)	(8)	(5)	(7)	(12)
Construction	(75)	(77)	(73)	(67)	(61)	(51)	(45)	(40)
Retail trade	(33)	(28)	(25)	(16)	(6)	9	4	3
Services	(44)	(41)	(36)	(31)	(20)	(8)	1	8
Consumers	(51)	(50)	(51)	(52)	(32)	(27)	(28)	(26)

Source: Central Statistical Bureau

Notes:

(1) Presented as ratio of positive to negative.

(2) Not seasonally adjusted in the period March 2010 to December 2010.

The table below shows selected economic indicators as at the end of each quarter in the years ended 31 December 2007, 2008, 2009 and 2010.

	2007				2008			
	31 March	30 June	30 September	31 December	31 March	30 June	30 September	31 December
Household consumption	24.7	20.2	17.1	1.6	1.9	(1.9)	(6.2)	(13.3)
Retail trade turnover	23.1	21.9	14.8	5.2	(3.2)	(4.4)	(7.6)	(13.6)
First registered passenger cars	53.4	23.3	0.6	(20.6)	(39.1)	(46.0)	(50.6)	(62.4)

	2009				2010			
	31 March	30 June	30 September	31 December	31 March	30 June	30 September	31 December
Household consumption	(22.3)	(26.7)	(27.2)	(19.6)	(6.2)	(2.4)	2.9	5.2
Retail trade turnover	(23.5)	(27.2)	(28.7)	(28.8)	(12.9)	(5.1)	2.2	7.2
First registered passenger cars	(75.7)	(71.9)	(66.5)	(50.2)	(13.0)	36.2	81.7	108.9

Source: Central Statistical Bureau

Note:

(1) Growth measured against the equivalent period of the preceding year.

Gross Domestic Product

Latvia's annual real GDP grew by 12.2 per cent. in 2006 and by 10.0 per cent. in 2007 before declining by 4.2 per cent. in 2008, 18.0 per cent. in 2009 and 0.3 per cent. in 2010, in each case compared to the previous year. Latvia's real GDP declined on a quarter-on-quarter basis from and including the first quarter of 2008 until and including the third quarter of 2009, but has been growing on a quarterly basis since the fourth quarter of 2009. Latvia's 2011 budget (as amended on 14 April 2011) projects nominal GDP for 2011 of LVL 13,415.9 million and real GDP for 2011 of LVL 7,029.3 million (based on an assumed inflation rate of 3.5 per cent.), an increase of 3.3 per cent. in real terms from the LVL 6,805.0 million real GDP figure for 2010.

Growth in nominal GDP in 2006 and 2007 was principally driven by private consumption, which showed real growth rates of 21.2 per cent. in 2006 and 14.8 per cent. in 2007, and by investment, with gross fixed capital formation growing by 16.4 per cent. in 2006 and 7.5 per cent. in 2007 in real terms. By contrast public consumption grew at less than 5 per cent. in real terms in each of 2006 and 2007.

The global financial crisis severely affected the economy of Latvia in 2008 and subsequent years. The effects of the financial crisis were intensified by the unbalanced position of the Latvian external sector, which had developed during the previous period of rapid growth. The growth in private consumption and investment, which was more rapid than overall economic growth, was largely based on a substantial inflow of foreign capital and gave rise to a high current account deficit of the balance of payments which in turn increased the vulnerability of the Latvian economy. With the onset of the global financial crisis, financial inflows to Latvia fell significantly leading to rapid declines in private consumption and investment.

The recession in Latvia ended in the fourth quarter of 2009 when real GDP grew by 0.1 per cent. compared to the previous quarter. Although growth continued in each quarter of 2010, reflecting the fact that growth resumed from a very low level, real GDP in 2010 as a whole was still 0.3 per cent. lower than in 2009.

The tables below set out Latvia's nominal GDP determined using the expenditure method in each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010 and the percentage contribution of each sector specified to such GDP.

	2006		2007		2008	
	(LVL millions)	*Contribution (per cent.)*	*(LVL millions)*	*Contribution (per cent.)*	*(LVL millions)*	*Contribution (per cent.)*
Private consumption	7,280.5	65.2	9,196.1	62.2	10,181.3	62.9
Public consumption	1,855.2	16.6	2,574.9	17.4	3,169.8	19.6
Gross fixed capital formation	3,644.1	32.6	4,975.1	33.7	4,748.5	29.3
Changes in inventories	789.9	7.1	994.7	6.7	298.1	1.8
Exports of goods and services	5,014.3	44.9	6,258.7	42.3	6,931.1	42.8
Imports of goods and services	(7,412.3)	(66.3)	(9,219.7)	(62.4)	(9,140.6)	(56.4)
GDP	**11,171.7**	**100.0**	**14,779.8**	**100.0**	**16,188.2**	**100.0**

	2009		2010	
	(LVL millions)	*Contribution (per cent.)*	*(LVL millions)*	*Contribution (per cent.)*
Private consumption	8,053.8	61.6	8,023.1	63.0
Public consumption	2,569.7	19.6	2,186.7	17.2
Gross fixed capital formation	2,806.8	21.5	2,286.3	17.9
Changes in inventories	(153.9)	(1.2)	346.0	2.7
Exports of goods and services	5,741.7	43.9	6,797.2	53.4
Imports of goods and services	(5,935.3)	(45.4)	(6,903.3)	(54.2)
GDP	**13,082.8**	**100.0**	**12,735.9**	**100.0**

Source: Central Statistical Bureau

The tables below set out the real growth rates of each sector specified to Latvia's nominal GDP determined using the expenditure method for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006	2007	2008	2009	2010
			(per cent.)		
Private consumption	21.2	14.8	(5.2)	(24.1)	(0.1)
Public consumption	4.9	3.7	1.5	(9.2)	(11.0)
Gross fixed capital formation	16.4	7.5	(13.6)	(37.3)	(19.5)
Exports of goods and services	6.5	10.0	2.0	(14.1)	10.3
Imports of goods and services	19.4	14.7	(11.2)	(33.5)	8.6
GDP	**12.2**	**10.0**	**(4.2)**	**(18.0)**	**(0.3)**

Source: Central Statistical Bureau

The tables below set out the total and per capita GDP of Latvia for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010, in both current and constant prices.

	2006	2007	2008	2009	2010
			(per cent.)		
Total GDP					
At current prices *(LVL millions)*	11,171.7	14,779.8	16,188.2	13,082.8	12,735.9
At constant prices *(LVL millions)*	7,903.1	8,691.7	8,322.8	6,828.5	6,805.0
Percentage change over previous period (constant prices)	12.2	10.0	(4.2)	(18.0)	(0.3)
Per capita(1)					
At current prices *(LVL)*	4,883	6,494	7,144	5,802	5,688
At constant prices *(LVL)*	3,454	3,819	3,673	3,028	3,039
Resident population					
At beginning of year	2,294,590	2,281,305	2,270,894	2,261,294	2,248,374
Average for the period(2)	2,287,948	2,276,100	2,266,094	2,254,834	

Source: Central Statistical Bureau
Note:
(1) Based on average population for the relevant period.
(2) No average for 2010 is currently available.

Principal Sectors of the Economy

In terms of broad sectoral classification, Latvia's primary sector (agriculture, hunting and forestry; fishing; and mining and quarrying) accounted for 4.7 per cent. of total value added in 2010 compared to 3.9 per cent. in 2006.

The secondary sector (manufacturing; electricity, gas and water supply; and construction) accounted for 21.3 per cent. of the total value added in 2010 compared to 21.6 per cent. in 2006. Within this sector, the share of construction has fallen as a result of the global financial crisis although the share of manufacturing increased significantly in 2010 and the share of utilities increased generally throughout the period.

The tertiary sector (services) accounted for 74.1 per cent. of total value added in 2010. Within the services sector, the main activities are wholesale and retail trade and repairing services; the provision of real estate renting and business services; and a range of public services.

Outside the services sector, the principal contributors to total value added are manufacturing and construction which accounted for 12.2 per cent. and 5.0 per cent., respectively, of total value added in 2010. Manufacturing grew at real rates of 6.2 per cent. in 2006 and 0.5 per cent. in 2007 before falling at real rates of 6.5 per cent. in 2008 and 19.2 per cent. in 2009 and increasing at a real rate of 15.4 per cent. in 2010. Construction grew at real rates of 21.5 per cent. in 2006 and 15.7 per cent. in 2007 before falling at real rates of 2.6 per cent. in 2008, 33.6 per cent. in 2009 and 24.2 per cent. in 2010.

The tables below set out nominal GDP (calculated using the production method) by primary, secondary and tertiary sector (and by each principal sub-sector within those sectors) and the percentage contribution of each sector to total value added for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006	2007	2008	2009	2010
			(LVL millions)		
Primary sector	379.0	521.1	501.7	444.5	532.4
Secondary sector	2,120.5	2,983.4	3,286.5	2,378.1	2,427.8
Manufacturing	1,159.4	1,487.3	1,563.0	1,171.4	1,389.4
Electricity, gas, water supply	235.0	319.2	414.1	425.8	468.4
Construction	726.1	1,176.9	1,309.4	780.8	570.0
Tertiary sector	7,336.2	9,555.2	10,731.5	8,965.9	8,448.6
Trade(1)	2,236.9	2,817.4	2,727.0	1,955.6	2,019.1
Transport, storage and communications	1,126.0	1,334.4	1,546.7	1,341.9	1,426.6
Other commercial services(2)	2,529.1	3,448.3	4,080.1	3,648.3	3,225.4
Public services(3)	1,444.3	1,955.2	2,377.7	2,020.0	1,777.5
Total value added	**9,835.7**	**13,059.7**	**14,519.7**	**11,788.5**	**11,408.8**
Taxes on products (minus subsidies)	1,335.9	1,720.1	1,668.5	1,294.3	1,327.2
Nominal GDP	**11,171.7**	**14,779.8**	**16,188.2**	**13082.8**	**12,735.9**

	2006	2007	2008	2009	2010
			Contribution (per cent.)		
Primary sector	3.9	4.0	3.5	3.8	4.7
Secondary sector	21.6	22.8	22.6	20.2	21.3
Manufacturing	11.8	11.4	10.8	9.9	12.2
Electricity, gas, water supply	2.4	2.4	2.9	3.6	4.1
Construction	7.4	9.0	9.0	6.6	5.0
Tertiary sector	74.6	73.2	73.9	76.1	74.1
Trade(1)	22.8	21.6	18.8	16.6	17.7
Transport, storage and communications	11.5	10.2	10.7	11.4	12.5
Other commercial services(2)	25.7	26.4	28.1	30.9	28.3
Public services(3)	14.7	15.0	16.4	17.1	15.6
Total value added	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source: Central Statistical Bureau

Notes:

(1) Includes wholesale and retail trade, repairing services and hotels and restaurants.

(2) Includes real estate, renting and business activities, financial intermediation and other community, social and personal services activities.

(3) Includes public administration, defence and compulsory social security, education and health and social work.

The tables below set out the real growth rate of each GDP sector and principal sub-sector (calculated using the production method) for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006	2007	2008	2009	2010
			(per cent.)		
Primary sector	(4.1)	10.0	0.5	3.0	3.8
Secondary sector	10.5	6.1	(4.6)	(23.2)	2.1
Manufacturing	6.2	0.5	(6.5)	(19.2)	15.4
Electricity, gas and water supply	3.1	4.4	(2.4)	(7.2)	12.7
Construction	21.5	15.7	(2.6)	(33.6)	(24.2)
Tertiary sector	13.1	10.0	(2.4)	(14.6)	(1.4)
Trade[1]	17.9	14.2	(8.4)	(29.0)	3.2
Transport, storage and communications	5.5	7.0	0.5	(14.8)	3.0
Other commercial services[2]	18.2	11.2	(0.0)	(5.5)	(3.6)
Public services[3]	4.7	3.3	1.3	(6.3)	(7.8)
Taxes on products (minus subsidies)	16.1	17.3	(15.8)	(37.7)	1.2
GDP	**12.2**	**10.0**	**(4.2)**	**(18.0)**	**(0.3)**

Source: Central Statistical Bureau

Notes:

(1) Includes wholesale and retail trade, repairing services and hotels and restaurants.

(2) Includes real estate, renting and business activities, financial intermediation and other community, social and personal services activities.

(3) Includes public administration, defence and compulsory social security, education and health and social work.

Services

The tables below set out a breakdown of the contribution of the services sector (calculated using the production method) to total value added by significant sub-sectors for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006		2007	
	(LVL millions)	*Contribution (per cent.)*	*(LVL millions)*	*Contribution (per cent.)*
Real estate, renting and business activities	1,466.9	14.9	2,108.2	16.1
Wholesale, retail trade; repairing services	2,050.5	20.8	2,577.7	19.7
Transport, storage and communications	1,126.0	11.4	1,334.4	10.2
Public administration and defence; compulsory social security	718.7	7.3	983.1	7.5
Financial intermediation	667.8	6.8	804.5	6.2
Education	441.3	4.5	611.2	4.7
Health and social work	284.3	2.9	361.0	2.8
Hotels and restaurants	186.5	1.9	239.6	1.8
Other community, social and personal service activities	394.4	4.0	535.6	4.1
All services	**7,336.2**	**74.6**	**9,555.2**	**73.2**

	2008		2009		2010	
	(LVL millions)	*Contribution (per cent.)*	*(LVL millions)*	*Contribution (per cent.)*	*(LVL millions)*	*Contribution (per cent.)*
Real estate, renting and business activities..........	2,533.4	17.4	2,354.5	20.0	2,157.8	18.9
Wholesale, retail trade; repairing services	2,486.1	17.1	1,792.9	15.2	1,868.1	16.4
Transport, storage and communications............	1,546.7	10.7	1,341.9	11.4	1,426.6	12.5
Public administration and defence; compulsory social security	1,169.9	8.1	980.7	8.3	871.3	7.6
Financial intermediation..	873.3	6.0	721.7	6.1	535.7	4.7
Education........................	744.6	5.1	649.7	5.5	538.4	4.7
Health and social work....	463.2	3.2	389.6	3.3	367.8	3.2
Hotels and restaurants.....	240.9	1.7	162.7	1.4	151.0	1.3
Other community, social and personal service activities.......................	673.5	4.6	572.1	4.9	531.9	4.7
All services	**10,731.5**	**73.9**	8,965.9	76.1	8,448.6	**74.1**

Source: Central Statistical Bureau

The tables below set out a breakdown of the real rates of growth of each significant sub-sector within the services sector (calculated using the production method) for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006	2007	2008	2009	2010
			(*per cent.*)		
Real estate, renting and business activities	17.6	11.4	1.5	(0.1)	(1.5)
Wholesale, retail trade; repairing services	17.8	14.6	(8.3)	(28.7)	3.3
Transport, storage and communications	5.5	7.0	0.5	(14.8)	3.0
Public administration and defence; compulsory social security	5.8	3.4	0.2	(7.2)	(11.3)
Financial intermediation	22.9	9.3	(8.8)	(12.6)	(10.5)
Education	4.2	3.0	0.5	(7.4)	(5.0)
Health and social work	2.8	3.9	5.3	(2.3)	(3.5)
Hotels and restaurants	20.0	8.6	(10.7)	(33.9)	0.8
Other community, social and personal service activities	14.4	13.2	5.5	(18.6)	(4.9)
Services total..................................	**13.1**	**10.0**	**(2.4)**	**(14.6)**	**(1.4)**

Source: Central Statistical Bureau

Within the services sector, the principal sub-sectors by contribution are real estate, renting and business activities (‘‘**real estate**’’); wholesale and retail trade and repairing services (‘‘**trade**’’); transport, storage and communications (‘‘**transport**’’); and public administration and defence and compulsory social security (‘‘**public administration**’’). Together, these activities accounted for 73.1 per cent. of total services in 2006, 73.3 per cent. of total services in 2007, 72.1 per cent. of total services in 2008, 72.2 per cent. of total services in 2009 and 74.9 per cent. of total services in 2010.

Real estate

The real estate sector developed rapidly in the years before 2008, due to an increase in available credit and levels of demand which substantially exceeded supply. Due to the global financial crisis, the demand for real estate has decreased since 2008 as evidenced by a significant decline in apartment prices in Riga since early 2007. However, growth rates for the real estate sector have remained above average in comparison to growth rates for the services sector as a whole, principally as result of the fact that demand for business services such as tax advisory, information technology and security services has remained steady as these services are less sensitive to declining economic conditions. Reflecting this trend, the contribution of the real estate sector to Latvia's total value added has grown from 14.9 per cent. in 2006 to 20.0 per cent. in 2009 before falling to 18.9 per cent. in 2010 as other sectors recovered.

In the World Bank's *Doing Business* 2011 report, Latvia was ranked 24 out of 183 countries on ease of doing business and ninth among EU Member States. Latvia is ranked among the 85 per cent. of countries surveyed which have made it easier for local entrepreneurs to operate in the past five years.

Trade

The table below shows a breakdown of trade (calculated using the production method) for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006	2007	2008	2009	2010[(1)]
			(LVL millions)		
Wholesale trade	1,060.3	1,167.0	1,206.2	818.5	
Retail trade	640.7	1,041.7	940.6	761.6	
Repairing services	349.5	369.1	339.3	212.8	
Wholesale and retail trade and repairing services	**2,050.5**	**2,577.7**	**2,486.1**	**1,792.9**	**1,868.1**

Source: Central Statistical Bureau

Note:

(1) Only total data is currently available for 2010.

For the purposes of calculating GDP, wholesale trade is defined as an intermediate process in the distribution of merchandise, whereas retail trade is defined as the final process in the distribution of merchandise. Repairing services comprise the maintenance and repair of goods associated with wholesale and retail trade.

Both wholesale trade and repairing services grew strongly in real terms in 2006, grew slightly in real terms in 2007, declined slightly in real terms in 2008 and declined significantly in real terms in 2009. By contrast, in real terms retail trade grew strongly in 2006 and 2007, grew slightly in 2008 and declined significantly in 2009. As a result, as a percentage of trade as a whole, retail trade was 31.2 per cent. in 2006 and 42.5 per cent. in 2009; wholesale trade was 51.7 per cent. in 2006 and 45.7 per cent. in 2009; and repairing services was 17.0 per cent. in 2006 and 11.9 per cent. in 2009.

In overall terms, trade grew strongly in real terms in 2006 and 2007, fell in 2008 and significantly in 2009 and then grew slightly in real terms in 2010. These trends reflected the fact that consumer demand was negatively affected in 2009 by declining disposable income as a result of increased unemployment, wage cuts and tax increases as well as by the effects of the liquidity crisis and reduced bank lending which adversely impacted the consumption of durable goods. During 2010, retail trade turnover increased by 7.9 per cent. (in real terms on a seasonally adjusted basis), although for 2010 as a whole retail turnover was 2 per cent. lower than in 2009. Since August 2010, retail turnover has exceeded the level of the corresponding month of the previous year.

In terms of real growth rates, the wholesale and retail trade and repairing services sector outperformed services as a whole in 2006, 2007 and 2010 but was significantly more adversely affected in 2008 and 2009.

Transport

Transport contributed 11.5 per cent. to Latvia's total value added in 2006, 10.2 per cent. in 2007, 10.7 per cent. in 2008, 11.4 per cent. in 2009 and 12.5 per cent. in 2010. In terms of real growth, transport grew in 2006, 2007 and 2008 (by 5.5 per cent., 7.0 per cent. and 0.5 per cent., respectively), fell by 14.8 per cent. in 2009 and grew by 3.0 per cent. in 2010, in each case compared to the previous year. Certain freight transport statistics are set out below under "– *Infrastructure*".

Public administration

Public administration contributed 7.3 per cent. to Latvia's total value added in 2006, 7.5 per cent. in 2007, 8.1 per cent. in 2008, 8.3 per cent. in 2009 and 7.6 per cent. in 2010. In terms of real growth, public administration grew by 5.8 per cent., 3.4 per cent. and 0.2 per cent. in 2006, 2007 and 2008, respectively, and fell by 7.2 per cent. in 2009 and 11.3 per cent. in 2010, in each case compared to the previous year.

Since Latvia's accession to the EU, real growth rates for the public administration sector have been lower than those for the services sector as a whole. However, in 2008 and 2009, the percentage of Latvia's total value added attributable to the public administration sector increased reflecting the fact that this sector is not as sensitive to global economic conditions as certain other services sectors. See also "*Public Finance – Impact of the Global Financial Crisis on Latvia's Budgets for 2009, 2010 and 2011*" for a discussion of budget cuts affecting the public sector since 2009.

Financial intermediation

Financial intermediation contributed 6.8 per cent. to Latvia's total value added in 2006, 6.2 per cent. in 2007, 6.0 per cent. in 2008, 6.1 per cent. in 2009 and 4.7 per cent. in 2010. The real growth rate for this sector was 22.9 per cent. in 2006 and 9.3 per cent. in 2007. Since 2007, the financial intermediation sector has declined at real rates of 8.8 per cent. in 2008, 12.6 per cent. in 2009 and 10.5 per cent. in 2010, in each case compared to the previous year.

In 2008, bank lending in Latvia slowed reflecting increased reserve requirements imposed by the Bank of Latvia in response to concerns about the overheating of the economy and reduced availability of finance to Latvian banks due to concerns about Latvia's economic vulnerability. Most Latvian banks are owned by non-Latvian groups and the only significant Latvian-owned bank, JSC Parex banka (**Parex Bank**), was nationalised in late 2008. In 2009, the level of financial intermediation fell compared to the equivalent period in the previous year as slackening economic activity led to lower levels of lending and other banking services. In 2010, the macroeconomic and financial environment improved which has had a positive impact on the financial intermediation sector. The core banking business of Parex Bank was transferred to a newly-established bank, JSC Citadele banka (**Citadele Bank**), in mid-2010, leaving Parex Bank with the troubled assets; see "*Monetary and Financial System – Financial Sector Supervision*". However, banks' lending continues to fall as a result of banks' deleveraging their balance sheets as well as reduced demand for credit from corporations and households. In addition, a lack of sustainable preconditions for lending recovery and write-offs of bad loans have also contributed to the decline in lending.

Education and health

Together, education and health and social work contributed 7.4 per cent. to Latvia's total value added in 2006 and in 2007, 8.3 per cent. in 2008, 8.8 per cent. in 2009 and 7.9 per cent. in 2010. In terms of real growth, education grew in the period between 2006 and 2008 although the rate of growth slowed in 2007 and was only 0.5 per cent. in 2008. Education declined in real terms by 7.4 per cent. in 2009 and by 5.0 per cent. in 2010, in each case compared to the previous year. The health and social work sub-sector grew in real terms between 2006 and 2008 with the rate of growth in 2008 being 5.3 per cent. as compared to 3.9 per cent. in 2007. Health and social work declined by 2.3 per cent. in real terms in 2009 and by 3.5 per cent. in 2010, in each case compared to the previous year.

Manufacturing

The tables below set out the contribution of manufacturing to Latvia's total value added, as well as the real growth rate in manufacturing (in each case, calculated using the production method) for each of the years ended 31 December 2006, 2007, 2008 and 2009 and as at 30 November 2010.

	2006	2007	2008	2009	2010
Manufacturing *(LVL millions)*	1,159.4	1,487.3	1,563.0	1,171.4	1,389.4
Contribution *(per cent.)*	11.8	11.4	10.8	9.9	12.2
Real growth rate *(per cent.)*	6.2	0.5	(6.5)	(19.2)	15.4

Source: Central Statistical Bureau

Latvia's industrial strength is principally in labour-intensive sectors such as wood processing, the food industry, the production of metal articles, the chemical industry and the paper industry, which together constituted 74.8 per cent. of the manufacturing sector's value added in 2010.

The table below shows an estimate by the Ministry of Economics of the structure of manufacturing by value added in the year ended 31 December 2010 and changes in production volumes in manufacturing in each of the years ended 31 December 2007, 2008 and 2009 and for the 11 months ended 30 November 2010.

	Structure	Changes in production volumes			
	2010	2007	2008	2009	2010(1)
	(per cent.)		*(per cent.)*		
Wood processing	26.3	(6.0)	(12.1)	2.6	29.2
Food industry	18.6	1.3	(5.3)	(16.5)	(2.9)
Metals and metal articles	11.3	11.5	1.8	(23.6)	21.4
Chemical, rubber, plastics and pharmaceuticals	9.4	3.1	(2.6)	(18.4)	7.1
Paper industry and publishing	9.2	0.2	(4.2)	(15.8)	19.5
Light industry	4.9	0.3	(11.0)	(37.6)	14.7
Machinery and equipment	4.5	5.0	12.2	(7.6)	16.1
Non-metallic mineral products	4.2	(17.1)	(5.6)	(34.3)	8.8
Transport vehicles	4.1	10.7	8.1	(48.8)	41.3
Electrical and optical equipment	3.2	3.8	4.5	(26.5)	27.6
Other industries	4.3	3.0	(8.0)	(18.8)	(3.2)
Total	**100.0**	0.3	(4.7)	(18.0)	14.1

Source: Ministry of Economics

Note:

(1) January to November only.

In the wood industry, declining production in 2007 and 2008 reflected decreased demand in Europe for processed wood products in those years. Approximately 75 per cent. of the wood processing industry's production is exported, principally to EU States. The decline in the food industry began at the end of 2007 and reflected both weaker domestic and export demand. Approximately 75 per cent. of the goods produced by the food industry are sold in the domestic market. The majority of the metal and metal products produced in Latvia are exported, principally to EU countries, and demand in these markets for these products did not significantly decline until mid-2008. In both the chemical and paper industries, production volumes declined in 2008 and 2009 before recovering in 2010. Around 75 per cent. of Latvia's chemical, rubber, plastics and pharmaceutical production is exported. Reflecting the recessions in Latvia, more than half of Latvia's paper production was exported in 2010 compared to less than 40 per cent. in 2007.

The general recovery in production volumes in most industries in 2010 reflects the fact that from the second half of 2009, many of Latvia's trade partner countries began to experience economic growth. This increase in external demand provided a positive growth stimulus to Latvian producers.

The expansion of export opportunities and a rise in competiveness due to increasing external demand is the principal reason for the increase in the production volume of manufacturing overall which, in November 2010, was 15.7 per cent. higher than in November 2009. The total revenues from manufacturing sales in the first 11 months of 2010 were 16.2 per cent. higher than in the corresponding period of 2009.

Construction

The tables below set out the contribution of construction to Latvia's total value added, as well as the real growth rate in construction, (in each case, calculated using the production method) for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006	2007	2008	2009	2010
Construction *(LVL millions)*	726.1	1,176.9	1,309.4	780.8	570.0
Contribution *(per cent.)*..................	7.4	9.0	9.0	6.6	5.0
Real growth rate *(per cent.)*	21.5	15.7	(2.6)	(33.6)	(24.2)

Source: Central Statistical Bureau

The construction sector grew strongly in real terms in 2006 and 2007, driven by both residential and commercial private construction in turn boosted by the ready availability of bank credit. In addition, construction was also boosted by public infrastructure projects, including port improvements, road repairs and sewage processing works, many of which were supported by EU financing. Construction contracted in real terms in each of 2008, 2009 and 2010 as bank financing ceased to be readily available as a result of the liquidity crisis in Latvia.

Primary sector

The primary sector accounted for between 3.5 per cent. and 4.7 per cent. of Latvia's total value added in the period from 2006 to 2010. Notwithstanding the global financial crisis, the real growth rate in the primary sector was 3.0 per cent. in 2009 and 3.8 per cent. in 2010. Forests cover about 45 per cent. of Latvia and are the country's most important natural resource, while wood production is one of Latvia's principal exports. Agriculture plays a considerable role as a source of employment and provides additional income for many families. According to the 2001 agricultural census, there were 180,263 farmsteads of all sizes spread over 2.2 million hectares of land, giving an average farm size of around 20 hectares. According to the provisional results of the 2010 agricultural census, there were 1.6 million hectares of managed agricultural land and the average farm size has increased by 15 per cent. Between 2001 and 2010, the total area of arable land in the country has decreased by 10 per cent. and 2,800, or 3 per cent., of the surveyed farms have ceased to be engaged in agriculture. The main reasons for this are the use of what was previously agricultural land for forestry and construction.

Tourism

The government is targeting tourism in Latvia as one of its priority industries for development. A new tourism marketing strategy for 2010-2015 has been developed by the Latvian Tourism Development Agency which focuses on specific markets considered to have high tourist potential in order to increase the efficiency of Latvian tourism promotion. Latvia is also considering ways to reduce the administrative burden for entrepreneurs operating in the tourist sector and to seek EU structural funding for tourism development.

Between 2006 and 2008, the number of border crossings by non-resident travellers in Latvia grew from 4.6 million to 5.5 million with the total expenditure of such travellers growing from LVL 266.2 million in 2006 to LVL 403.2 million in 2008. In 2009, the number of border crossings by non-resident travellers in Latvia was 4.7 million, approximately 14.5 per cent. lower than in the previous year, and the total expenditure of those travellers was LVL 344.1 million, approximately 14.7 per cent. lower than in 2008. In 2010, the number of non-resident travellers in Latvia reached 5.0 million, a 6.7 per cent. increase over 2009. The total expenditure of those travellers declined slightly in 2010, to LVL 336.9 million.

Inflation

Between 2006 and 2008, inflation (as measured by changes in the CPI) in Latvia increased sharply as a result of high domestic demand fuelled by rapid credit growth. The increase in inflation initially reflected increased import prices and the effect of EU accession (including increases in indirect taxes and heightened inflation expectations). Thereafter, demand-driven pressure and increases in global food and energy prices (which together constitute around 36 per cent. of Latvia's consumer price basket) also became significant contributors to the increase in inflation.

Inflation measured on a year-on-year basis peaked at 17.9 per cent. in May 2008 and then declined steadily until February 2010 (when it was -4.2 per cent.). The decline in inflation reflected both significant weakening of domestic demand as a result of increasing unemployment, wage reductions and other measures taken to combat the effects of the global financial crisis on Latvia, and a decline in global energy and food prices as a result of the deterioration in the global economic environment. Although domestic demand remained fragile in 2010, increases in world energy and food prices in indirect tax rates in Latvia resulted in increased inflation from February 2010. In April 2011, the inflation rate in Latvia was 4.5 per cent. and the 12-month average inflation rate was 1.5 per cent.

The table below sets out the growth rates of the CPI for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006	**2007**	**2008**	**2009**	**2010**
CPI *(annual 12-month average rate of change in per cent.)*	6.5	10.1	15.4	3.5	(1.1)
CPI *(end of year compared to the end of the previous year in per cent.)*	6.8	14.1	10.5	(1.2)	2.5

Source: Central Statistical Bureau

Wages

Between 2006 and 2007 average monthly wages increased sharply in Latvia reflecting economic growth and productivity gains, with average monthly gross wage growth reaching 31.8 per cent. in 2007. In 2008, the rate of increase in average monthly gross wages in Latvia declined to 20.4 per cent. as a result of the economic downturn and average monthly wages fell in both 2009 and 2010.

The average monthly gross wage in 2010 was LVL 445, 7.1 per cent. lower than in 2008 but 11.8 per cent. higher than in 2007.

Although the growth rates in average monthly wages in Latvia since EU accession were among the highest in the EU according to Eurostat, the nominal wage level in Latvia remains low when compared to the EU average. In 2007, the average annual net earnings in the EU-27 countries (being all the existing Member States of the EU), the EU-25 countries (being all the existing Member States of the EU except Romania and Bulgaria which joined in 2007) and in Latvia were €17,797.26, €18,657.51 and €4,151.1, respectively, according to Eurostat. No equivalent data subsequent to 2007 are currently available.

The table below sets out the average monthly gross and net wages in Latvia and their growth rates for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006	**2007**	**2008**	**2009**	**2010**
Average monthly gross wages *(LVL)*	302	398	479	461	445
Gross growth *(per cent.)*	22.8	31.8	20.4	(3.8)	(3.5)
Average monthly net wages *(LVL)*	216	286	350	342	316
Growth *(per cent.)*	22.7	32.4	22.4	(2.3)	(7.6)
Real wage index *(per cent. of previous year)*	115.6	119.9	106.2	94.4	93.5

Source: Central Statistical Bureau

Between January 2006 and January 2011, the minimum monthly wage in Latvia increased from LVL 90 to LVL 200. Over the period between January 2006 and January 2009, the basic personal allowance was increased from LVL 32 to LVL 90, although from 1 July 2009 this was decreased to

LVL 35 as part of the measures taken to combat the effects of the global financial crisis on Latvia. In January 2011, the basic personal allowance was increased from LVL 35 to LVL 45.

The monthly tax allowance for dependent persons has increased from LVL 22 at 1 January 2006 to LVL 70 at 1 January 2011.

Employment

In 2007 and 2008, the number of employed persons between the ages of 15 and 74 in Latvia increased by 2.9 per cent. and by 0.5 per cent., respectively. In addition, in the same period the labour participation rate (which measures the active population (that is, employed persons and persons actively seeking a job) as a percentage of the total population) and the employment rate (being the number of employed persons aged 15 to 64 expressed as a percentage of the total population) both increased. The labour participation rate increased from 71.3 per cent. in 2006 to 74.5 per cent. in 2008 and the employment rate increased from 66.3 per cent. in 2006 to 68.6 per cent. in 2008.

Reflecting the impact of the global financial crisis, unemployment increased rapidly after 2008 and the number of employed persons also decreased. The lowest point was reached in the first quarter of 2010 when the employment rate was 57.7 per cent. and the unemployment rate (being unemployed non-working persons aged 15 to 62 actively seeking a job who are registered with the State Employment Agency as a percentage of the active population) was 17.3 per cent. At the end of 2010, the unemployment rate had improved to 14.3 per cent.

The table below sets out the registered unemployment rate at 31 December in each of 2006, 2007, 2008, 2009 and 2010 and the labour participation rate and the employment rate (by gender) in Latvia in each of 2006, 2007, 2008, 2009 and 2010.

	2006	**2007**	**2008**	**2009**	**2010[(1)]**
Registered unemployment rate, end of period *(per cent.)*[(2)]	6.5	4.9	7.0	16.0	14.3
Labour participation rate, annual data *(per cent.)*[(3)]	71.3	72.9	74.5	73.9	73.2
Employment rate *(per cent.)*[(4)]	66.3	68.4	68.6	61.1	59.3
Men	70.5	72.6	72.0	61.3	59.2
Women	62.3	64.4	65.5	60.9	59.4

Sources: State Employment Agency, Central Statistical Bureau

Notes:

(1) Preliminary.

(2) Unemployed non-working persons aged 15 to 62 actively seeking a job who are registered with the State Employment Agency as a percentage of the active population.

(3) The active population as a percentage of the total population.

(4) Employed persons aged 15 to 64 expressed as a percentage of the total population.

The recession in Latvia impacted male employment more significantly than female employment. The male employment rate fell marginally in 2008 and then decreased from 72.0 per cent. in 2008 to 61.3 per cent. in 2009. The female employment rate increased marginally in 2008 before falling from 65.5 per cent. in 2008 to 60.9 per cent. in 2009. Reflecting Latvia's emergence from recession, in the second and third quarters of 2010 the male employment rate increased faster than the female employment rate. Female unemployment did not change significantly in 2010 while male unemployment fell to 18.4 per cent. in the fourth quarter of 2010 compared to 25.6 per cent. in the first quarter of 2010.

Social Security System

Social insurance

The State social security system guarantees a defined amount of compensation for loss of income in certain situations to persons paying social insurance contributions. The amount of compensation depends on the income from which the amount of the contribution has been calculated. The receipt of social benefits requires contributions to have been made.

The types of social insurance available in Latvia are state pension insurance; unemployment insurance; insurance for work-related accidents and diseases; disability insurance; maternity and sickness insurance; and parents' insurance.

In 2011, an employee insured for all types of social insurance has a compulsory contribution rate of 35.09 per cent. of his gross wage. The total social insurance contribution is split between the employer and the employee at 24.09 per cent. and 11.00 per cent., respectively.

Social insurance contribution payments are calculated based on the likely risks for various groups of tax payers. As a result, certain categories of payers do not make contributions for certain types of insurance. For example, pensioners would not pay for unemployment and disability insurance. These types of exclusions reduce the rate of contribution for many payers.

Benefits and contributions paid are financed by the State Social Security Fund budget and, where necessary, social security costs can also partly be financed by accumulated budget resources. At the end of 2008, the State Social insurance special budget had an accumulated surplus of LVL 951.1 million. With the start of the recession in Latvia and the subsequent fall in wages and rise in unemployment in 2009, the State Social insurance special budget expenditures exceeded revenues in both 2009 and 2010, by LVL 213.1 million and LVL 335.7 million, respectively. For 2011, the State Social insurance special budget is planned with an LVL 237.4 million deficit. The reduced deficit reflects a number of measures taken with a view to balancing the budget and creating a sustainable social insurance framework, including an increase in social contribution; a general reduction in certain types of compensation; and setting upper limits for compensation amounts. In addition, the retirement age will be increased from 62 to 65 years with effect from 2016.

Pension system

In 1996, Latvia commenced a reform of the pension system in order to create greater flexibility with regard to demographic fluctuations and to provide long-term stability given an aging population. The pension system focuses on incentives for the working age population to remain in the labour market as long as possible beyond the minimum retirement age (62 years for both men and women). The pension system in Latvia consists of three non-exclusive tiers:

- Tier I comprises a national defined contribution pension scheme which has been in operation since 1 January 1996. Under this scheme, contributions from socially insured persons are accounted as their pension capital and provide pensions for current pensioners. The pension amount depends on the accumulated pension capital, the age at retirement and the forecasted life expectancy after retiring. The number of socially insured persons in 2010 was approximately one million, or 86.5 per cent. of the economically active population (for this purpose defined as people aged 15 to 74), of which 76.9 per cent. were employees and 1.5 per cent. were self-employed. Expenditures for old age pensions were 8.6 per cent. of GDP in 2010.
- Tier II comprises a State mandatory-funded pension scheme which has been in operation since 1 July 2001. Under this scheme, part of the contributions for old-age pensions made under Tier I (at the total contribution rate of 20 per cent. of gross wages) is invested in capital markets instruments in Latvia and abroad. The number of participants in the Tier II scheme at the end of 2010 was approximately 1.1 million. The net assets of the investment plans of the scheme were 6.6 per cent. of GDP at the end of 2010. In 2010, the contribution rate was 2.0 per cent. of gross wages, although this will increase up to 6.0 per cent. from 2013.
- Tier III comprises a voluntary private pension scheme which has been in operation since 1 July 1998. Under this scheme, voluntary contributions are accumulated and invested by private pension funds. At the end of 2010, there were seven private pension funds operating in Latvia, consisting of six open pension funds and one closed pension fund, offering 21 pension plans to approximately 200,000 participants. In 2010, 38.5 per cent. of total contributions were made by employers and 61.5 per cent. were made by individual participants. The net capital of the scheme was 0.89 per cent. of GDP at the end of 2010.

Infrastructure

Since EU accession, Latvia has been investing in improving its transport infrastructure with the help of EU structural funds. A number of transport and communications sectors have also been liberalised and competition and service levels are increasing.

The table below sets out certain transport statistics for Latvia for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006	2007	2008	2009	2010[(1)]
	(in thousands, except where indicated)				
Road					
Passenger cars (*no. at period end*)....	822.0	904.9	932.8	904.3	636.7[(2)]
Goods vehicles (*no. at period end*)...	121.1	129.6	129.8	120.6	71.6[(2)]
Freight (*tonnes*)...............................	54,187	59,905	54,459	37,820	46,809
Rail					
Freight traffic (*tonnes*)....................	48,731	52,164	56,061	53,679	49,164
International freight, exports (*million tonnes*)	2.1	2.4	2.7	2.2	3.2
International freight, imports (*million tonnes*)	39.4	42.8	47.1	47.1	41.0
Air					
Cargo loaded and unloaded (*tonnes*)	14	11	12	13	12.3[(3)]
Sea					
Outward cargo handled (*tonnes*)	53,069	55,178	57,654	57,566	55,724
Inward cargo handled (*tonnes*)........	6,428	7,256	5,995	4,415	5,436
Telecommunications					
Fixed lines (*per 100 inhabitants*)......	28.9	28.4	28.5	28.6	
Mobile subscribers (*per 100 inhabitants*)	95.8	97.7	98.9	105.4	
Estimated internet users (*per 100 inhabitants*)	53.6	59.1	63.4	66.8	

Source: Central Statistical Bureau; International Telecommunications Union.

Notes:

(1) Certain information is not available for 2010.

(2) In September 2009, new regulations allowing vehicles to be removed from the register of vehicles were introduced. Vehicles can be removed from the register:

- if the vehicle is permanently registered in a foreign country; or
- if the vehicle is five or more years old and has not satisfied technical inspection requirements.

(3) Provisional data.

Road

The number of registered passenger cars in Latvia grew from 822.0 thousand at 31 December 2006 to 932.8 thousand at 31 December 2008 before falling in 2009 and 2010 to 636.7 thousand at 31 December 2010, principally as a result of new regulations permitting the removal of vehicles from the register of vehicles in certain cases. Road transport freight increased from 54,187 tonnes in 2006 to 59,905 tonnes in 2007 before falling to 37,820 tonnes in 2009. In 2010, road transport freight recovered to 46,809 tonnes. Two significant road transport links in Latvia are the Via Baltica, a motorway linking the Baltic States to Germany through Poland, and the east-west Latgale Highway, which links Riga with Moscow and which is being upgraded using EU funding.

Rail

Latvia had 1,851 km of broad gauge railways at 31 December 2009, linking it with the other Baltic States, Russia and, through Poland, western Europe. The main rail corridor connects Moscow with Latvia's three ports. Railway connections with Estonia, Lithuania and Poland are due to be upgraded with the construction of a European standard railway linking the four countries. In October 2008, the government created an independent state-owned company to manage the passenger component of the State-owned Latvian Railways with a view to promoting passenger rail travel and relieving road congestion. Overall freight traffic carried by rail increased from 48,731 tonnes in 2006 to 56,061 tonnes in 2008 and then declined in each of 2009 and 2010 to 49,164 tonnes in 2010. The principal reason for the decrease in 2009 was a fall in domestic freight carried while in 2010 the principal reason for the decline was a fall in international freight imports.

Air

Latvia's only airport operating international flights is at Riga. Riga International Airport had a passenger turnover of 2.5 million passengers in 2006 which had increased to 4.7 million in 2010, reflecting increased business travel and tourism. Riga International Airport was completely refurbished in 2001 and a second runway, part-financed by EU structural and cohesion funds, is expected to be completed by 2013. There are flights to 86 destinations from Riga International Airport.

Sea

Latvia has three major year-round ice-free ports, Ventspils, Riga and Liepaja, which are central to the country's transit trade. Riga accounted for approximately 49 per cent. and Ventspils for 42 per cent. of cargo loaded in 2010. In terms of cargo unloaded in 2010, Riga accounted for approximately 58 per cent., Ventspils for approximately 28 per cent. and Liepaja for approximately 12 per cent.

Telecommunications

The expansion of mobile telephone services has caused a small decline in the number of fixed lines in Latvia from 657,380 in 2006 to 644,000 in 2009, reflecting a penetration rate (defined as the number of lines per 100 inhabitants) of 28.63 per cent. in 2009 (according to International Telecommunication Union ("**ITU**") statistics). Over the same period, the number of mobile subscribers grew from 2,183,696 million to 2,370,860 million, reflecting a penetration rate of 105.40 per cent. in 2009, according to ITU statistics. The estimated number of internet users per 100 inhabitants in Latvia in 2009 was 66.8.

The number of telecommunications operators in Latvia has grown significantly since the fixed line market opened to competition in 2003 but state-owned Lattelecom remains the dominant fixed line operator.

Energy

Both imported (coal, coke, petroleum products, natural gas and electricity) and local (used tyres, municipal waste for heating, peat, wood, charcoal, straw, biogas, bioethanol and biodiesel) energy resources are used in Latvia to supply fuel, electricity and heat to commercial and residential consumers. Electricity is generated in Latvia by hydro-electric power plants ("**HPPs**"), combined heat and power plants ("**CHPs**"), landfill biogas and wind power plants and is also imported. Heat is generated in Latvia using both local and imported fuels (including natural gas and fuel oil). In 2009, the total consumption of primary energy resources in Latvia amounted to 183.3 picojoules ("**PJ**"), and self-sufficiency in the total consumption of primary energy resources was 35.9 per cent. Wood was the most widely used local energy resource, and natural gas was the principal imported energy resource, in the total consumption of primary energy sources, whereas electricity generated by Latvian HPPs and wind power stations accounted for 6.9 per cent. of total energy consumption in Latvia in 2009.

The volume of electricity generation in Latvia depends directly on the flow in the Daugava River. After the closure of the Ignalina Nuclear Power Plant in Lithuania at the end of 2009, Latvia no longer imports nuclear energy from Lithuania and now imports electricity only from Estonia and Russia. In 2009, 23 per cent. of Latvia's electricity requirements were imported.

The consumption structure of Latvia's centralised heat supply has remained relatively constant in past years, with central heating comprising between 65 and 70 per cent. and hot water accounting for between 30 and 35 per cent. of total supplies. Of the total amount of heat sold, 1.4 per cent. was sold to industrial users, 73.7 per cent. to residential users and 24.9 per cent. to other consumers. Heat is produced in 679 boiler houses and 56 cogeneration stations, which in 2009 produced 7.31 terawatt hours ("**TWh**") of heat. The principal fuel source for heat production is natural gas which accounted for 76.8 per cent. of total heat production in 2009.

Energy policy

Latvia's energy policy is aimed at improving the security of the country's energy supply by encouraging diversification and by creating conditions for increasing Latvia's own electricity generation. In addition, Latvia is seeking to increase competition in the energy market, promote the use of renewable and local energy resources, and ensure environmental protection. In 2006, the Cabinet of Ministers approved Latvia's Energy Development Guidelines for 2007-2016. These guidelines contain the government's policy, development objectives and priorities in the sphere of energy over both the medium and long term.

More than 90 per cent. of all electricity generated in Latvia is generated by the State-owned JSC Latvenergo ("**Latvenergo**"), which is also responsible for all electricity imports and the supply of electricity to consumers. Since September 2005, the electricity transmission system has been operated by JSC Augstsprieguma tīkls and, since July 2007, the electricity distribution system has been operated by JSC Sadales tīkls. Both operators are wholly owned by Latvenergo.

JSC Latvijas Gāze carries out almost all natural gas transmission, distribution, storage and sale activities in Latvia in compliance with licences issued by the Public Utilities Commission. The gas supply system of Latvia is not connected to the EU common gas supply system, and Latvia has only one gas supplier – JSC Gazprom ("**Gazprom**"). In February 2009, JSC Latvijas Gāze signed new gas supply controls with Gazprom and a company owned by Gazprom which provide for the supply of Latvia's forecasted gas requirements until 2030.

Latvia is seeking to increase the proportion of the energy produced from renewable energy resources in the total final gross consumption of energy from 32.6 per cent. in 2005 to 40 per cent. by 2020. In this connection, a draft renewable energy law has been prepared but not yet approved. In 2010, the proportion of biofuel used in transport in Latvia was 3.0 per cent. of the total amount of transport fuel used.

For a discussion of risks related to Latvia's importation of energy from Russia, see "*Risk Factors – Deterioration in Latvia's relations with Russia or other major energy suppliers may adversely affect the supply of energy resources and therefore have a negative effect on the Latvian economy*".

Privatisation

A Privatisation Completion Law was introduced in Latvia in September 2005. The law determines how, and the suggested timescale by when, the privatisation process (which is substantially complete) and land reform in Latvia is to be completed. The law also deals with how any remaining privatisation certificates may be utilised pending their expiry. The law also provides that certain state companies (including the Latvian post office, the Latvian railways, Latvian air traffic control, the Latvian state forestry company, Riga International Airport and Latvenergo) will not be privatised. In November 2007, the government rejected a leveraged buyout of Lattelecom by a consortium of its management and a private equity firm, although it is possible that this company could still be privatised in the future as it is not included in the companies exempt from privatisation in the Privatisation Completion Law. In addition, the government is currently considering options for the sale of its shareholdings in Citadele Bank and Parex Bank and/or the liquidation of Parex Bank; see "*Monetary and Financial System – Financial Sector Supervision*".

Environment

Environmental protection in Latvia is primarily the responsibility of the Ministry of the Environment, a central executive institution.

The area of environmental protection includes protection of the environment and nature, maintenance and rational utilisation of natural resources, as well as sub-sectors of hydrometeorology and use of subsoil. The Ministry of the Environment develops the national policy of environmental protection and is responsible for and coordinates the implementation of environment policy. The Ministry of the Environment also proposes legislation, prepares environmental papers (including concepts, programmes and plans), delivers opinions on projects prepared by other institutions, and represents the interests of Latvia to international and foreign institutions. The Ministry of the Environment also provides information about the work of its supervised institutions.

Exchange Rates

The rate of exchange of the Latvian currency, the Lat, has been fixed since February 1994. Initially it was pegged to the IMF's SDR basket of currencies within fluctuation bands of +/-1 per cent. Following Latvia's accession to the EU and further integration with other EU countries, in January 2005 the Lat was re-pegged from the SDR basket of currencies to the euro, again within fluctuation bands of +/-1 per cent.

Since May 2005, Latvia has participated in the Exchange Rate Mechanism II ("**ERM II**"). The central rate for the Lat in ERM II was set at 0.702804 Lats per euro (the same level as the rate adopted since the beginning of 2005). The unilateral +/-1 per cent. fluctuation bands have been maintained within the ERM II arrangement.

Through a currency board arrangement, the Bank of Latvia maintains the monetary base with foreign exchange reserves that consist of liquid foreign assets. The Bank of Latvia offers market participants the opportunity to conduct foreign exchange interventions of unlimited amount whenever the market exchange rate hits the +/-1 per cent. fluctuation bands.

Latvia remains committed to maintaining the exchange rate peg with a view to adopting the euro as the national currency by 2014 as soon as the necessary criteria for adoption are met. See "*Monetary and Financial System – Foreign Assets*" and "*Public Finance – Impact of the Global Financial Crisis on Latvia's Budgets for 2009, 2010 and 2011*".

BALANCE OF PAYMENTS AND FOREIGN TRADE

Balance of Payments

Current Account

Latvia's trade deficit increased significantly in 2006 and 2007 as imports (financed by the easy availability of credit) increased at a significantly greater rate than exports. However, the onset of the global financial crisis and the significant contraction of liquidity in Latvia in 2008 meant that imports fell slightly in 2008 and significantly in 2009, before increasing gradually in 2010 as an increase in exports and industrial production took place requiring more intermediate and capital goods. Exports increased in each of 2006, 2007 and 2008 before falling significantly in 2009 and recovering strongly in 2010. The increase in exports in 2010 was underpinned by a gradual recovery in the economies of Latvia's major trading partners, and exports exceeded the pre-global financial crisis peak by September 2010, while imports remained significantly below the pre-crisis levels. As a result, the trade deficit narrowed in each of 2008, 2009 and 2010. As a percentage of nominal GDP, Latvia's trade deficit was 25.6 per cent. in 2006, 23.9 per cent. in 2007, 17.7 per cent. in 2008, 7.1 per cent. in 2009 and 6.5 per cent. in 2010.

Latvia's services balance has been positive in all periods since 2006 and increased in nominal terms in each year up to 2009. In 2010, Latvia's services balance was marginally lower than its 2009 level in nominal terms. As a percentage of nominal GDP, Latvia's services balance was 3.3 per cent. in 2006, 3.5 per cent. in 2007, 4.0 per cent. in 2008, 6.0 per cent. in 2009 and 6.2 per cent. in 2010.

Latvia's income account was negative in each year between 2006 and 2008 but turned positive in 2009. The principal reason for this reversal was significant foreign direct investment ("**FDI**") losses experienced in the banking sector, in particular, reflecting the fact that Latvia's banking sector is predominantly foreign-owned which is reflected in the income account as an increase in income. In 2010, this trend reversed gradually and by the end of year the income account had a small annual surplus equal to 0.2 per cent. of nominal GDP.

Latvia's balance of transfers (reflecting remittances from Latvians working abroad and including certain fiscal transfers from the EU) has remained positive in each period since 2006. In 2009 and 2010 the transfers balance was equal to 3.4 per cent. and 3.6 per cent. of nominal GDP, respectively.

Reflecting the above factors, and primarily driven by the trade balance, Latvia's current account balance showed deficits in each of 2006, 2007 and 2008 and a surplus in 2009 and 2010. As a percentage of nominal GDP, Latvia's current account deficit was 22.5 per cent. in 2006, 22.3 per cent. in 2007 and 13.1 per cent. in 2008. Latvia's current account surplus was equal to 8.6 per cent. of nominal GDP in 2009 and 3.6 per cent. of nominal GDP in 2010.

Capital and Financial Account

Latvia's capital account has been positive in each period since 2006. Latvia's financial account was positive in 2006, 2007 and 2008 but turned negative in 2009 and 2010. In 2009, the principal outflows recorded in the financial account were related to decreases in the short-term and long-term liabilities of the banking sector (both outflows of foreign deposits and loans). In 2009, the corporate sector also tended to reduce its long- and short-term liabilities to reduce the risks associated with the recession. In addition, corporate foreign deposits created significant financial outflows in 2009. In 2010, the outflow of funds reduced although a decrease in the long-term liabilities of the banking sector was still evident.

Latvia saw significant funding inflows covering the current account deficit until late 2008 when the full effects of the global financial crisis on the country's large external imbalances (principally a lack of liquidity in international markets and a collapse of both external and domestic demand) became apparent. Latvia's funding inflows are principally in the form of equity investment and reinvested earnings and other investment, which, prior to 2008, was principally lending by non-Latvian banks to their subsidiaries in Latvia. For more information, see "– *Foreign Direct Investment*". In December 2008, the European Commission (the "**EC**"), the IMF, the World Bank, the EBRD and several Member States of the EU agreed to provide financial support to Latvia in an amount of EUR 7.5 billion. See "*Indebtedness – Financial Assistance from International Lenders*". The financing remains available until the end of 2011. In 2008, Latvia received the first tranche of the IMF Stand-By Arrangement (in an amount of €600 million). In 2009, Latvia received €2,700 million in assistance and in 2010 it received €1,100 million. This assistance, together with the actions taken by Latvia to stabilise its banking system and ensure economic recovery, contributed to restoring the confidence of foreign investors and other non-residents. As a result, Latvia experienced an increase in both foreign deposits and net FDI in 2010, both of which contributed to the reduction in the financial account deficit. A contraction in short-term borrowings in the banking sector and foreign direct investor losses, as well as outflows of non-resident deposits and an increase in corporate foreign deposits, were the principal financial outflows in 2009. In 2010, the principal trend was reducing long-term liabilities in the banking sector.

Reflecting the above, Latvia's capital and financial account surplus as a percentage of nominal GDP was 21.8 per cent. in 2006, 23.1 per cent. in 2007 and 14.9 per cent. in 2008 while its capital and financial account deficit amounted to 9.4 per cent. of nominal GDP in 2009 and 3.4 per cent. in 2010.

The table below sets out Latvia's balance of payments for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006	2007	2008	2009	2010
			(LVL millions)		
Current account	(2,510.0)	(3,297.0)	(2,113.4)	1,128.6	455.8
Trade balance	(2,856.4)	(3,536.1)	(2,862.3)	(931.6)	(821.1)
Exports	3,431.8	4,214.4	4,587.1	3,708.2	4,766.9
Imports	(6,288.2)	(7,750.5)	(7,449.4)	(4,639.7)	(5,588.0)
Services balance	372.3	512.8	644.2	790.6	787.5
Exports	1,476.6	1,894.7	2,169.7	1937.3	1,964.5
Imports	(1,104.3)	(1,382.0)	(1,525.4)	(1,146.7)	(1,177.0)
Income balance	(297.8)	(466.3)	(254.8)	826.2	30.9
Credit	601.9	760.8	857.1	670.5	590.3
Debit	(899.7)	(1,277.1)	(1,111.9)	155.6	(559.4)
Current transfers	271.9	192.6	359.5	443.3	458.6
Credit	1,002.8	1,035.4	1,043.1	997.9	868.4
Debit	(730.8)	(842.7)	(683.6)	(554.6)	(409.9)
Capital and financial account	2,438.4	3,415.2	2,404.5	(1,229.0)	(430.9)
Capital account	134.0	288.1	239.8	317.3	247.9
Financial account	2,304.4	3,127.1	2,164.8	(1,546.4)	(678.8)
Direct investment	836.6	1,003.6	489.6	78.9	176.6
Portfolio investment	17.3	(347.0)	178.2	86.8	(99.1)
Other investment	2,520.9	2,857.0	1,226.8	(1,277.3)	(128.4)
Reserve assets	(1,103.0)	(502.2)	320.2	(647.6)	(509.3)
Errors and omissions	71.6	(118.2)	(291.2)	100.6	(24.9)

Source: Bank of Latvia

The table below sets out Latvia's balance of payments as a percentage of nominal GDP for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006	2007	2008	2009	2010
			(as a percentage of GDP)		
Current account	(22.5)	(22.3)	(13.1)	8.6	3.6
Trade balance	(25.6)	(23.9)	(17.7)	(7.1)	(6.4)
Services balance	3.3	3.5	4.0	6.0	6.2
Income balance	(2.7)	(3.2)	(1.6)	6.3	0.2
Current transfers	2.4	1.3	2.2	3.4	3.6
Capital and financial account	21.8	23.1	14.9	(9.4)	(3.4)
Capital account	1.2	1.9	1.5	2.4	1.9
Financial account	20.6	21.2	13.4	(11.8)	(5.3)
Reserve assets	(9.9)	(3.4)	2.0	(5.0)	(4.0)
Errors and omissions	0.6	(0.8)	(1.8)	0.8	(0.2)

Source: Bank of Latvia

Foreign Trade

Reflecting the impact of the global financial crisis, Latvia's imports started to fall on a year-on-year basis in the second quarter of 2008 although its exports only started to fall from the fourth quarter of 2008. The earlier decline in imports reflected the fact that economic conditions in Latvia deteriorated more significantly than in its principal trading partners and the fact that the share of cyclically sensitive goods (such as capital goods) in imports is higher than in exports. In addition, as Latvia emerged from recession its exports recovered faster than its imports. On a year-on-year basis, Latvia's exports have increased since the end of 2009 although its imports only started to grow from March 2010. Increased foreign demand, price increases in foreign markets and competitiveness gains by Latvian producers have all contributed to export growth in nearly all types of goods exported in all of Latvia's main export markets. In terms of imports, after the sharp fall in 2009, imports began to increase from March 2010 and, since October 2010, the annual growth rate in imports has exceeded the annual growth rate in exports. The increase in imports has been closely related to export growth as reflected in the growth in imports of intermediate goods and capital goods.

The principal product groups exported by Latvia are wood products (principally sawn wood, fuel wood and round wood), machinery (principally appliances and electronic equipment), metal products (principally iron and steel) and agricultural products (being prepared foodstuffs, principally fish and dairy products, and vegetable products). As a percentage of exports, wood products fell from 22.5 per cent. in 2006 to 16.5 per cent. in 2009 and then increased to 19.2 per cent. in 2010. Machinery exports increased from 9.8 per cent. of exports in 2006 to 14.1 per cent. in 2009 and then fell to 12.8 per cent. in 2010. The contribution of metal products to exports between 2006 and 2010 fluctuated with the highest level being 16.7 per cent. in 2008 and the lowest level being 12.4 per cent. in 2009. The contribution of agricultural products also fluctuated with the highest level being 14.1 per cent. in 2009 and the lowest level being 10.5 per cent. in 2009, reflecting the fact that these exports were the least affected by the recession.

The principal product groups imported by Latvia are machinery (principally machine parts, electrical equipment, office equipment and cables and wires), mineral products (principally oil, petroleum and gas), base metal products (principally iron and steel) and chemical products (principally pharmaceuticals). Machinery product imports declined from 20.8 per cent. of imports in 2007 to 15.7 per cent. in 2009 and then increased to 16.5 per cent. in 2010. The contributions of mineral products and chemical products to imports fluctuated over the period from 2006 to 2010 with the highest level for each being 17.2 per cent. and 11.8 per cent., respectively, in 2009 and the lowest level for each being 11.5 per cent. and 8.1 per cent., respectively, in 2007. Base metal products increased from 9.5 per cent. of imports in 2006 to 10.3 per cent. of imports in 2008 and were 8.1 per cent. and 10.3 per cent. of imports in 2009 and 2010, respectively.

Latvia's main trading partners are the 27 EU Member States, which accounted for approximately 70 per cent. of Latvia's exports and approximately 75 per cent. of its imports for each year in the period between 2006 and 2010. In 2010, the EU Member States accounted for 71.3 per cent. of Latvia's exports and 75.3 per cent. of its imports. Within the EU Member States, the principal export destinations for Latvia's goods in 2010 were Lithuania (which accounted for 16.2 per cent. of Latvia's total exports in that year), Estonia (which accounted for 13.2 per cent. of Latvia's total exports in that year) and Germany (which accounted for 8.7 per cent. of Latvia's total exports in that year). In terms of imports, the principal EU sources of imports for Latvia in 2010 were Lithuania (which accounted for 16.8 per cent. of Latvia's total imports in that year) and Germany (which accounted for 11.6 per cent. of Latvia's total imports in that year).

Outside the EU, the share of the states comprising the Commonwealth of Independent States (the "**CIS**") in Latvia's exports was 14.0 per cent. in 2006 and 15.2 per cent. in 2010. Within the CIS states, Russia is the principal export market for Latvian goods, accounting for 71.0 per cent. of Latvian exports to the CIS states in 2010. In terms of imports, the CIS states accounted for 14.2 per cent. of Latvia's imports in 2006 and 15.6 per cent. in 2010. As with exports, within the CIS Russia is the principal source of Latvia's imports, accounting for 66.3 per cent. of CIS imports to Latvia in 2010.

Other countries accounted for 13.5 per cent. of Latvian exports and 9.1 per cent. of its imports in 2010. Outside the EU and the CIS states, Latvia primarily trades with countries in Asia and the Americas. Asia accounted 5.7 per cent. of Latvia's exports and 5.4 per cent. of its imports in 2010. The Americas accounted for 1.9 per cent. of Latvia's exports and 1.4 per cent. of its imports in 2010.

The tables below set out the geographic distribution of Latvian exports of goods for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006		2007	
	(LVL millions)	*(per cent.)*	*(LVL millions)*	*(per cent.)*
EU				
Germany	332.3	10.1	353.1	8.7
UK	257.2	7.8	277.1	6.9
Sweden	212.9	6.5	313.0	7.7
Denmark	164.8	5.0	161.1	4.0
Lithuania	483.0	14.7	638.6	15.8
Estonia	419.1	12.7	581.8	14.4
Poland	79.7	2.4	146.0	3.6
Other EU(1)	518.7	15.8	595.2	14.7
Total(1)	**2,467.7**	**74.9**	**3,065.9**	**75.9**
EU-27	2,472.4	75.1	3,076.7	76.2
CIS				
Russia	291.9	8.9	386.2	9.6
Ukraine	57.7	1.8	59.8	1.5
Belarus	75.9	2.3	92.6	2.3
Other CIS	35.7	1.1	47.7	1.2
Total	**461.2**	**14.0**	**586.4**	**14.5**
Other	364.3	11.1	388.0	9.3
Total	**3,293.2**	**100.0**	**4,040.3**	**100.0**

	2008		2009		2010	
	(LVL millions)	*(per cent.)*	*(LVL millions)*	*(per cent.)*	*(LVL millions)*	*(per cent.)*
EU						
Germany	358.4	8.1	314.0	8.7	405.0	8.7
UK	166.7	3.8	115.3	3.2	166.0	3.6
Sweden	293.4	6.6	219.5	6.1	296.3	6.3
Denmark	202.1	4.6	148.6	4.1	184.0	3.9
Lithuania	739.8	16.7	590.4	16.4	757.7	16.2
Estonia	621.7	14.0	518.4	14.4	614.0	13.2
Poland	165.5	3.7	138.3	3.8	234.1	5.0
Other EU(1)	676.4	15.3	526.6	14.6	650.1	13.9
Total(1)	**3,224.0**	**72.8**	**2,571.1**	**71.4**	**3,307.1**	**70.9**
EU-27	3,245.4	73.3	2,586.9	71.8	3,327.8	71.3
CIS						
Russia	442.2	10.0	316.4	8.8	503.8	10.8
Ukraine	64.5	1.5	37.7	1.0	52.8	1.1
Belarus	98.0	2.2	92.2	2.6	99.9	2.1
Other CIS	59.3	1.3	55.1	1.5	52.0	1.1
Total	**664.0**	**15.0**	**501.4**	**13.9**	**708.5**	**15.2**
Other	540.9	12.2	529.7	14.7	630.1	13.5
Total	**4,428.9**	**100.0**	**3,602.2**	**100.0**	**4,666.5**	**100.0**

Source: Central Statistical Bureau
Note:
(1) These rows exclude Bulgaria and Romania which joined the EU in 2007. The EU-27 row includes those countries in each year.

The tables below set out the geographic distribution of Latvian imports of goods for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006		2007	
	(LVL millions)	*(per cent.)*	*(LVL millions)*	*(per cent.)*
EU				
Germany	988.5	15.5	1,218.0	15.7
Finland	363.0	5.7	397.3	5.1
Sweden	321.0	5.0	379.8	4.9
Italy	216.8	3.4	285.9	3.7
Lithuania	827.7	13.0	1,080.6	13.9
Estonia	494.1	7.7	629.9	8.1
Poland	459.4	7.2	544.0	7.0
Other EU(1)	1,218.9	19.1	1,510.7	19.4
Total(1)	**4,889.4**	**76.7**	**6,046.2**	**77.7**
EU-27	—	—	6,060.8	77.9
CIS				
Russia	499.1	7.8	653.5	8.4
Belarus	297.7	4.7	256.7	3.3
Other CIS	105.9	1.7	118.9	1.5
Total	**902.7**	**14.2**	**1,029.1**	**13.2**
Other	586.4	9.2	704.9	9.1
Total	**6,378.5**	**100.0**	**7,780.2**	**100.0**

	2008		2009		2010	
	(LVL millions)	*(per cent.)*	*(LVL millions)*	*(per cent.)*	*(LVL millions)*	*(per cent.)*
EU						
Germany	981.7	13.0	543.1	11.5	675.3	11.6
Finland	330.8	4.4	168.6	3.6	292.2	5.0
Sweden	332.6	4.4	168.3	3.6	208.8	3.6
Denmark	218.0	2.9	126.6	2.7	130.3	2.2
Lithuania	1,241.4	16.5	800.9	17.0	980.7	16.8
Estonia	535.7	7.1	375.7	8.0	675.3	7.1
Poland	540.7	7.2	397.2	8.4	449.8	7.7
Other EU(1)	1,521.3	20.2	943.7	20.0	1,235.0	21.1
Total(1)	**5,702.2**	**75.7**	**3,524.1**	**74.8**	**4,385.5**	**75.1**
EU-27	5,716.5	75.9	3,541.3	75.2	4,400.7	75.3
CIS						
Russia	801.3	10.6	505.7	10.7	603.7	10.3
Belarus	250.0	3.3	163.3	3.5	202.4	3.5
Other CIS	145.0	1.9	78.4	1.7	103.1	1.8
Total	1,196.3	15.9	747.4	15.9	909.2	15.6
Other	629.2	8.4	438.3	9.3	530.9	9.1
Total	**7,527.7**	**100.0**	**4,709.8**	**100.0**	**5,840.8**	**100.0**

Source: Central Statistical Bureau

Note:

(1) These rows exclude Bulgaria and Romania which joined the EU in 2007. The EU-27 row includes those countries in each year.

Composition of Trade

The tables below set out the composition of Latvia's exports of goods for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006		2007	
	(LVL millions)	*(per cent.)*	*(LVL millions)*	*(per cent.)*
Live animals and animal products	115.3	3.5	149.4	3.7
Vegetable products	67.6	2.1	110.7	2.7
Prepared foodstuffs	245.2	7.4	314.1	7.8
Mineral products	182.2	5.5	165.4	4.1
Products of the chemical and allied industries	222.6	6.8	300.3	7.4
Plastics, rubber and articles thereof	100.8	3.1	119.5	3.0
Wood and articles of wood	739.5	22.5	908.5	22.5
Textiles and textile articles	269.3	8.2	271.0	6.7
Base metals and articles of base metals	488.1	14.8	589.7	14.6
Machinery and mechanical appliances; electrical equipment	324.0	9.8	444.0	11.0
Transport vehicles	198.5	6.0	281.4	7.0
Miscellaneous manufactured articles	149.3	4.5	157.8	3.9
Other goods	190.9	5.8	228.4	5.7
Total	**3,293.2**	**100.0**	**4,040.3**	**100.0**

	2008		2009		2010	
	(LVL millions)	*(per cent.)*	*(LVL millions)*	*(per cent.)*	*(LVL millions)*	*(per cent.)*
Live animals and animal products	165.9	3.8	157.3	4.4	200.8	4.3
Vegetable products	224.1	5.1	214.9	6.0	260.1	5.6
Prepared foodstuffs	349.1	7.9	290.3	8.1	351.1	7.5
Mineral products	184.0	4.2	199.6	5.5	283.0	7.5
Products of the chemical and allied industries	371.4	8.4	307.0	8.5	352.2	7.5
Plastics, rubber and articles thereof	126.3	2.9	102.9	2.9	153.0	3.3
Wood and articles of wood	735.0	16.6	595.4	16.5	898.4	19.2
Textiles and textile articles	242.8	5.5	178.8	5.0	205.1	4.4
Base metals and articles of base metals	738.9	16.7	447.8	12.4	650.2	13.9
Machinery and mechanical appliances; electrical equipment	553.7	12.5	509.4	14.1	599.7	12.8
Transport vehicles	326.5	7.4	254.7	7.1	277.6	5.9
Miscellaneous manufactured articles	154.4	3.5	121.0	3.4	130.1	2.8
Other goods	256.9	5.8	223.2	6.2	309.6	6.6
Total	**4,428.9**	**100.0**	**3,602.2**	**100.0**	**4,670.8**	**100.0**

Source: Central Statistical Bureau

The tables below set out the composition of Latvia's imports of goods for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006		2007	
	(LVL millions)	*(per cent.)*	*(LVL millions)*	*(per cent.)*
Live animals and animal products	140.8	2.2	165.1	2.1
Vegetable products	153.4	2.4	196.8	2.5
Prepared foodstuffs	379.2	6.0	475.5	6.1
Mineral products	854.8	13.4	894.8	11.5
Products of the chemical and allied industries	530.4	8.3	631.5	8.1
Plastics and articles thereof; rubber and articles thereof.	322.6	5.1	371.9	4.8
Wood and articles of wood	161.0	2.5	262.3	3.4
Pulp of wood; paper and paperboard	164.5	2.6	184.4	2.4
Textiles and textile articles	297.0	4.7	335.6	4.3
Articles of stone, plaster, cement, glassware, ceramic	171.0	2.7	203.1	2.6
Base metals and articles of base metals	606.7	9.5	747.8	9.6
Machinery and mechanical appliances; electrical equipment	1,257.0	19.7	1,618.6	20.8
Transport vehicles	868.3	13.6	1,136.2	14.6
Miscellaneous manufactured articles	213.8	3.4	261.0	3.4
Other goods	258.1	4.0	295.7	3.8
Total	**6,378.5**	**100.0**	**7,780.2**	**100.0**

	2008		2009		2010	
	(LVL millions)	*(per cent.)*	*(LVL millions)*	*(per cent.)*	*(LVL millions)*	*(per cent.)*
Live animals and animal products	204.2	2.7	181.7	3.9	199.8	3.4
Vegetable products	264.2	3.5	222.9	4.7	248.7	4.2
Prepared foodstuffs	514.2	6.8	416.9	8.9	425.0	7.3
Mineral products	1,171.2	15.6	808.6	17.2	927.1	15.8
Products of the chemical and allied industries	732.8	9.7	557.3	11.8	669.1	11.4
Plastics and articles thereof; rubber and articles thereof	356.3	4.7	237.8	5.0	332.7	5.7
Wood and articles of wood	139.9	1.9	66.0	1.4	96.5	1.7
Pulp of wood; paper and paperboard	180.1	2.4	134.6	2.9	165.8	2.8
Textiles and textile articles	303.4	4.0	230.4	4.9	263.3	4.5
Articles of stone, plaster, cement, glassware, ceramic	157.8	2.1	98.0	2.1	100.0	1.7
Base metals and articles of base metals	775.2	10.3	379.7	8.1	600.9	10.3
Machinery and mechanical appliances; electrical equipment	1,374.0	18.3	740.3	15.7	967.5	16.5
Transport vehicles	807.8	10.7	304.6	6.5	414.7	7.1
Miscellaneous manufactured articles	227.3	3.0	115.2	2.5	137.1	2.3
Other goods	319.4	4.2	215.8	4.6	314.1	5.4
Total	**7,527.7**	**100.0**	**4,709.8**	**100.0**	**5,862.3**	**100.0**

Source: Central Statistical Bureau

Trade Policy

Member States of the EU benefit from a common trade policy negotiated on their behalf by the European Commission, which establishes a common position that is co-ordinated with all Member States through the Trade Policy Committee of the Council of Ministers. The Trade Policy Committee plays a key role in shaping the EU's external trade policy, is made up of trade experts from each Member State and is chaired by whichever country holds the EU presidency. Latvia's trading relations with other non-EU countries are regulated under agreements concluded by the EU where such agreements exist.

The principal priority of EU trade policy has been its participation in the WTO's Doha Development Agenda negotiations, in which the European Commission seeks to provide leadership and facilitate consensus. This and other key EU trade policy issues, such as the negotiation of new WTO-compatible free trade agreements with certain priority trading partners, including ASEAN countries, India and Ukraine; regulatory convergence with strategic economic partners such as the United States of America, China, Japan and Russia; successful implementation of the Common EU Investment Policy and the EU Market Access Strategy; and enforcement of intellectual property rights, are set out in the EU's mid-term trade policy strategy entitled "Trade, Growth and World Affairs".

Latvia has concluded bilateral economic cooperation agreements with the Republic of Armenia, the Republic of Azerbaijan, the Republic of Belarus, the People's Republic of China, Georgia, the Republic of Kazakhstan, the Republic of Kyrgyzstan, the Republic of Moldova, the Russian Federation, the Republic of Tajikistan, Turkmenistan, Ukraine and the Republic of Uzbekistan. These agreements are aimed at enhancing bilateral economic cooperation between Latvia and countries outside the EU in industry, transport, pharmaceuticals, agriculture, financial services, communications, tourism, professional training, investment policy, technologies and innovation, among other fields. Although Latvia and Russia have concluded an agreement on economic cooperation, active cooperation is also carried out with the regions of the Russian Federation and agreements on economic cooperation have been concluded with the governments of the Vologda Region and the administration of the Pskov Region. Negotiations are currently ongoing with the governments of the Kirov Region, the Ivanovo Region and the Yaroslavl Region, as well as with the government of the Republic of Bashkortostan.

Foreign Direct Investment

At the end of 2010, the sectors with the largest accumulated FDI inflows in Latvia were real estate; financial intermediation; manufacturing; and trade which together accounted for 71.4 per cent. of accumulated FDI. Prior to the global financial crisis, FDI inflows were more concentrated in the financial intermediation and real estate sectors. However, with an improvement in the business climate and gains in competitiveness as Latvia emerged from recession, investors' interest in Latvia's manufacturing sector has revived. In 2010, FDI inflows in manufacturing were the second largest FDI inflows in Latvia (after the real estate sector) and were principally aimed at expanding existing production units and building new units. In 2009, net FDI inflows amounted to 0.4 per cent. of nominal GDP. In 2010, net FDI inflows in Latvia were 1.5 per cent. of GDP.

Cumulative FDI in the real estate sector increased by 55.5 per cent. at 31 December 2007, in each case compared to the level at the end of the preceding year. Cumulative FDI in the real estate sector remained unchanged in 2008 and then grew by 6.5 per cent. at 31 December 2009 compared to the level at 31 December 2008 and by 14.1 per cent. at 31 December 2010 compared to the level at 31 December 2009.

Cumulative FDI in the financial intermediation sector increased by 54.1 per cent. at 31 December 2007, by 10.8 per cent. at 31 December 2008 and by 0.4 per cent. at 31 December 2009, in each case compared to the level at the end of the preceding year. At 31 December 2010, cumulative FDI in the financial intermediation sector had fallen by 19.8 per cent. compared to the level at 31 December 2009, reflecting significant losses incurred by the banking sector.

Cumulative FDI in the manufacturing sector increased by 30.7 per cent. at 31 December 2007, by 18.4 per cent. at 31 December 2008, by 0.7 per cent. at 31 December 2009 and by 10.7 per cent. at 31 December 2010, in each case compared to the level at the end of the preceding year.

Cumulative FDI in the trade sector increased by 19.2 per cent. at 31 December 2007 and by 27.8 per cent. at 31 December 2008, in each case compared to the level at the end of the preceding year. At 31 December 2009, cumulative FDI in the trade sector fell by 5.0 per cent. compared to the level at

31 December 2008 and, at 31 December 2010, it fell by 9.3 per cent. compared to the level at 31 December 2009.

In 2010 and 2011, with the assistance of the Investment and Development Agency of Latvia ("**LIAA**"), 10 foreign entities, including Cytec (USA), AGA/Linde Gas (Germany) and Brabantia (the Netherlands), have announced intentions to invest in aggregate approximately €31 million in new or existing business structures in Latvia.

LIAA has developed the Polaris strategy, which is an investment strategy focused on economic growth and development in Latvia. The strategy is based on an alliance between the public sector (including national and local governments), the private sector (including national and international companies and investors willing to invest in Latvia) and major Latvian academic institutions (including the main universities and research institutions). The Polaris strategy comprises seven prospective sectors for FDI: woodworking; metalworking and mechanical engineering; transport and storage; information technology; green technology; health-care; and life-sciences.

The principal source of FDI into Latvia is from EU countries which, at 31 December 2006, accounted for 71.6 per cent. of cumulative Latvian FDI. This percentage had increased to 77.2 per cent. at 31 December 2008. From 2009, cumulative FDI from EU countries decreased and, at 31 December 2010, it was 73.0 per cent. Apart from EU countries, Russia, the United States and Norway have each been important sources of FDI for Latvia, accounting for 4.1 per cent., 3.3 per cent. and 3.1 per cent., respectively, of cumulative FDI into Latvia at 31 December 2010.

The table below sets out the cumulative FDI stock as at 31 December in each of 2006, 2007, 2008, 2009 and 2010.

	2006	**2007**	**2008**	**2009**	**2010**
			(LVL millions)		
Foreign investment stock	4,007.2	5,247.4	5,711.0	5,673.4	5,798.2
in equity capital	3,103.8	4,158.7	4,236.8	3,932.0	4,483.0
in other capital	903.4	1,088.7	1,474.3	1,741.4	1,315.2

Source: Bank of Latvia

The tables below set out the distribution of cumulative FDI by sector and as a percentage of total FDI in enterprises as at 31 December in each of 2006, 2007, 2008, 2009 and 2010.

	2006		**2007**	
	(LVL millions)	*(per cent.)*	*(LVL millions)*	*(per cent.)*
Financial intermediation	964.7	24.1	1,486.2	28.3
Real estate, renting and business activities	743.8	18.6	1,156.3	22.0
Wholesale and retail trade, repair	525.3	13.1	626.0	11.9
Manufacturing	395.3	9.9	516.7	9.8
Transport, storage and communication	347.1	8.7	392.5	7.5
Electricity, gas and water supply	348.1	8.7	270.7	5.2
Construction	67.6	1.7	85.5	1.6
Hotels and restaurants	36.9	0.9	50.4	1.0
Other	578.4	14.4	663.1	12.6
Total	**4,007.2**	**100.0**	**5,247.4**	**100.0**

	2008		2009		2010	
	(LVL millions)	*(per cent.)*	*(LVL millions)*	*(per cent.)*	*(LVL millions)*	*(per cent.)*
Financial intermediation	1,647.2	28.8	1,653.7	29.1	1,326.8	22.9
Real estate, renting and business activities	1,157.3	20.3	1,232.4	21.7	1,406.3	24.3
Wholesale and retail trade, repair	800.4	14.0	760.2	13.4	689.6	11.9
Manufacturing	611.8	10.7	654.9	11.5	725.1	12.5
Transport, storage and communication	466.3	8.2	431.5	7.6	424.7	7.3
Electricity, gas and water supply	204.9	3.6	190.5	3.4	216.0	3.7
Construction	107.1	1.9	124.7	2.2	109.4	1.9
Hotels and restaurants	61.5	1.1	61.8	1.1	47.8	0.8
Other	654.5	11.5	563.7	9.9	852.5	14.7
Total	**5,711.0**	**100.0**	**5,673.4**	**100.0**	**5,798.2**	**100.0**

Source: Bank of Latvia

The tables below set out the distribution of cumulative FDI by country and as a percentage of total cumulative FDI as at 31 December in each of 2006, 2007, 2008, 2009 and 2010.

	2006		2007	
	(LVL millions)	*(per cent.)*	*(LVL millions)*	*(per cent.)*
Estonia	466.5	11.6	775.7	14.8
Sweden	606.2	15.1	706.8	13.5
Germany	443.2	11.1	446.2	8.5
Denmark	331.6	8.3	462.9	8.8
Finland	233.9	5.8	334.3	6.4
Netherlands	222.7	5.6	295.8	5.6
Cyprus	167.4	4.2	263.0	5.0
Lithuania	100.9	2.5	128.4	2.4
Other EU	295.7	7.4	539.2	10.3
Total EU	2,868.1	71.6	3,952.3	75.3
Russian Federation	264.8	6.6	242.5	4.6
United States	234.9	5.9	233.1	4.4
Norway	152.7	3.8	187.8	3.6
Switzerland	72.8	1.8	64.3	1.2
Other countries	209.2	5.2	317.3	6.0
Ex-territorial societies(1)	—	—	—	—
Countries not classified	204.8	5.1	250.1	4.8
Total	**4,007.2**	**100.0**	**5,247.4**	**100.0**

Source: Bank of Latvia
Note:
(1) EBRD, EU and other international organisations.

	2008		2009		2010	
	(LVL millions)	*(per cent.)*	*(LVL millions)*	*(per cent.)*	*(LVL millions)*	*(per cent.)*
Estonia	921.1	16.1	959.7	16.9	801.4	13.8
Sweden	820.5	14.4	782.9	13.8	724.0	12.5
Germany	360.7	6.3	362.6	6.4	299.7	5.2
Denmark	459.2	8.0	390.6	6.9	402.6	6.9
Finland	335.6	5.9	234.9	4.1	269.3	4.6
Netherlands	312.2	5.5	326.2	5.7	396.6	6.8
Cyprus	205.8	3.6	234.8	4.1	287.5	5.0
Lithuania	212.2	3.7	193.4	3.4	182.8	3.2
Other EU	783.1	13.7	853.5	15.0	870.8	15.0
Total EU	4,410.4	77.2	4,338.6	76.5	4,234.7	73.0
Russian Federation	262.3	4.6	260.1	4.6	236.7	4.1
United States	222.6	3.9	214.6	3.8	189.5	3.3
Norway	171.4	3.0	169.5	3.0	179.0	3.1
Switzerland	53.9	0.9	60.7	1.1	104.9	1.8
Other countries	343.1	6.0	375.8	6.6	378.1	6.5
Ex-territorial societies(1)	—	—	53.6	0.9	35.2	0.6
Countries not classified	247.3	4.3	200.2	3.5	440.0	7.6
Total	**5,711.0**	**100.0**	**5,673.4**	**100**	**5,798.2**	**100**

Source: Bank of Latvia
Note:
(1) EBRD, EU and other international organisations.

MONETARY AND FINANCIAL SYSTEM

The Bank of Latvia

The Bank of Latvia was established as the central bank of Latvia on 7 September 1922, following the proclamation of the Republic of Latvia in 1918. The Bank of Latvia operated as a central bank and a commercial bank until June 1940 when Latvia was occupied by the Soviet Union. The Bank of Latvia was liquidated in October 1940 following the annexation of Latvia to the Soviet Union in August of that year.

After regaining independence in 1991, the Bank of Latvia once again became Latvia's central bank with the right to issue the national currency. The Bank of Latvia took over and incorporated into its structure the Latvian Republican Bank of the State Bank of the Soviet Union present in Latvia and other state credit institutions present in Latvia. The legal status of the Bank of Latvia, and its role as an independent central bank, were reinforced by new legislation passed in May 1992. Following the introduction of this legislation, the Bank of Latvia was divested of its commercial operations through the restructuring and privatisation of its 49 branches.

The law regulating the Bank of Latvia sets out its role and confers authority on it to operate as an independent institution which is solely responsible to the Saeima. The Bank of Latvia is administered by its Council and its Board. The Council consists of eight members: the Governor (who is also the Chairman of the Council), the Deputy Governor and six other members. The Council makes decisions on behalf of the Bank of Latvia. The Board, which is nominated by the Council and also consists of six members, is responsible for the management and day-to-day functions of the Bank of Latvia. The Governor and the members of the Council are appointed by the Saeima for a six-year term and can only be removed by the Saeima in limited circumstances.

Following EU accession in May 2004, the Bank of Latvia has become a part of the European System of Central Banks and has started preparations for the introduction of the euro. Latvia joined ERM II in May 2005 as a necessary precondition for the entry into the European Monetary System.

Monetary Policy

The main task of the Bank of Latvia is to maintain price stability. To achieve this, the Bank of Latvia's monetary policy aims to maintain exchange rate stability and to control the amount of bank reserves. The exchange rate policy of the Bank of Latvia is similar to that of a currency board, and the monetary base is backed by gold and foreign currency reserves. The Bank of Latvia may grant loans to the banking sector but is prohibited by law from issuing credits to the government or purchasing government securities on the primary market. The national currency, the Lat, is fully convertible and there are no restrictions for current or capital account transactions.

The Bank of Latvia uses a wide range of instruments to implement its monetary policy, the main one being the buying and selling of foreign exchange, including through swap operations. The Bank of Latvia uses reserve requirements and a deposit facility as tools for withdrawing liquidity from the system and refinancing operations as a liquidity providing instrument. These monetary policy instruments of the Bank of Latvia are in line with those used in the euro area.

Reflecting interest rate increases in the euro area and macroeconomic development trends in Latvia, the Bank of Latvia generally tightened monetary conditions in 2006 and 2007 as shown by increases in its principal refinancing rate from 4.0 per cent. at the beginning of 2006 to 6.0 per cent. in May 2007. The Bank of Latvia's reserve ratio was 8.0 per cent. in December 2006.

As economic activity weakened domestically and globally in 2008 and inflationary pressures were expected to ease significantly, the Bank of Latvia began to reduce its reserve requirements so that by December 2008 the reserve ratio for liabilities with a maturity over two years was 3.0 per cent. and the reserve ratio for other liabilities was 5.0 per cent.

As a result of these reductions, a considerable liquidity surplus built up. In order to stimulate the absorption of this excess liquidity, the Bank of Latvia reduced its overnight deposit facility rate from 3.0 per cent. at the end of 2008 to 0.375 per cent. in November 2010. In addition, the refinancing rate was cut in three stages and stood at 3.5 per cent. in February 2011.

Money supply

Overall domestic liquidity (M3) grew by 14.6 per cent. in 2007 from LVL 5,506.8 million at the end of 2006 to LVL 6,311.6 million. Since then, reflecting the sharp downturn in the Latvian economy with both domestic and external demand shrinking, as well as the impact of the global financial crisis on the Latvian banking system and money market, M3 decreased by 4.3 per cent. in 2008 and by 2.8 per cent. in 2009. Along with real economy indicators, the growth in money supply also marked the end of recession in Latvia and M3 increased by 11.5 per cent. in 2010. At 31 March 2011, M3 was LVL 6,513.4 million, marginally down from LVL 6,547.6 million at 31 December 2010.

The increase in the most liquid assets, comprised in the base money aggregate (M0), contributed significantly to the shrinking of M3 in 2008 and 2009. Against a background of inflation deceleration and rising interest rates on time deposits and savings deposits, and the wider use of cashless payment methods, M0 decreased by 14.6 per cent. in 2008 and by 22.1 per cent. in 2009. The additional components of M1 are overnight deposits (which contracted by 18.3 per cent. in 2008 and by 6.7 per cent. in 2009) and currency in circulation (which contracted by 3.8 per cent. in 2008 and 23.0 per cent. in 2009). As a result, M1 as a percentage of M3 declined from 55.4 per cent. at the end of 2008 to 50.7 per cent. at 31 December 2009. By contrast, the demand for longer term monetary components increased. Partly reflecting increased interest rates, time deposits up to two years increased in 2008 by 19.5 per cent. and in 2009 by 8.9 per cent. In 2010, M0 increased by 6.6 per cent. and M1 increased by 26.6 per cent., reflecting increased use of cash payments and greater overnight cash deposits driven by growth in industrial sectors. In contrast to these developments, the demand for longer term monetary components included in M2 decreased. Partly reflecting low interest rates, time deposits up to two years decreased by 5.2 per cent. in 2010. As a result, M1 as a percentage of M3 increased to 57.6 per cent. at 31 December 2010. At 31 March 2011, M0 was LVL 1,665.9 million, down from LVL 1,755.2 million at 31 December 2010. At the same date, M1 was LVL 3,689.7 million, down from LVL 3,770.6 million at 31 December 2010 and M2 was LVL 6,407.4 million, only marginally down from LVL 6,445.6 million at 31 December 2010. At 31 March 2011, M1 as a percentage of M3 was 56.6 per cent.

Loans to domestic enterprises (including financial institutions and public non-financial corporations) and households in Latvia (''**private sector credit**''), which had increased in each of 2006, 2007 and 2008, fell in both 2009 and 2010 and continued to fall in the first quarter of 2011, reflecting both reduced availability and demand. Private sector credit in Latvia had expanded by 58.4 per cent. in 2006. Following measures taken by the government and the Bank of Latvia and a more conservative approach to lending by banks in Latvia as concerns about an overheating economy grew, credit growth started to slow from the middle of 2007, with the annual growth rate of private sector credit in Latvia falling to 34.2 per cent. in 2007 and 11.7 per cent. in 2008. In 2009 and 2010, private sector credit in Latvia declined by 7.3 per cent. and 8.3 per cent., respectively. At 31 March 2011, private sector credit was LVL 12,072.0 million, 2.6 per cent. lower than the level at 31 December 2010.

On the liability side of the Latvian banking sector's balance sheet, deposits from private domestic enterprises (excluding public non-financial corporations and financial institutions) and households (''**private sector deposits**'') grew in 2006 and 2007, by 39.4 per cent. and by 12.1 per cent., respectively. However, concerns about the stability of the banking sector (and in particular Parex Bank) towards the end of 2008 saw total private sector deposits fall by 6.5 per cent. in 2008 and by 5.7 per cent. in 2009. In 2010, private sector deposits grew by 12.6 per cent. (with the growth in Lat-denominated deposits being 27.4 per cent.) as confidence in Latvia's banking sector returned. At 31 March 2011, private sector deposits were LVL 4,579.3 million, 1.1 per cent. higher than the level at 31 December 2010.

The negative net foreign assets of the Latvian banking sector (excluding the Bank of Latvia) grew by LVL 1,285.8 million between 31 December 2006 and 31 December 2009. Latvian banks' foreign liabilities increased by LVL 2,514.9 million over the same period as a result of significant borrowing from non-resident credit institutions, which grew by LVL 2.0 billion (including borrowing from parent banks of LVL 1.9 billion). Over the same period, the foreign assets of Latvian banks grew by LVL 1,229.1 million.

In 2010, the negative net foreign assets of Latvian banks (excluding the Bank of Latvia) declined by LVL 1.1 billion, reflecting a fall in liabilities to non-resident credit institutions (LVL 0.9 billion, of which the fall in liabilities to parent banks was LVL 0.1 billion as these entities stabilised the availability of funding to their subsidiaries). Over the same period, the growth in foreign assets of Latvian banks (excluding the Bank of Latvia) was LVL 0.7 billion.

In the first quarter of 2011, the negative net foreign assets of Latvian banks (excluding the Bank of Latvia) declined by LVL 0.5 billion, reflecting a fall in liabilities to non-resident credit institutions (LVL 0.5 billion, of which the fall in liabilities to parent banks was LVL 0.1 billion as these entities stabilised the availability of funding to their subsidiaries). Over the same period, the fall in foreign assets of Latvian banks (excluding the Bank of Latvia) was LVL 0.3 billion.

The table below sets out certain Latvian liquidity indicators as at 31 December in each of 2006, 2007, 2008, 2009 and 2010 and as at 31 March 2011.

	2006	2007	2008	2009	2010	2011
Currency in circulation	1,073.9	1,049.5	1,018.1	788.2	937.9	909.3
Overnight deposits at the Bank of Latvia	1,174.9	1,421.7	1,093.4	857.6	817.3	756.6
Base money (M0)	2,248.8	2,471.2	2,111.5	1,645.8	1,755.2	1,665.9
Currency in circulation (less vault cash balances)	969.3	900.0	866.1	667.3	807.4	795.6
Overnight deposits	3,096.5	3,035.2	2,479.0	2,312.0	2,963.2	2,894.1
Money supply (M1)	4,065.8	3,935.2	3,345.1	2,979.3	3,770.6	3,689.7
Deposits with agreed maturity of up to 2 years	1,241.9	1,971.9	2,356.1	2,565.2	2,430.6	2,466.9
Deposits redeemable at notice of up to 3 months	148.2	335.0	263.7	251.6	244.4	250.8
Private domestic liquidity (M2)	5,456.0	6,242.0	5,964.9	5,796.2	6,445.6	6,407.4
Debt securities issued with maturity of up to 2 years	4.8	28.2	4.4	0.9	20.6	20.6
Money market fund shares and units	46.1	41.3	70.2	76.1	81.4	85.4
Overall domestic liquidity (M3)	5,506.8	6,311.6	6,039.5	5,873.1	6,547.6	6,513.4
Broad money (M2) to nominal GDP (*per cent.*)	48.8	42.2	36.8	44.3	50.6	—(1)
Private sector credit	9,722.9	13,050.6	14,577.7	13,514.9	12,399.3	12,072.0
Private sector credit to nominal GDP (*per cent.*)	87.0	88.3	90.1	103.3	97.4	—(1)
Private sector deposits	4,162.5	4,666.8	4,360.6	4,110.4	4,628.5	4,579.3

Source: Bank of Latvia

Note:

(1) No GDP figure for the first three months of 2011 is available.

Foreign Assets

The table below sets out a breakdown of the foreign assets held by the Bank of Latvia as at 31 December in each of 2006, 2007, 2008, 2009 and 2010.

	2006	2007	2008	2009	2010
	(LVL millions, except for months of imports of goods)				
Gold	83.7	99.1	109.0	134.4	187.2
Convertible foreign currencies	2,333.3	2,687.7	2,488.7	3,151.0	3,782.2
Net foreign assets	2,414.4	2,776.0	2,332.3	3,313.1	4,032.1
Reserve assets (in months of imports of goods)	4.4	4.2	3.8	8.1	8.1

Source: Bank of Latvia

As at 31 December 2006, Latvia's gold and convertible foreign currency assets amounted to LVL 2,417.0 million. In 2006 and 2007, the country's net foreign assets (being its foreign assets less its foreign liabilities) increased, reaching LVL 2,776.0 million as at 31 December 2007. During this period, the net foreign assets grew mainly through net purchases by the Bank of Latvia of foreign currency, reflecting inflows of foreign investment and EU structural funds. In addition, growth in euro loans subsequently converted into Lats and the expansion of the minimum reserve base created additional demand for Lat liquidity.

As at 31 December 2008, the net foreign assets declined to LVL 2,332.3 million, reflecting significant sales of euro by the Bank of Latvia in an effort to enhance liquidity and to defend the exchange rate against speculation relating to a possible devaluation of the Lat although the effect of these sales was partially offset through the receipt of the first tranche of funds under the IMF Standby Arrangement agreed at the end of 2008. During 2009 and 2010, net foreign assets grew, principally as a result of foreign assistance funding received and, as at 31 December 2010, Latvia's net foreign assets amounted to LVL 4,032.1 million. At 31 December 2009 and 31 December 2010, net foreign assets were equal to around 8.1 months of imports of goods. At 31 March 2011, Latvia's net foreign assets had declined to LVL 3,723.6 million.

The Bank of Latvia is the only institution responsible for exchange rate policy in Latvia and remains committed to pursuing a fixed narrow band exchange rate strategy prior to the country's adoption of the euro as its national currency. Maintenance of the fixed exchange rate is also the central goal of the economic reform programme agreed with the EU and the IMF as part of the financial assistance package. Latvia has been a full member of the EU exchange rate mechanism ERM II since May 2005.

Interest Rates

Latvian bank interest rates for loans and deposits in Lats were relatively stable in 2006 but since the beginning of 2007 have been more volatile and generally increased up to the second half of 2009, after which they generally decreased (although they remained volatile). Latvian bank interest rates for loans and deposits in euro grew gradually from 2006 until 2008. Since October 2008, Latvian bank interest rates for euro-denominated loans and deposits have substantially declined.

The weighted average interest rate for short-term deposits in Lats was 3.4 per cent. in January 2006 and 0.5 per cent. in January 2011. The corresponding interest rate on deposits in euro was 2.1 per cent. in January 2006 and 1.3 per cent. in January 2011. The weighted average interest rate for long-term deposits denominated in Lats was 4.0 per cent. in January 2006 and 3.7 per cent. in January 2011, while the equivalent rate for long-term deposits in euro was 3.6 per cent. in January 2006 and 4.1 per cent. in January 2011.

Overall, the weighted average interest rate on loans in Lats to domestic enterprises and households increased by 3.4 per cent. to 9.9 per cent. for short-term transactions and by 2.4 per cent. to 11.8 per cent. for long-term transactions in the period from January 2006 to January 2011. The weighted average interest rate on short-term loans in euro declined from 4.6 per cent. to 3.9 per cent., while the weighted average interest rate on long-term loans in euro increased from 5.6 per cent. to 7.6 per cent. over the same period.

Financial Sector Supervision

The Latvian Financial and Capital Market Commission (the "**FCMC**") is a unified supervisory authority for the financial sector in Latvia. The FCMC is an autonomous public institution and its purpose is to promote the protection of the interests of investors, depositors and insured persons as well as the development and stability of the financial and capital markets. To this end, the FCMC regulates and supervises the financial and capital markets and the activities of participants in those markets. In addition, the FCMC administers the Latvian Deposit Guarantee Fund, the Fund for the Protection of Insured Persons and the Investor Protection Scheme. The FCMC's objectives and responsibilities are defined by law.

Latvia has implemented the EU Financial Sector Assessment Programme (FSAP) Directives and post FSAP Directives, which were required to be implemented in Member States by 31 December 2010. These directives include the Capital Requirements Directive (**CRD**) and its amendments, the Prospectus Directive, the Transparency Directive, the Markets in Financial Instruments Directive, the Third Money Laundering Directive and the Payment Services Directive. The FCMC participates in the work of the recently established European Systemic Risk Board and European Supervisory Authorities and also closely follows discussions on further developments in the regulatory framework proposed by the European Commission and international organisations. The FCMC is strongly committed to ensuring the effective implementation of the regulatory framework for the financial sector.

Since the beginning of 2009, in response to the global financial crisis, a number of steps have been taken to improve the intervention capacity of the FCMC. In particular, a new law on bank takeovers and amendments to laws relating to credit institutions, deposit guarantees and the FCMC, as well as the Bank of Latvia's regulations on emergency liquidity support, have enhanced the ability of the authorities to intervene in the banking sector. The FCMC has enacted new regulations on bank asset quality assessment and provisioning and has issued supervisory guidance relating to banks' internal capital adequacy assessment procedures, with a view to improving capital reserves.

In 2010, Latvia implemented the provisions of CRD II and those provisions of CRD III which were required to be implemented in Member States by the end of the year. Amendments to the deposit guarantee law have resulted in an increase of the deposit amount guaranteed by the state up to €100,000. The FCMC has also introduced amended regulations on liquidity risk management and credit risk management. The FCMC continues to monitor the banking sector closely, based on increased bank reporting frequencies. During inspections, particular attention has been paid to assessing capital adequacy, risk management and compliance functions and policies in banks and cooperation with parent banks' supervisors has been strengthened.

Following the nationalisation of Parex Bank in November 2008, the government participated in a rescheduling agreement of the bank's syndicated loans in March 2009 and, in April 2009, agreed with the EBRD that the EBRD would take a 25 per cent. shareholding in Parex Bank and advance the bank new subordinated funds as its contribution to the financial assistance package. This investment was made in September 2009. In July 2009, the European Commission commenced an investigation in relation to State aid to Parex Bank and, in September 2010, the European Commission confirmed that the State aid rules had been complied with and the restructuring of Parex Bank was successfully completed. As part of the restructuring process, on 1 August 2010, Parex Bank was split into two banks, with the performing assets being transferred to the newly established Citadele Bank and the non-performing assets remaining in Parex Bank. The EBRD became a shareholder of Citadele Bank at the same time and currently owns 25 per cent. and one share in Citadele Bank and nearly 15 per cent. of Parex Bank's shares. The Government's exposure to Parex Bank has fallen from LVL 1,219 million at 22 May 2009 to LVL 613 million at 25 May 2011. Similarly, the Government's exposure to Citadele Bank has fallen from LVL 246 million at 1 August 2010 to LVL 221 million at 25 May 2011.

In May 2011, the government approved in principle the sale of shares in Citadele Bank and determined that shares in Parex Bank would not be offered to investors and that the bank should continue to focus on maintaining or increasing the value of its assets in order to maximise the State's recovery of the financial assistance granted to Parex Bank. A transformation plan in respect of the government-owned Mortgage and Land Bank of Latvia was approved by the Cabinet of Ministers in April 2011 and is being submitted to the EU to receive European Commission approval for state aid granted to the bank. The aim of the plan is to create a development finance institution and to sell the commercial assets of the bank which are not required by it to fulfil its development function.

Money Laundering and Terrorist Financing Regulations

The money laundering prevention framework in Latvia is based on law, regulations promulgated by the Cabinet of Ministers, regulations for enhanced customer due diligence approved by the FCMC and recommendations made by the Bank of Latvia to licensed foreign exchange dealers. A new law relating to the prevention of money laundering and terrorist financing was introduced in July 2008 and is compliant with applicable EU Council Directives.

Banking Sector Development

Banks dominate the financial sector in Latvia, accounting for about 93 per cent. of its total assets. Currently there are 21 licensed domestic banks in Latvia and branches of eight banks licensed elsewhere in the EU. Two more EU banks, one Finnish and one Estonian, are scheduled to open branches in Latvia in 2011. All the banks in Latvia have been licensed as universal banks and can provide a full range of financial and investment services.

As at 31 December 2010, almost 65 per cent. of the Latvian banks' share capital was owned by foreign investors. Four subsidiaries of EU banks (Skandinaviska Enskilda Banken AB (publ), Swedbank AB (publ), Bank DNB Nord and UniCredit Bank Austria AG) and eight branches of EU banks (Nordea Bank Finland Plc, Skandinaviska Enskilda Banken AB (publ), Svenska Handelsbanken AB (publ), Allied Irish Banks p.l.c., Danske Bank A/S, BIGBANK plc, AB Bank SNORAS and Scania Finans Aktiebolag) accounted for approximately 58 per cent. of total Latvian bank assets and approximately 68 per cent. of total Latvian bank loans. All other banks in Latvia are privately owned, except for three banks that are controlled by the government (Parex Bank, Citadele Bank and

Mortgage and Land Bank of Latvia). The market share of these State-owned banks was 15.5 per cent. of total assets at 31 December 2010.

Since 2008, the global financial crisis has had a material adverse impact on Latvia's economy and its banking sector. In particular, the growth rate of loans (which averaged 48 per cent. per annum between 2003 and 2007) dropped to 11.2 per cent. in 2008 and shrank by 7.0 per cent. and 7.1 per cent. in each of 2009 and 2010, respectively, as low household income, a high unemployment rate and uncertain future prospects resulted in a significantly reduced demand for loans in 2009 and 2010.

The recession in Latvia during 2009 also adversely affected the financial position of both corporate and retail borrowers, resulting in a deterioration of loan quality and an increase in provisions in Latvian banks. As at 31 December 2009 and 2010, 74.5 per cent. and 73.4 per cent., respectively, of Latvian bank loans were without payment delays (compared to 85.0 per cent. as at 31 December 2008). The amount of Latvian bank loans with payments more than 90 days overdue ("**NPLs**") was 16.4 per cent. and 19.0 per cent., respectively, at 31 December 2009 and 2010, compared to 3.6 per cent. at 31 December 2008. The greatest concentration of NPLs (around 58 per cent. at 31 December 2010) is in the real estate sector, including housing loans and construction loans. As at 31 March 2011, 73.3 per cent. of Latvian bank loans were without payment delays, while the amount of NPLs was 18.7 per cent.

Loan loss provisions in the Latvian banking sector have grown since 31 December 2008, when they amounted to 2.2 per cent. of the total bank loan portfolio, and totalled LVL 1.3 billion, or 8.6 per cent., of the total bank loan portfolio at 31 December 2009 and LVL 1.6 billion, or 11.3 per cent., of the total bank loan portfolio at 31 December 2010. Banks in Latvia continued to restructure their loans during 2010 and the amount of restructured loans reached LVL 2.9 million, or 19.9 per cent. of total banking loans at 31 December 2010 (compared to 16.1 per cent. at 31 December 2009). The loans in a work-out process totalled LVL 2.2 million, or 15.3 per cent. of total banking loans at 31 December 2010 (compared to 9.5 per cent. at 31 December 2009).

At 31 March 2011, the liquidity ratio of all banks in Latvia exceeded the minimum requirement of 30 per cent., with the average liquidity ratio at 31 March 2011 being 65.1 per cent. compared to 67.9 per cent. at 31 December 2010 and 62.8 per cent. at 31 December 2009. In addition, the capital adequacy ratio ("**CAR**") of all banks in Latvia was above the minimum requirement of 8 per cent., with the average CAR of the banking sector at each of 31 March 2011, 31 December 2010 and 31 December 2009 being 15.2 per cent., 14.6 per cent. and 14.6 per cent., respectively, and the Tier I CAR at the same dates being 12.0 per cent., 11.5 per cent. and 11.6 per cent., respectively.

Non-bank deposits in the Latvian banking sector grew by 25.1 per cent. in 2006 and 31.2 per cent. in 2007 before falling by 4.1 per cent. in 2008 and by 2.2 per cent. in 2009. The deposit base of banks in Latvia stabilised in 2010. Both resident and non-resident depositors' confidence has been restored, as shown by a 16.3 per cent. increase in deposits (9.6 per cent. for resident deposits and 27.4 per cent. for non-resident deposits) during 2010, with total deposits at 31 December 2010 amounting to LVL 11.1 billion.

Total assets in the Latvian banking sector grew by 45.4 per cent. in 2006, by 37.8 per cent. in 2007 and by 6.1 per cent. in 2008, before falling by 6.7 per cent. in 2009 and then growing by 1.3 per cent. in 2010. The Latvian banking sector is mainly financed by borrowings from banks (which accounted for 31.2 per cent. of total liabilities at 31 December 2010) and deposits (which accounted for 50.6 per cent. of total assets at 31 December 2010). Funding from parent banks, which had increased by 101.8 per cent. in 2006, 46.4 per cent. in 2007 and 22.6 per cent. in 2007, decreased by 17.8 per cent. in 2009 and by 2.3 per cent. in 2010.

The profit of the Latvian banking sector for each of 2006, 2007 and 2008 was LVL 265.9 million, LVL 371.3 million and LVL 60.1 million, respectively. In 2009 and 2010, the losses of the Latvian banking sector were LVL 773.4 million and LVL 360.7 million, respectively, in each case driven by significant loan loss provisioning.

All statistical data under the heading "Banking Sector Developments" in this section has been derived from Financial Capital Markets Commission reports.

The table below sets out certain performance indicators of the Latvian banking sector and the quality of its loan portfolio as at the last day of each quarter from 1 January 2006 to 31 March 2011.

	2006				2007				2008				2009				2010				2011
	31 Mar	30 Jun	30 Sep	31 Dec	31 Mar	30 Jun	30 Sep	31 Dec	31 Mar	30 Jun	30 Sep	31 Dec	31 Mar	30 Jun	30 Sep	31 Dec	31 Mar	30 Jun	30 Sep	31 Dec	31 Mar
Liquidity (*per cent.*)																					
Liquidity ratio	49.0	51.5	51.1	51.1	51.0	48.1	54.7	55.7	51.4	50.7	49.1	52.8	48.0	49.6	54.4	62.8	62.8	64.5	66.4	67.9	65.1
Loans issued to non-banks/ total assets	65.9	65.2	66.9	68.4	69.4	70.6	69.5	68.1	71.3	71.1	73.0	71.4	73.8	73.6	73.1	71.2	70.7	70.1	69.6	65.3	65.5
Loans to non-banks/ deposits	119.6	124.1	134.3	140.2	150.6	151.2	158.1	146.5	158.9	154.5	164.8	170.0	169.8	173.0	175.1	161.6	155.0	145.7	143.6	129.0	129.0
Long-term loans to non-banks/ total loans	49.2	49.7	51.0	52.1	53.7	55.0	55.8	56.5	57.2	57.9	58.1	59.1	58.9	59.7	59.8	60.2	60.3	60.6	60.3	61.0	61.8
Demand deposits/ total deposits	67.5	67.5	68.4	68.3	68.1	66.9	65.2	60.9	58.1	59.8	55.9	49.7	46.8	47.4	45.2	45.0	46.8	49.0	49.4	53.2	53.5
Capital adequacy (*per cent.*)																					
Capital adequacy	10.9	10.5	10.5	10.2	10.4	10.5	11.0	11.1	12.6	12.2	12.3	11.8	11.4	12.4	13.6	14.6	14.2	14.2	15.2	14.6	15.2
Risk weighted assets/ total assets	72.5	73.1	74.0	72.9	73.0	74.0	71.1	68.5	67.4	65.8	66.6	65.0	68.0	69.2	66.6	65.0	64.6	63.5	62.5	59.9	59.9
Profitability (*per cent.*)																					
Return on equity	28.6	24.0	24.5	25.6	27.7	25.9	24.2	24.2	19.5	17.7	14.7	3.6	(11.2)	(38.1)	(42.1)	(41.6)	(29.8)	(28.7)	(24.5)	(20.4)	7.2
Return on assets	2.2	1.9	1.9	2.1	2.1	2.1	2.0	2.0	1.6	1.5	1.2	0.3	(0.9)	(3.1)	(3.5)	(3.5)	(2.5)	(2.3)	(2.0)	(1.6)	0.6
Net interest rate margin	2.6	2.6	2.6	2.7	2.6	2.7	2.7	2.7	2.5	2.5	2.5	2.5	2.0	1.9	1.8	1.6	1.0	1.0	1.1	1.1	1.3
Quality of the loan portfolio (*per cent. of principal amount*)																					
Not yet due for repayment	94.6	94.2	95.1	96.1	94.3	95.1	92.8	93.2	90.9	89.5	88.3	85.0	79.5	76.5	74.8	74.5	72.5	71.4	71.5	73.4	73.3
Up to 30 days overdue	3.8	4.0	3.3	3.1	4.6	3.6	5.6	4.9	5.6	6.6	6.7	7.2	7.4	7.3	7.2	5.2	6.1	7.0	6.8	5.1	5.4
31 – 90 days overdue	0.6	0.6	0.5	0.4	0.6	0.7	0.9	1.2	2.0	1.9	2.5	4.2	6.0	4.2	3.5	3.9	3.6	2.6	2.2	2.5	2.6
91 – 180 days overdue	0.2	0.3	0.2	0.1	0.1	0.2	0.3	0.4	0.8	1.2	1.0	1.5	3.8	5.4	3.9	3.3	2.8	2.3	1.8	1.8	1.4
More than 180 days overdue	0.8	0.8	0.9	0.3	0.3	0.3	0.4	0.4	0.6	0.9	1.4	2.1	3.3	6.6	10.6	13.1	15.1	16.7	17.6	17.2	17.3

Source: Financial Capital Markets Commission

NASDAQ OMX Riga

NASDAQ OMX Riga is the only licensed stock exchange in Latvia. It was established in 1993 and commenced trading in 1995. NASDAQ OMX Riga also owns the Latvian Central Depository (the "**LCD**"). The LCD is the national depository for public securities responsible for custody and settlement of all public securities issued in Latvia.

NASDAQ OMX is the major shareholder of NASDAQ OMX Riga, with a 92.98 per cent. ownership interest.

Only licensed NASDAQ OMX Riga members, being banks and brokerage companies, may trade on the exchange. Currently, NASDAQ OMX Riga has 28 trading members. NASDAQ OMX Riga operates four lists: the Main List, the Secondary List, the Bond List and the Funds List.

At 28 February 2011, 34 Latvian companies' equity securities, 12 corporate debt securities, 41 Government treasury bill and bonds issues and 22 investment funds were listed on NASDAQ OMX Riga.

The table below sets out certain information relating to NASDAQ OMX Riga as at 31 December in each of 2007, 2008, 2009 and 2010 and as at 31 March 2011.

	As at 31 December				As at 31 March
	2007	**2008**	**2009**	**2010**	**2011**
			(*LVL millions*)		
Equity market capitalisation	1,474.8	819.8	925.6	661.7	708.5
Debt market capitalisation	428.9	804.9	782.6	745.3	769.1
Total market turnover	100.5	46.9	26.6	22.7	12.9
Equity market turnover	69.3	20.0	9.8	14.6	12.0
Debt market turnover	31.3	26.9	16.8	8.0	0.9

Source: NASDAQ OMX

During each trading session, on-line price information is distributed via Reuters, Bloomberg, FT Interactive Data, Infront, SIX, Telekurs and other market data customers.

NASDAQ OMX Riga has a guarantee fund (the "**Guarantee Fund**"), financed through an initial contribution and a variable contribution, which depends on an individual member's trading activity. The Guarantee Fund is used in case of a member's cash default.

The LCD is the sole central securities depository in Latvia. The LCD provides safe-custody of all publicly issued securities in Latvia, clearing and settlement services for securities trading on NASDAQ OMX Riga and also manages corporate actions related to securities. The proprietary accounts of the LCD's intermediaries and custodians are segregated from their client accounts, thus reducing risk in case of a default by a bank or a brokerage company. The LCD is a member of ANNA (the Association of National Numbering Agencies) and has obtained National Numbering Agency status in Latvia. As a result, the LCD assigns ISIN codes and CFI codes for all issues registered with the LCD. The LCD also administers the state funded pension (the second pillar of the pension system). The LCD has established relationships with its Estonian and Lithuanian central depositories and also with International Central securities depositories, Euroclear Bank and Clearstream, allowing LCD's participants to act as custodians of financial instruments registered with those depositories.

PUBLIC FINANCE

The general government budget consists of a consolidation of the central government budget and local government budgets, with transfers between the budgets being eliminated on consolidation. The central government budget includes the central government basic budget, a special budget (being the social security budget) and budgets of derived public persons (being those bodies which are partially financed from the State budget). The consolidated general government budget is prepared on a cash basis.

Prior to the supplementary budget prepared in June 2009, Latvia maintained a privatisation fund (which was liquidated during 2009 in accordance with the privatisation law) and a long-term stabilisation reserve. The operations of the stabilisation fund have been suspended until the end of 2012.

In 2012, a new fiscal discipline law is scheduled to come into effect which aims to reduce the effects of economic cyclicality through, among other measures, setting targets for allowable deficits in times of economic growth.

Preparation and Approval of the Central Government Budget

The annual budget formulation process involves the Cabinet of Ministers, the Ministry of Finance, the State Chancellery, the Ministry of Regional Development and Local Government as well as the other government ministries and the Latvian Association of Local and Regional Governments. Currently, the IMF and the European Commission also exert a substantial influence over budgetary decisions through their influence on structural reforms to various sectors, including the public sector, the education sector and the social sector, as part of the financial assistance package. See "*Indebtedness – Financial Assistance from International Lenders*".

In February of each year, the Minister of Finance submits to the Cabinet of Ministers a draft schedule for the preparation and submission of the Annual Law on the State Budget for the following financial year (the "**State Budget Law**"), as well as a draft schedule for the preparation and submission of a framework for medium-term macroeconomic development and fiscal policy for the next three financial years (the "**Medium-term Framework**"). If there are planned resources for new policy initiatives, the Minister of Finance together with the State Chancellery, will prepare a legal act on medium-term budget goals and priority development directions for the next three years, to be submitted to the Cabinet of Ministers by 1 February.

In addition to the approval of the State Budget Law for one year, the Medium-term Framework must set out the maximum permitted amount of expenditures for ministries and other central state institutions for the following three years. The medium-term expenditure ceiling calculations are made twice a year, first when preparing the Medium-term Framework and second when revising the Medium-term Framework at the point when the State Budget Law is submitted to Parliament. The Medium-term Framework also includes expected macroeconomic development, fiscal policy goals, budget revenue forecasts and the appropriation reserve over the medium term.

All ministries must submit proposals for applicable line items, measured against the current State Budget Law, on the basis of which the Ministry of Finance calculates base budget expenditures for the next three years. The subtraction of base budget expenditures from available resources in the upcoming budget year and the following two years determines the part of the budget that is available for development over the medium term. Should planned revenue decrease, budget expenditures may also decrease. During the preparation of the central government budget for 2011, the division of budget expenditures was also screened by function and an analysis of the need for each function was also undertaken.

Ministries and other state central institutions prepare budget requests according to the scope of the maximum permitted expenditure amount. Budget requests are reviewed and collated by the Budget Department of the Ministry of Finance. The Minister of Finance seeks to obtain agreement on these draft budgets with the heads of ministries and other central institutions. Should agreement not be obtained, the Cabinet of Ministers may resolve the dispute by a majority vote.

The Cabinet of Ministers is required to submit to the Saeima by 1 October of each year a draft of the State Budget Law, together with appropriate explanations and proposals for amendments to laws to conform them with budgetary requests and the Medium-term Framework. Reflecting the elections which were held in October 2010, an exception was approved to permit the submission of the draft

State Budget Law to Parliament to occur before 31 October and the State Budget Law for 2011 was approved by Parliament in mid-December 2010.

The Saeima is authorised to amend the draft State Budget Law proposed by the Cabinet of Ministers. However, the Constitution restricts the amendment powers of the Saeima by providing that decisions involving additional expenditures must allocate funds to cover such expenditures. The budget adopted by the Saeima enters into force at the beginning of the year in respect of which the law has been prepared. If a budget has not come into force in due time, the Minister of Finance approves the State budget expenditures, provided that the monthly amount of expenditures cannot exceed one twelfth of the appropriations of the previous year until the relevant State Budget Law has been passed.

Execution of the Central Government Budget

The Law on Budget and Financial Management (the "**Budget Management Law**") authorises the Treasury, as the administrative institution directly subordinate to the Ministry of Finance, to organise the execution and financial accounting of the central government budget. The Treasury grants spending allocations to all entities financed from the budget and ensures that payments executed by those entities comply with the appropriations limits set out in the central government budget.

As part of its implementation of the central government budget, the Treasury opens budget accounts for budget executors, grants allocations based on financial plans, ensures payments made by entities financed from the budget and maintains records of budget execution transactions effected by entities financed from the budget.

The Treasury prepares daily, monthly, quarterly and annual reports on the execution of the central government budget and local government budgets. Reports on budget execution are compiled and submitted by the central government budget entities and local governments in accordance with the Budget Management Law and other laws and regulations, including the Law on Local Governments, the Law on Local Government Budgets, the relevant State Budget Law and the regulations of the Cabinet of Ministers.

As prescribed by law, local governments independently prepare, approve and implement their respective budgets. According to procedures specified by the Cabinet of Ministers, local governments prepare and submit to the Treasury monthly and annual reports regarding the implementation of their budgets, financing and the amount of their borrowings and guarantees, and the Ministry of Finance prepares a financial year report, submitted to the Cabinet by the Minister for Finance (The Annual Report of the Republic of Latvia on the Implementation of the State Budget and Budgets of Local Governments) (the "**Annual Report**"). The submission of the Annual Report is accompanied by an opinion of the State Audit Office ("**SAO**") in accordance with the Law on the State Audit Office. The Cabinet then submits the Annual Report and the opinion of the SAO to the Saeima by 15 October of the financial year following the reporting year.

The Annual Report is prepared in accordance with the requirements and structure stipulated in Article 31 of the Budget Management Law. Article 31 also governs the form of the financial and budget execution information to be included in the Annual Report, as well as the explanations to be provided for significant changes in the accounting year.

The SAO conducts a financial audit and renders an opinion on the correctness of preparation of the Annual Report according to the Budget Management Law and the Law on the State Audit Office. The audit is conducted in accordance with international auditing standards as recognised by the Republic of Latvia. The SAO inspects the preparation of the Annual Report and the correspondence of transactions with regulatory requirements. The audit also assesses the accounting principles applied.

The SAO sends draft audit reports relating to the Ministry of Finance for review to the units and subordinated institutions of the Ministry of Finance which are responsible for the evaluation of audit proposals and problematic issues. The Internal Audit Department of the Ministry of Finance supervises the implementation of the SAO recommendations related to the Ministry of Finance and its subordinated institutions.

Relationship between Central Government and Local Government Budgets

Local governments prepare, approve and execute their budgets independently. The central government budget is consolidated with local government budgets in the general government budget.

During the initial phases of the budget preparation process, the Ministry of Finance, together with local governments, determines the amount of grants for equalisation of local government finances and the total amount of central government budget financing and its distribution by local governments for the next financial year. Local governments are represented by The Latvian Association of Local and Regional Governments. The Cabinet of Ministers includes a protocol setting out the results of negotiations between the Ministry of Finance and the local governments with the draft State Budget Law when it is submitted to the Saeima.

An Equalisation Fund for Local Government Finance, formed from local government payments and grants from the central government budget, focuses on providing equal conditions for execution of local government functions by transferring financial resources from certain local governments with higher socio-economic conditions to local governments with lower socio-economic conditions.

The State Budget Law may provide for grants and subsidies from the central government budget to ensure the execution of State functions.

Local governments are empowered to take loans and provide guarantees, but the State Budget Law sets a maximum amount for total increases of such loans and guarantees.

Impact of the Global Financial Crisis on Latvia's Budgets for 2009, 2010 and 2011

When originally passed in November 2008, the central government 2009 budget envisaged a central government fiscal deficit equal to 1.5 per cent. of projected nominal GDP. However, as economic conditions worsened, it became apparent that the assumptions underlying the original 2009 central government budget were too optimistic and would be likely to result in a significantly higher central government deficit. As a result, in December 2008, the original central government budget was revised to indicate a central government deficit of 4.7 per cent. of projected nominal GDP. To achieve this, the government envisaged a programme of shifting the tax burden from direct to indirect taxation over the 2008 to 2011 period, tax increases (principally in VAT and excise tax), broadening the direct tax base for capital gains and real estate taxes in 2010 and improvements in tax collection. On the expenditure side, the revised budget set out targets for cuts in public sector wages and in other areas of current expenditure, but left the detail of these cuts to a further supplementary budget to be prepared during 2009. In addition, the government agreed a protocol with local governments in December 2008 in relation to the adjustments to be made by them to their own budgets although, again, the detail was left for later agreement.

On 16 June 2009, the Latvian parliament adopted a second supplementary budget which aimed to restrict the central government deficit to around 5.1 per cent. of projected nominal GDP and the general government deficit to around 7.1 per cent. of projected nominal GDP (compared to an eventual outcome of a deficit equal to 6.8 per cent. of nominal GDP). The June supplementary budget envisaged revenue increases, including through increased dividends from state-owned companies, increased excise taxes, reductions in the basic personal allowance and increases in gambling tax. On the expenditure side, cuts were introduced across all ministry and state agency budgets. The cuts also sought to increase the efficiency and quality of education and healthcare services, make limited and targeted pension reductions and reduce less targeted social security spending.

On 1 December 2009, the Saeima passed the 2010 State Budget Law. This budget targeted a central government deficit of 4.4 per cent., and a consolidated general government deficit of 7.6 per cent. (compared to an eventual outcome of a deficit equal to 6.3 per cent. of nominal GDP), of projected nominal GDP and assumed a deflation rate of 3.7 per cent., anticipated economic growth in the second half of the year and stabilisation of the unemployment rate at 13.8 per cent. To achieve this, on the revenue side, the government proposed the introduction of measures to broaden the personal income tax base and increase the rate of personal income tax, to introduce a progressive real estate tax on dwellings, to increase the annual vehicle tax, to extend excise tax to natural gas, to remove a number of exemptions in the tax system and to reform the real estate tax base. On the expenditure side, the 2010 budget proposed a number of structural reforms, including consolidating state agencies and ministries, reducing state support to agriculture; cutting defence procurement costs, optimising its network of embassies, reducing the level of social benefits whilst expanding the social safety net, reducing road maintenance and improving the targeting of public transport subsidies.

In December 2010, the State Budget Law for 2011 was approved by the new Parliament. This budget targeted a central government deficit of 4.4 per cent., and a consolidated general government deficit of 5.4 per cent., of projected nominal GDP and assumed an inflation rate of 1.1 per cent., continued economic growth throughout the year and an unemployment rate of 17.1 per cent. The 2011 budget proposes a number of revenue raising measures including an increase in the rates of the real estate tax on dwellings, an increase in dividends from state-owned enterprises, an increase of the standard rate of VAT from 21 per cent. to 22 per cent. and changes in the application and rate of certain reduced rates of VAT, the introduction of a financial stability levy and an action plan to combat the gray economy (aimed at improving the business environment and increasing tax revenues). On the expenditure side, the expenditure of certain ministries (including Transport, Welfare, Health, Defence, Agriculture, Justice, Education and Science and Interior) was reduced and a net expenditure cut in the budgets of local governments was proposed.

Key aspects of the 2011 budget included measures to promote growth in the economy, the stabilisation of the state social budget through the freezing of pension indexation and not increasing contributions to the second tier and an emphasis social fairness in tax policy by gradually switching the tax burden from payroll taxes to consumption and increasing progressivity in the tax system.

On 14 April 2011, the Latvian parliament adopted a supplementary budget which targeted a reduced central government deficit of 3.9 per cent., and a reduced consolidated general government deficit of 4.1 per cent., of projected nominal GDP and assumes an average inflation rate of 3.5 per cent., continued economic growth throughout the year and an unemployment rate of 16.4 per cent. The 2011 supplementary budget principally aimed to increase revenues through a number of measures including increases in excise taxes on alcoholic beverages, tobacco products and petrol, the abolition of the reduced rate of VAT for natural gas and medicines and an increase in gambling tax.

As part of the terms of the financial assistance package, the government has agreed general government budget deficit targets of 10 per cent. of nominal GDP in 2009, 8.5 per cent. of nominal GDP in 2010, 6 per cent. of nominal GDP in 2011 and below 3 per cent. of nominal GDP in 2012. The targets are calculated based on the European System of National and Regional Accounts ("**ESA 95**"), which differs significantly from the cash flow-based budget deficit numbers referred to above.

As a percentage of nominal GDP, the general government budget deficits calculated according to ESA 95 were 0.5 per cent. in 2006, 0.3 per cent. in 2007, 4.2 per cent. in 2008, 9.7 per cent. in 2009 and 7.7 per cent. in 2010. According to Ministry of Finance forecasts, the general government budget deficit calculated according to ESA 95 in 2011 will be 4.5 per cent. Latvia's objective remains to reach an ESA 95 deficit level of 2.5 per cent. of nominal GDP in 2012 and to introduce the euro in 2014.

Consolidated General Government Budget

The table below sets out a summary of the consolidated general government budget outcome for each of the years ended 31 December in each of 2006, 2007, 2008, 2009 and 2010 and a summary of the general government budget for the year ended 31 December 2011.

		2006	2007	2008	2009	2010	2011[1]
				(LVL millions)			
General government budget revenues		**4,015.6**	**5,350.1**	**5,727.2**	**4,728.4**	**4,600.5**	**5,123,8**
1.	Tax revenues	3,299.0	4,363.1	4,737.4	3,509.7	3,398.3	3,713.8
1.1	Direct taxes	1,935.8	2,626.9	3,004.6	2,161.1	2,069.4	2,152,9
	of which: Corporate income tax	*253.8*	*399.8*	*503.1*	*197.2*	*112.2*	*121.3*
	Personal income tax	*657.2*	*888.0*	*1,029.1*	*724.1*	*778.8*	*739.4*
	Social security contributions	*958.4*	*1,265.0*	*1,401.7*	*1,166.7*	*1088.7*	*1,192.8*
	Property tax	66.4	74.2	70.7	73.1	89.7	99.5
1.2	Indirect taxes	1,331.1	1,331.1	1,696.1	1,320.2	1,304.2	1,471.6
	of which: Valued added tax	*930.5*	*1,202.9*	*1,117.2*	*798.4*	*825.2*	*972.1*
	Excise tax	*366.2*	*448.1*	*540.9*	*504.1*	*458.1*	*476.2*
	Car tax	*13.7*	*16.7*	*9.5*	*2.6*	*3.6*	*4.0*
	Customs duties	*20.7*	*27.8*	*26.4*	*15.1*	*17.3*	*19.3*
1.3	Other taxes[2]	32.0	40.6	38.8	28.4	24.7	89.3
2.	Non-tax revenues	245.8	265.9	297.0	424.6	382.9	300.6
3.	Grants and donations	12.4	31.9	24.6	5.6	6.7	0
4.	Self-earned revenues	182.0	227.6	237.3	249.0	212.7	210.7
5.	Foreign financial assistance	265.0	461.5	430.8	528.1	599.9	898.7
General government budget expenditures		**4,070.9**	**5,255.4**	**6,266.5**	**5,626.3**	**5,409.7**	**5,671.6**
1.	Non-capital expenditure	3,535.8	4,495.0	5,523.2	5,191.1	5,016.3	5,045.8
2.	Capital expenditure	535.1	760.3	743.3	435.0	389.6	624.4
Financial balance		**(55.3)**	**94.7**	**(539.4)**	**(897.9)**	**(802.7)**	**(547.8)**

Source: Ministry of Finance

Notes:

(1) The amended central government budget approved by the Saeima on 14 April 2011 and Ministry of Finance projections of local government budgets.

(2) Including vehicle operating tax and tax on company cars introduced on 1 January 2011.

The table below summarises the performance of the consolidated general government budget for each of the years ended 31 December in each of 2006, 2007, 2008, 2009 and 2010 and the budget for the year ended 31 December 2011, in each case as a percentage of nominal GDP (calculated on a cash flow based budget basis).

		2006	2007	2008	2009	2010	2011[1]
				(as a percentage of nominal GDP)			
General government budget revenues		**35.9**	**36.2**	**35.4**	**36.1**	**36.2**	**38.2**
1.	Tax revenues	29.5	29.5	29.3	26.9	26.7	27.7
1.1	Direct taxes	17.3	17.8	18.5	16.6	16.3	16.0
1.2	Indirect taxes	11.9	11.5	10.4	10.3	10.4	11.0
1.3	Other taxes	0.3	0.3	0.2	—	—	0.7
2.	Non-tax revenues	2.2	1.8	1.9	3.2	3.0	2.2
3.	Grants and donations	0.1	0.1	0.1	0.0	0.1	0.0
4.	Self-earned revenues	1.6	1.5	1.5	1.9	1.7	1.6
5.	Foreign financial assistance	2.4	3.1	2.7	4.0	4.7	6.7
General government budget expenditures		**36.4**	**35.6**	**38.6**	**43.0**	**42.5**	**42.3**
1.	Non-capital expenditure	31.8	30.4	34.0	39.7	39.4	37.6
2.	Capital expenditure	4.8	5.1	4.6	3.3	3.1	4.6
Financial balance		**(0.5)**	**0.6**	**(3.3)**	**(6.8)**	**(6.3)**	**(4.1)**

Source: Ministry of Finance

Note:

(1) The amended central government budget approved by the Saeima on 14 April 2011 and Ministry of Finance projections of local government budgets. GDP for 2011 is projected to amount to LVL 13,415.9 million.

Revenues

Latvia's general government budget revenues comprise tax revenues and revenues from a limited number of other sources. The government's tax revenues are described below. The government's principal non-tax revenues are derived from a range of fees (such as licensing and land registration fees), dividends and interest income. The government's self-earned revenues reflect income from services provided by budget institutions (for example, guarantee fees for guarantees provided by the Treasury). Foreign financial assistance reflects infrastructure funds from the EU and other similar assistance.

Latvia's general government budget revenues increased by 25.5 per cent. in 2006, by 33.2 per cent. in 2007 and by only 7.0 per cent. in 2008 as the effects of the recession began to be felt. In 2009, Latvia's general government budget revenues decreased by 17.4 per cent., notwithstanding the revenue enhancement measures implemented by the government in its December 2008 and June 2009 supplementary budgets. In 2010, Latvia's general government budget revenues decreased by 2.6 per cent. compared to 2009. In 2011, Latvia's general government budget revenues are budgeted to increase by 9.3 per cent. compared to 2010.

Tax revenues

The majority of the government's revenues are derived from taxes. As a percentage of total general government revenues, tax revenues were 82.2 per cent. in 2006, 81.6 per cent. in 2007, 82.7 per cent. in 2008, 74.2 per cent. in 2009 and 73.7 per cent. in 2010. The declines in percentage terms in 2009 and 2010 reflected increased non-tax revenues and foreign financial assistance. In 2011, revenues from taxes are budgeted to equal 72.5 per cent. of total general government revenues, principally reflecting increased foreign financial assistance.

Latvia's tax revenues are principally made up of direct taxes and indirect taxes. Direct taxes comprise social security contributions, personal income tax, corporate income tax and real estate tax. As a percentage of total general government tax revenues, revenues from direct taxes were 59.2 per cent. in 2006, 61.2 per cent. in 2007, 65.4 per cent. in 2008, 63.3 per cent. in 2009 and 61.7 per cent. in 2010. In 2011, revenues from direct taxes are budgeted to equal 58.0 per cent. of total general government tax revenues.

The tax rate for social security contributions represents employer and employee contributions which, in 2011, will aggregate 35.1 per cent. of salary. These contributions are paid by the employer and recorded in a special budget (which is consolidated into the general government budget). The special budget is used to pay a range of social benefits, including sickness benefit, unemployment benefit, incapacity benefit and maternity benefit. Social security contributions equalled 49.5 per cent. of direct tax revenues (excluding contributions to the state funded pension scheme) in 2006, 48.2 per cent. in 2007 and 46.7 per cent. in 2008. Social security contributions equalled 54.0 per cent. of direct tax revenue in 2009 and 52.7 per cent. of direct tax revenue in 2010, in each case principally as a result of decline in revenue from corporate income tax. In 2011, social security contributions are budgeted to equal 55.4 per cent. from direct tax revenue, principally reflecting an anticipated decline in revenue from personal income tax.

Personal income tax is levied on employees' salaries and is deducted at source by employers and paid to the Treasury. Prior to 2009, personal income tax was charged at a flat rate of 25 per cent., although this was decreased to 23 per cent. in the January 2009 supplementary budget and increased to 26 per cent. in the 2010 budget. In the 2011 budget, the personal income tax rate has been reduced to 25 per cent. Personal income tax equalled 33.9 per cent. of direct tax revenues in 2006, 33.8 per cent. in 2007 and 34.3 per cent. in 2008. Personal income tax equalled 33.5 per cent. of direct tax revenue in 2009 and 37.6 per cent. of direct tax revenue in 2010. In absolute terms, personal income tax receipts increased in 2010, reflecting the increase in the personal income tax rate. In 2011, personal income tax revenues are budgeted to equal 34.3 per cent. of direct tax revenue.

Corporate income tax is levied at a rate of 15 per cent. on company profits. Corporate income tax equalled 13.1 per cent. of direct tax revenues in 2006, 15.2 per cent. in 2007 and 16.7 per cent. in 2008. This reflected increasing profitability of companies in Latvia. In 2009 and 2010, corporate income tax equalled 9.1 per cent. and 5.4 per cent., respectively, of direct tax revenue, reflecting the effect of the recession on corporate profitability. The 2010 and 2011 budgets also broadened the scope of certain corporate tax allowances with a view to encouraging investment. In 2011, revenues from corporate income tax are budgeted to equal 5.6 per cent. of direct tax revenue.

Real estate tax is levied on the value of land and buildings used for business purposes at a rate of 1.5 per cent. in each case. The government reformed property tax in its 2010 budget by increasing the tax rate on unused agricultural land and broadening the real estate tax base by including residential property and civil engineering structures. From 2011, the real estate tax rate for residential property was increased from between 0.1 and 0.3 per cent. to between 0.2 and 0.6 per cent., depending on cadastral value. Revenues from property tax have been less than 5.0 per cent. of total revenues from direct taxes in each year since 2006 and are budgeted to equal 4.6 per cent. of total revenues from direct taxes in 2011.

Indirect taxes principally comprise value added tax and excise tax. In addition, customs duties, car tax and, since 2007, electricity tax also generate a small proportion of the revenues from indirect taxes. In 2011, new indirect taxes on vehicles have been introduced. As a percentage of total general government tax revenues, revenues from indirect taxes were 39.8 per cent. in 2006, 37.9 per cent. in 2007, 33.9 per cent. in 2008, 35.9 per cent. in 2009 and 37.6 per cent. in 2010. In 2011, revenues from indirect taxes are budgeted to equal 39.6 per cent. of total general government tax revenues, principally as a result of the introduction of the new vehicle taxes.

VAT in Latvia is charged on a wide range of goods and services. Prior to 2009, VAT was charged at rates of 18 per cent. except for certain reduced rate goods where it was charged at 5 per cent. Since 2009, VAT has been charged at 21 per cent. with the reduced rate being increased to 10 per cent. and the range of goods benefitting from the reduced rate being significantly narrowed. In 2011, VAT is charged at 22 per cent. with the reduced rate being increased to 12 per cent. Revenues from VAT equalled 69.9 per cent. of total revenues from indirect taxes in 2006, 70.9 per cent. in 2007 and 65.9 per cent. in 2008. In 2009, notwithstanding the changes described above, revenues from VAT equalled 60.5 per cent. of total revenues from indirect taxes, reflecting the impact of the recession on personal spending habits. In 2010, revenues from VAT increased to 63.2 per cent. of total revenues from indirect taxes as the economy emerged from recession. Economic recovery is also expected to favourably impact VAT revenues in 2011, with those revenues being budgeted to be higher in absolute terms than in 2010 and to equal 65.3 per cent. of total revenues from indirect taxes.

Excise tax in Latvia is charged on alcoholic beverages (including beer), tobacco products, mineral oils, natural gas, non-alcoholic beverages and coffee. There is a wide range of different charges which have generally increased over the period since 2006. Revenues from excise tax equalled 27.5 per cent. of total revenues from indirect taxes in 2006, 26.4 per cent. in 2007, 31.9 per cent. in 2008, 38.2 per cent. in 2009 and 35.1 per cent. in 2010. In 2011, revenues from excise tax are budgeted to equal 32.4 per cent. of total revenues from indirect taxes, although they are still expected to be higher in absolute terms than in 2010.

Expenditure

Latvia's general government budget classifies expenditure as either capital expenditure or non-capital (or maintenance) expenditure. As a percentage of total expenditure, non-capital expenditure was 87.2 per cent. in 2006, 85.5 per cent. in 2007, 88.1 per cent. in 2008, 92.3 per cent. in 2009 and 92.7 per cent. in 2010. In 2011, non-capital expenditure is budgeted to equal 88.9 per cent. of total expenditure.

Non-capital expenditure grew by 21.4 per cent. in 2006, by 26.6 per cent. in 2007 and by 22.9 per cent. in 2008. Non-capital expenditure declined by 5.9 per cent. in 2009 and by 3.4 per cent. in 2010. Non-capital expenditure is budgeted to decline by 0.2 per cent. in 2011, reflecting the anticipated effects of further expenditure cuts in the 2011 budget.

The table below provides a breakdown of non-capital expenditure in the consolidated general government budget for each of the years ended 31 December 2007, 2008, 2009 and 2010 and of budgeted non-capital expenditure for 2011. No comparable breakdown for 2006 is available as budget classification principles changed in 2007.

	2007	2008	2009	2010	2011[(1)]
			(LVL millions)		
Non-capital expenditure	4,495.0	5,523.2	5,195.1	5,016.3	5,005.6
Current expenditure	2,191.7	2,612.8	2,012.5	1,778.3	1,874.5
Remuneration	1,392.5	1,679.2	1,337.5	1,086.9	1,143.3
Wages and salaries	1,059.7	1,269.8	1,028.3	846.3	888.7
Employers' social security contributions	332.8	409.4	309.1	240.6	254.6
Goods and services	799.2	933.6	675.1	691.4	731.3
Interest payments	51.7	64.0	150.6	179.6	226.8
Subsidies, grants and social support	2,112.4	2,692.8	2,883.8	2,937.1	2,773.2
Subsidies and grants	1,012.5	1,296.2	1,224.4	1,177.7	1,116.6
Social support	1,088.5	1,384.6	1,646.3	1,744.8	1,633.0
Pensions	768.9	954.2	1,081.9	1,252.2	—
Other social support	319.6	430.4	564.3	492.5	—
International collaboration	11.5	12.0	13.1	14.6	23.6
Payments to EU budget	139.1	153.5	148.2	121.3	131.0

Source: Ministry of Finance

Note:

(1) The amended central government budget approved by the Saeima on 14 April 2011 and Ministry of Finance projections of local government budgets.

Non-capital expenditure principally comprises current expenditure and subsidies, grants and social support. Together, these two expenditure classifications made up 95.8 per cent. of total non-capital expenditure in 2007, 96.1 per cent. in 2008, 94.2 per cent. in 2009 and 94.0 per cent. in 2010. In 2011, current expenditure and subsidies, grants and social support are together budgeted to account for 92.9 per cent. of total non-capital expenditure. In addition, interest payments on Latvia's outstanding debt and international collaboration payments and Latvia's contributions to the EU budget makes up the balance of non-capital expenditure. The increase in interest payments from 2008 principally reflects the cost of foreign financial assistance received.

Current expenditure

Current expenditure comprises remuneration of central and local government employees as well as payments for goods and services used by the central and local governments. As a percentage of total non-capital expenditure, current expenditure was 48.8 per cent. in 2007, 47.3 per cent. in 2008, 38.7 per cent. in 2009 and 35.5 per cent. in 2010. Current expenditure is budgeted to be 37.5 per cent. of total non-capital expenditure in 2011.

Remuneration includes both wages and employers' social security contributions. In 2008, remuneration increased by 20.6 per cent. whereas in 2009 and 2010, remuneration fell by 20.4 per cent. and 18.7 per cent., respectively, reflecting the effects of wage reductions and rationalisation measures set out in budgets since 2009. In 2011, remuneration is budgeted to increase by 5.2 per cent. As a percentage of total current expenditure, remuneration was 63.5 per cent. in 2007, 64.3 per cent. in 2008, 66.5 per cent. in 2009 and 61.1 per cent. in 2010 and is budgeted to be 61.0 per cent. in 2011.

In 2008, payments for goods and services increased by 16.8 per cent. and then fell by 27.7 per cent. in 2009 in accordance with the overall budget expenditure reduction. In 2010, payments for goods and services increased by 2.4 per cent. and these payments are budgeted to increase by 5.8 per cent. in 2011. As a percentage of total current expenditure, payments for goods and services were 36.5 per cent. in 2007, 35.7 per cent. in 2008, 33.5 per cent. in 2009 and 38.9 per cent. in 2010. Latvia's payments for goods and services are budgeted to be 39.0 per cent. of total current expenditure in 2011.

Subsidies, grants and social support

As a percentage of total non-capital expenditure, subsidies, grants and social support was 47.0 per cent. in 2007, 48.8 per cent. in 2008, 55.5 per cent. in 2009 and 58.6 per cent. in 2010. Subsidies, grants and social support are budgeted to be 55.4 per cent. of total non-capital expenditure in 2011.

Subsidies and grants principally comprise payments by government entities to enterprises for ensuring certain functions which are necessary to society (for example, subsidising the costs of mail delivery in rural areas). In addition, subsidies for agriculture and payments to non-governmental organisations make up the balance of subsidies and grants expenditure. Subsidies and grants increased by 28.0 per cent. in 2008 before falling by 5.5 per cent. and 3.8 per cent., respectively, in 2009 and 2010, reflecting general cuts in expenditure designed to minimise the level of the projected deficit. In 2011, subsidies and grants are budgeted to decline by 5.2 per cent. As a percentage of total subsidies, grants and social support, subsidies and grants were 47.9 per cent. in 2007, 48.1 per cent. in 2008, 42.5 per cent. in 2009 and 40.1 per cent. in 2010. Subsidies and grants are budgeted to be 40.3 per cent. of total subsidies, grants and social support in 2011.

Social support principally comprises pensions and other social insurance payments made from the Central Government Social Security Budget. Social support increased by 27.2 per cent. in 2008, by 18.9 per cent. in 2009 and by 6.0 per cent. in 2010 and is budgeted to decline by 6.4 per cent. in 2011, principally reflecting the fact that in 2010 a significant one-off payment of withheld pensions was made following a constitutional court judgment to that effect. The significant increases in social support in 2008 and 2009 reflect the effects of the recession in Latvia, including significantly rising unemployment levels.

As a percentage of total subsidies, grants and social support, social support was 51.5 per cent. in 2007, 51.4 per cent. in 2008, 57.1 per cent. in 2009 and 59.4 per cent. in 2010 and is budgeted to be 58.9 per cent. in 2011.

INDEBTEDNESS

All central government debt and cash management activities are entrusted to the Treasury, which is an independent administrative institution but reports to the Minister of Finance. The main objective for central government medium-term debt management has been to provide the Latvian government with the necessary financial resources at the lowest possible cost, including through the use of appropriate hedging tools, but also to take into account the proposed introduction of the euro in the medium term and the need to develop the Latvian capital markets and financial system. This latter objective is a principal reason for the government's issues of domestic debt securities. Prior to 2006, the Treasury reviewed its funding plan on an annual basis. Since 2006, the planning horizon has been extended to three years, with a more detailed annual plan also being prepared.

Central government debt is issued to ensure the financial liquidity of the central government, to finance the central government budget deficit and to refinance central government debt.

The ceiling on total central government debt (comprising both domestic and external debt incurred by the central government) is set out in the annual budget law. The ceiling of central government debt outstanding at the end of 2011 specified in the budget is LVL 6.0 billion (at nominal value).

The table below sets out Latvia's outstanding central government debt in Lats and as a percentage of nominal GDP at 31 December in each of 2006, 2007, 2008, 2009 and 2010 and as at 30 April 2011.

	2006	**2007**	**2008**	**2009**	**2010**	**2011**[(1)]
			(LVL millions)			
Central government debt .	1,001.1	1,031.8	2,640.1	4,169.2	4,942.6	4,950.4
External	581.5	635.1	1,260.4	3,261.3	4,146.5	4,077.1
Domestic.......................	419.6	396.7	1,379.7	907.9	796.1	873.4
			(*as a percentage of nominal GDP*)			
Central government debt .	9.0	7.0	16.3	31.9	38.8	36.9
External	5.2	4.3	7.8	24.9	32.6	30.3
Domestic.......................	3.8	2.7	8.5	6.9	6.3	6.5

Source: The Treasury

Note:

(1) As at 30 April. GDP for 2011 is projected to amount to LVL 13,415.9 million.

Latvia has met all principal and interest obligations on its central government debt since the renewal of its independence in 1991.

The table below sets outs Latvia's debt service payments (excluding interest amounts) in respect of its total outstanding central government debt as at 30 April 2011, expressed in millions of Lats, and as a percentage of the total amount outstanding at 30 April 2011, for each of the periods stated.

	2011	**2012**	**2013**	**2014**	**2015**	**2016**	**2017**
				(*LVL millions*)			
Total principal payments....................	8.1[(1)]	233.0	345.9	1,163,8	955.9	68.7	63.3
	(*per cent. of total outstanding central government debt as at 30 April 2011*)						
As percentage	0.2	5.7	8.5	28.5	23.4	1.7	1.6

	2018	**2019**	**2020**	**2021**	**2022**[(2)]	**Total**
			(*LVL millions*)			
Total principal payments	343.8	406.7	6.3	5.7	475.7	**4,077.7**
	(*per cent. of total outstanding central government debt as at 30 April 2011*)					
As percentage	8.4	10.0	0.2	0.1	11.7	**100.0**

Source: The Treasury

Notes:

(1) Amount due to be repaid between 1 May 2011 and 31 December 2011.

(2) Amount due to be repaid from 2022 onward.

As at 30 September 2010, Latvia's general government debt as measured by the EU, comprising both central government debt and local government debt, constituted 43.4 per cent. of GDP and was the tenth lowest ratio of general government debt to GDP among the 27 Member States of the EU as at that date.

Central Government External Debt

Latvia's central government external debt (the "**External Debt**") comprises borrowings from the international financial markets and from international financial institutions. Latvia has issued four series of international bonds, all of which were denominated in euro. The issues which took place in 1999 and 2001 have both been redeemed in accordance with their terms. The two issues currently outstanding are each in an amount of €400,000,000 and mature in 2014 and 2018, respectively. As at 30 April 2011, these bonds comprised 14 per cent. of the External Debt. The balance of the External Debt was made up of IMF loans (21 per cent.), a European Commission loan (49 per cent.), European Investment Bank loans (7 per cent.) and loans from other international financial institutions (9 per cent.).

The servicing cost of Latvia's External Debt varies based upon interest rate fluctuations. Currently, the Latvian Central Government debt management strategy (the "**Debt Management Strategy**") envisages that the rates of at least 60 per cent. of the central government debt will be fixed and, at 30 April 2011, the fixed rate proportion was 74.9 per cent. The fixed rate proportion of the External Debt was 81.0 per cent. at the same date.

The table below set outs Latvia's debt service payments in respect of its External Debt for each of the years ended 31 December 2006, 2007, 2008, 2009 and 2010.

	2006	**2007**	**2008**	**2009**	**2010**
			(LVL millions)		
Principal payments	14.7	13.6	172.7	15.2	13.3
Interest payments	27.1	26.6	28.9	47.6	101.0
Total	**41.8**	**40.2**	**201.7**	**62.8**	**114.3**

Source: The Treasury

The table below set outs Latvia's projected debt service payments in respect of its External Debt for each year between 2011 and 2016, based on the External Debt outstanding at 30 April 2011.

	2011	**2012**	**2013**	**2014**	**2015**
			(LVL millions)		
Principal payments	11.4	233.0	345.9	1,163.8	955.9
Interest payments	136.2	134.5	127.2	118.3	79.7
Total	**147.6**	**367.5**	**473.1**	**1,282.1**	**1,035.6**

Source: The Treasury

The significant increase in principal repayments in 2012 reflects the fact that the first repayment instalments of the first and second tranches of the IMF Standby Arrangement fall due for repayment in 2012. Further instalments of the first two tranches of the IMF Standby Arrangement fall due in 2013. The significant increase in principal repayments in 2014 principally reflects the fact that the first EU loan of €1 billion, as well as €400 million in Eurobonds issued in 2004, fall due for repayment.

The table below sets out Latvia's central government external debt broken down by currency as at 31 December in each of 2006, 2007, 2008, 2009 and 2010 and as at 30 April 2011.

	2006	2007	2008	2009	2010	2011[(1)]
			(LVL millions)			
CHF	0.59	0.55	0.56	0.52	0.57	0.52
EUR	542.47	608.06	824.25	2,591.19	3,210.97	3,209.60
SEK	0.03	—	—	—	—	—
USD	31.42	25.68	23.66	20.56	19.38	16.04
XDR[(2)]	—	—	409.00	639.31	904.51	840.53
Total	**574.51**	**634.28**	**1,257.48**	**3,251.59**	**4,135.43**	**4,066.70**

Source: The Treasury
Notes:
(1) As at 30 April.
(2) IMF special drawing rights.

Central Government Domestic Debt

Central government domestic debt (the "**Domestic Debt**") mainly comprises tradable government securities and short-term funding facilities (such as overdrafts and credit lines) which are used for liquidity management purposes. Historically, domestic government securities were used both as a financing instrument and with a view to furthering the development of a domestic securities market in Latvia. As part of its debt management objectives, the Treasury seeks to ensure that at least 35 per cent. of the government's overall outstanding debt is denominated in Lats. Currently, the government has six-month and 12-month short-term treasury bills, two-, three- and five-year medium-term treasury bonds and 10- and 11-year long-term treasury bonds outstanding in the domestic market. The short-term bills are issued at a discount and redeemed at par on maturity. The medium- and long-term bonds are issued with a fixed interest rate, which is paid annually, and are redeemed at par on maturity. The legal issuer of the domestic securities is the Ministry of Finance, but all the conditions of each issue are set by the Treasury, which acts on behalf of the Ministry of Finance.

The government's domestic debt securities are issued in dematerialised form and sold through NASDAQ OMX Riga's SAXESS trading system at competitive multi-price and non-competitive uniform price auctions at a discount for bills or yield for bonds. All government domestic debt securities are registered with the LCD and the majority are listed on NASDAQ OMX Riga.

The table below sets out the structure of the Domestic Debt at 30 April 2011.

Type of Instrument	Composition	Nominal value
	(per cent.)	*(LVL millions)*
6 month bills	13.4	117.3
12 month bills	24.0	209.5
2 year bonds	6.7	58.6
3 year bonds	5.8	50.7
5 year bonds	15.9	138.5
10 year bonds	29.1	254.3
11 year bonds	3.7	32.5
Other borrowings (overdrafts, credit lines etc.)	1.4	12.2
Total	**100.0**	**873.6**

Source: The Treasury

Between 1 September 2010 and 30 April 2011, the Republic successfully completed 35 competitive multi-price auctions of six-month and 12-month treasury bills and of five-year and 10-year bonds.

The table below sets out the aggregate amount and average bid-to-cover ratios of six-month and 12-month treasury bills and of the five-year and 10-year bonds issued by competitive multi-price auctions during each month from 1 November 2010 to 30 April 2011

2010, 1 November and 2011, 30 April

	November		December		January		February		March		April	
Type of Instrument	**Aggregate amount issued** (*LVL millions*)	**Average bid-to-cover ratio** (*per cent.*)	**Aggregate amount issued** (*LVL millions*)	**Average bid-to-cover ratio** (*per cent.*)	**Aggregate amount issued** (*LVL millions*)	**Average bid-to-cover ratio** (*per cent.*)	**Aggregate amount issued** (*LVL millions*)	**Average bid-to-cover ratio** (*per cent.*)	**Aggregate amount issued** (*LVL millions*)	**Average bid-to-cover ratio** (*per cent.*)	**Aggregate amount issued** (*LVL millions*)	**Average bid-to-cover ratio** (*per cent.*)
6 month bills	16	4.7	35	1.89	16	4.7	35	1.89	24	2.93	3	0.75
12 month bills	20	3.35	45	1.34	20	3.35	45	1.34	40	2.88	24	1.63
5 year bonds												
10 year bonds											8	2.71
Total	**36**		**80**		**40**		**32**		**64**		**35**	

Source: The Treasury

The Treasury has been increasing the average maturity of its domestic securities portfolio since 1 January 2010. At 30 April 2011, the Treasury had no one-month or three-month treasury bills outstanding and six-month treasury bills represented only 13 per cent. of the Treasury's total domestic securities portfolio.

During 2010 and up to February 2011, the Treasury auctions were principally of longer term securities, with a view to decreasing the refinancing risks related to government domestic debt and ensuring that debt servicing costs were fixed at relatively lower levels. In 2010, two-year, three-year and five-year bonds were reopened and, on 2 February 2011, the 10-year bond programme was reopened.

The average weighted yields in the domestic primary market declined during 2010 and are at pre-crisis levels. By way of example, the rates of six-month government bills decreased from 13.758 per cent. at 26 August 2009 to 1.086 per cent. at 6 April 2011 and the rates of 12-month government bills decreased from 14.75 per cent. at 7 October 2009 to 1.781 per cent. at 13 April 2011).

Debt Management Strategy

Latvia pursues a strategy of central government debt management through a dual framework of central government debt portfolio management and central government borrowing management. Central government debt portfolio management is aimed at optimising central government debt service costs over long term while hedging and preventing financial risks in relation to the central government debt portfolio. Central government borrowing management is aimed at ensuring borrowing opportunities, liquidity and favourable terms and conditions, focusing on the long-term development of the financial market and promoting relationships with financial market participants.

The Debt Management Strategy targets a number of key parameters, including the following:

- *the amount of Lat denominated debt*. The Debt Management Strategy envisages that the proportion of the debt portfolio denominated in Lats should not be less than 35 per cent. of the total portfolio where this is consistent with Latvian macroeconomic developments, the condition of the capital markets and the overall financial systems and if the weighted average yield of medium-term and long-term government domestic securities offered at auctions held by the Treasury is less than 100 basis points above the yield that could be achieved by the Treasury borrowing in euro;

- *the maturity profile of the portfolio.* The Debt Management Strategy envisages that not more than 25 per cent. of the portfolio should mature within one year and that not more than 50 per cent. should mature within three years;

- *the fixed rate proportion.* The Debt Management Strategy envisages that not less than 60 per cent. of the portfolio should have fixed rates of interest;

- *the Macaulay Duration of the portfolio* (which, in relation to each security, is determined as the weighted average maturity of the security where the weights are the relative discounted cash flows in each period). The Debt Management Strategy envisages that the Macaulay Duration should be within a corridor of between 3.4 and 4.0 years; and
- *the foreign currency net debt composition.* The Debt Management Strategy envisages that foreign currency-denominated net debt (which is foreign currency-denominated debt incurred less foreign currency-denominated loans made by the Treasury and cash in foreign currencies held by it) should be 100 per cent. in euro plus or minus 5 per cent.

The Treasury typically uses hedging instruments to help it achieve the above parameters, although its ability to do so depends on the availability of such instruments and counterparties willing to deal with the Treasury. The Treasury has developed and applies a cost-at-risk model to evaluate the parameters set and to determine whether the defined performance levels are optimal and financially justified over time. The Treasury's debt management committee, which includes the Treasurer and the Deputy Treasurer, meets at least monthly to review the portfolio and its performance against the parameters. The strategy itself is reviewed at least annually. The last review was accomplished during March 2011.

Reflecting the deterioration in the global economy and the effects of the recession in Latvia, Latvia's credit ratings were reduced as follows:

- by Standard & Poor's from BBB+ to BBB in October 2008, to BBB- in November 2008, to BB+ in February 2009 and to BB in August 2009;
- by Moody's from A2 to A3 in November 2008, to Baa1 in January 2009 and to Baa3 in April 2008; and
- by Fitch from BBB+ to BBB in October 2008, to BBB- in November 2008 and to BB+ in April 2008.

Since August 2009, the following positive rating actions have occurred:

- Standard & Poor's upgraded Latvia's rating to BB+ in December 2010 and, in March 2011, changed the rating outlook from stable to positive;
- Moody's affirmed its Baa3 rating but changed the outlook from stable to positive in June 2011; and
- Fitch upgraded Latvia's rating from BB+ to BBB- with a positive outlook in March 2011.

As a result, Latvia's current ratings are BB+ (positive outlook) from Standard & Poor's, Baa3 (stable outlook) from Moody's and BBB- (positive outlook) from Fitch. The table below sets out the key parameters for the central government overall debt portfolio discussed above and the actual parameters achieved as of 31 December 2009 and 31 December 2010.

Parameters	**31 December 2009**		**31 December 2010**		**Strategy**	
Amount of Lat denominated debt	20%		16%		⩾35%[1]	
Maturity profile	1 year or less	3 years or less	1 year or less	3 years or less	1 year or less	3 years or less
	14%[3]	24%	8%	25%	⩽25%	⩽50%
Fixed rate proportion	66%		76%		⩾60	
Macaulay duration	3.08 years		3.62 years		from 3.4 to 4.0 years	
Foreign currency net debt composition	EUR	100.04%	EUR	100.05%	EUR 100% +/- 5%	

Source: The Treasury

Note:

(1) The minimum share of Lat-denominated debt in medium term should be at least at the 35 per cent. level where this is consistent with Latvian macroeconomic developments, the condition of the capital markets and the overall financial system and if the weighted average yield of medium-term and long-term government domestic securities offered at auctions held by the Treasury is less than 100 basis points above the yield that could be achieved by the Treasury borrowing in euro.

Financing and Liquidity Strategy

The Treasury's financing strategy focuses on the maintenance of liquidity. As at 30 April 2011, Latvia's balance of resources was approximately LVL 918.4 million, of which LVL 456 million is earmarked for support of the banking sector. The central government's financing requirements are currently funded by issuances of domestic securities and international support.

For the year ended 31 December 2011, the Treasury projects that the central government will require LVL 1,315 million in financing, with planned funding activities amounting to LVL 1,119 million, consisting of LVL 528 million from domestic securities issuances, LVL 520 million from borrowing in international financial markets and LVL 70 million from international support. The Treasury projects that, as at 31 December 2011, Latvia's balance of resources will be approximately LVL 913 million. The Treasury anticipates that the central government's average borrowings over the three years 2011 to 2013 will be approximately LVL 500 million a year.

Financial Assistance from International Lenders

In the second half of 2008, due to the global financial crisis, Latvia's limited financial resource availability and the liquidity support provided by the government to stabilise the banking sector, the government sought financial assistance from the IMF and other members of the international community.

At the end of December 2008, the IMF, the EU, the World Bank, the EBRD and certain Nordic countries and other EU Member States agreed to provide a package of support to Latvia in an amount of up to approximately €7.5 billion (equal to approximately U.S.$10.5 billion). The table below sets out the support planned to be made available to Latvia.

	Planned to be made available during			
	2009	**2010**	**2011**	**Total**
	(EUR millions)			
EU	2,900	100	100	3,100
IMF	1,200[(1)]	400	105	1,705
Nordic countries (Finland, Sweden, Estonia, Denmark and Norway)	100	1,800	—	1,900
World Bank	200	—	200	400
EBRD, Czech Republic and Poland	100	300	—	400
Total by years	**4,500**	**2,600**	**405**	**7,505**

Source: The Treasury

Note:

(1) Including €600 million received on 29 December 2008.

Within the IMF Standby Arrangement and the EU loan, the government has agreed to implement a number of reforms over a two- to three-year timeframe. Implementation of these reforms in a timely manner is a condition to Latvia receiving tranches of the planned financial support from those lenders.

Latvia is a party to a Memorandum of Understanding with the EU and Letters of Intent to the IMF. These documents contain the reforms and pledges Latvia has committed to implement as a condition of receiving financial assistance. The IMF and EU have undertaken four programme review missions, each of which has resulted in positive evaluations recommending the continued availability of financial assistance.

On 15 April, 2011, the IMF and the EU issued a joint statement at the conclusion of their latest staff visit to Latvia. They noted that the Latvian economy is showing clear signs of recovery and that the Latvian policy agenda sets the stage for meeting the conditions for euro adoption in January 2014 and for sustaining the economic recovery. On the fiscal side, they noted that Latvia is aiming at a 2012 budget deficit of 2.5 per cent. of GDP and that preliminary estimates suggest that achieving this target in 2012 will require a further LVL 150 to 180 million in net additional measures, a smaller remaining adjustment need than the large adjustment measures implemented in 2011 and in previous years. The joint statement recorded that there had been good progress also in other areas of the programme and, in particular, significant financial system stabilisation measures had been taken which have reduced potential banking sector funding needs. In this context, an agreement was reached with the Latvian authorities for phased release of the funds earmarked for banking sector support (€650 million in total) for the purpose of financing general government operations, subject to continued progress on financial sector reforms. On 25 May 2011, the Executive Board of the IMF completed its fourth review of Latvia's performance in connection with the provision of the financial assistance package and confirmed that funds would continue to made available to Latvia under the package. On 7 June 2011, the EU and Latvia entered into a supplemental memorandum of understanding in relation to the financial assistance provided by the EU and following completion of its fourth review of Latvia's performance in connection with the provision of the financial assistance package. The EU also confirmed that funds would continue to be made available to Latvia under the package.

At the end of 2010, loans amounting to €4.4 billion had been made by the international lenders within the scope of the financial assistance programme. No further borrowings within the programme are planned by Latvia in 2011, except for the last portion of the World Bank loan amounting to €100 million. The funds received have principally been used to finance deficits, make State loans and finance debt repayment. In addition, a portion of the funds received has been used to support Parex Bank and ensure the stability of the Latvian banking sector.

The table below sets out the amounts and dates of financial assistance disbursements made to date.

	Amount disbursed	Date disbursed
	(€ millions)	
IMF		
First tranche	600,000,000	December 2008
Second tranche	200,000,000	July 2009
Third tranche	200,000,000	February 2010
Fourth tranche	100,000,000	August 2010
EU		
First tranche	1,000,000,000	February 2009
Second tranche	1,200,000,000	August 2009
Third tranche	500,000,000	March 2010
Fourth tranche	200,000,000	October 2010
EBRD (investment in Parex Bank and subordinated loan)	100,000,000	September 2009
World Bank		
First tranche	200,000,000	November 2009
Second tranche	100,000,000	September 2010
Total	**4,400,000,000**	

Source: The Treasury

The support made available to Latvia under the financial assistance package has a range of interest costs. Latvia has generally sought to borrow the concessional funding first. As a result, as and when this less expensive funding falls due to be repaid, if and to the extent that Latvia refinances it from other sources, this may give rise to a limited increase in Latvia's overall debt servicing costs depending on the price at which Latvia is able to secure refinancing at the time.

State Guarantees and Loans granted by the State

Each State Budget Law sets a limit on the amount of the net increase of loans granted by the State for the year. Under the State Budget Law for 2010, the net increase of State loans granted is planned to be LVL 208.0 million (including the State loan limit for municipalities in an amount of LVL 66.0 million).

Under the Budget Management Law, the Minister of Finance is authorised to borrow State loans in accordance with a decision of the Cabinet of Ministers, provided the loans are borrowed for the purposes specified in the Budget Law and do not exceed 10 per cent. of nominal GDP as specified in the annual State Budget Law.

Under the Budget Law, the State may make loans to local governments, special state budget executors, certain state- or local government-owned companies, scientific institutes and higher education establishments that have been assigned the status of a derived public entity and port authorities. On 30 April 2011, the amount of such loans outstanding was LVL 758.6 million.

Each State Budget Law also lists the State guarantees planned for the relevant year. In 2010, the authorised amount of those guarantees was LVL 171.6 million.

Until 2009, State guarantees were issued only for project financing and for commercial bank financing advanced to students. Starting in 2009, the Budget Management Law permits State guarantees to be issued to reduce general economic risks, to avoid a social-economic crisis or mitigate its effects and to ensure the availability of financial resources in an emergency situation. On 30 April 2011, the total amount of State guarantees issued and outstanding was LVL 578.6 million.

The table below shows the cumulative amount of State guarantees outstanding and the amount of State loans made at 31 December in each of 2007, 2008, 2009 and 2010 and at 30 April 2011.

	2007	2008	2009	2010	2011(1)
			(LVL millions)		
State guarantees outstanding...........	158.1	208.3	713.8	597.1	605.9
State loans made............................	335.4	432.8	537.9	786.7	758.6

Source: The Treasury
Note:
(1) As at 30 April 2011.

In order to improve the State budget lending procedure, as well as to reduce the overall risk of the State budget loan portfolio, new Cabinet of Ministers regulations were introduced in January 2010 which prescribe increasingly strict provisions for granting State budget loans. In addition, in June 2010, new Cabinet of Ministers regulations were introduced to improve the procedure for issuing state guarantees and to decrease the overall risk of the State guarantee portfolio.

Pursuant to the State Budget Law for 2011, the total increase of State budget loans in 2011 is determined to be LVL 208 million, including a total increase of local government loans amounting to LVL 96 million. Under the same law, State guarantees for a total amount of LVL 162 million are budgeted. In addition, the State Budget Law approved a State guarantee of a loan to Citadele Bank from the European Investment Bank amounting to LVL 71.0 million in accordance with the Parex Bank State Support Restructuring Plan approved by the European Commission.

Local Government Debt

Local governments in Latvia have the right to borrow and issue guarantees only in amounts provided for in the annual State Budget Law. Any borrowing or guarantee by a local government can only be made after having been approved by the Council for the Control and Surveillance of Local Government Borrowing and Guarantees (the "**Council**"). Before approving a proposed borrowing or guarantee, the Council evaluates the relevant proposal and assesses the financial capacity of the local government concerned to repay any loans received or comply with the terms of the relevant guarantee.

The table below sets out Latvian local government borrowing by principal source as at 31 December in each of 2007, 2008, 2009 and 2010 and as at 30 April 2011.

	2007	2008	2009	2010	2011(1)
			(LVL millions)		
Total local government debt	368.2	480.4	495.4	535.0	518.8
From the Treasury.................	250.8	354.5	369.7	396.6	383.9
From other lenders	117.4	125.9	125.7	138.3	134.9

Source: The Treasury
Notes:
(1) As at 30 April 2011.

The Treasury is the main lender to local governments. Local governments may borrow from other lenders only if the financial terms of the other lender are more advantageous than those of the Treasury and after receiving permission from the Minister of Finance.

Under the 2011 State Budget Law, local governments may only borrow in limited circumstances, including to:

- implement projects co-financed by the EU and other providers of financial assistance;
- stabilise the finances of the local government;
- fund infrastructure projects in which the local government is responsible for at least 75 per cent. of the total costs and the loan comprises not more than 25 per cent. and where the project is implemented within the budget year; and
- fund social programmes and boarding-school investment projects.

TAXATION

The following is a general description of certain tax considerations relating to the Notes. It does not purport to be a complete analysis of all tax considerations relating to the Notes. Prospective purchasers of Notes should consult their tax advisers as to the consequences under the tax laws of the country of which they are resident for tax purposes and the tax laws of the Republic of Latvia of acquiring, holding and disposing of Notes and receiving payments of interest, principal and/or other amounts under the Notes. This summary is based upon the law in effect on the date of this Offering Circular and is subject to any change in law that may take effect after such date.

Latvian Taxation

Under existing Latvian laws and regulations, payments of principal and interest on the Notes to an individual who is a non-resident of Latvia or to a legal entity that does not maintain a permanent establishment in Latvia (together "**Non-Latvian Holders**") will not be subject to taxation in Latvia and no withholding of any Latvian tax will be required on any such payments. In addition, gains realised by Non-Latvian Holders which are legal entities derived from the sale or exchange of the Notes will not be subject to any Latvian income or capital gains tax. However, although the point is not free from doubt, it is possible to construe the Latvian Law on Personal Income Tax, as in effect on the date of this Offering Circular, in a manner that suggests that gains realised by Non-Latvian Holders which are private individuals derived from the sale or exchange of any Notes could be subject to Latvian income tax at the rate of 15 per cent. In that regard, the Ministry of Finance of the Republic of Latvia has provided a written confirmation that, in its view, the gains realised by Non-Latvian Holders which are private individuals derived from the sale or exchange of any Notes are exempt from Latvian income tax, although, according to Latvian law, this confirmation is not legally binding and the holders of Notes cannot rely on it.

The Ministry of Finance of the Republic of Latvia has also confirmed that it has introduced in the Parliament (Saeima) a draft amendment to the Latvian Law on Personal Income Tax to clarify that gains realised by Non-Latvian Holders which are private individuals derived from the sale or exchange of any Notes are exempt from Latvian income tax and that it will propose a further amendment ensuring reimbursement of any tax paid by such holders prior to the amendments taking effect. The Ministry of Finance estimates that the draft amendments, if approved, would come into force in July 2011 at the earliest.

No Latvian stamp duty, registration, transfer or similar taxes will be payable in connection with the acquisition, ownership, sale or disposal of Notes by Non-Latvian Holders providing that any sale or exchange of Notes takes place outside the territory of Latvia.

United States

TO ENSURE COMPLIANCE WITH INTERNAL REVENUE SERVICE (IRS) CIRCULAR 230, EACH TAXPAYER IS HEREBY NOTIFIED THAT: (A) ANY TAX DISCUSSION HEREIN IS NOT INTENDED OR WRITTEN TO BE USED, AND CANNOT BE USED, BY THE TAXPAYER FOR THE PURPOSE OF AVOIDING U.S. FEDERAL INCOME TAX PENALTIES THAT MAY BE IMPOSED ON THE TAXPAYER; (B) ANY SUCH TAX DISCUSSION WAS WRITTEN TO SUPPORT THE PROMOTION OR MARKETING OF THE TRANSACTIONS OR MATTERS ADDRESSED HEREIN; AND (C) THE TAXPAYER SHOULD SEEK ADVICE BASED ON THE TAXPAYER'S PARTICULAR CIRCUMSTANCES FROM AN INDEPENDENT TAX ADVISER.

The following is a summary of certain U.S. federal income tax considerations relevant to U.S. Holders (as defined below) acquiring, holding and disposing of Notes. This summary addresses only the U.S. federal income tax considerations for initial purchasers of Notes at their issue price (as defined below) that will hold the Notes as capital assets (generally, property held for investment). This summary is based on the U.S. Internal Revenue Code of 1986 (the "**Code**"), final, temporary and proposed U.S. Treasury regulations and, administrative and judicial interpretations, all of which are subject to change, possibly with retroactive effect.

This summary does not discuss all aspects of U.S. federal income taxation that may be relevant to investors in light of their particular circumstances, such as investors subject to special tax rules (including, without limitation: (i) certain financial institutions; (ii) insurance companies; (iii) dealers or traders in stocks, securities, or notional principal contracts; (iv) regulated investment companies; (v) real estate investment trusts; (vi) tax-exempt organisations; (vii) partnerships, pass-through entities, or persons that hold Notes through pass-through entities; (viii) investors that hold Notes as part of a straddle, hedge, conversion, constructive sale or other integrated transaction for U.S. federal income tax purposes; (ix) investors that have a functional currency other than the U.S. dollar and (x) U.S. expatriates and former long-term residents of the United States), all of whom may be subject to tax rules that differ significantly from those summarised below. This summary does not address U.S. federal estate, gift or alternative minimum tax considerations, or non-U.S., state or local tax considerations.

For the purposes of this summary, a "**U.S. Holder**" is a beneficial owner of Notes that is for U.S. federal income tax purposes (i) an individual who is a citizen or resident of the United States, (ii) a corporation created in, or organised under the laws of, the United States or any state thereof, including the District of Columbia, (iii) an estate the income of which is includible in gross income for U.S. federal income tax purposes regardless of its source or (iv) a trust that is subject to U.S. tax on its worldwide income regardless of its source.

Payments of interest

Interest on a Note, including the payment of any additional amounts, will be taxable to a U.S. Holder as ordinary income at the time it is received or accrued, in accordance with the holder's method of accounting for tax purposes. Interest paid by the Republic on the Notes and payments of any additional amounts will generally constitute income from sources without the United States.

Sale or other disposition of Notes

A U.S. Holder's tax basis in a Note will generally be its cost. A U.S. Holder will generally recognise gain or loss on the sale or other disposition of a Note equal to the difference between the amount realised on the sale or other disposition and the tax basis of the Note. The amount realised will not include any amount attributable to accrued but unpaid interest, which will be taxed as described in "– *Payments of interest*" above. Gain or loss recognised on the sale or other disposition of a Note will be capital gain or loss and will be treated as from U.S. sources for purposes of the U.S. foreign tax credit limitation. In the case of a U.S. Holder that is an individual, estate or trust, the maximum marginal federal income tax rate applicable to capital gains is currently lower than the maximum marginal rate applicable to ordinary income if the Notes are held for more than one year. The deductibility of capital losses is subject to significant limitations.

U.S. Holders should consult their own tax advisers about how to account for any Latvian taxes withheld on the sale or other disposition of a Note. Please see the discussion above under Taxation – Latvian Taxation.

Backup withholding and information reporting

In general, payments of principal, interest on, and the proceeds of a sale, redemption or other disposition of, the Notes, payable to a U.S. Holder by a U.S. paying agent or other U.S.-related intermediary will be reported to the IRS and to the U.S. Holder as may be required under applicable regulations. Backup withholding will apply to these payments if the U.S. Holder fails to provide an accurate taxpayer identification number or certification of exempt status or otherwise to comply with the applicable backup withholding requirements. Certain U.S. Holders are not subject to information reporting and backup withholding.

U.S. Holders should consult their own tax advisers regarding any reporting obligations they may have as a result of their acquisition, ownership or disposition of Notes. Failure to comply with certain reporting obligations could result in the imposition of substantial penalties.

EU Savings Tax Directive

Under EC Council Directive 2003/48/EC on the taxation of savings income, each Member State is required to provide to the tax authorities of another Member State details of payments of interest or other similar income paid by a person within its jurisdiction to, or collected by such a person for, an individual resident or certain limited types of entity established in that other Member State; however, for a transitional period, Austria and Luxembourg may instead apply a withholding system in relation to such payments, deducting tax at rates rising over time to 35 per cent. The transitional period is to terminate at the end of the first full fiscal year following agreement by certain non-EU countries to the exchange of information relating to such payments.

A number of non-EU countries and certain dependent or associated territories of certain Member States, have adopted similar measures (either provision of information or transitional withholding) in relation to payments made by a person within its jurisdiction to, or collected by such a person for, an individual resident or certain limited types of entity established in a Member State. In addition, the Member States have entered into provision of information or transitional withholding arrangements with certain of those dependent or associated territories in relation to payments made by a person in a Member State to, or collected by such a person for, an individual resident or certain limited types of entity established in one of those territories.

On 13 November 2008 the European Commission published a proposal for amendments to the Directive, which included a number of suggested changes which, if implemented, would broaden the scope of the requirements described above. Investors who are in any doubt as to their position should consult their professional advisers.

CLEARING AND SETTLEMENT ARRANGEMENTS

*The information set out below is subject to any change in or reinterpretation of the rules, regulations and procedures of DTC, Euroclear or Clearstream, Luxembourg (together, the "**Clearing Systems**") currently in effect. The information in this section concerning the Clearing Systems has been obtained from sources that the Republic believes to be reliable, but neither the Republic or the Managers takes any responsibility for the accuracy of this section. Investors wishing to use the facilities of any of the Clearing Systems are advised to confirm the continued applicability of the rules, regulations and procedures of the relevant Clearing System. None of the Republic and any other party to the Fiscal Agency Agreement will have any responsibility or liability for any aspect of the records relating to, or payments made on account of, beneficial ownership interests in the Notes held through the facilities of any Clearing System or for maintaining, supervising or reviewing any records relating to such beneficial ownership interests.*

Clearing Systems

Euroclear and Clearstream, Luxembourg

Euroclear and Clearstream, Luxembourg each hold securities for their customers and facilitate the clearance and settlement of securities transactions by electronic book-entry transfer between their respective account holders. Euroclear and Clearstream, Luxembourg provide various services including safekeeping, administration, clearance and settlement of internationally traded securities and securities lending and borrowing. Euroclear and Clearstream, Luxembourg also deal with domestic securities markets in several countries through established depositary and custodial relationships. Euroclear and Clearstream, Luxembourg have established an electronic bridge between their two systems across which their respective participants may settle trades with each other.

Euroclear and Clearstream, Luxembourg customers are worldwide financial institutions, including underwriters, securities brokers and dealers, banks, trust companies and clearing corporations. Indirect access to Euroclear and Clearstream, Luxembourg is available to other institutions that clear through or maintain a custodial relationship with an account holder of either system.

DTC

DTC has advised the Republic that it is a limited purpose trust company organised under the New York Banking Law, a member of the Federal Reserve System, a "banking organisation" within the meaning of the New York Banking Law, a "clearing corporation" within the meaning of the New York Uniform Commercial Code and a "clearing agency" registered pursuant to Section 17A of the Exchange Act. DTC holds securities that its participants ("**Direct Participants**") deposit with DTC. DTC also facilitates the settlement among Direct Participants of securities transactions, such as transfers and pledges, in deposited securities through electronic computerised book-entry changes in Direct Participants' accounts, thereby eliminating the need for physical movement of securities certificates. Direct Participants include both U.S. and non U.S. securities brokers and dealers, banks, trust companies, clearing corporations and certain other organisations. DTC is a wholly-owned subsidiary of The Depository Trust & Clearing Corporation ("**DTCC**"). DTCC is the holding company for DTC, National Securities Clearing Corporation and Fixed Income Clearing Corporation, all of which are registered clearing agencies. DTCC is owned by the users of its regulated subsidiaries. Access to the DTC system is also available to others such as both U.S. and non U.S. securities brokers and dealers, banks and trust companies that clear through or maintain a custodial relationship with a Direct Participant, either directly or indirectly ("**Indirect Participants**" and, together with Direct Participants, "**Participants**"). More information about DTC can be found at www.dtcc.com and www.dtc.org.

Under the rules, regulations and procedures creating and affecting DTC and its operations (the "**DTC Rules**"), DTC makes book-entry transfers of Registered Notes among Direct Participants on whose behalf it acts with respect to Notes accepted into DTC's book-entry settlement system ("**DTC Notes**") as described below and receives and transmits distributions of principal and interest on DTC Notes. The DTC Rules are on file with the Securities and Exchange Commission. Direct Participants and Indirect Participants with which beneficial owners of DTC Notes ("**Owners**") have accounts with respect to the DTC Notes similarly are required to make book-entry transfers and receive and transmit such payments on behalf of their respective Owners. Accordingly, although Owners who hold DTC Notes through Direct Participants or Indirect Participants will not possess Registered Notes, the DTC Rules, by virtue of the requirements described above, provide a mechanism by which Direct

Participants will receive payments and will be able to transfer their interest in respect of the DTC Notes.

Purchases of DTC Notes under the DTC system must be made by or through Direct Participants, which will receive a credit for the DTC Notes on DTC's records. The ownership interest of each actual purchaser of each DTC Note ("**Beneficial Owner**") is in turn to be recorded on the Direct and Indirect Participant's records. Beneficial Owners will not receive written confirmation from DTC of their purchase, but Beneficial Owners are expected to receive written confirmations providing details of the transaction, as well as periodic statements of their holdings, from the Direct or Indirect Participant through which the Beneficial Owner entered into the transaction. Transfers of ownership interests in the DTC Notes are to be accomplished by entries made on the books of Participants acting on behalf of Beneficial Owners. Beneficial Owners will not receive certificates representing their ownership interests in DTC Notes, except in the event that use of the book-entry system for the DTC Notes is discontinued.

To facilitate subsequent transfers, all DTC Notes deposited by Participants with DTC are registered in the name of DTC's partnership nominee, Cede & Co., or such other name as may be requested by an authorised representative of DTC. The deposit of DTC Notes with DTC and their registration in the name of Cede & Co. or such other DTC nominee effect no change in beneficial ownership. DTC has no knowledge of the actual Beneficial Owners of the DTC Notes; DTC's records reflect only the identity of the Direct Participants to whose accounts such DTC Notes are credited, which may or may not be the Beneficial Owners. The Participants will remain responsible for keeping account of their holdings on behalf of their customers.

Conveyance of notices and other communications by DTC to Direct Participants, by Direct Participants to Indirect Participants, and by Direct Participants and Indirect Participants to Beneficial Owners will be governed by arrangements among them, subject to any statutory or regulatory requirements as may be in effect from time to time.

Redemption notices shall be sent to DTC. If less than all of the DTC Notes within an issue are being redeemed, DTC's practice is to determine by lot the amount of the interest of each Direct Participant in such issue to be redeemed.

Neither DTC nor Cede & Co. (nor any other DTC nominee) will consent or vote with respect to DTC Notes unless authorised by a Direct Participant in accordance with DTC's MMI Procedures. Under its usual procedures, DTC mails an Omnibus Proxy to the Republic as soon as possible after the record date. The Omnibus Proxy assigns Cede & Co.'s consenting or voting rights to those Direct Participants to whose accounts the DTC Notes are credited on the record date (identified in a listing attached to the Omnibus Proxy).

Principal and interest payments on the DTC Notes will be made to Cede & Co., or such other nominee as may be requested by an authorised representative of DTC. DTC's practice is to credit Direct Participants' accounts upon DTC's receipt of funds and corresponding detail information from the Republic or the relevant agent (or such other nominee as may be requested by an authorised representative of DTC), on the relevant payment date in accordance with their respective holdings shown in DTC's records. Payments by Participants to Beneficial Owners will be governed by standing instructions and customary practices, as is the case with securities held for the accounts of customers in bearer form or registered in "street name", and will be the responsibility of such Participant and not of DTC, relevant agents or the Republic, subject to any statutory or regulatory requirements as may be in effect from time to time. Payment of principal and interest to DTC is the responsibility of the Republic, disbursement of such payments to Direct Participants is the responsibility of DTC, and disbursement of such payments to the Beneficial Owners is the responsibility of Direct and Indirect Participants.

Under certain circumstances, including if there is an Event of Default under the Notes, DTC will exchange the DTC Notes for definitive Registered Notes, which it will distribute to its Participants in accordance with their proportionate entitlements and which, if representing interests in a Rule 144A Global Note, will be legended as set forth under "*Subscription and Sale*" and "*Transfer Restrictions*".

A Beneficial Owner shall give notice to elect to have its DTC Notes purchased or tendered, through its Participant, to the relevant agent, and shall effect delivery of such DTC Notes by causing the Direct Participant to transfer the Participant's interest in the DTC Notes, on DTC's records, to the relevant agent. The requirement for physical delivery of DTC Notes in connection with an optional tender or a mandatory purchase will be deemed satisfied when the ownership rights in the DTC

Notes are transferred by Direct Participants on DTC's records and followed by a book-entry credit of tendered DTC Notes to the relevant agent's DTC account.

DTC may discontinue providing its services as depository with respect to the DTC Notes at any time by giving reasonable notice to the Republic or the relevant agent. Under such circumstances, in the event that a successor depository is not obtained, DTC Note certificates are required to be printed and delivered.

The Republic may decide to discontinue use of the system of book-entry-only transfers through DTC (or a successor securities depository). In that event, DTC Note certificates will be printed and delivered to DTC.

Since DTC may only act on behalf of Direct Participants, who in turn act on behalf of Indirect Participants, any Owner desiring to pledge DTC Notes to persons or entities that do not participate in DTC, or otherwise take actions with respect to such DTC Notes, will be required to withdraw its Registered Notes from DTC.

The information in this section concerning DTC and DTC's book-entry system has been obtained from sources that Republic believes to be reliable, but Republic takes no responsibility for the accuracy thereof.

Registration and Form

Book-entry interests in the Notes held through Euroclear and Clearstream, Luxembourg will be represented by the Unrestricted Global Certificate registered in the name of a nominee of, and held by, a common depositary for Euroclear and Clearstream, Luxembourg. Book-entry interests in the Notes held through DTC will be represented by the Restricted Global Certificate registered in the name of Cede & Co., as nominee for DTC, and held by a custodian for DTC. As necessary, the Registrar will adjust the amounts of Notes on the Register for the accounts of Euroclear, Clearstream, Luxembourg and DTC to reflect the amounts of Notes held through Euroclear, Clearstream, Luxembourg and DTC, respectively. Beneficial ownership of book-entry interests in Notes will be held through financial institutions as direct and indirect participants in Euroclear, Clearstream, Luxembourg and DTC.

The aggregate holdings of book-entry interests in the Notes in Euroclear, Clearstream, Luxembourg and DTC will be reflected in the book-entry accounts of each such institution. Euroclear, Clearstream, Luxembourg or DTC, as the case may be, and every other intermediate holder in the chain to the beneficial owner of book-entry interests in the Notes will be responsible for establishing and maintaining accounts for their participants and customers having interests in the book-entry interests in the Notes. The Registrar will be responsible for maintaining a record of the aggregate holdings of Notes registered in the name of a common nominee for Euroclear and Clearstream, Luxembourg, a nominee for DTC and/or, if individual Certificates are issued in the limited circumstances described under "*The Global Certificates – Registration of Title*", holders of Notes represented by those individual Certificates. The Fiscal Agent will be responsible for ensuring that payments received by it from the Republic for holders of book-entry interests in the Notes holding through Euroclear and Clearstream, Luxembourg are credited to Euroclear or Clearstream, Luxembourg, as the case may be, and the Fiscal Agent will also be responsible for ensuring that payments received by the Fiscal Agent from the Republic for holders of book-entry interests in the Notes holding through DTC are credited to DTC.

The Republic will not impose any fees in respect of holding the Notes; however, holders of book-entry interests in the Notes may incur fees normally payable in respect of the maintenance and operation of accounts in Euroclear, Clearstream, Luxembourg or DTC.

Clearing and Settlement Procedures

Initial Settlement

Upon their original issue, the Notes will be in global form represented by the two Global Certificates. Interests in the Notes will be in uncertified book-entry form. Purchasers electing to hold book-entry interests in the Notes through Euroclear and Clearstream, Luxembourg accounts will follow the settlement procedures applicable to conventional Eurobonds. Book-entry interests in the Notes will be credited to Euroclear and Clearstream, Luxembourg participants' securities clearance accounts on the business day following the Closing Date against payment (value the Closing Date). DTC participants acting on behalf of purchasers electing to hold book-entry interests in the Notes through DTC will follow the delivery practices applicable to securities eligible for DTC's Same Day Funds Settlement system. DTC participants' securities accounts will be credited with book-entry interests in the Notes following confirmation of receipt of payment to the Republic on the Closing Date.

Secondary Market Trading

Secondary market trades in the Notes will be settled by transfer of title to book-entry interests in the Clearing Systems. Title to such book-entry interests will pass by registration of the transfer within the records of Euroclear, Clearstream, Luxembourg or DTC, as the case may be, in accordance with their respective procedures. Book-entry interests in the Notes may be transferred within Euroclear and within Clearstream, Luxembourg and between Euroclear and Clearstream, Luxembourg in accordance with procedures established for these purposes by Euroclear and Clearstream, Luxembourg. Book-entry interests in the Notes may be transferred within DTC in accordance with procedures established for this purpose by DTC. Transfer of book-entry interests in the Notes between Euroclear or Clearstream, Luxembourg and DTC may be effected in accordance with procedures established for this purpose by Euroclear, Clearstream, Luxembourg and DTC.

General

None of Euroclear, Clearstream, Luxembourg or DTC is under any obligation to perform or continue to perform the procedures referred to above, and such procedures may be discontinued at any time.

None of the Republic or any of their agents will have any responsibility for the performance by Euroclear, Clearstream, Luxembourg or DTC or their respective participants of their respective obligations under the rules and procedures governing their operations or the arrangements referred to above.

SUBSCRIPTION AND SALE

Citigroup Global Markets Limited and Credit Suisse Securities (Europe) Limited (the "**Joint Lead Managers**") and Skandinaviska Enskilda Banken AB (publ) and Swedbank AB (publ) (together with the Joint Lead Managers, the "**Managers**") have in a subscription agreement dated 13 June 2011 (the "**Subscription Agreement**") and made between the Republic and the Managers upon the terms and subject to the conditions contained therein, agreed to subscribe and pay for the Notes at an issue price of 98.164 per cent. of their principal amount less a combined management and underwriting commission of 0.20 per cent. of their principal amount. The Managers are entitled in certain circumstances to be released and discharged from their obligations under the Subscription Agreement prior to the closing of the issue of the Notes.

United States of America

The Notes have not been and will not be registered under the Securities Act and, subject to certain exceptions, may not be offered or sold within the United States or to or for the account or benefit of a U.S. person except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act. Accordingly, the Notes are being offered and sold only (a) outside the United States to persons other than U.S. persons as defined in Regulation S in offshore transactions in reliance on, and in compliance with, Regulation S and (b) in the United States to a limited number of QIBs as defined in the Securities Act in connection with resales by the Managers, in reliance on, and in compliance with, Rule 144A.

In addition, until 40 days after the commencement of the offering, an offer or sale of Notes within the United States by any dealer (whether or not participating in the offering of the Notes) may violate the registration requirements of the Securities Act if such offer or sale is made otherwise than in accordance with Rule 144A.

Each Manager has represented and agreed that it has offered and sold, and will offer and sell, the Notes (a) as part of its distribution at any time and (b) otherwise until 40 days after the later of the commencement of the offering and the Closing Date, only in accordance with Rule 903 of Regulation S or Rule 144A. Accordingly, neither such Manager nor its affiliates, nor any persons acting on its or their behalf, have engaged or will engage in any directed selling efforts (as defined in Regulation S) with respect to the Notes, and such Manager, its affiliates and all persons acting on its or their behalf have complied and will comply with the offering restrictions requirement of Regulation S. Each Manager has agreed that, at or prior to confirmation of sale of the Notes (other than a sale pursuant to Rule 144A), it will have sent to each distributor, dealer or person receiving a selling concession, fee or other remuneration that purchases the Notes from it during the restricted period a confirmation or notice to substantially the foregoing effect.

Each purchaser of a Note, by its acceptance thereof, will be deemed to have acknowledged, represented to and agreed with the Republic and the Managers as follows:

(a) It understands and acknowledges that the Notes have not been registered under the Securities Act or any other applicable securities law, and that the Notes are being offered for sale in transactions not requiring registration under the Securities Act or any other securities laws, including sales pursuant to Rule 144A and Regulation S and, unless so registered, may not be offered, sold or otherwise transferred except in compliance with the registration requirements of the Securities Act or any other applicable securities laws, pursuant to an exemption therefrom or pursuant to a transaction not subject thereto.

(b) It is either (i) a QIB and is aware that any sale of the Notes to it will be made in reliance on Rule 144A and it is acquiring the Notes for its own account or for the account of another QIB with respect to which it exercises full investment discretion, or (ii) it is not a U.S. person (as defined in Regulation S) or purchasing for the account or benefit of a U.S. person and is purchasing the Notes in an offshore transaction (as defined in Regulation S) in accordance with Regulation S.

(c) It is purchasing the Notes for its own account or for the account of investors meeting the requirements of paragraph (b) above for which it is acting as a fiduciary or agent and with respect to which it has the authority to make these acknowledgements, representations and agreements, in each case not with a view to, or for offer or sale in connection with, any distribution thereof in violation of the Securities Act.

(d) If it is a QIB purchasing the Notes pursuant to Rule 144A, it will not offer, sell, pledge or otherwise transfer the Notes except (i) (A) to the Republic, (B) to a person whom the purchaser reasonably believes is a QIB in a transaction meeting the requirements of Rule 144A, (C) in an offshore transaction complying with Rule 903 or Rule 904 of Regulation S or (D) in a transaction that is otherwise exempt from the registration requirements of the Securities Act but only upon delivery to the Republic of an opinion of counsel in form and scope satisfactory to the Republic and (ii) in accordance with all applicable securities laws of the States of the United States.

(e) It acknowledges that certificates in respect of Notes purchased pursuant to Rule 144A, unless otherwise agreed by the Republic, will bear a legend to the following effect:

THE SECURITIES REPRESENTED HEREBY HAVE NOT BEEN AND WILL NOT BE REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE SECURITIES ACT). THE HOLDER HEREOF, BY PURCHASING THE NOTES IN RESPECT OF WHICH THIS CERTIFICATE IS ISSUED, AGREES, FOR THE BENEFIT OF THE REPUBLIC, THAT SUCH NOTES MAY BE OFFERED, SOLD, PLEDGED OR OTHERWISE TRANSFERRED ONLY (A)(1) TO THE REPUBLIC, (2) IN COMPLIANCE WITH RULE 144A UNDER THE SECURITIES ACT TO A PERSON THAT THE HOLDER REASONABLY BELIEVES IS A QUALIFIED INSTITUTIONAL BUYER WITHIN THE MEANING OF RULE 144A UNDER THE SECURITIES ACT PURCHASING FOR ITS OWN ACCOUNT OR FOR THE ACCOUNT OF A QUALIFIED INSTITUTIONAL BUYER WHOM THE HOLDER HAS INFORMED, IN EACH CASE, THAT THE OFFER, SALE, PLEDGE OR OTHER TRANSFER IS BEING MADE IN RELIANCE ON RULE 144A, (3) IN AN OFFSHORE TRANSACTION COMPLYING WITH RULE 903 OR 904 OF REGULATION S UNDER THE SECURITIES ACT, OR (4) IN A TRANSACTION THAT IS OTHERWISE EXEMPT FROM THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT BUT ONLY UPON DELIVERY TO THE REPUBLIC OF AN OPINION OF COUNSEL IN FORM AND SCOPE SATISFACTORY TO THE REPUBLIC; AND (B) IN COMPLIANCE WITH ALL APPLICABLE SECURITIES LAWS OF THE STATES OF THE UNITED STATES.

(f) It acknowledges that certificates in respect of Notes purchased pursuant to Regulation S, unless otherwise agreed by the Republic, will bear a legend to the following effect:

THIS NOTE HAS NOT BEEN AND WILL NOT BE REGISTERED UNDER THE US 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 MAY NOT BE OFFERED OR SOLD, PLEDGED OR OTHERWISE TRANSFERRED WITHIN THE UNITED STATES EXCEPT PURSUANT TO AN EXEMPTION FROM REGISTRATION UNDER THE SECURITIES ACT

(g) Each purchaser further acknowledges that the Managers and their affiliates and otherwise will rely upon the truth and accuracy of the foregoing acknowledgements, representations and agreements. If it is acquiring any Restricted Global Certificates for the account of one or more QIBs, the purchaser thereof represents that it has sole investment discretion with respect to each such account and that it has full power to make the foregoing acknowledgements, representations and agreements on behalf of each such account.

United Kingdom

Each Manager has represented, warranted and agreed that:

(a) ***Financial promotion***: it has only communicated or caused to be communicated and will only communicate or cause to be communicated any invitation or inducement to engage in investment activity (within the meaning of section 21 of the Financial Services and Markets Act 2000 (the "**FSMA**") received by it in connection with the issue or sale of any Notes in circumstances in which section 21(1) of the FSMA does not apply to the Republic; and

(b) ***General compliance***: it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to any Notes in, from or otherwise involving the United Kingdom.

Latvia

The Managers have represented and agreed that the Notes have not been registered under the Law on the Financial Instruments Market of Latvia and may not be publicly offered or sold within the territory of Latvia. The Managers have represented and agreed that they have not publicly offered or sold, and will not offer or sell, any Note within Latvia and that neither they nor any of their affiliates, nor any persons acting on their or their affiliates behalf, have engaged or will engage in any directed public selling efforts in Latvia with respect to the Notes. The Managers have further represented and agreed that they (A) have not offered or sold, and will not offer or sell, the Notes to a person who is a resident of Latvia other than in accordance with the laws of the Republic of Latvia and the Rules of the Financial and Capital Market Commission in Latvia and (B) have not delivered and will not deliver within Latvia any Notes in definitive form that are sold.

General

No action has been or will be taken in any jurisdiction by the Republic or the Managers that would, or is intended to, permit a public offering of the Notes, or possession or distribution of this Offering Circular or any other offering material, in any country or jurisdiction where action for that purpose is required. Persons into whose hands this Offering Circular comes are required by the Republic and the Managers to comply with all applicable laws and regulations in each country or jurisdiction in which they purchase, offer, sell or deliver Notes or have in their possession, distribute or publish this Offering Circular or any other offering material relating to the Notes, in all cases at their own expense.

Delivery of the Notes will be made against payment therefor on or about the date specified in the last paragraph of the second page of this Offering Circular, which will be the fifth business day following the date of pricing of the Notes (such settlement being herein referred to as "T+5"). Under Rule 15c6-1 under the Exchange Act, trades in the secondary market generally are required to settle in three business days, unless the parties to any such trades expressly agree otherwise. Accordingly, purchasers who wish to trade the Notes on the date of pricing or the next succeeding business day will be required, by virtue of the fact that the Notes initially will settle in T+5, to specify an alternate settlement cycle at the time of any such trade to prevent failed settlement. Purchasers of the Notes who wish to trade the Notes on the date of pricing or the next three succeeding business days should consult their own adviser.

TRANSFER RESTRICTIONS

Due to the following significant transfer restrictions applicable to the notes, investors are advised to consult legal counsel prior to making any reoffer, resale, pledge, transfer or disposal of the Notes.

The Notes have not been registered under the Securities Act, and may not be offered or sold in the United States or to, or for the account or benefit of, U.S. persons (as defined in Regulation S under the Securities Act) except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act. Accordingly, the Notes are being offered and sold (1) in the United States only to persons reasonably believed to be "qualified institutional buyers," which are referred to as QIBs, as defined in Rule 144A under the Securities Act in compliance with Rule 144A and (2) to persons outside the United States ("**foreign purchasers**") in offshore transactions pursuant to Regulation S under the Securities Act.

By its purchase of Notes, each purchaser of Notes will be deemed to:

(a) represent that it is purchasing the Notes for its own account or an account with respect to which it exercises sole investment discretion and that it and any such account is (i) a QIB, and is aware that the sale to it is being made in reliance on Rule 144A or (ii) a foreign purchaser that is outside the United States;

(b) acknowledge that the Notes have not been registered under the Securities Act and may not be offered or sold within the United States except as set forth below;

(c) if it is a person other than a foreign purchaser outside the United States after the expiration of the distribution compliance period, agree that if it should resell or otherwise transfer the Notes within the time period referred to in Rule 144(k) under the Securities Act after the original issuance of the Notes, it will do so only (i) to the Republic, (ii) to a QIB in compliance with Rule 144A, (iii) outside the United States in an offshore transaction in compliance with Rule 903 or 904 of Regulation S under the Securities Act, (iv) pursuant to a transaction that is otherwise exempt from the registration requirements of the Securities Act but only if available and upon delivery to the Republic of an opinion of counsel in form and scope satisfactory to the Republic or (v) pursuant to an effective registration statement under the Securities Act. Subject to the procedures set forth in the Agency Agreement, prior to any proposed transfer of the Notes (other than pursuant to an effective registration statement) within the time period referred to in Rule 144(k) under the Securities Act after the original issuance of the Notes, the holder thereof must check the appropriate box set forth on the reverse of its Notes relating to the manner of such transfer and submit the Notes to the Fiscal Agent;

(d) agree that it will deliver to each person to whom it transfers Notes notice of any restriction on transfer of such Notes;

(e) understand and agree that Notes initially offered in the United States to QIBs will be represented by one or more Restricted Global Certificates and that Notes offered outside the United States in offshore transactions pursuant to Regulation S will be represented by one or more Unrestricted Global Certificates;

(f) understand that unless registered under the Securities Act, the Notes (other than those issued to foreign purchasers after expiration of the distribution compliance period) will bear a legend to the following effect, unless otherwise agreed by the Republic and the holder thereof:

THE NOTES REPRESENTED HEREBY HAVE NOT BEEN AND WILL NOT BE REGISTERED UNDER THE SECURITIES ACT OF 1933, AS AMENDED (THE SECURITIES ACT), OR ANY SECURITIES LAW OF ANY STATE IN THE UNITED STATES OF AMERICA, AND MAY NOT BE REOFFERED, RESOLD, PLEDGED OR OTHERWISE TRANSFERRED EXCEPT AS PERMITTED BY THE FOLLOWING SENTENCES. THE HOLDER HEREOF, BY PURCHASING THE NOTES IN RESPECT OF WHICH THIS CERTIFICATE IS ISSUED, ACKNOWLEDGES AND AGREES, FOR THE BENEFIT OF THE ISSUER, THAT SUCH NOTES MAY BE OFFERED, SOLD, PLEDGED OR OTHERWISE TRANSFERRED ONLY (A)(1) TO THE ISSUER, (2) IN COMPLIANCE WITH RULE 144A UNDER THE SECURITIES ACT TO A PERSON THAT THE HOLDER REASONABLY BELIEVES IS A QUALIFIED INSTITUTIONAL BUYER WITHIN THE MEANING OF RULE 144A UNDER THE SECURITIES ACT PURCHASING FOR ITS OWN ACCOUNT OR FOR THE ACCOUNT OF A QUALIFIED INSTITUTIONAL BUYER WHOM THE HOLDER HAS INFORMED, IN EACH CASE, THAT THE OFFER, SALE, PLEDGE OR OTHER TRANSFER IS BEING MADE IN RELIANCE ON RULE 144A, (3)

IN AN OFFSHORE TRANSACTION COMPLYING WITH RULE 903 OR 904 OF REGULATION S UNDER THE SECURITIES ACT, (4) IN A TRANSACTION THAT IS OTHERWISE EXEMPT FROM THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT BUT ONLY IF AVAILABLE AND UPON DELIVERY TO THE ISSUER OF AN OPINION OF COUNSEL IN FORM AND SCOPE SATISFACTORY TO THE ISSUER OR (5) PURSUANT TO AN EFFECTIVE REGISTRATION STATEMENT UNDER THE SECURITIES ACT; AND (B) IN EACH CASE IN COMPLIANCE WITH ALL APPLICABLE SECURITIES LAWS OF THE STATES OF THE UNITED STATES;

(g) acknowledge that the Republic and the Managers will rely upon the truth and accuracy of the foregoing acknowledgments, representations and agreements, and agree that if any of the acknowledgments, representations or warranties deemed to have been made by it by its purchase of Notes are no longer accurate, it shall promptly notify the Republic and the Managers; and

(h) if it is acquiring Notes as a fiduciary or agent for one or more investor accounts, represent that it has sole investment discretion with respect to each such account and it has full power to make the foregoing acknowledgments, representations and agreements on behalf of each such account.

GENERAL INFORMATION

1. Under the Law on Budget and Financial Management adopted on 24 March 1994, the Treasury, on behalf of the Republic of Latvia, is entitled to borrow up to the aggregate limit of borrowing set down in the budget law for the respective year. The budget law for 2011 has set a debt ceiling outstanding of LVL 6,000 million for the year end 2011. The Minister of Finance, in a letter dated 13 June 2011, has confirmed that this issue of U.S.$500,000,000 5.25 per cent. Notes due 2021 does not breach the budget law for 2011 or the Law on Budget and Financial Management and conforms with the Debt Management Strategy and the Resource Attraction Plan approved by the Minister of Finance.

2. The Republic is not involved in any litigation or arbitration proceedings relating to claims or amounts which are material in the context of the issue of the Notes nor, so far as the Republic is aware, is any litigation or arbitration pending or threatened.

3. Application has been made to list the Notes on the Official List of the Luxembourg Stock Exchange and to admit the Notes to trading on the Luxembourg Stock Exchange's regulated market. Copies (and certified English translations where the documents in question are not in English) of the following documents may be obtained during normal business hours at the offices of the Listing Agent in Luxembourg:

   (a) the Fiscal Agency Agreement;

   (b) the Subscription Agreement;

   (c) the Deed of Covenant;

   (d) certified English translations of an extract from the Law on Budget and Financial Management adopted on 24 March 1994;

   (e) the letter of the Minister of Finance dated 13 June 2011 confirming that the issue of Notes does not breach the budget law for 2011 or the Law on Budget and Financial Management and conforms with the Debt Management Strategy and the Resource Attraction Plan approved by the Minister of Finance;

   (f) the Regulations of the Treasury of the Republic of Latvia issued by the Cabinet of Ministers;

   (g) Internal Regulation of Ministry of Finance of the Republic of Latvia No.12-29/52 dated 29 October 2010 ''Procedure of Exercising the Treasury Authorisation''; and

   (h) the current summary version (relating to 2011) of the Latvian consolidated and general government budget (as set out on page 79).

4. Application has been made for acceptance of the Restricted Global Certificates into DTC's book-entry settlement system. The Unrestricted and Restricted Global Certificates have been accepted for clearance through Euroclear and Clearstream, Luxembourg. The ISIN for the Unrestricted Global Certificates is XS0638326263 and for the Restricted Global Certificates is US518417AA89. The Common Code for the Unrestricted Global Certificates is 063832626 and for the Restricted Global Certificates is 063842630. The CUSIP number for the Restricted Global Certificates is 518417AA8.

5. The Notes appertaining thereto will bear a legend to the following effect: ''Any United States person who holds this obligation will be subject to limitations under the United States income tax laws, including the limitations provided in Sections 165(j) and 1287(a) of the Internal Revenue Code''. The sections referred to in such legend provide that a United States person who holds a Note will generally not be allowed to deduct any loss realised on the sale, exchange or redemption of such Note and any gain (which might otherwise be characterised as capital gain) recognised on such sale, exchange or redemption will be treated as ordinary income.

6. As at the date of this Offering Circular, a judgment obtained in an English court against the Republic should be enforceable against the Republic in Latvia, as Council Regulation 44/2001 is directly applicable in Latvia. According to the Civil Procedure law of the Republic of Latvia the application of the recognition and enforcement of the foreign judgment in Latvia shall be submitted for decision to a district (city) court. The judgment of a foreign court after its recognition in Latvia shall be executed according to the procedures specified in the Latvian Civil Procedure Law.

7. Information relating to "The National Budget" is available on the Ministry of Finance of the Republic of Latvia website at *www.fm.gov.lv* and on the Treasury of the Republic of Latvia website at *www.kase.gov.lv*.

ISSUER

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