

Flash Comment

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Latvia: A helping hand from Copenhagen and Stockholm

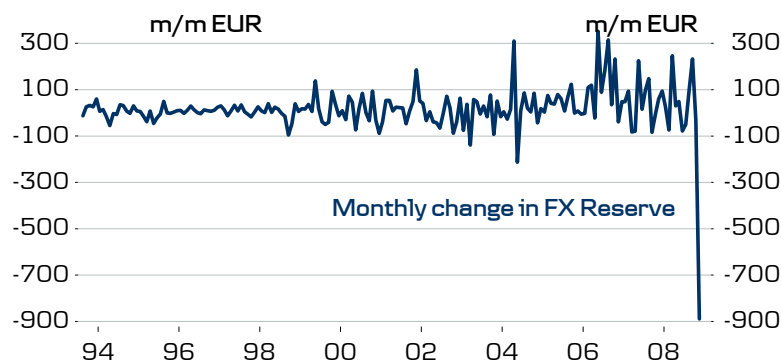
This afternoon it was announced that the Swedish and Danish central banks have agreed to provide the Latvian central bank with a euro facility totalling EUR 500m (EUR 375m from Riksbanken and EUR 125m from Danmarks Nationalbank). This is good news for the Latvian markets and a clear signal that the Swedish and the Danish central banks are concerned about possible contagion from the Baltic crisis to the Nordic region. Nevertheless, this announcement does not solve Latvia's problems overnight, and caution is still very much warranted in the Latvian markets.

There is little doubt that last week's passing of the significant fiscal austerity package in Latvia has helped convinced the Swedish and Danish central banks that it can now provide some help to the Latvian central bank. Hence, the fiscal austerity package should contribute to reducing imbalances in the Latvian economy, while the contribution from the Nordic central banks (with a possible IMF package) should provide some external support during the difficult adjustment process.

That said, the situation remains tense in the Baltic region, and the markets would probably need more good news before getting back to "normal". Furthermore, it should be noted that during November, the Latvian currency reserves dropped by nearly EUR 900m – hence significantly more than the EUR 500m facility that the Latvian central bank will receive from the Danish and the Swedish central banks. Hence, there is no guarantee that everything will be fine. The question is whether more support would be forthcoming if necessary.

Looking ahead, we would be looking for similar agreements between the Nordic central banks and the Lithuanian and the Estonian central banks.

Latvian FX reserves



Source: EcoWin

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