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Statement by Mr. Fridriksson on Latvia
Executive Board Meeting 92/156
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Only three months have lapsed since the stand-by arrangement for Latvia was endorsed by the Executive Board. As the paper on the first review under the arrangement shows, the Latvian authorities have shown their commitment to the program and implemented all the measures agreed, and all the performance criteria set in the program for end-September were met. This they have achieved in the face of extremely difficult circumstances. Trade with traditional partners has yet to recover. Exports to non-traditional markets have revived, but from an extremely low level, and remain insignificant. The need for essential imports is severe, but the acute reserve shortage limits the import ability, and, so far, of the international financial institutions, only the Fund has made disbursements to Latvia, and nothing has as yet been disbursed of the amounts which were committed within the G-24 framework.

Economic developments in Latvia in the latter half of the year have been even more unfavorable than expected when the program was formally adopted by the Board in September. The non-recovery of traditional trade relations has led to a sharper contraction in output than was anticipated, resulting in an even more painful initial period under the program than had been expected. As indicated in the staff report and the supplement, the revised figures for real GDP in 1992 and in the program year show a much greater contraction than earlier envisaged. The ability to weather such a contraction is being seriously tested. Not surprisingly, the fiscal side has come under severe pressure, although partly as a result of tax arrears of enterprises. The authorities have made strong efforts to keep budgetary developments broadly on track.

The problems in the trade relations with the ruble area have been compounded by the fact that the payments and settlements system is functioning poorly, leading to long delays in the settlement of payments for exports. This has, i.a., resulted in calls on the Government and the Bank of Latvia to provide credit to firms exporting to Russia and other ruble area countries. As emphasized in several previous meetings, there is, therefore, an urgent need to shore up the payments system. In this respect, the staff paper on Interstate Monetary and Payments Arrangements in the Former Soviet Union provides a useful insight into the difficulties in the payments system and makes recommendations for its improvement which should be heeded. This is an issue of profound importance for the ruble area and the Baltic countries.

Monetary policy has been implemented with great conviction in Latvia, and the monetary side of the program remains on track. Inflation has come down, but is still higher than earlier expected.

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Although the program remains on track so far, serious difficulties could lie ahead. Disenchantment with the current severe squeeze on living standards is intensifying, and the Government will find it an increasing challenge to maintain the necessary public support for the continuation of the aggressive policies so far pursued. For the authorities' strategy to succeed, it is vitally important that other creditors begin to disburse from their commitments as soon as possible. Further delays can seriously undermine the program, with unforeseen consequences for Latvia and for the involvement of the Fund. In this connection, my authorities would like to extend their appreciation to the staff of the Fund for its efforts in generating the bridge financing operation from the BIS which is mentioned in the supplement to the staff report.

The staff indicates in its appraisal that there may be a need for some measure of flexibility in policy implementation to ensure continued broad political support for the adjustment and reform efforts. I fully agree with this, which is not a question of weakening these efforts, but rather an indication of the fact that we are moving in extremely difficult and partly unknown waters. A successful conclusion of the next review, which will commence with a mission to Riga in January, will be crucial to the continuation of the overall strategy.

The staff paper correctly mentions that progress in the area of privatization has been slow. I want to assure the Board, however, that my authorities intend to move more aggressively in this area in the coming year. This includes not only the privatization of state enterprises, but also of the former branches of the Bank of Latvia. The government of Latvia is negotiating with the European Community to set up a privatization agency to speed up the process. The Fund has provided technical assistance to the Bank of Latvia, and experts have come from outside the international financial institutions to assist in the restructuring and reorganization of the banks. It is to be hoped that the World Bank and the EBRD can quickly begin to provide assistance in this particular area, as the banks are generally weak and banking expertise scarce.

Considerable technical assistance has been provided in a number of areas, but much work is still needed, in banking, as I mentioned, fiscal affairs and statistics, just to mention some priority areas. The statistical base is extremely weak, and most figures on the evolution of economic aggregates can be subject to large revisions. Not only does this create possible problems--at least in the near term--in the interpretation of available information, but it can also complicate the setting of targets and performance criteria.

In conclusion, I wish to repeat that my Latvian authorities remain firmly committed to the program as is convincingly demonstrated by their efforts so far. The Fund has provided tremendous assistance--for which my authorities are grateful--and it is to be hoped that other multilateral institutions quickly intensify their activities in Latvia.