

Latvia

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IN A NUTSHELL

- The economy stagnated due to subdued private consumption and exports with investment increasing from low levels.
- The housing market remained relatively weak, but recovering purchasing power and improving affordability will support gradual recovery.
- Following substantial rate hikes, lending decelerated but outstanding mortgages grew slightly.
- Domestic deposits continue to dominate the funding of banks.

MACROECONOMIC OVERVIEW

Due to the ongoing war in Ukraine, other geopolitical uncertainties and tight monetary policy, both foreign and domestic demand were weak. Real GDP remained constant with private consumption and exports fell and investment increased from low levels.

Private consumption decreased by 1.3% y-o-y due to the weak purchasing power in the first half of the year and high interest rates encouraging saving. Tight monetary policies in major trading partners held back foreign demand, which, complemented by the housing crisis in Sweden resulted in overall exports dropping by 5.8%. Gross fixed capital formation grew by 7.1% primarily due to government investment in large-scale projects and defence and overall investment in dwellings.

The labour market remained relatively tight. Unemployment dropped to 6.5% despite the absence of economic growth. The number of job vacancies declined at year end, slightly lagging GDP. Real wage growth turned positive and HICP inflation falling from 21.4% in January to 0.9% at year-end (9.1% in 2023 on average) strengthening household purchasing power.

The general government deficit dropped to 2.2% of GDP, with tax revenues increasing on the back of elevated price levels and expenditure on support measures (such as energy support) decreasing. The debt-to-GDP ratio increased due to additional borrowing resulting from the cash-flow deficit from 41.8% in 2022 to 43.6%.

HOUSING MARKETS

Hampered by diminished household purchasing power, elevated interest rates and worse affordability of new dwellings, real estate activity remained relatively weak in 2023 and the first quarter of 2024. In January-March 2024, the number of transactions was 5.8% lower y-o-y. The number of purchases of newly build apartments in Riga fell particularly sharply - by 20.7% y-o-y. The decline in

market activity over the last two years has been rather moderate. The number of transactions in 2023 was 8.1% lower than seen the 2017-2019 average.

Gradually recovering household purchasing power, an end to increasing (and expected decreasing from H224) rates and slowly improving affordability will support a gradual recovery in market activity. Activity in regions outside and counties adjacent to Riga will be supported by an increase in the state guarantees for families with children¹.

Supply of housing remained weak - according to Central Statistical Bureau's data, the total area of new dwellings commissioned decreased by 13.2% y-o-y. As the housing market recovers, limited new supply is likely to upward pressure on prices.

As the housing market has slowed, price growth has slowed significantly. In Q423, the Central Statistical Bureau house price index was 1.0% higher than a year ago, but 2.5% less than the previous quarter. The growth in house prices continued to vary considerably by segment. Due to continued supply of Soviet-era standard series apartments in the secondary market, existing dwelling prices have been slightly decreasing (-2.1% y-o-y in Q423), yet the growth of newly built dwelling prices remained swift (11.6% y-o-y in Q423).

Affordability for existing properties is largely unchanged but for new properties is worse given the sharp increase in prices and interest rates over the last two years, was still rather weak. However, as the growth in construction costs has moderated and the activity in the newly built housing segment has declined considerably, the selling prices (from selling advertisements) of newly built housing stabilized at the end of the year.

MORTGAGE MARKETS

The outstanding amount of residential and commercial mortgage loans held by banks grew by 2.6%. Residential mortgages increased by 1.6% still facilitated by the state support programme² for house purchase. Following substantial interest rate hikes, new household lending decelerated.

LTVs of new residential mortgage loans remained stable. LTVs exceeded 90% for 24% of new loans, mainly related to the state guarantee program.

Total residential mortgages are still only 12% of GDP (the lowest of all Euro area countries) and overall household indebtedness remains low. Interest rates on mortgages have increased rapidly – from an average of 2.9% in 2022 to 5.6% in 2023 (or from 4.3% at year-end 22 to 5.8% at year-end 2023). As of end of 2023, 94% of mortgage loans outstanding were with a floating rate.

The quality of the loan portfolio has not changed significantly, NPLs were 1.4% of total domestic loans and 1.2% of residential mortgage loans at year end.

¹ The amount of the state guarantee has been increased up to 50% of the loan amount, encouraging lending of houses outside Riga and Pierīga, which has been slow until now. The guarantee amounts of up to 50% of the loan amount, but not more than 50,000 euros, can be granted to families with at least three children. See footnote 2 for more detail on the guarantee programme and more detail (in Latvian language) on the programme extension: [Palielinās valsts garantiju mājokļa būvniecībai vai iegādei ģimenēm Latvijās rezidžos](https://www.em.gov.lv/latvian/ekonomikas-ministrija/palielinas-valsts-garantiju-majokla-buvniecibai-vai-iegadei-gimenem-latvijas-rezidjos) | Ekonomikas ministrija (em.gov.lv)

² Within the programme, a guarantee for a bank loan for purchase or construction of the housing for the families with children, young specialists or the National armed forces soldiers with regular income but not enough savings to make the downpayment is provided. The LTV requirement for these state-guaranteed loans is set at a maximum of 95% (the general maximum LTV requirement is 90%). More details on the programme available here: <https://www.altum.lv/en/services/individuals/housing-guarantees-for-families/> <https://www.altum.lv/en/services/individuals/housing-guarantees-for-young-professionals/> <https://www.altum.lv/en/services/individuals/for-the-armed-forces-soldiers/>

MORTGAGE FUNDING

Credit institutions obtain funding mostly from domestic retail and non-financial corporations' deposits.

Some banks participated in TLTRO III operations, but most of this has been repaid. Some banks replaced TLTRO III operations with EU online platform deposits (at year 2023 EU this was 3.1% of total non-bank deposits, compared 2.0% in 2022). Credit institutions are not active in the financial markets for funding.

Domestic deposits remained stable and were 67.2% at year-end (68.2% the year before) of banks' total liabilities, while the share of liabilities to foreign parent MFIs (mostly Nordic parent banks) was 4.7% (4.3% in 2022), as only small foreign branches used their parent bank funding and the banking sector domestic loan to deposit ratio was still low – 72.5% (72.0% in 2021). In 2023, there were no mortgage covered bonds issued by Latvian banks. However, an Estonian bank's Latvian branch mortgages were included in an Estonian covered bond programme.

	LATVIA 2022	LATVIA 2023	EU 27 2023
MACROECONOMIC VARIABLES			
Real GDP growth (%) (1)	3.0	-0.3	0.4
Unemployment Rate (LSF), annual average (%) (1)	6.9	6.5	6.1
HICP inflation (%) (1)	17.2	9.1	6.4
HOUSING MARKET			
Owner occupation rate (%) (1)	83.1	82.8	69.2
Gross Fixed Investment in Housing (annual change) (1)	-11.4	11.1	-3.1
Building Permits (2015=100) (2)	126.1	115.3	94.0
House Price Index - country (2015=100) (2)	184.3	191.3	170.2*
House Price Index - capital (2015=100) (2)	n/a	n/a	165.1*
Nominal house price growth (%) (2)	13.9	3.8	3*
MORTGAGE MARKET			
Outstanding Residential Loans (mn EUR) (2)	4,713	4,790	6,782,375
Outstanding Residential Loans per capita over Total Population (EUR) (2)	2,513	2,544	15,114
Outstanding Residential Loans to disposable income ratio (%) (1) (2)	18.8	18.8	71.3
Gross residential lending, annual growth (%) (2)	n/a	n/a	-26.6
Typical mortgage rate, annual average (%) (2)	2.9	5.6	4.7

* Please note that this value is a simple average of the available values in 2023.

Sources:

(1) Eurostat.

(2) European Mortgage Federation - Hypostat 2024, Statistical Tables.

LATVIA FACT TABLE

Which entities can issue mortgage loans in your country?

Credit institutions, credit unions and non-bank financial institutions can issue mortgage loans in Latvia.

What is the market share of new mortgage issuances between these entities?

Not available

Which entities hold what proportion of outstanding mortgage loans in your country?

The mortgage market is significantly dominated by mortgage loans issued by banks.

What is the typical LTV ratio on residential mortgage loans in your country?

According to the Latvian legislation LTV cannot exceed 90%. For the participants of the state support programme for house purchase and construction, the upper LTV limit is 95%.

How is the distinction made between loans for residential and non-residential purposes in your country?

The distinction is based on the loan issuing purpose (defined by Latvijas Banka's Regulation Compiling the Monthly Financial Position Report of Monetary Financial Institutions and Regulation for the Credit Register).

What is/are the most common mortgage product(s) in your country?

Housing loans

What is the typical/average maturity for a mortgage in your country?

The typical maturity of a new issued mortgage is 20 years.

What is/are the most common ways to fund mortgage lending in your country?

See section on Mortgage funding.

What is the level of costs associated with house purchase in your country (taxes and other transaction costs)?

A stamp duty of 0.5-1.5% of the home price applies when registering the purchase. Regularly, the 1.5% fee applies, and the stamp duty is reduced to 0.5% under the support programme for house purchase. The reduced cost is applied only to families with children, and not for young specialists (please see question 10 on the overview of the support programmes).

In addition to the stamp duty, 0.1% of the mortgage loan amount should be paid for the registration of the mortgage. These are the main fees associated with house purchase, there are also some additional registration fees, but they are usually small, and their amount is fixed (does not depend on the loan amount or real estate price).

For home purchases under the state guarantee programme buyers face additional costs:

- for families with children, the one-time fee is applied - 2.5% of the outstanding amount of the guarantee.
- for young specialists, the guaranteed fee of 2.4% per annum (of outstanding amount of the guarantee) applies.
- for national armed forces soldiers, the guaranteed fee of 2.5% per annum (of outstanding amount of the guarantee) applies

It is possible to obtain a state guarantee up to 30% of the loan amount, but not exceeding EUR 30,000 for families with children (the exact amount of the guarantee depending on the number of children). In addition, an extra 5% increase in the guarantee (but not exceeding the amount of EUR 30,000) is possible if the dwelling corresponds to the "A" energy efficiency class of buildings or is nearly zero energy building. Moreover, families with at least three children that have applied for a mortgage in the largest commercial banks in Latvia starting from July 1st 2020 are eligible as of second half of November 2020 to receive a state subsidy in the amount of 8 to 12 thousand euro (the exact amount depending on the number of children in the family and energy efficiency of the housing to be purchased/built). Although approved 17th of November, it applies retroactively to mortgages granted since 1 July 2020, and was announced already before 1 July 2020.

The state guarantee has been in March 2024 additionally increased for families with children obtaining property in regions outside Riga and the counties adjacent to Riga. The amount of the state guarantee has been increased up to 50% of the loan amount in these regions. The guarantee amounts of up to 50% of the loan amount, but not more than 50,000 euros, can be granted to families with at least three children.

For young specialists (individuals up to 35 years old who have acquired the vocational secondary or higher education) it is possible to obtain a guarantee up to EUR 50,000 or 20% of the loan amount.

For national armed forces soldiers it is possible to obtain a guarantee up to EUR 20,000 or 25% of the loan amount.