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Financial stability: a condition of the financial system enabling it to withstand shocks, thereby mitigating the likelihood of disruptions in the provision of financial services in the financial intermediation process.

Systemic risk: the risk of disruption in the financial system with the potential to have a significant negative impact on the functioning of the financial system as a whole along with the real economy.

The objective of the Financial Stability Report is to raise public awareness regarding the development of the Latvian financial system and to draw attention to systemic risks.

The Financial Stability Report analyses and assesses the functioning and risks of the Latvian financial system based on data up to the end of March 2026 or at the time of compiling the current report.

The following terms are used synonymously in the report: "company" and "NFC", "bank" and "credit institution", "loan" and "credit". The information on credit institutions presented in the report also includes information on branches of credit institutions of EU Member States in Latvia, unless otherwise indicated. The significant credit institutions are Swedbank AS, AS Citadele banka, and AS SEB banka – all supervised by the ECB.

The calculation of the ROE, the TC ratio, T1 capital ratio, CET1 ratio, liquidity, and credit risk stress test results excludes data on branches of foreign credit institutions registered in the Republic of Latvia.

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Abbreviations

ADC – acquisition, development, and construction

AI – artificial intelligence

AS – joint stock company

CCRI – composite cyclical risk indicator

CCyB – countercyclical capital buffer

CDS – credit default swaps

CET1 – Common Equity Tier 1

CISS – composite indicator of systemic stress

COREP – common reporting framework

CRPC – Consumer Rights Protection Centre

CSB – Central Statistical Bureau of Latvia

DSCR – debt service coverage ratio

DSTI – debt-service-to-income

DTI – debt-to-income

EBA – European Banking Authority

EBITDA – earnings before interest, taxes, depreciation, and amortisation

ECB – European Central Bank

EDS – Electronic Declaration System of the State Revenue Service

EEA – European Economic Area

EIOPA – European Insurance and Occupational Pensions Authority

EMIR – European Market Infrastructure Regulation

ER – Enterprise Register

ESRB – European Systemic Risk Board

EU – European Union

EURIBOR – Euro Interbank Offered Rate

FINREP – financial reporting framework

GaR – growth-at-risk or a percentile (typically 5% or 10%) of the future probability distribution of GDP growth rates, capturing downside risks (e.g. in times of shocks)

GDP – gross domestic product

ICR – interest coverage ratio

IFRS – International Financial Reporting Standards

IRB – internal ratings based

IT – information technologies

LCR – liquidity coverage ratio

LGD – loss given default

LLM – large language model

LREA – leverage ratio exposure amount

LTV – loan-to-value

MBP – Monthly Financial Position Report

MFI – monetary financial institution

ML/FT – money laundering and the financing of terrorism

NFC – non-financial corporation

NPLs – non-performing loans

NSFR – net stable financing ratio

OECD – Organisation for Economic Co-operation and Development

O-SII – other systemically important institution

PD – probability of default

P&L – profit and loss statement

RE – real estate

ROA – return on assets

ROE – return on equity

SFPS – state-funded pensions system

SIA – limited liability company

SSM – ECB single supervisory mechanism

TC – total capital

TREA – total risk exposure amount

T1 – Tier 1

US – United States of America

Summary

Global geopolitical uncertainty has been further heightened by warfare in the Middle East. **The global and domestic impact of persistently high uncertainty and geopolitical shocks, including warfare in the Middle East – supply chain constraints, higher inflation, deterioration of economic sentiment, and sharp fluctuations in the prices of financial assets, as well as cyber incidents and other large-scale unexpected disruptions to financial intermediation – also pose a systemic risk to the stability of the Latvian financial sector.**

The effects of geopolitical shocks on Latvia's financial system are mitigated by its still limited direct financial link to the epicentres of these shocks. However, **warfare in the Middle East has increased the credit risk of borrowers in the most energy-intensive sectors and may slow the previously strong growth in lending**. The extent of the indirect impact of warfare on the Latvian financial system largely depends on its intensity and duration.

Lower interest rates, a better financial situation for borrowers, and a stronger incentive for banks to lend significantly spurred domestic lending, and previously persistently insufficient lending support for investment has started to increase. At the same time, the loan-to-GDP ratio remains low. In addition, several structural business environment factors – highlighted in previous financial stability reports – continue to limit investment and lending. These include the shadow economy, the availability of human capital, and the financial capital market. **A weak investment environment has long constituted a significant systemic structural deficiency hampering Latvia's development and competitiveness**.

More active housing lending contributed to the activity of the housing market and also facilitated the development of new real estate projects. In 2025, the share of bank-financed housing purchase transactions reached its highest level in the last seven years. **Amid declining supply, housing prices have started to grow at a faster pace, dampening the improvement in affordability, while price increases remain moderate overall. Insolvency risks in the real estate sector generally continued to decline, and the commercial real estate market started to gradually stabilise. However, a number of structural risks, including high construction costs, continue to affect the development of this market**. In the office space segment, a mismatch between supply and demand persists, and tenant relocation to newer office buildings is reinforcing market polarisation and affecting occupancy rates. **More sustainable development of the real estate market and the promotion of a high-quality and accessible housing stock require a significantly faster pace of building renovations, including large investments in improving energy efficiency**.

Overall, solvency and resilience of borrowers in Latvia remain solid. Household debt payment discipline is very good. In the corporate sector, loan quality deteriorated somewhat already towards the end of 2025, mainly as the risk of deteriorating quality in forborne loans identified in the previous report materialised; yet the deterioration affected only a narrow group of companies. However, **rising energy and labour costs, together with the increase in EURIBOR already priced in by financial markets, will continue to exert downward pressure on corporate profitability and debt-servicing capacity**.

Latvia is implementing a clear commitment to strengthening its defence capabilities which is of crucial importance for promoting financial stability. However, a more substantial improvement in the return on public spending required to provide financing for defence and other priority public expenditure has been delayed, while public debt continues to rise. Accordingly, there are growing risks of rapid changes in fiscal policy, including tax policy, which may negatively affect the business and investment environment, as well as their predictability. **Delays in a more substantial improvement in the return on public expenditure increases the risk of sharp future adjustments to fiscal policy, including tax policy, and creates systemic vulnerabilities. This is amplified by weaker economic growth in Latvia caused by global uncertainty and geopolitical shocks**.

Latvia's financial system remains stable. The short- and longer-term liquidity indicators of credit institutions are at a sufficient level, and the level of funding and liquidity risk in the credit institution sector remains low. Overall, the capital buffers of credit institutions are sufficient to absorb potential losses in the event of financial shocks. While the profits of credit institutions decreased in 2025 due to lower interest rates, higher provisioning expenses, and solidarity contributions, they remain robust and continue to underpin strong capitalisation. The growing Latvian non-bank financial sector still has a limited impact on financial stability in Latvia.

Latvijas Banka's macroprudential policy focuses on the sustainability of the financial sector and the proportionality of regulation. As part of a positive neutral CCyB approach, the CCyB base rate of 1% further strengthens the resilience of banks. This is particularly important amid heightened external uncertainty. Borrower-based measures continue to promote compliance with responsible and sustainable lending standards. In 2025, Latvijas Banka revised and simplified the analytical framework for the identification of O-SIIs and the calculation of O-SII capital buffer rates. As a result, the number of O-SIIs declined from five to three institutions. The revised framework is more appropriate for the specificities of the Latvian financial sector and more proportionate from a supervisory perspective.

Systemic risks and vulnerabilities surrounding the stability of Latvia's financial system

Systemic risks

Global and domestic impact of persistently high uncertainty and geopolitical shocks, including warfare in the Middle East, which may weaken bank asset quality and profitability through:

supply chain constraints and higher inflation

deteriorated economic sentiment

intensified fluctuations in financial asset prices

cyber incidents and other unexpected large-scale disruptions in financial intermediation

Persistently weak investment environment

Potential systemic vulnerability

Delays in a more substantial improvement in the return on public expenditure that increase the risk of sharp future adjustments to fiscal policy, especially amid lower economic growth

Risks associated with climate change and other nature-related risks, including biodiversity loss

The resilience of credit institutions against shocks is good, as their capital and liquidity buffers overall are sufficient

Macroprudential policy focuses on the resilience of the financial sector and the proportionality of regulation

1% CCyB rate within a positive neutral approach further enhances resilience

Borrower-based measures are a backstop for sustainable lending standards

1. Macrofinancial environment and borrowers' solvency

External macrofinancial environment

Prepared by Andrejs Semjonovs

Persistently high global uncertainty remains a fertile ground for financial market and sentiment volatility, posing a threat to financial stability.

The war in the Middle East has further increased uncertainty and tensions. The extent of its adverse impact on the EU and Latvian financial systems – including supply chain constraints and disruptions resulting from hostilities, higher inflation, slower growth, and increasing borrower credit risk – depends on the duration and intensity of hostilities. The impact on credit institutions in EU countries, including Latvia, is mitigated by their low exposure to countries in the Middle East.

The resilience of the EU banking sector to shocks is strong, underpinned by ample bank liquidity and capitalisation, as well as persistently healthy profitability and credit quality.

Economic growth in Latvia's important trading partner countries was robust in 2025 and even accelerated in several of them, despite increased global uncertainty and trade tariffs imposed by the US Administration. However, **the war in the Middle East can significantly delay further growth in several export markets that are important for Latvia**. The war has further increased geopolitical tensions and uncertainty in a number of areas affecting global economic growth and financial stability. **The impact of geopolitical shocks on Latvian credit institutions is mitigated by their still low direct financial exposure to shock epicentres** (see Box 1.1).

Box 1.1. Direct financial links of Latvian credit institutions with Russia, Belarus, Ukraine, Middle East countries, and the United States

Prepared by Andrejs Semjonovs, Jānis Strazdiņš, Mārcis Risbergs

The direct financial link between Latvian credit institutions and the epicentres of geopolitical shocks is small.

After the annexation of Crimea in 2014, the investments of credit institutions in Russia, Belarus, and Ukraine dropped significantly and have been low for several years. In February 2026, investments accounted for only 0.2%[1] of credit institutions' total assets: these are mainly loans and, to a small extent, claims on credit institutions. In February 2026, funding (mainly deposits) raised from Russia, Belarus, and Ukraine accounted for 1.2% of credit institutions' total assets.

Investments in and financing from the countries of the Middle East[2] are also low, at 0.04%[3] and 0.2% of assets respectively in February 2026 (Chart 1.1).

Payments made by customers of Latvian credit institutions to and from these countries also account for only a small proportion of total cross-border payment flows (Chart 1.2).

[1] 0.4% of assets, including credits where Russia, Belarus, or Ukraine is indicated as the country of risk transfer (according to the national risk transfer basis in accordance with Appendix 11 to Latvijas Banka's Regulation No 160 "Regulation on the Credit Register" of 18 January 2018) and thus indirect exposure to risks related to these countries is taken into account.

[2] The analysis covers the following countries: Bahrain, Egypt, Iraq, Iran, Israel, Jordan, Kingdom of Saudi Arabia, Kuwait, Lebanon, Libya, Oman, Pakistan, Palestine, Qatar, Syria, Turkey, United Arab Emirates, Yemen.
[3] 0.08% of assets, including credits where the respective countries are indicated as risk transfer countries.

Payment flows to and from Russia dropped significantly after Russia's invasion of Ukraine and, in 2025, accounted for less than 1% of all payments received and sent by customers of Latvian credit institutions. Trade sanctions also had a significant impact on these payment flows. At the same time, circumvention of sanctions through third countries has so far been an unresolved issue[4]. Looking at the flows of payments made by customers of Latvian credit institutions from and to countries with an increased risk of sanctions[5], it can be concluded that the share of incoming payments has slightly increased since 2022. However, overall, the share of payments made from and to these countries is minimal. Consequently, further trade restrictions between Latvian companies and Russia will not have a significant impact on the stability of the Latvian financial system.

As the impact of US trade tariffs may materialise over a longer period of time and uncertainty continues over the future trading conditions with the US, taking into account the decisions of the US International Trade Court, the portfolio of loans granted by Latvian credit institutions to NFCs exporting to the US is also discussed below.

According to Latvijas Banka and CSB statistics, the total loan portfolio of the NFCs[6] with the largest volume of goods exports to the United States accounted for 6% of the total loan portfolio issued by credit institutions and leasing companies to NFCs at the end of 2025. Furthermore, **the total loan portfolio of NFCs for which the US market represents a substantial share of turnover, based on annual reports, is minimal (Chart 1.3)**[7].

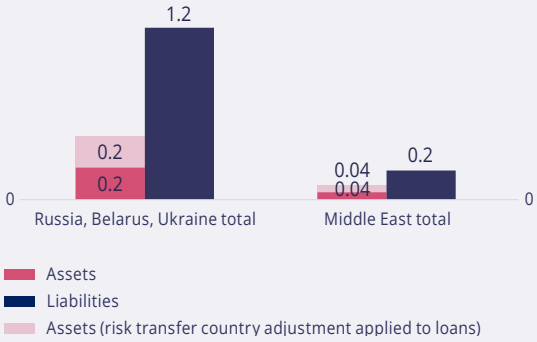
[4] For more information, see: Mirošņikovs, M., "How have sanctions affected trade with Russia?", makroekonomika.lv, 30.10.2024.

[5] Countries at increased risk of sanctions include Armenia, Azerbaijan, China (including Hong Kong), Georgia, India, Kazakhstan, Kyrgyzstan, Mongolia, Serbia, Tajikistan, Thailand, Turkey, United Arab Emirates, and Uzbekistan. See: "Managing Sanctions Risks in Transactions with High-Risk Countries", Financial Intelligence Unit, 2025.

[6] The sample of 210 NFCs includes NFCs whose exports of goods to the US in 2024 amounted to at least EUR 100 000. Data from 2024 are used, as a large part of the sampled NFCs have not yet published the 2025 annual report and, consequently, it is not possible to determine whether exports to the US for each of the NFCs represent a significant share of the total turnover. The total exports of these NFCs account for 92% of Latvia's total exports of goods to the US. Of these, 106 NFCs had liabilities with credit institutions or leasing companies at the end of 2025, according to the Credit Register.

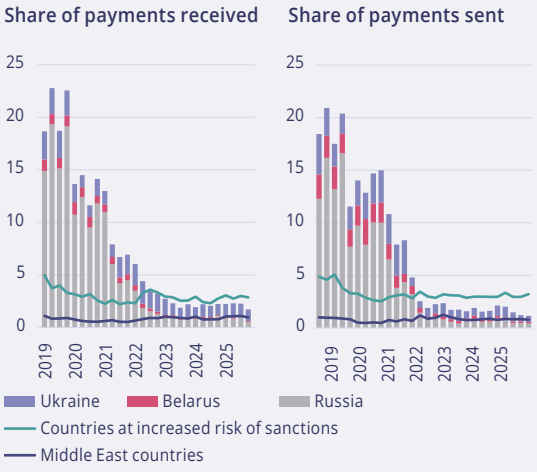
[7] The analysis determines whether the goods exports of these NFCs to the US accounted for at least 20% or at least 50% of their turnover in 2024. In December 2025, the total loan portfolio of NFCs whose exports to the US exceeded 20% and 50% of turnover represented 1.1% and 0.01% respectively of the total loan portfolio issued to NFCs by credit institutions and leasing companies.

Chart 1.1
Share of liabilities and investments of Latvian credit institutions in Russia, Belarus, Ukraine, and the Middle East in total assets in February 2026 (%)



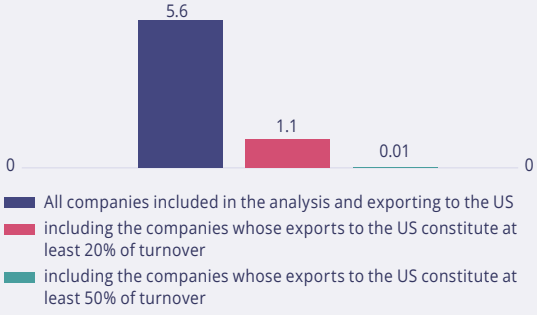
Source: Latvijas Banka (MBP data) and its calculations.

Chart 1.2
Share of cross-border payments in the total amount of incoming and outgoing cross-border payments made by customers of Latvian credit institutions to and from Russia, Belarus, Ukraine, and countries of the Middle East (%)



Sources: payments by customers of Latvian credit institutions, Latvijas Banka's calculations

Chart 1.3
Share of credit to NFCs with the highest volume of goods exports to the United States in the total loan portfolio of NFCs of credit institutions and leasing companies in December 2025 (%)



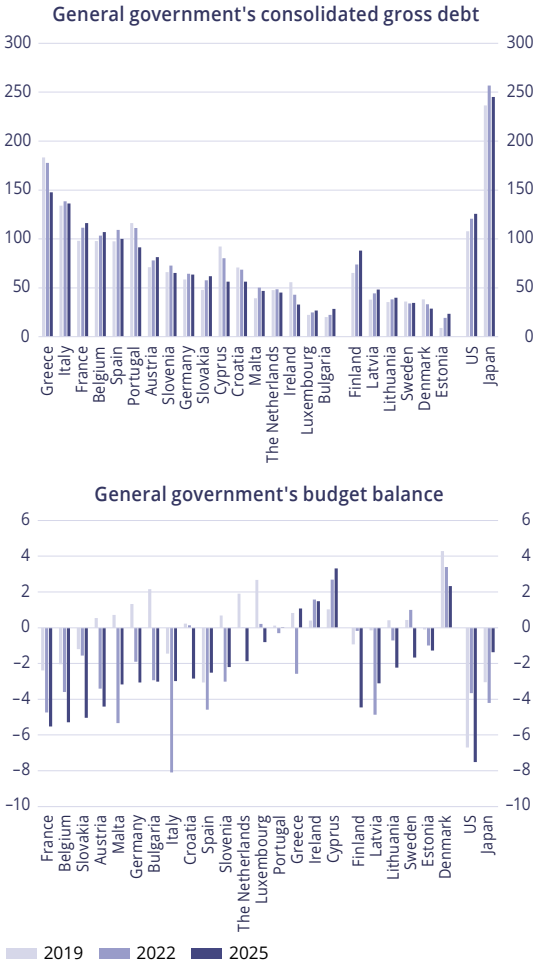
Sources: CSB, Latvijas Banka, and its calculations.

Direct financial links between EU/EEA banks and countries in the Middle East are also limited[8]**. More significant risks to the financial system stem from the indirect effects of the war in the Middle East, including shocks to the global markets for energy resources, fertilisers, and certain metals, as well as higher inflation and slower economic growth.** The attacks on oil and gas infrastructure already carried out in the Middle East mean that a lasting impact is expected[9]. Due to ongoing wars, the credit risk of borrowers in the most energy-intensive sectors in Latvia has increased (see the Section "Credit risk"). Credit growth, which has been active until now, may slow (see the Section "Lending development"). With an impact on the economy and economic sentiment, as well as on reference interest rates, warfare will also determine banks' future profitability prospects (see the Section "Profitability"). **The intensity and duration of the Middle East war will determine the extent of its indirect impact on the Latvian financial system.**

In a context of persistently high global uncertainty and geopolitical tensions, the fiscal vulnerabilities of a number of countries with high debt levels are increasing. Several EU countries' debt levels and/or budget deficits are significantly higher than before the increase in energy prices in 2022 (Chart 1.4), and in addition, large-scale investments in defence, climate resilience, etc. in strategically important areas are needed in the future. On top of that, additional funds may also be needed for targeted support to mitigate the impact of the war in the Middle East. **The persistently high uncertainty creates grounds for sudden changes in financial market sentiment, while a deterioration in confidence in the sustainability of the debt of countries important to global financial markets, such as the United States, may also affect borrowing costs and financial markets in the EU.** The fiscal vulnerabilities in the Baltic and Scandinavian countries are generally lower than in countries with very high debt levels.

The very rapid and massive increase in investment by US leading tech companies also increases the risk of sharp fluctuations in financial markets.

Chart 1.4
Level of government debt and budget balances in the US, Japan, euro area, and individual EU countries (% of GDP)



Source: European Commission's AMECO database.
Note: data for 2025 reflect European Commission estimates.

Competition between leading tech companies in the development of the best AI solutions has contributed to a rapid and massive increase in investment in data centres. An increasing share of these investments is financed by borrowed funds, mainly from the non-bank financial sector. Given the important role of these companies in global financial markets, **an increase in expectations regarding AI productivity and the opportunities that offers in the future may lead to significant fluctuations in stock markets. Market stress may have adverse effects on the financial situation of the non-bank financial sector in the United States and the euro area, in particular the rapidly growing private credit segment**[10]**, which has**

[8] Exposure to countries in the Middle East region accounts for less than 0.5% of total EU/EEA banking sector assets. For more information, see: "The European banking sector enters period of geopolitical uncertainty from a position of strength", European Banking Authority, Press Release, 23.03.2026.

[9] Among them, the reconstruction of Qatar's Ras Laffan gas infrastructure can take three to five years according to various estimates.

[10] Non-bank financial intermediaries (alternative investment funds, private equity funds, and other non-bank financial institutions) providing debt financing to NFCs. This debt financing is not issued or traded on public financial markets.

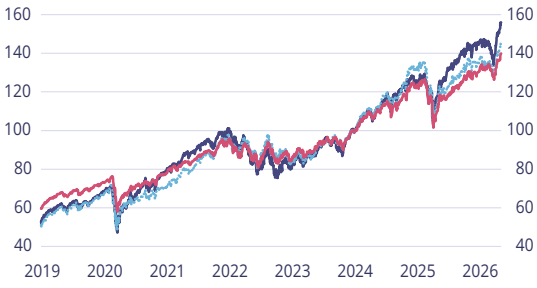
been significantly exposed to technology companies in recent years, and may further exacerbate volatility in the financial sector.

Overall, the likelihood of volatility in the value of securities, driven by unexpected changes of global significance, remains high. Significant changes, including in the value of exchange rates, may adversely affect the value of securities held by Latvian residents. Given the relatively high importance of the US market, the return on the active[11] investment plans of Latvia's SFPS has, historically, also been significantly correlated with fluctuations in US stock prices, but in 2025 the return on these plans has been adversely affected by the weakening of the US dollar (Chart 1.5). A sharp decline in asset values could strengthen political support for changes to the SFPS in Latvia, such as introducing voluntary participation, as has been done in Estonia and Lithuania. Such changes could increase economic imbalances and other risks (see the Chapter "Development and risks in the non-bank financial sector"), while also weakening the pension system. **Risks to Latvia's financial stability stemming from the rapid repricing of individual assets are mitigated by the relatively low proportion of securities within the total assets of Latvian credit institutions** (see the Section "Funding and liquidity risk").

In a context of geopolitical shocks, systemic risks related to cyber-attacks and other large-scale unexpected disruptions to financial intermediation in the region and globally remain significant. On the other hand, growing divergences in public opinion on climate issues weaken efforts to mitigate climate change and contribute to future risks to financial stability.

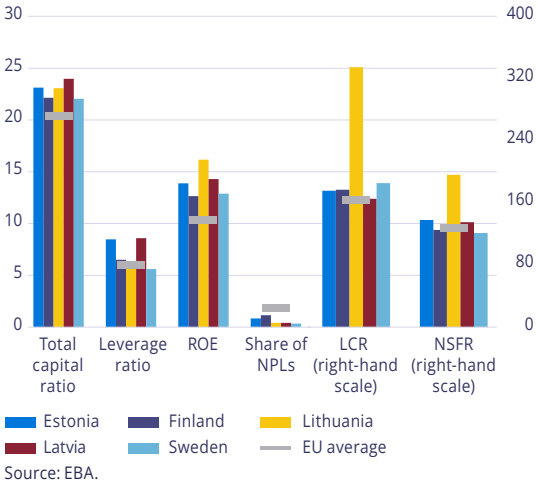
The resilience of the Latvian, Nordic, and EU banking sectors to shocks is generally strong. It is underpinned by high liquidity and capitalisation, as well as persistently good profitability and credit quality. Due to the war in the Middle East, credit risk may increase, especially in the most energy-intensive sectors. However, to date, the quality of EU banks' loan portfolios has been sound (the share of NPLs in banks' loan portfolios remained broadly unchanged in 2025, with a slight increase in credit risk in the real estate, construction, and trading sectors). At the same time, the profitability of EU banks was higher in 2025 than prior to the interest rate hikes, and their capitalisation

Chart 1.5
Evolution of the US stock index price and the weighted average value of the active investment plans of the SFPS (beginning of 2024 = 100)



Sources: Bloomberg, manapensija.lv, Latvijas Banka's calculations.

Chart 1.6
Key capitalisation, profitability, credit quality, and liquidity indicators of Nordic, Baltic, and EU banks (Q4 2025; EBA sample of major banks; %)



Source: EBA.

and liquidity levels remain strong (Chart 1.6). This will contribute to resilience against risks stemming from high uncertainty and geopolitical shocks. **The magnitude of oil and gas price hikes and financial market volatility experienced until mid-April 2026 has been lower than modelled in the severe scenario of the EBA stress tests in 2025**[12]**, under which the largest EU banks are resilient to this adverse counterfactual stress scenario.**

[11] Those with a 100% proportion of investments in shares.

[12] See: 2025 EU-wide Stress Test – Results, European Banking Authority.

Domestic macrofinancial environment

Prepared by Valdis Grudulis and Jekaterina Petkeviča

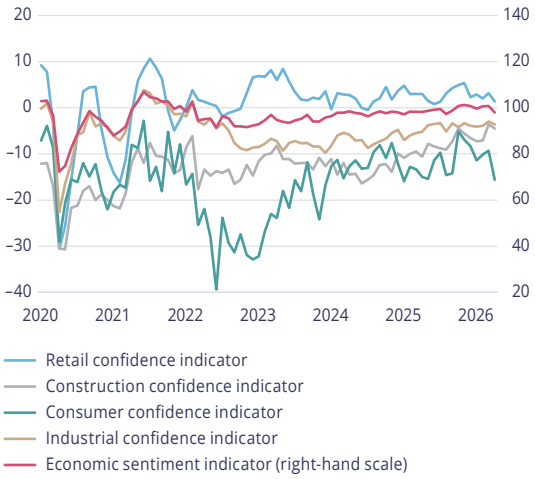
Economic growth picked up again in 2025, but the geopolitical enviroment poses risks to the stability of this trend. In 2025, the economic improvement was supported by high investment activity and more substantial credit expansion, as well as a slow recovery in household consumption. Further growth will be underpinned by public and private investment, including EU fund projects and increased investment in defence. At the same time, it continues to be constrained by rising labour costs, geopolitical shocks, and uncertainty, in particular related to risks of disruptions in the supply of raw materials and energy prices, which may once again provoke caution among consumers and private investors. Sustained low unemployment and labour shortages sustain rapid wage growth. Risks to inflation are on the upside as energy prices rise due to the current global context. In such circumstances, the strengthening of purchasing power may slow.

After two years of stagnation, **the Latvian economy returned to stronger growth in 2025**. **This was mainly driven by strong investment activity, including for defence purposes, and a slow recovery in household consumption**. GDP grew by 2.1% in 2025 (at real prices prices; seasonally and calendar adjusted data). These growth factors, together with increasing lending, are expected to continue to support economic growth in 2026. According to Latvijas Banka's June 2026 forecasts, GDP will grow by 2.0% in 2026, but there are downside risks to the forecast due to the geopolitical environment.

Geopolitical instability slows down global trade and the recovery of Latvian exports. Economic growth will continue to be constrained by the rapid rise in labour costs in Latvia and the geopolitical situation, including warfare and the associated heightened uncertainty in the external economic environment, as well as possible increases in energy prices, logistical disruptions, and shortages of certain raw materials.

The improvement in economic activity in 2025 was reflected in the economic sentiment indicator, which stood above its long-term average. This reflected an improvement in overall sentiment and more optimistic expectations regarding future economic developments. However, economic sentiment deteriorated sharply in spring 2026 (Chart 1.7). Geopolitical tensions in the Middle East negatively affect the sentiment of both Latvian entrepreneurs and consumers. Economic sentiment deteriorated particularly strongly among retailers and consumers. Households' assessment of both the current and expected financial situation as well as the overall economic situation and willingness to make larger purchases weakened. In the industrial and construction sectors, the deterioration in sentiment was more moderate compared to other sectors and overall positive sentiment dynamics have remained since early 2025, driven by growth trends in these sectors and relatively stable business expectations for further growth in business activity.

Chart 1.7
Latvian business economic sentiment indicator (100 = long-term average)**, industry and consumer sentiment indicators** (in points; net result of replies)



Source: European Commission.

Inflation dynamics in Latvia are once again being increasingly affected by rising global energy prices, while medium-term developments are driven by wage changes. While inflation slowly decelerated towards the end of 2025 and remained moderate at the beginning of 2026, inflation already reflected a significant fuel cost effect in March as a result of geopolitical developments. Companies are gradually passing rising labour costs on to final consumers, and the sustained rise in wages continues to support the rise in service prices (Chart 1.8). According to Latvijas Banka's June 2026 forecasts, inflation is expected to rise moderately to 3.8%[13] over the next two years. This

[13] Latvijas Banka's annual inflation projections as of June 2026 are 3.6%, 3.8% and 3.4% for 2026, 2027 and 2028 respectively.

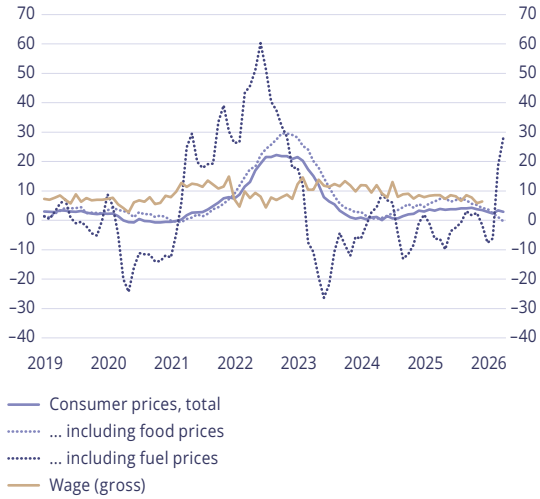
will mainly be driven by the rise in fuel prices and its impact on the prices of goods and services, while the rise in food prices will be dampened by both the base effect and a reduction in the VAT rate[14]. At the same time, the heightened geopolitical shock in the Middle East sustains high uncertainty in global energy and fertiliser markets. The war in the Middle East poses a significant threat to the stability of supply of raw materials, and a price shock may contribute to a faster rise in consumer prices in Latvia.

The labour market remains highly resilient, reflecting sustained demand for labour alongside structural labour shortage. Unemployment continues to decline gradually, driven by private sector labour demand. In 2025, average wage growth reached 7.7%. According to Latvijas Banka's June 2026 forecasts, the growth rate of nominal wages will moderate slightly to 7.4%[15] in 2026. The sustained rise in wages will support a further improvement in the purchasing power of the population. At the same time, this puts additional pressure on the competitiveness of companies, so that rising costs need to be offset by productivity gains. Labour cost increases also provide an incentive for further inflationary growth.

High levels of government investment and increased private sector investment activity will continue to be important drivers of economic growth and competitiveness in the coming periods. Investment activity picked up in 2025, driven by higher corporate investment in the private sector, greater utilisation of EU funding, and an increase in lending. Investment growth is concentrated mainly in the manufacturing and energy sectors. Government investment remained high and will remain so in the future. This will be driven by the government's decision to significantly increase defence investment towards 5% of GDP, as well as the final phase of the implementation of Latvian Recovery and Resilience Facility (RRF) projects in 2026. Investment dynamics will also continue to be supported by the implementation of EU fund projects and the development of the Rail Baltica project, although more rapid progress is currently forecast after 2027.

The operational assessment of the 2025 budget implementation points to a deficit of 2.5% of GDP. The increase in the deficit compared to the previous year was due to higher investment in security and defence. In 2026, according to Latvijas Banka's June 2026 forecasts, a budget deficit of 3.3% is expected, taking into account the financing for the expansion of national defence capabilities and the increase in the amount of borrowing required for this. As a result, the projected government debt will exceed 50% of GDP in 2027. **The debt level remains below the 60% of GDP threshold set in the Maastricht criteria. However, the increase in its size increases the cost of debt servicing and underlines the importance of sustainable fiscal policy and effective public spending.**

Chart 1.8
Annual changes in consumer prices and wages in Latvia (%)



Source: CSB.

Development of the RE market

Improving household solvency, falling interest rates, and accelerating lending for house purchase supported housing market activity and, contributed to the development of new real estate projects. In a context of declining supply, house prices have started to grow at a faster pace, which slows down the improvement in housing affordability, although price increases are moderate overall.

The commercial real estate market gradually started to stabilize, and investment activity in the market resumed, mainly thanks to transactions by investors from the Baltic States. Market developments remain constrained by external uncertainty and low liquidity, while yields remained unchanged. Overall,

[14] From July 2026, the VAT rate for milk, bread, eggs, and chicken has been reduced for one year (from 21% to 12%).
[15] Latvijas Banka's June 2026 forecasts for annual changes in nominal gross wages are 7.4%, 7.3%, and 7.5% for 2026, 2027 and 2028 respectively.

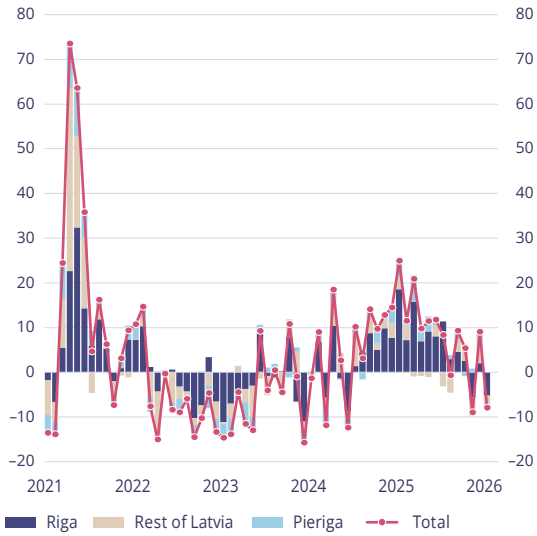
the market is characterised by a gradual adjustment to the increasing demand for energy-efficient and quality facilities, while structural challenges remain in certain segments. Structural changes and shifts in demand towards better quality premises continued in the office space segment, while stable growth and low occupancy rates remained in the industrial and warehouse space segment and the retail space segment developed cautiously.

Housing market

Prepared by Valdis Grudulis

Boosting real household income and declining interest rates contributed to improving housing market activity. In 2025, the activity of house purchase transactions exceeded the previous peak reached in 2021, with a particularly pronounced increase observed in Riga (Chart 1.9), where 51% of all apartment transactions in the country were concluded. In the segment of private houses, the largest activity, as usual, was in Pieriga, where 40% of all transactions involving private houses were registered. Meanwhile, in the rest of Latvia, housing purchase activity grew sluggishly, by only 0.7% year-on-year. Growth in residential loans outpaced overall housing market growth as the role of the banking sector in financing purchase transactions increased (see Box 1.2). However, activity growth was uneven: unlike growth in the housing segment, the number of land acquisitions continued to decline[16].

Chart 1.9
Annual change in the number of housing transactions (%)



Sources: Latvian Open Data Portal and Latvijas Banka's calculations.

Households continued to purchase series-type apartments most frequently[17], which are mostly energy inefficient and require more investment[18]. The new projects segment experienced a steep increase in business activity of 38% year-on-year in 2025, but its share in the overall structure of the market remained relatively low (14%). In the second half of the year, growth in the number of house purchase transactions gradually moderated and activity volumes stabilised at the end-2024 level.

[16] According to the Latvian Open Data Portal's real estate purchase data statistics, the number of land acquisition transactions decreased by 9.4% in 2025 compared to 2024.

[17] According to the Latvian Open Data Portal real estate purchase data statistics, in 2025, series- type apartments accounted for 68% of all apartment purchase transactions.

[18] According to The State Audit Office audit "Unused Opportunities for Housing Insulation", there are more than 39 500 multi-apartment residential buildings in Latvia, and at least 26 600 houses need renovations, but only about 4% of them have been renovated so far.

Box 1.2. The role of banks in financing home purchases

Prepared by Valdis Grudulis

The dominant role in the Latvian housing lending market is played by banks. In addition to these, housing lending services are also offered by non-bank lenders, credit unions, and AS Attīstības finanšu institūcija Altum. According to the Credit Register of Latvijas Banka, in 2025, housing loans were granted by a total of 23 lenders, including 11 banks, which accounted for more than 98% of the total number of transactions (Chart 1.10). In terms of the amount of funding provided, the dominance of banks is even more pronounced, exceeding 99% of the amount of new funding provided. Worth noting is that only non-bank lenders related to banks[19] are included in the Credit Register (two in 2025). Although the Credit Register data do not cover all non-bank lenders, the decisive role of banks in housing lending is clear, as according to the report[20] published by the CRPC, all licensed non-bank lenders issued 177 mortgage-backed loans in the first half of 2025, representing 1.5% of

[19] For a detailed list of Credit Register participants, see: Law on the Credit Register.

[20] CRPC report on the functioning of the consumer (non-bank) lending market in the 1st half of 2025.

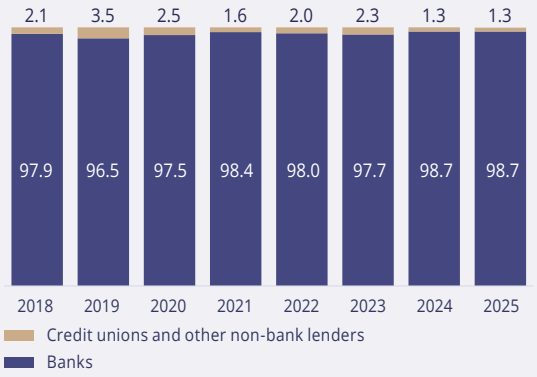
the total number of housing loans granted by banks to Latvian residents during the period in question. At the end of 2025, AS Attīstības finanšu institūcija Altum joined housing lenders, and started lending to promote housing availability in the regions, however, its market share is currently low (0.1 % of the new housing loans granted in 2025).

Among participants in the housing lending market, there are differences in the amount of credit granted between different groups of lenders. In the banking sector, which covers a wide range of financed housing and loans granted for the purchase of housing, from small homes to exclusive private homes, the average amount of loans granted over the last seven years has fluctuated between EUR 40 000 and 50 000 (Chart 1.11). At the same time, the average amount of housing loans granted by non-bank lenders, including credit unions, is significantly lower, suggesting a stronger focus on home renovation or the purchase of cheaper property[21].

Together with lower EURIBOR rates and an increase in housing market activity across the Baltics, the role of banks in financing housing acquisitions is strengthening. In Estonia and Latvia, the role of banks in lending to housing has been markedly smaller than in Lithuania, but the share of bank-financed transactions has increased over the past two years (Chart 1.12). In Latvia, this share exceeded 30% in 2025, the highest level in the last seven years. This shows that bank credit has become an increasingly accessible and widespread tool for meeting people's housing expectations.

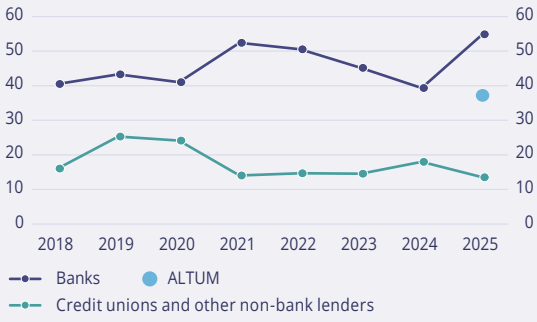
The approaches used in the analysis differ across the Baltic States, as the definitions of housing in the national registers are not harmonised. Moreover, housing lending statistics may include not only housing acquisition transactions but also financing for housing renovation and construction. Latvia's figures are based on the identification of individual transactions, which is ensured by the connection of Latvijas Banka's Credit Register data with the Latvian Open Data Portal's real estate purchase data[22]. In turn, the indicators for Estonia and Lithuania are determined on an aggregated basis. They are calculated by assigning the total number of new housing loans to the housing market activity (total number of transactions) of the respective country and thus indicatively measure the share of bank-financed transactions in total housing market statistics.

Chart 1.10
Number of new housing loans granted by lenders (%)



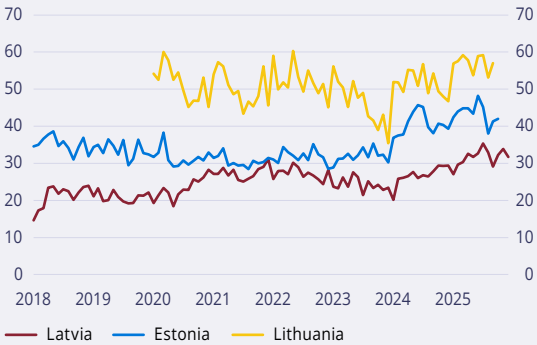
Source: Latvijas Banka (Credit Register data) and its calculations.

Chart 1.11
Average amount of new housing loans granted (thousand euro)



Source: Latvijas Banka (Credit Register data) and its calculations.

Chart 1.12
Share of bank-funded purchase transactions in the housing market (%)



Sources: Latvijas Banka (data from the Credit Register), Eesti Pank, Lietuvos bankas, data on real estate purchases from the Latvian Open Data Portal (housing purchases in Latvia), Land and Spatial Development Board (housing purchases in Estonia), the Centre of Registers (housing purchases in Lithuania).

[21] In recent years, around 8–9% of the number of housing loans granted by credit unions and other non-bank lenders has been used for the purchase of primary residences, mostly outside Riga and Pieriga. The data have been identified by combining Credit Register information and the Latvian Open Data Portal's real estate purchase data.

[22] For more details on the identification of transactions, see: Semjonovs, A., Strazdiņš, J., Siņenko, N., "Through pandemic, cost and interest rate shocks: dynamics of purchases of credited housing", makroekonomika.lv, 18.01.2024.

The gradual recovery in housing market activity contributed to a faster decline in the number of dwellings available for purchase, which exerted upward pressure on prices. After a record high in 2024, the number of listings decreased in 2025 in all market segments. The decline was more pronounced in Riga, where supply fell by 15% on average (Chart 1.13).

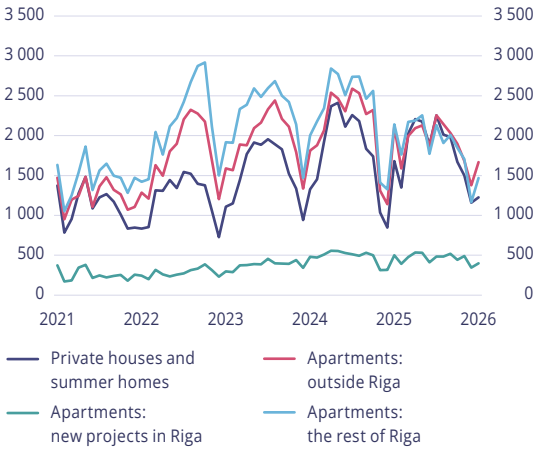
The improvement in household solvency and the stabilisation of interest rates, together with moderate growth in construction costs, contributed to an increase in construction activity in the new housing segment. In 2025, an increase in demand contributed to a decrease in the number of completed new and renovated apartments available for purchase. According to data from SIA Colliers International Advisors, the number of unsold apartments decreased by 22% during 2025. At the same time, as the supply of available apartments declined, the number of apartments under construction increased (Chart 1.14).

The progress made in 2025 in reducing administrative burdens is to be welcomed in promoting the efficiency of the construction sector[23]. The improvements introduced, including the unified exchange of building process data between national information systems[24] and a significantly facilitated framework for large-scale industrial projects and the construction of multi-apartment and private houses[25], are important steps in the arrangement of the sector. However, it should be stressed that these changes are only part of the comprehensive reform plan, and it is important to continue working on the organisation of the construction environment and ensure the full implementation of the plan.

The pace of house price growth remains moderate overall, although it increased gradually over the past year. In 2025, the CSB's house price index increased by 7.7% year-on-year. The acceleration in price growth towards the end of the year[26] was mainly driven by price increases in the existing housing segment, while in the new housing market price increases were more moderate (Chart 1.15). House price increases were largely driven by a decline in supply and an increase in market activity in 2025. At the same time, the moderation in the growth rate of housing market activity suggests that risks of house prices overheating have not increased. The housing market is considered to be resilient, with no rapid price adjustment expected. Even if these risks materialised, sustained wage growth and historically low household indebtedness would help mitigate them.

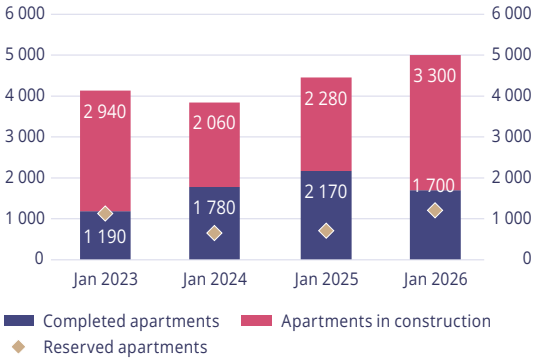
House price growth is gradually approaching wage growth, which limits further improvements in housing affordability. In 2025, housing affordability returned to levels observed before the sharp increase in interest rates (Chart 1.16). However, the improvement in housing

Chart 1.13
Number of apartment and private house sales listings



Sources: advertisement portals (ss.com, until 2022 also city24.lv and inch.lv) and Latvijas Banka's calculations.

Chart 1.14
Number of new apartments completed and under construction in Riga and Pieriga



Sources: SIA Colliers International Advisors housing market annual reports for 2025, 2024, 2023, and 2022.

[23] Information report "On the Action Plan for Reducing Administrative Burdens in the Field of Real Estate Development".
[24] Automatic transfer of data between the Construction Information System, the Cadastre Information System, and the Land Register to eliminate the need for separate cadastral surveying.
[25] As of 2025, the possibility has been introduced to put objects into operation in rounds and to start the preparation of the construction site in parallel with the design, while as of 2026, in the construction of private houses up to 200 m^2, the decisions of the building authority have been replaced by an explanatory memorandum.
[26] Compared to the 4th quarter of 2024, the CSB house price index increased by 11% in Q4 2025.

affordability came to a halt at the end of 2025, as interest rates stabilised and house prices continued to rise. As this trend continues, a large part of household housing purchases will continue to be concentrated in the segment of standard-type apartments. Although this segment offers more affordable solutions, it often implies a lower energy efficiency class and the risks associated with an outdated housing stock.

The rental market for apartments remains broadly stable and rent growth in this segment lags only slightly behind the growth rate of house prices[27]. In Latvia, the rental market still accounts for a small share of the total housing stock[28]. Listing platform data show that in 2025, housing supply remained stable[29], with a seasonal rise in autumn driven by student activity.

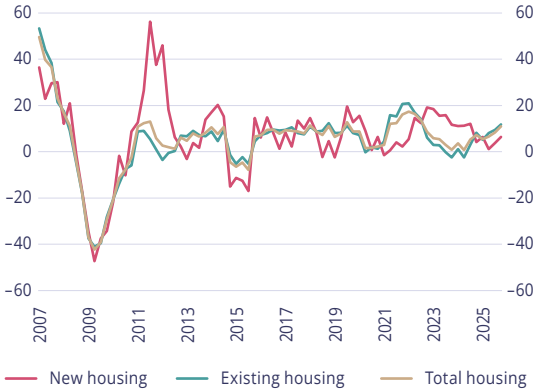
Commercial real estate market

Prepared by Jekaterina Petkeviča

Investment activity in the Latvian commercial real estate market recovered in 2025 and the market gradually started to stabilise. This was facilitated by better access to finance, the stabilisation of interest rates and inflation, as well as the adjustment of investors to the **increasing demand for energy-efficient and quality facilities.** According to the data of SIA Colliers International Advisors, the total amount of investments in the commercial property market in Latvia reached to approximately EUR 316 million, a significant increase compared to 2024, when the market activity was at its lowest in the previous 10-year period. Similar to 2024, in 2025, the Latvian commercial property market was dominated by local capital, with Baltic investors providing the largest share of the deal volume, reaching more than 90% of the total investment volume. Foreign investor activity remained subdued as they preferred larger and more liquid markets.

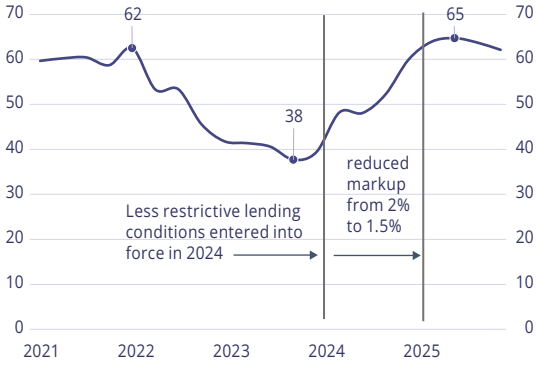
By segment, activity increased in the industrial and warehouse space segments, while the retail space segment continued to provide the largest volume and number of transactions. In the office space segment, investment remained low due to the mismatch between supply and investor requirements: the supply of high-quality

Chart 1.15
Annual changes in house prices (%)



Sources: CSB and Latvijas Banka's calculations.

Chart 1.16
Maximum apartment area in Riga which the average wage recipient can purchase in a new dwelling with bank co-financing (m^2)



Assumptions: schedule of equal payments, 30-year maturity, 15% contribution, interest rate 2.0% (1.5% as of December 2024) + current 6-month EURIBOR.

Sources: CSB, ECB, SIA ARCO REAL ESTATE, and Latvijas Banka's calculations.

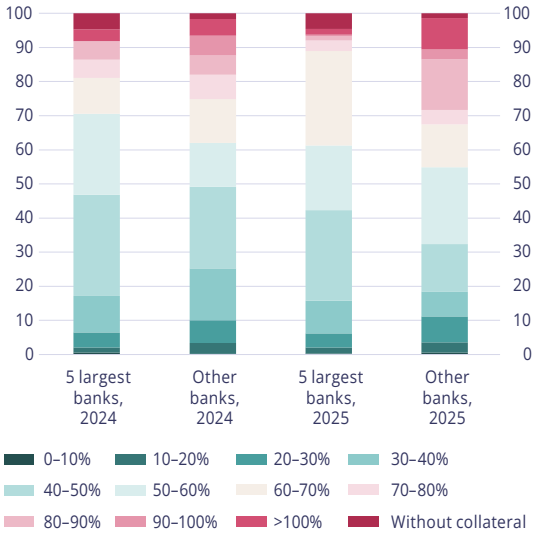
Class A office space is limited, while lower-quality office space often does not meet investors' requirements in terms of quality and energy efficiency. Investment is likely to remain close to its long-term average in 2026, pointing to further market stabilisation. **More rapid growth in commercial property market activity will be constrained by external risks, including uncertainty regarding global economic developments.**

As financing costs stabilised, upward pressure on commercial real estate yields eased in 2025. However, **market data do not yet show a significant decline in yields.** This reflects investor prudence and continued subdued business activity. The gradual decline in yields is constrained both by high uncertainty in the external environment and by structural factors in the commercial real estate market. At the same time, given

[27] According to pricebanka.lv, the annual rent increase in Riga (December 2025) was 8% for apartments in new projects and 9% for standard-type apartments.
[28] According to Eurostat's publication "Housing in Europe – 2025 edition", the share of tenants in Latvia was 16.3% in 2024.
[29] Web scraping data collected by Latvijas Banka from ad platforms ss.com and city24.lv.

the increasingly cautious investor approach and the dominant role of local capital, **no significant increase in the value of commercial properties is expected in the near term as well.** Accordingly, the increase in commercial property prices is likely to be moderate and depends mainly on the evolution of rent. The market value of pledged commercial property objects significantly exceeds the outstanding amount of the corresponding loans. **The ratio of loans to the real estate sector to the value of collateral increased slightly to 49.4% with the increase in lending**[30]**.** Approximately two-thirds of the RE sector's loan portfolio consists of loans with a loan-to-value ratio not exceeding 60% (Chart 1.17).

Chart 1.17
LTV breakdown of the five largest banks and other banks' domestic NFCs for the real estate sector at the end of 2024 and 2025 (%)



Sources: Latvijas Banka (Credit Register data) and its calculations.

Risks of insolvency of the RE sector in general continue to decrease as the profitability of companies in the sector improves and interest rates have fallen. Despite a possible deterioration in payment discipline, risks have not materialised and there is currently no increase in forced sales or a significant increase in the share of distressed loans in the commercial property market (NPLs of 2.1% at the end of 2025)[31]. This shows that the **payment discipline of borrowers** in the RE sector **remains generally good and that companies in the commercial property sector have overcome the lower end of the RE cycle.**

Corporate ability to refinance commercial property loans is gradually improving. This is supported by lower interest rates, stable property values, improved solvency, and higher bank lending activity.

The activity of the RE investment funds remained moderate in 2025 and was provided by funds from the Baltic States[32]. Sales of commercial property may be subject to a discount to market value, especially in times of market uncertainty. However, given that these Baltic funds are mostly closed-ended, the **redemption risk, or the risk that the fund manager will not be able to meet investors' requests to sell units in a timely manner, is significantly limited.**

The development of commercial property market segments continues to be affected by several structural risks, including high construction costs and rising labour wages, but these are not the only determinants of development. According to the evaluation by SIA Colliers International Advisors, at the current cost level, the implementation of new projects is often economically difficult, because the rental fee necessary to ensure the return on investment is not always competitive in the market. Not only in the office space and industrial and warehouse space segments, but now also in the retail space segment, there is a **growing demand for smaller, energy-efficient and environmentally friendly areas.** The move of tenants to newer and higher quality premises contributes to structural changes in the market. This leads to fluctuations in space occupancy rates and increases the downward impact on rents in less energy efficient premises.

In 2025, the office space segment continued to adapt to changes in demand, characterised by a shift of tenants towards more high-quality and energy-efficient premises. The growing importance of environmental, social, and governance (ESG) requirements continues to influence market developments, strengthening the competitiveness of Class A offices while increasing risks for lower quality facilities requiring additional investment. The market continues to show a mismatch between supply and demand, and the move of tenants to newer offices contributes to the structural polarisation of the market, impacting occupancy rates. The mismatch between market demand and supply is mitigated by the commissioning of new

[30] 46.87% at the end of 2024.
[31] NPLs of 1.8% at the end of 2024.
[32] For example, in 2025, one of the largest local funds, INDEXO REAL ESTATE FUND AS, carried out about one tenth of the total volume of transactions in the Baltics, actively participating in significant commercial property transactions.

Class A offices. At the same time, the increase in supply in the segment may increase the share of unoccupied premises of these offices in the short term, as it takes time to attract new tenants. **In the Class B office space segment, the occupancy rate remains higher and competition between owners is increasing**, with rent conditions being adjusted more frequently. In the Class B office space segment, insolvency risks are increasing, but the exposure of banks in this segment is limited, mitigating the impact on financial stability.

Activity in the industrial and warehouse space segment in Latvia remained high in 2025, stimulated by sustained demand for logistics and storage facilities. Demand focused mainly on modern and energy-efficient premises[33] which meet the increasing requirements of tenants in terms of quality and operating costs. In response to the growing interest in multifunctional office and warehouse buildings combining store, office, and warehouse functions in one site, a greater number of such spaces are entering the market, increasing the vacant space in the existing commercial space pool. However, the overall vacancy rate remains low, with the new premises being gradually filled, indicating high demand.

The retail premises segment in Latvia developed unevenly in 2025, reflecting both a slow recovery in consumption and caution regarding the implementation of new projects and the expansion of sales areas. In the largest and strategically located shopping centres, space occupancy rates remained high, while in less attractive locations there was less interest in premises. Regional markets outside Riga are playing an increasingly important role, as retailers are expanding their presence in search of strategically beneficial locations beyond the saturated segments of large cities. Lease fees remained broadly unchanged, although in some cases they were influenced by competition and the tenants' cost sensitivity.

The hotel space segment continued its gradual recovery in 2025, reflected in an increase in hotel room occupancy and the number of guests served. However, activity in the sector is still lagging behind pre-pandemic levels, pointing to an incomplete recovery.

[33] Including new buildings with a high energy efficiency class and meeting certified sustainability standards.

Financial vulnerability of borrowers

As household income growth outpaces inflation, the financial situation of households continues to strengthen. Household debt has increased, but the overall debt payment burden – the ratio of debt payments to both household disposable income and GDP – declined slightly in 2025, in line with a gradual decline in interest rates. The possible increase in EURIBOR may lead to an increase in the debt burden in the future, but its impact on the economy and financial stability is constrained by the still low level of household indebtedness. The repayment discipline remains very good.

While NFCs' financial position and debt servicing capacity are improving, their further development is constrained by the uncertainty of the external environment. The increase in energy and labour costs, as well as the increase in the EURIBOR priced in by financial markets, will put downward pressure on NFCs' profitability and debt service capacity.

Household solvency

Prepared by Valdis Grudulis

The financial situation of households is broadly resilient. This is ensured by an increase in real income. Although the growth rate of the average wage is slowing, it continues to outpace the rise in consumer prices, contributing to the strengthening of the real purchasing power of the population. According to Latvijas Banka's December 2025 forecasts, the growth rate of income will also outpace inflation in 2027 and 2028.

Household solvency risks were limited by the decline in MFI interest rates in 2025. This was due to both the pass-through of reduced EURIBOR rates and the eased re-financing, which intesified competition between MFIs and led to more favourable conditions for housing borrowers[34]. The average markup on newly-issued mortgage loans stabilised at around 1.6 percentage points (Chart 1.18), while financial market forecasts expect interest rates to rise in 2026, e.g. with the 6-month EURIBOR rising from 2.5% to 2.9%. This will put upward pressure on the burden of credit payments in the future.

[34] Between the beginning of 2025 and February 2026, markups set in loan agreements have been reduced for around 12 000 mortgage loan agreements, representing almost 19% of the total mortgage loan portfolio at the beginning of 2025.

The growth in household deposits held by MFIs and the persistently low share of NPLs in the household loan portfolio indicate that borrowers are able to absorb potential economic shocks and indicate that borrowers' solvency remains generally sound (see the Section "Credit risk").

As household debt continued its steady upward trend[35]**, the debt servicing burden decreased.** Total interest expenditure increased slightly further in 2025. This was facilitated by loans granted by non-banks. At the same time, interest payments on loans granted by MFIs and leasing companies declined. However, the debt burden – the ratio of total debt service expenditure to household disposable income as well as to GDP – declined. The resilience of household solvency remains high overall, and the historically low level of indebtedness limits the potential negative impact on economic stability.

Households' payment discipline remains very good. This is evidenced by the persistently narrow spread between calculated and recognised interest payments on loans (Chart 1.19). Income growth continues to strengthen the solvency of the entire population.

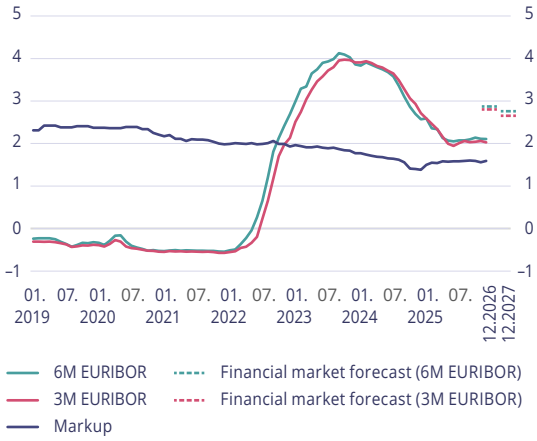
NFC solvency

Prepared by Jekaterina Petkeviča

In 2025, with a rebound in economic growth, the financial situation of NFCs improved significantly, and their debt servicing capacity is sound. Household consumption started to grow gradually, and growth rebounded in a number of sectors. However, **the development of NFCs is significantly constrained by the high uncertainty of the external environment.** Moreover, **labour costs and energy prices are expected to increase further, putting further downward pressure on companies' profitability.**

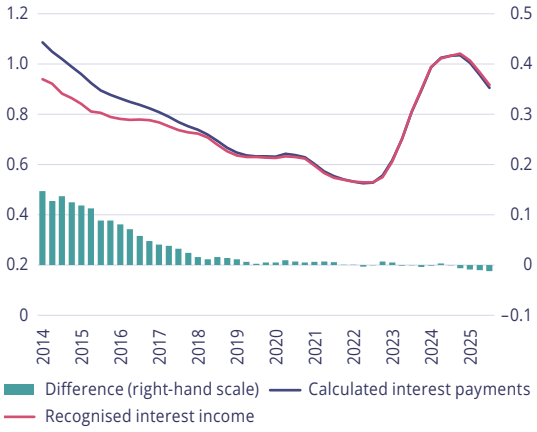
The overall turnover of NFCs increased by 5.8% in 2025, reflecting a rise in turnover in most sectors, with the exception of transportation and storage (Chart 1.20). In nominal terms, the trade, construction, and manufacturing sectors contributed the most to the increase in turnover. Transport activity gradually increased in 2025, but the sluggish recovery in cross-border trade

Chart 1.18
Evolution and forecasts of interest rates on newly issued mortgage loans (%)



Sources: Latvijas Banka and Chatham Financial forecast as of 30.03.2026.

Chart 1.19
Household interest payments to MFIs and the difference between the calculated and recognised interest payments (relative to GDP, %)



Source: Latvijas Banka.

activity[36] was not able to compensate for the drop in turnover in the air transport and transit as well as transport-serving sub-sectors (–5.7%). Growth in the construction sector recovered significantly (+13.6%), especially in the civil engineering segment, largely driven by the implementation of infrastructure projects in road construction and urban development. On the other hand, previous large-scale investment in manufacturing contributed to an increase in turnover in this sector (+6.4%).

Despite the adverse weather conditions and the related drop in the turnover of the grain sub-sector (–10.2%), the

[35] In December 2025, the household loan portfolio for banks was 10.5%, for leasing companies 4.4%, and for other non-bank lenders 21.6%, higher than the previous year.

[36] In 2025, the turnover of freight transport by road and related sub-sectors increased by 3.7%.

total turnover of the agriculture, forestry, and fishing sector in 2025 remained at the level of the previous year. However, **insolvency risks increased in the sector, especially in the agricultural segment. In 2025, the sector suffered from adverse meteorological conditions, which weakened the financial resilience of NFCs. It is expected to decline further,** reflecting the depletion of financial resources accumulated in previous years, high production costs, and rising fertiliser prices, driven by the ongoing war in the Middle East.

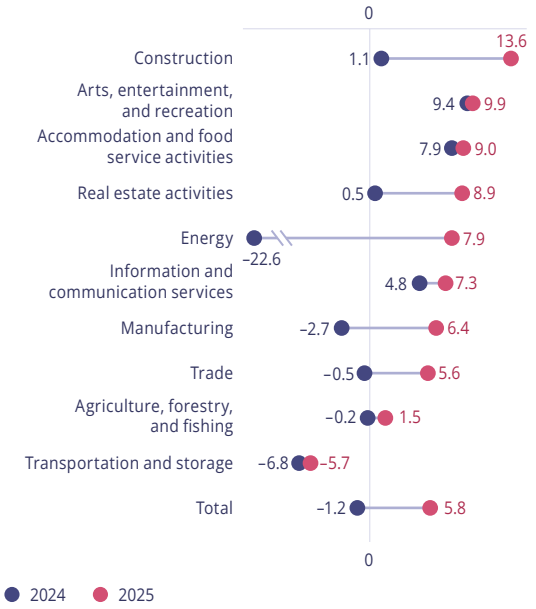
The overall profitability (profit-to-turnover ratio) of NFCs increased moderately in 2025 (by 0.2 percentage points; see Chart 1.21). However, the improvement in profitability was uneven and concentrated in certain sectors: agriculture, forestry, and fishing, construction, transportation and storage, and real estate activities. The improvement in the profitability of these sectors can also be seen without taking into account lower interest expenditure due to lower EURIBOR rates. At the same time, the most significant drop in profitability was observed in the energy sector (–3.6 percentage points) and in the arts, entertainment, and recreation sector (–3.2 percentage points). The decrease in profitability in the energy sector was mainly due to the drop in the sales price of electricity compared to the previous year, but the level of profitability remained close to pre-pandemic values. **Moving forward, rising labour costs and energy prices may have a negative impact on profitability. Additional pressure comes from external factors, including geopolitical tensions and high uncertainty, as well as disruptions in logistics chains.**

At the end of 2025, NFCs' capital remained over-indebted despite the recovery in lending activity (see the Section "Lending development") and the debt-to-equity ratio reached 0.98. Earlier accumulated capital and higher profitability contributed to the reduction of the debt burden. The total indebtedness of NFCs amounts to 53.2% of GDP, including debt to credit institutions and related leasing companies at 17.8% of GDP[37].

Total interest payments by NFCs decreased in 2025, in line with the decline in EURIBOR, despite the acceleration in lending and the increase in liabilities (Chart 1.22). **Debt servicing capacity improved**, with earnings before interest and taxes being 7.4 times higher than interest payments, compared

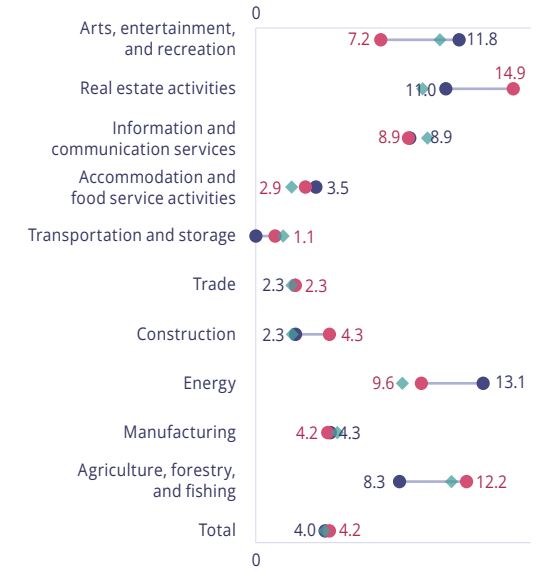
[37] In 2024 – 47.1% and 16.6% of GDP respectively.

Chart 1.20
Annual changes in NFC turnover (%)



Source: CSB.

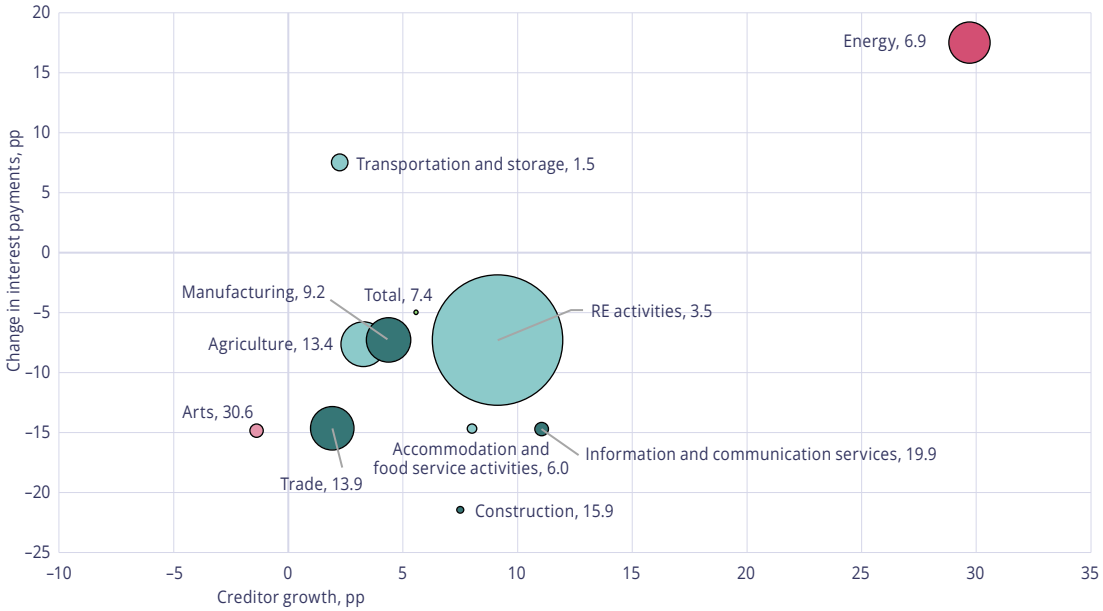
Chart 1.21
NFC profitability* (%)



* The ratio of pre-tax profit to turnover in the respective sector and period.

Source: CSB.

Chart 1.22
Changes in the interest payment burden* of NFCs in 2025, depending on changes in debt (horizontal scale) and interest payments (vertical scale). The size of the circle reflects the share of the sector in the total NFC loan portfolio of credit institutions in 2025. The colour of the circle describes the change in the percentage coverage ratio: red – negative change, light green – increase to 1 percentage point, green – increase above 1 percentage point. By industry name – percentage coverage rate in 2025



* Profit before tax and interest payments in relation to interest payments in the sector concerned.
Source: CSB.

with 6.4 times higher the previous year. The lowest debt service ratio remained in the transportation and storage sector (1.52 times). Also in the energy sector, the fall in profitability and the sizeable investment programme, including debt-financed ones, led to a slight deterioration, but remained relatively high at 6.87 times. In a number of sectors, the interest coverage ratio is improving, and debt service capacity is at a sufficient level. **In 2026, the debt service burden, conditional on stable EURIBOR rates, is expected to be moderate and manageable.**

Business demographic indicators point to a cautious increase in business activity. In 2025, the number of newly registered companies reached pre-pandemic levels[38]. On the other hand, the number of the number of insolvency cases initiated insolvency cases of legal persons decreased by 7% and was below its pre-pandemic level. Historically, the number of liquidated companies significantly exceeded the number of insolvency cases opened. This is partly explained by the choice of companies to use insolvency proceedings less frequently, as the associated costs often exceed the potential recoverable value, especially for smaller creditors. Instead, companies more often agree with creditors on the resolution of liabilities and opt for self-liquidation. **High external uncertainty constrains business activity and the pace of new business formation is unlikely to pick up.**

[38] In 2025, compared to 2024, 12% more new NFCs were registered and 16% less NFCs were liquidated.

2. Credit institution sector development and risks

Lending development

Lower interest rates, a better financial situation for borrowers, and a stronger incentive for banks to lend significantly boosted domestic lending. As this increase took place from a very low base, the bank-to-GDP ratio remains low after a prolonged period of weak lending. Geopolitical shocks and uncertainty could significantly limit further growth in the loan portfolio.

The development of non-bank lending was strongly supported by the state support programme for the purchase of electric cars and new externally chargeable hybrid cars. Such public support is expected to continue and thus contribute to the further growth of the household leasing portfolio. At the same time, the amount of loans granted to households by other non-bank financial sector participants, with the exception of leasing companies, is also growing rapidly.

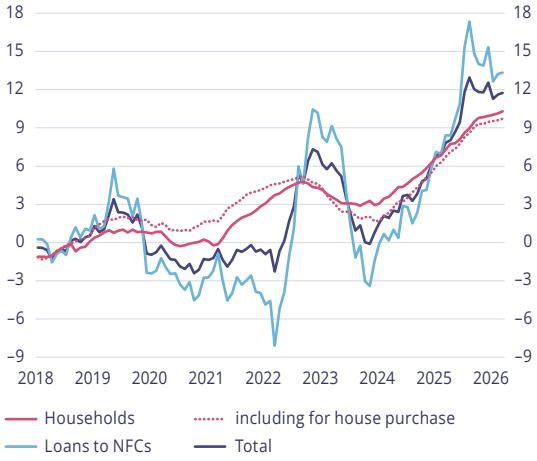
Lending by credit institutions

Prepared by Andrejs Kurbatskis

Domestic lending has increased rapidly, but after a long period of weak lending, the bank loan-to-GDP ratio, credit-to-GDP ratio remains generally low. In addition, the increase was driven by factors whose effect will not be permanent. Lending activity was facilitated both by lower interest rates and the realisation of deferred demand, as well as by the possibility laid down in the Solidarity Contribution Law for a credit institution to receive a contribution rebate if its lending increase reaches or exceeds the specified threshold. In March 2026, the annual growth rate of loans to domestic NFCs and households was 11.8%[39], compared with 7.8% in March 2025 (Chart 2.1).

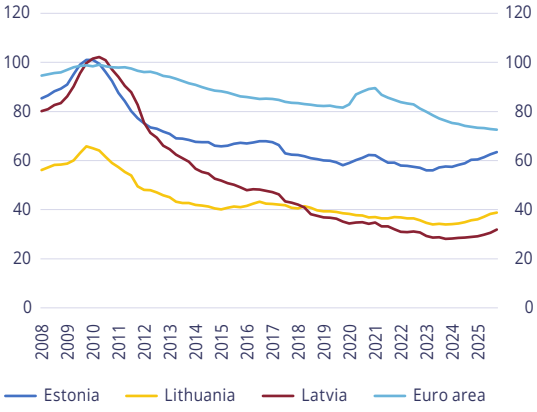
After a sustained contraction, the loan-to-GDP ratio increased, but remains at low levels. The balance of loans to NFCs and households to GDP ratio stood at only 32% at the end of 2025. The ratio of loans to GDP rose similarly across the Baltic States in 2025 (Chart 2.2)

Chart 2.1
Annual rate of change in balance of loans to domestic NFCs and households by credit institutions (%)



Source: Latvijas Banka (MBP data) and its calculations.

Chart 2.2
Balance of loans to domestic NFCs and households to GDP ratio (%)



Sources: ECB, Eurostat, Latvijas Banka (MBP data) and its calculations.

The annual growth of balance of loans to NFCs was 13.3% in March this year, compared to 8.4% in March 2025.

The main driver of the growth in balance of loans to NFCs is long-term loans (Chart 2.3), which are usually granted to finance investment projects. The growth of this loan portfolio could be more resilient than the previous activation of lending to NFCs at the end of

[39] For the purposes of comparison, the one-off effects associated with the structural changes in the banking sector and the sectoral reclassification have been excluded from the Sections "Lending development" and "Credit risk" (including Charts 2.1, 2.3–2.4, 2.6, 2.13–2.16).

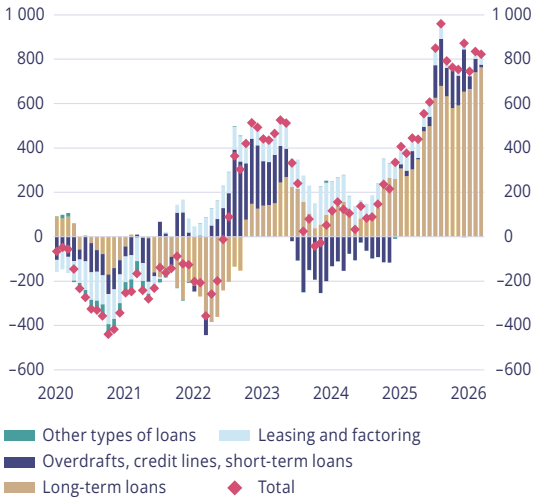
2022–beginning of 2023, as short-term loans that were repaid in the course of the year made a significant contribution at that time. Underinvestment is a structural problem for the Latvian economy, and the long-term activation of lending, which contributed significantly to investment growth in 2025, was long-awaited. The growth of lending to NFCs was supported by both supply and demand factors. On the one hand, previously postponed corporate demand for investment began to materialise as interest rates declined. On the other hand, banks also became less conservative, driven by the incentives provided by the Solidarity Contribution Law. The growth of the balance of long-term loans to NFCs is fairly diversified across sectors, with the largest positive contribution coming from the real estate sector and the manufacturing industry.

Currently, strong lending growth to NFCs is taking place both in large foreign capital banks and in medium- and small-sized banks, most of which are domestic capital banks. The growth rate of lending in medium- and small-sized banks remains very high. Lending to NFCs, especially the five largest banks, was facilitated by the possibility for credit institutions to receive a discount from 2025 onwards, as set out in the Solidarity Contribution Law, when meeting certain loan portfolio growth targets. In these major banks, lending picked up significantly in 2025 (Chart 2.4). While there were periods of strong growth in the past (e.g. between end-2022 and beginning-2023), lending at that time was temporarily supported by higher corporate demand for short-term financing to provide working capital due to rising energy and commodity prices. Econometric model assessments also point to a positive impact of the provisions of the Solidarity Contribution Law on lending activity[40].

While the loan portfolio of medium and small-sized banks still accounts for a small share of the total loan portfolio of domestic NFCs in the banking sector (21% in March 2026), lending growth in these banks remains robust. Active lending policies of medium and small banks ensure access to finance for a wider range of companies. This is positive from the point of view of economic development, but the rapid growth of the loan portfolio for a few consecutive years, especially in the current context of high uncertainty related to the war in the Middle East, increases the vulnerability of these banks to adverse scenarios.

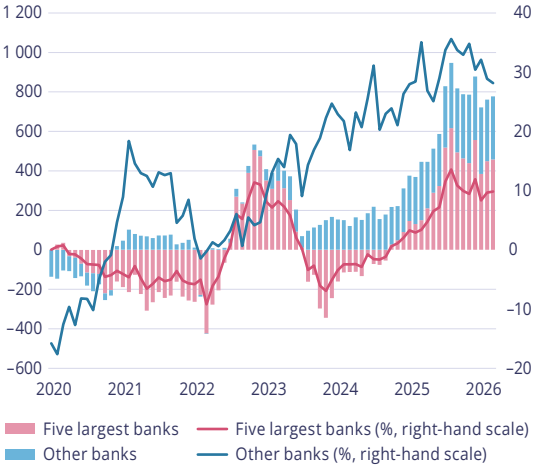
[40] For more details, see Box 1 of the Macroeconomic Projections Report of December 2025.

Chart 2.3
Annual changes in the loan portfolio of domestic NFCs of credit institutions and related leasing companies (million euro)



Source: Latvijas Banka (Credit Register data) and its calculations.

Chart 2.4
Annual changes in balance of credit institution loans to domestic NFCs in the five banks with the largest domestic NFC loan portfolio and in other banks (million euro)



Source: Latvijas Banka (MBP data) and its calculations.

A marked upward trend in corporate lending can also be observed outside the banking sector. This also demonstrates a higher demand for long-term loans to finance investment activity. The balance of loans to NFCs by international organisations[41] increased sharply in 2025. The balance of loans granted to NFCs by the state AS Attīstības finanšu institūcija Altum has also increased significantly since 2024 (Chart 2.5), and this growth has also been driven by long-term loans.

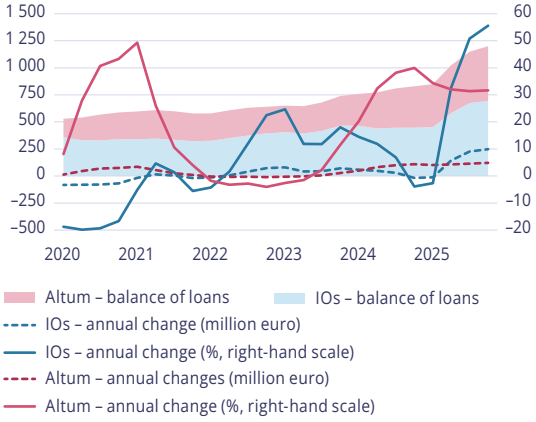
[41] International organisations such as the European Investment Bank, the Council of Europe Development Bank, the European Bank for Reconstruction and Development, the Nordic Investment Bank.

Growth in lending to households accelerated, largely as a result of stronger dynamics in housing loans (Chart 2.6). **Deferred demand for housing loans continued to materialise as interest rates declined, including as a result of greater competition among banks.** The annual growth rate of domestic loans to households reached 10.3% in March (including 9.7% for housing loans and 13.0% for consumer and other loans). This compares to 7.3% (6.7% and 10.1%) in March 2025.

Housing lending was supported by a sustained improvement in household solvency and by a sizeable stock of liquid financial assets, including the historically highest level of deposits, which continues to grow rapidly (see the Section "Funding and liquidity risk" for more details). The largest share of new housing loans is still issued in Riga and Pieriga. Although mortgage lending in regions has developed faster in the second half of 2025 than in Riga and Pieriga, this is an increase from a very low base.

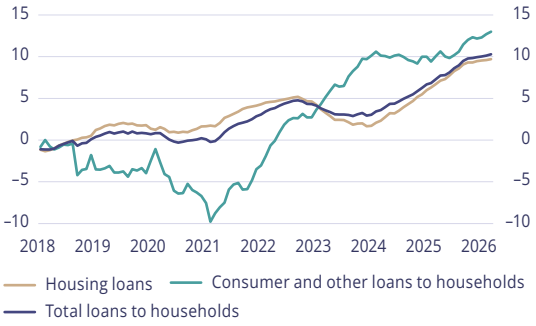
Although the increase in the volume of new residential loans was mainly driven by relatively large loans with a volume of more than EUR 100 000, the average volume of mortgage loans is growing moderately and is not yet considered high. The increase in the average volume of mortgage loans was influenced both by the changes in the structure of transactions and the increase in the prices of RE. Although most of the new loans are still issued for the purchase of standard-type apartments, it is positive that loans for the purchase of property in energy-efficient new projects were issued significantly more often. The average amount of mortgage loans also rose due to a higher amount of financing for the purchase of housing in historical properties in the centre of Riga, the prices of which are significantly higher than those of standard-type apartments. The role of small housing loans, on the other hand, declined sharply, so that the average amount of housing loans also increased significantly (Chart 2.7). In the past, housing loans without mortgage collateral and with a loan volume of up to EUR 20 000–30 000 were actively granted. Given that there were fewer opportunities to buy property during the period of high interest rates, households were more likely to use these small housing loans for renovations.

Chart 2.5
Balance of loans by international organisations (IOs) and the state AS Attīstības finanšu institūcija Altum to domestic NFCs and its annual changes (million euro; %)



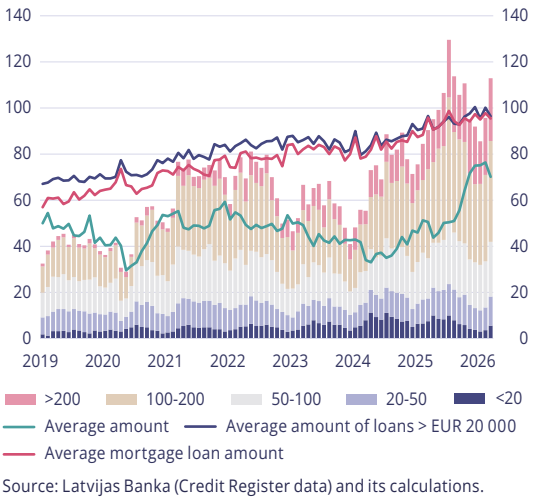
Source: Latvijas Banka (international investment balance sheets, Credit Register data) and its calculations.

Chart 2.6
Annual rate of change in balance of loans to domestic NFCs by credit institutions (%)



Source: Latvijas Banka (MBP data) and its calculations.

Chart 2.7
New loans issued by credit institutions for house purchase by amount (million euro) **and the average loan amount** (thousand euro)



Source: Latvijas Banka (Credit Register data) and its calculations.

A significant proportion of new housing loans is still issued with a state guarantee. In 2025 and the first three months of 2026, the share of these loans exceeded 40% each quarter. The share of these loans in the housing loan balance also continues to increase, approaching 40%. Against this background, the issue of improving public policies to better target state aid remains relevant. Above all, it would be important to avoid inefficient use of programme funds, as some borrowers apply to the programme only because the stamp duty for registering property in the Land Register is lower in such a case. In order to reduce this incentive, Latvijas Banka proposes to set a lower (0.5%) stamp duty for the registration of property rights in the Land Register, at least for all families with children (currently such a reduced stamp duty is set only for families of at least three children).

Although the balance of consumer and other (non-housing) loans to households continues to increase significantly (Chart 2.6), **the share of these loans in the total household loan portfolio remains relatively small** (19% in March 2026). The increase in the balance of consumption and other loans could still largely be explained by a more active provision of these credits for energy efficiency solutions, home improvement, as well as for the self-employed: the volume and number of relatively large new loans exceeding EUR 10 000 has grown much more significantly.

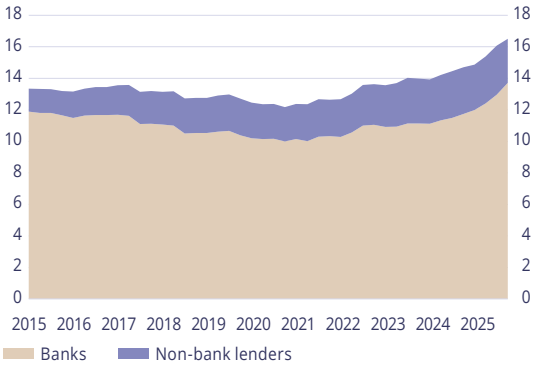
The domestic loan portfolio could continue to increase in 2026, but the growth rate is likely to slow down. The development of lending will be constrained by geopolitical shocks, which could increase the prices of resources and limit their availability, increase interest rates, burden borrowers' financial situation, and consequently make both banks and borrowers more conservative. In the NFC sector, lending could be facilitated by large loan agreements that had already been concluded but under which little or no funding had been disbursed by March.

Lending by the non-bank financial sector

Prepared by Kārlis Ločmelis

The lending market for leasing underwent structural changes in 2025. The main change occurred at the end of 2025, when SIA SEB līzings was added to AS SEB banka[42]. As a result, the share of loans granted by non-bank lenders to domestic NFCs and households in the total loan portfolio of domestic NFCs and households by banks and non-bank lenders decreased significantly (Chart 2.8)[43].

Chart 2.8
Balance of loans granted by banks and non-bank lenders to domestic NFCs and households (billion euro)



Source: Latvijas Banka (MBP, 1-fp quarterly report), CSB.

Non-bank lending was strongly supported by household activity. In 2025, households continued to purchase passenger cars with leasing financing, as well as continued to rapidly increase their borrowing for consumption. On the other hand, interest in new commitments was more cautious in the NFC sector, despite the fact that EURIBOR rates continued to decline in early 2025.

The total loan portfolio of credit institutions and non-bank domestic NFCs and households grew by 12.0% in 2025.

The balance of loans to domestic NFCs from bank-linked leasing companies grew by 4.2% in 2025 (by 3.7% in 2024). Demand in the sectors dominated by the leasing portfolio was uneven: it was strong in construction and real estate activities, but weak in agriculture, forestry, and fishing as well as transportation and storage.

The balance of loans to domestic households by bank-linked leasing companies increased strongly in 2025 and was 23.3% higher than in the previous year. The substantial increase in demand was stimulated by state aid for the purchase of electric cars and new externally chargeable plug-in cars, with a total financing of

[42] "SEB Leasing to be added to SEB banka", AS SEB banka, 02.10.2025.

[43] In this section, lending growth rates are calculated by excluding, to the extent possible, the impact of one-off structural factors.

EUR 30 million[44]. A further increase in the balance of loans granted to households by leasing companies is also expected, as the Ministry of Climate and Energy has submitted, and the government has approved, a new draft support programme for the purchase of environmentally friendly cars for residents with a total financing of EUR 40 million.

Loans to households from other non-bank financial sector companies, which are not leasing companies, continue to grow rapidly and their growth rate increased by 21.6% in 2025 (by 12.9% in 2024), with loans amounting to EUR 822 million at the end of 2025 (Chart 2.9). Interest rates on non-bank consumption loans (excluding finance leases) are high (Charts 2.10 to 2.12), which, as leverage increases, will put additional pressure on household finances as well as constrain household consumption in the future.

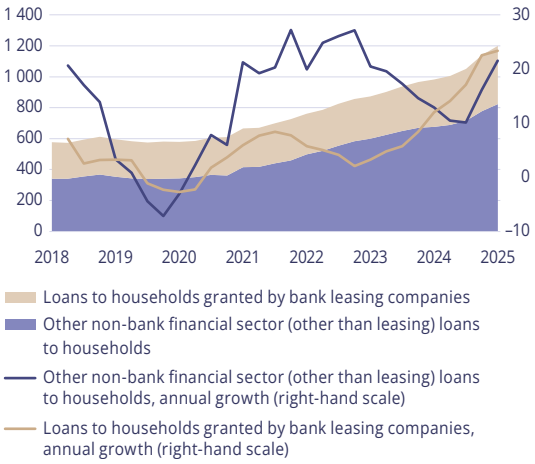
Credit risk

Prepared by Andrejs Kurbatskis

The war in the Middle East worsens the future credit risk assessment of the banking sector. In the corporate sector, credit quality deteriorated somewhat already towards the end of 2025, mainly as a result of the materialisation of the risk of deterioration in the quality of forborne loans identified in the previous Financial Stability Report. Accordingly, the amount of loan loss provisions made by banks also increased. Continued bank profitability and high capitalisation make the banking sector resilient to a possible deterioration in the quality of the loan portfolio.

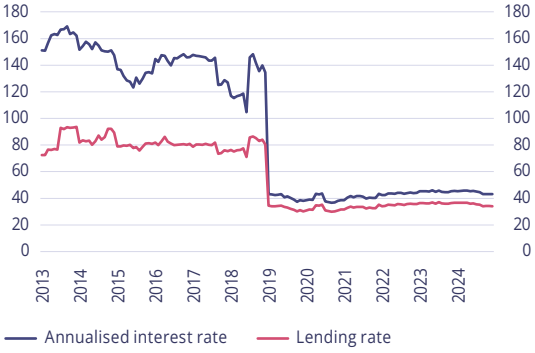
The NPLs and their share increased slightly from historically low levels (Chart 2.13). The share of NPLs in the total loan portfolio reached 2.7%[45] in March 2026, compared to 2.5% in March 2025. With long-term credit arrears remaining relatively stable[46], the growth of unlikely-to-pay loans and their share was limited to the domestic NFC sector. The increase in NPLs was

Chart 2.9
Balance (million euro) **and annual growth rate** (%) **of loans (excluding finance leases) granted to households by leasing companies and other non-bank financial sector companies**



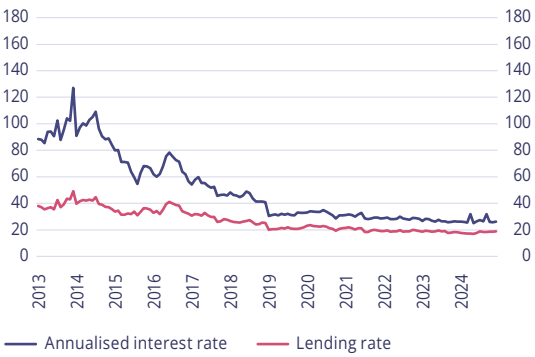
Source: Latvijas Banka (1-fp quarterly report).

Chart 2.10
Non-bank lenders, except finance leases: annualised interest rate and lending rate of distance loan contracts with a loan repayment schedule and/or credit line



Sources: Latvijas Banka (MFI interest rate statistics data) and CRPC.

Chart 2.11
Non-bank lenders, except finance leases: annualised interest rate and lending rate of consumer loan contracts with a loan repayment schedule and/or credit line



Sources: Latvijas Banka (MFI interest rate statistics data) and CRPC.

[44] Cabinet Regulation No 896 of 21 December 2021 "By-laws of the Open Tender "Reduction of Greenhouse Gas Emissions in the Transport Sector – Support for the Purchase of Zero- and Low-emission Vehicles" for projects financed by the Emission Allowance Auction Instrument".

[45] This section analyses the most operational credit quality data, which are non-consolidated data.

[46] Their balance increased marginally, while their share declined marginally as a result of a significant increase in the total loan portfolio.

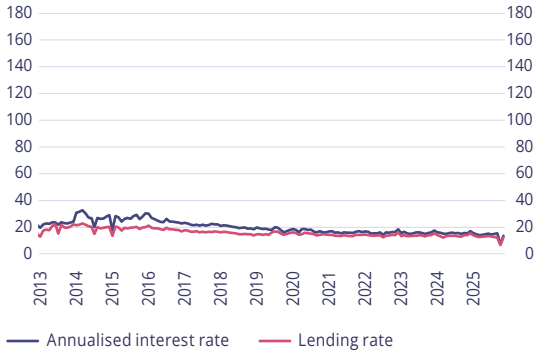
also followed by a corresponding increase in provisions, as well as the creation of additional provisions for existing NPLs. The balance of Stage 2 loans[47], on the other hand, has not changed significantly overall since March 2025, but the share of these loans in the total loan portfolio has slightly decreased, with the total loan balance increasing.

The increase in NPLs is mainly due to loans that had previously been forborne. Despite this, the overall share of NPLs and forborne loans other than NPLs continues to decline (Chart 2.14). In the previous Financial Stability Reports, we drew attention to the high share of forborne loans in the NFC sector as a potential source of risk. At the end of 2025, this risk materialised for a number of borrowers with relatively high outstanding liabilities, who were already granted relief a few years prior due to financial difficulties. The current balance of forborne loans is small (Charts 2.14 and 2.15), and therefore no longer poses significant additional risks in the future.

Provisions for NPLs and their ratio to balance of these loans increased at the end of 2025 (Chart 2.14), but this is largely explained by the one-off transaction of AS Rietumu Banka. In this transaction, provisions were made for loans related to Russia[48], which had had a long standing NPL status and had already been subject to a significant capital adjustment in previous years[49].

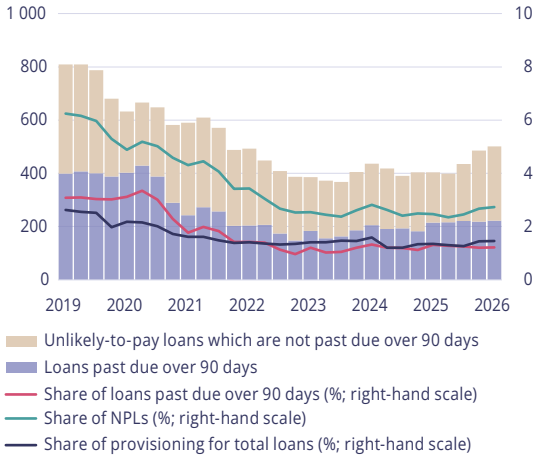
The deterioration in credit quality has hit a narrow range of companies for the time being. From a sectoral perspective, the most pronounced deterioration in loan quality was observed in manufacturing. While many companies in the sector are highly dependent on developments in the external environment, which is affected by persistently high uncertainty, so far only a few loans to relatively risky borrowers have become NPLs, including those that had previously been granted the status of forborne loans. The deterioration of credit quality in the trade sector was affected by a borrower

Chart 2.12
Credit institutions: annualised interest rate and lending rate for consumer loans



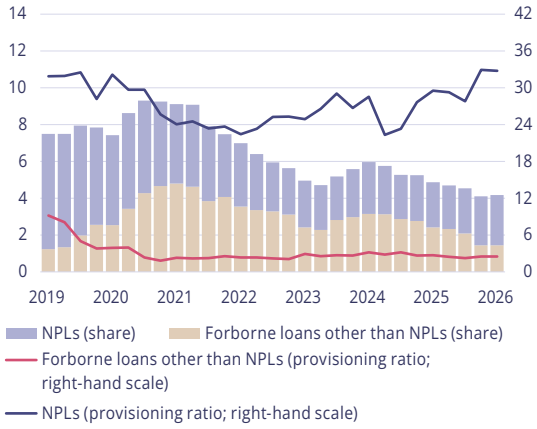
Sources: Latvijas Banka (MFI interest rate statistics data) and CRPC.

Chart 2.13
NPLs (million euro) **and share of NPLs and provisions in the total loan portfolio of credit institutions** (%)



Source: Latvijas Banka (Credit Register data) and its calculations.

Chart 2.14
NPLs, forborne loans other than NPLs (% of total loan portfolio) **and provisions created** (% of outstanding loans)



Source: Latvijas Banka (Credit Register data) and its calculations.

[47] Stage 2 loans are loans whose credit risk has increased significantly since the initial recognition, but they are not yet credit-impaired within the meaning of IFRS 9.

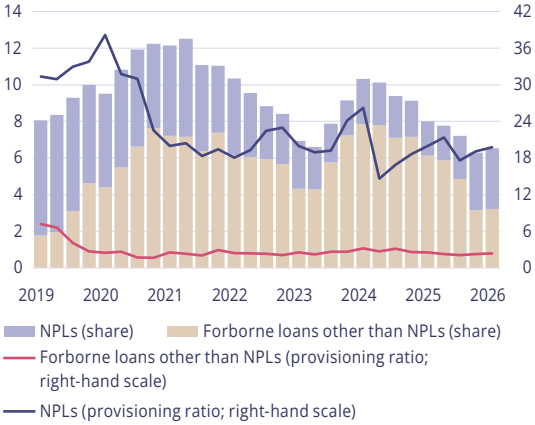
[48] See: Note 4 Risk management to the financial statements in "Group's consolidated and Bank's Separate Annual Report for the year ended 31 December 2025" of AS Rietumu Banka, p. 238.

[49] CET1 capital reduction in accordance with Article 3 of Regulation (EU) 2024/1623 of the European Parliament and of the Council of 31 May 2024 amending Regulation (EU) No 575/2013 as regards requirements for credit risk, credit valuation adjustment risk, operational risk, market risk, and the output floor. Some Latvian credit institutions make capital adjustments to compensate for insufficient provisions for credit risk.

associated with one of the above-mentioned NPL borrowers in the manufacturing sector, whose credit had previously been granted the status of forborne credit. Overall, a slight deterioration in credit quality in the agricultural sector affects a slightly wider range of borrowers and could be explained mainly by severe adverse weather conditions in the summer of 2025 for cereals. The share of NPLs in the household sector (both residential and consumer loans and other loans) remains stable (Chart 2.16). Early warning indicators such as extended or unchanged residential loans were also at historically low levels until the end of 2025, pointing to the overall strong financial position of households.

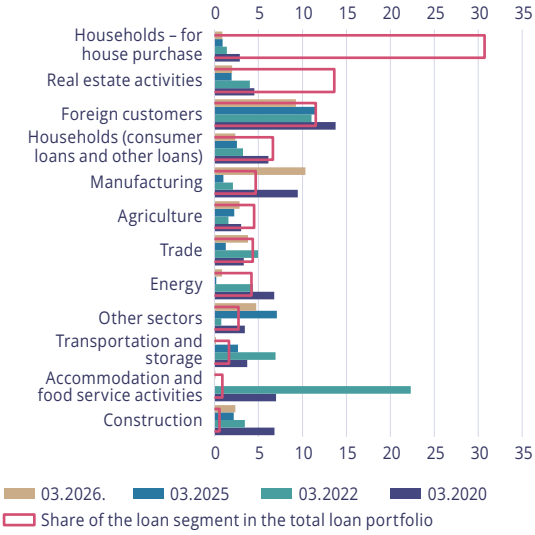
A further deterioration in the quality of the loan portfolio is likely as the outlook for economic growth deteriorates, as a result of the war in the Middle East and the increase in uncertainty, in particular related to the magnitude and duration of the rise in energy prices. The direct exposure of Latvian credit institutions to the epicentres of geopolitical shocks is very small (for more details, see Box 1.1). The indirect impact is greater: the rising global energy and fertiliser prices due to hostilities can have a greater impact on the NFCs with a more significant share of expenditure on energy or fertilisers in their cost structure. The most significant increase in credit risk could be for the agricultural sector and the transport sector, as well as for energy-intensive manufacturing NFCs and some NFCs in the trade sector, which account for a small share of the sector's loan portfolio. It should be noted that the 2022 energy price shock created serious solvency problems for a small number of borrowers. In the household sector, a significant deterioration in the quality of the loan portfolio is less likely. Households' financial position is generally strong and has improved significantly over the past years. Also from a longer-term perspective, the quality of the household loan portfolio has continued to improve despite several shocks. The continued strong profitability of banks, and in particular their high capitalisation, points to their good capacity to absorb potential NPL growth, including in case of more negative scenarios (see the Chapter "Stress tests of credit institutions").

Chart 2.15
NPLs, forborne loans other than NPLs, in the domestic NFS portfolio (% of domestic NFS loan portfolio) and provisions created (% of outstanding loans)



Source: Latvijas Banka (Credit Register data) and its calculations.

Chart 2.16
Structure of the loan portfolio and share of NPLs in the respective loan portfolio (%)



Source: Latvijas Banka (Credit Register data) and its calculations.

Funding and liquidity risk

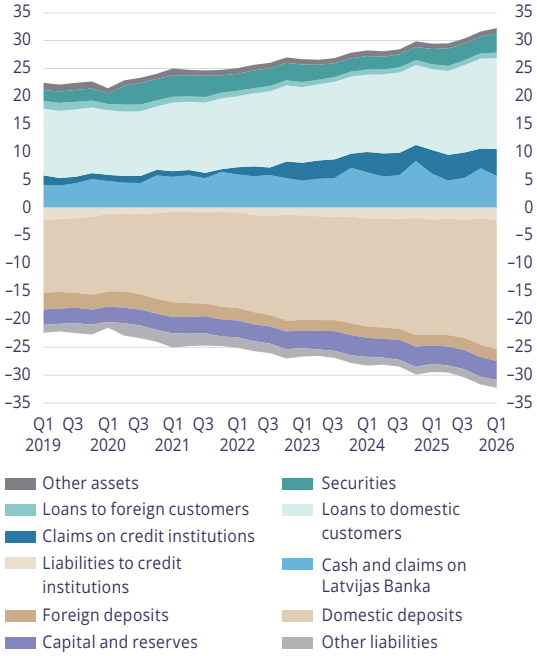
Prepared by Mārcis Risbergs

The level of funding and liquidity risk in the banking sector remained at the previous year, low. The main factors behind this have not changed significantly during the year: the steadily growing deposit base of the domestic private sector, which provides the majority of banks with sufficient funding and reduces the need to borrow on the financial markets; a high share of liquid assets, mainly held in deposit facilities with Latvijas Banka and in government securities of the Baltic States, as well as a minimal amount of pledged assets.

The assets of the banking sector as a whole continued to grow gradually and reached EUR 32.2 billion in March 2026, an increase of 9% compared to the same period in the previous year. The stable growth in assets was mainly driven by the four largest banks[50], which account for 82% of total banking sector assets, while the remaining banks also increased their business volumes significantly. The growth was mainly driven by a steady increase in deposits attracted by the domestic private non-financial sector, which were used for domestic lending, and the surplus of these deposits was mainly placed in the parent banks and deposit facilities of Latvijas Banka (Chart 2.17). Investments in claims against parent banks are diversified both with different maturities and by investing in covered securities issued by credit institutions in the parent banking group, which resulted in an increase of more than 25% in the banking sector's total securities portfolio over the past year.

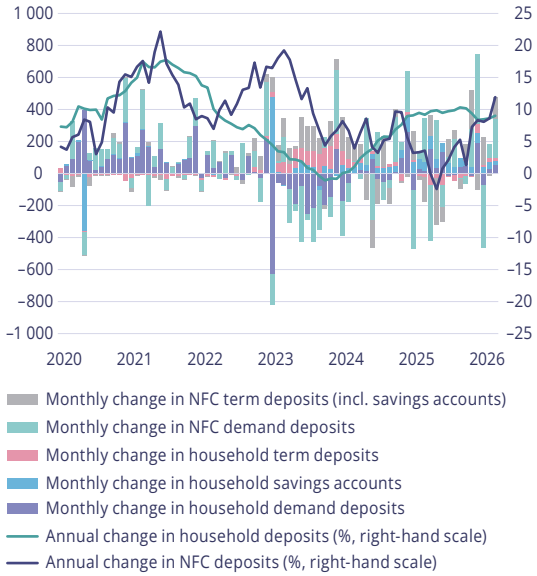
Domestic private non-financial sector deposits remain the most important item on credit institutions' balance sheets. In March 2026, they accounted for 75% of all banks' financial liabilities (domestic non-bank[51] deposits as a whole account for 83% of total banks' financial liabilities) and their annual growth rate increased to 10.2%. This growth was sustained by both household deposits, at 9.0%, and domestic NFC deposits, which recorded a significant increase of 11.9% in March (Chart 2.18). Monthly changes in domestic deposits by type of deposit show

Chart 2.17
Structure of the assets and liabilities of credit institutions (billion euro)



Source: Latvijas Banka (MBP data).

Chart 2.18
Development of domestic household deposits[52] and NFCs by type of deposit (million euro, %)



Source: Latvijas Banka (MBP data).

that demand deposits dominate the growth of NFC deposits; however, they are volatile, as they depend on changes in the cash flows of different sectors of the economy. Furthermore, the fundamental objective of

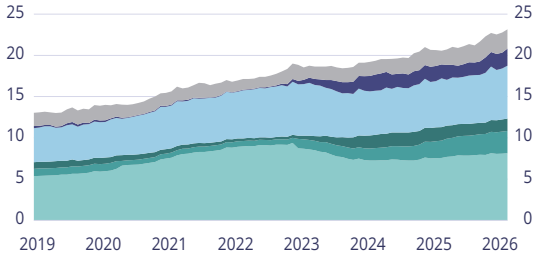
[50] The largest banks are Swedbank AS, AS SEB banka, AS Citadele banka, and the Latvian branch of Luminor Bank AS.
[51] Non-financial private sector, government, and non-bank financial sector.
[52] Household deposits have been adjusted by transferring savings account balances redeemable on the same day from sight deposits to fixed-term deposits.

NFCs is not to accumulate large deposit balances on a lasting basis, but to direct them to the development of enterprises. In turn, not only demand deposits have a significant impact on household deposits, but also deposits in savings accounts, which, in terms of the speed of availability of funds[53], do not differ significantly from current accounts in most banks, but significantly higher remuneration is paid for deposits in savings accounts. Deposits on household savings accounts (Chart 2.19), which account for 22% of total domestic household deposits, also remain the most significant increase in total deposit balances and their annual growth rate remains around 30%. Investments in savings accounts generally replace fixed-term deposits held by households.

Despite the high volatility in the second quarter of 2025 in a number of areas affecting global financial markets, households' direct[54] investment in alternative financial instruments, mainly investment funds, quoted shares and long-term debt securities, continued to grow robustly in 2025 (Chart 2.20). The second half of 2025 also saw a moderate increase in investments in savings bonds issued by the Treasury, which was significantly affected by investments in newly offered savings bonds with a three-month maturity (Chart 2.21). Overall, domestic households' alternative investment[55] reached a level equivalent to 24% of household deposits in the Latvian banking sector at the beginning of 2026.

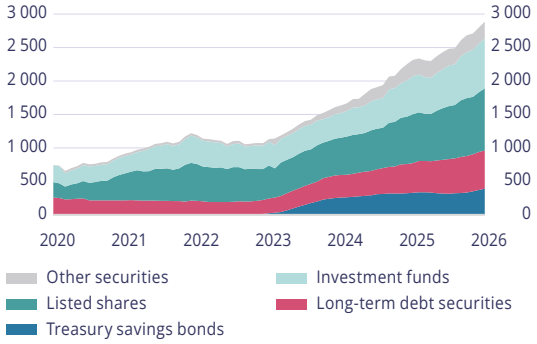
Deposit balances of foreign customers increased moderately, but their share in non-bank deposit balances did not change significantly, remaining below 10% (Chart 2.22), most of which were deposits attracted from euro area countries. It can be observed that some medium-sized and smaller banks continue to attract deposits from online deposit platforms, while some have shifted more towards domestic deposits, mainly from legal entities. Deposits attracted outside the euro area continue to decline, accounting for 3.4% of total non-bank deposits in March 2026. Deposits attracted by Latvian credit institutions from the countries of the Middle East were insignificant (see Box 1.1).

Chart 2.19
Evolution of domestic non-bank customer deposits (billion euro)



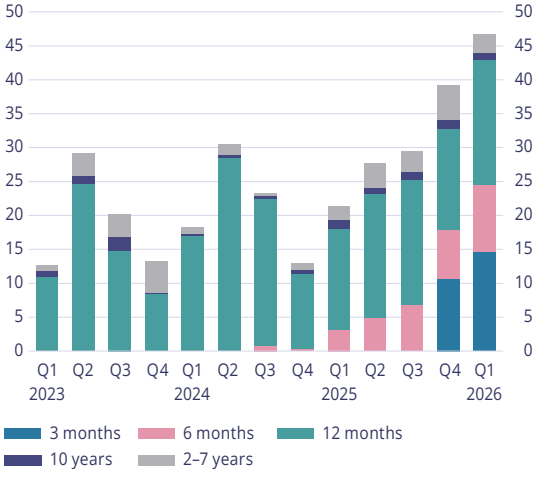
Source: Latvijas Banka (MBP data).

Chart 2.20
Securities owned by Latvian households purchased through euro area financial institutions and Treasury savings bonds (million euro)



Source: Latvijas Banka (securities statistics data).

Chart 2.21
Term structure of newly acquired Treasury savings bonds (million euro)



Source: Latvijas Banka (securities statistics data).

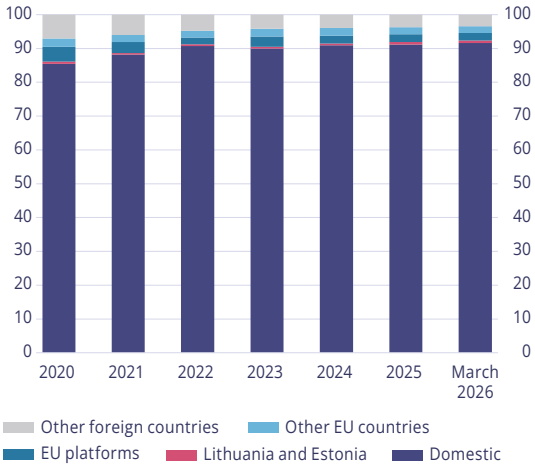
[53] Availability of funds within one to seven days.
[54] Investments by households in the 2nd and 3rd pillar pensions, as well as investments through financial institutions outside the euro area, are not considered here.
[55] Domestic households' investments in financial instruments acquired through euro area financial institutions, and in Treasury savings bonds.

Despite the rapid growth rate of domestic lending, credit institutions do not yet need to raise market financing to finance their loan portfolio. The domestic loan-to-deposit ratio remains low (70% in March 2026) and each of the four largest credit institutions with domestic deposits can fully finance domestic loans granted. If deposits attracted from euro area countries (mainly those raised from deposit platforms) are additionally considered, almost all credit institutions can finance domestic loans without attracting additional market funding, except for small branches of foreign credit institutions, which usually use parent bank financing in Latvia. At the same time, there are credit institutions in the Baltic States which regularly attract funds from the financial markets, and their branches also operate in Latvia.

The liquidity ratios of regulatory requirements remain stable above the EEA average (Chart 2.23). The most significant amount of highly liquid assets in banks is still placed in deposit facilities at Latvijas Banka. In February 2026, claims on Latvijas Banka accounted for 74% of LCR liquid assets. This share has even slightly increased compared to March 2025. This could be due to uncertainty in the global financial markets, as the funds held at Latvijas Banka are available much faster and with stable profitability. In addition, Latvian banks still have one of the lowest ratios of encumbered assets to total assets, at 1.6% at the end of 2025 (EEA average 24.7%). This suggests that banks have immediate access to cash to provide additional liquidity.

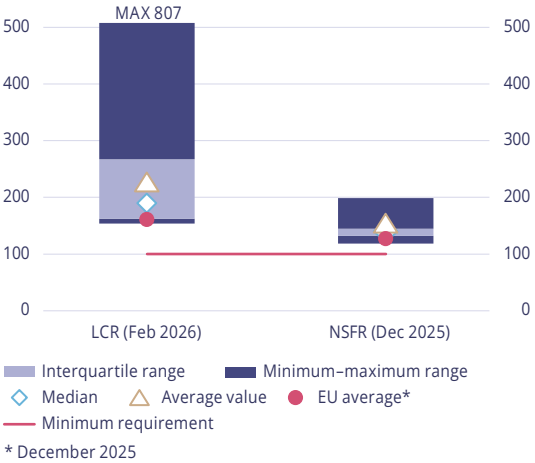
Also, the liquidity stress test conducted by Latvijas Banka does not show a significant increase in liquidity risk in the course of 2025 (see the Section "Liquidity stress tests of credit institutions").

Chart 2.22
Structure of deposits attracted by credit institutions by country (%)



Source: Latvijas Banka (MBP data).

Chart 2.23
LCR and NSFR of credit institutions



* December 2025

Sources: Latvijas Banka (COREP data), EBA.

Profitability

Prepared by Mikus Āriņš

In terms of profits generated by credit institutions, 2025 marked a turning point. As market interest rates declined, the net interest income of credit institutions fell sharply. However, with the decline in interest rates, the outstanding loans also grew more rapidly. This partly offset the impact of interest rate decrease on profitability. Profits were also dampened by the solidarity contribution and an increase in provisioning expenses. Despite declining profits, the overall profitability of credit institutions remained good compared to 2018–2022. The future profitability prospects of credit institutions may be affected by risks associated with geopolitical uncertainty.

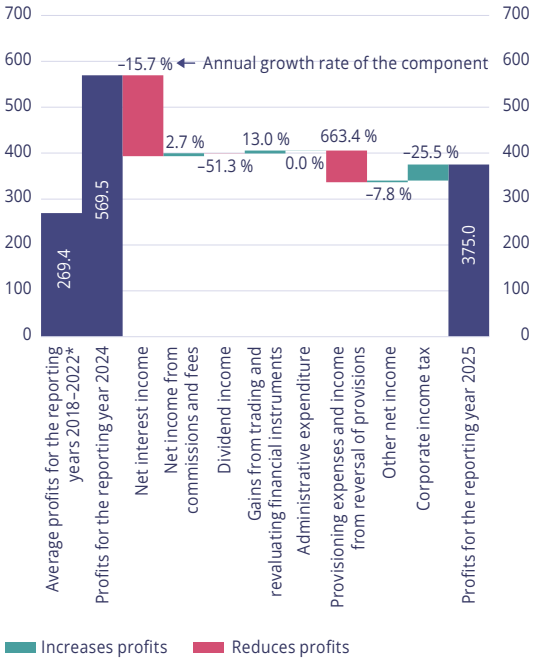
In 2025, the profits of credit institutions decreased by a third, from EUR 569.5 million in 2024 to EUR 375.0 million in 2025 (Chart 2.24). The decrease was mainly driven by a decline in net interest income and a rise in provisioning expenses.

Although the profits of credit institutions decreased in 2025 compared to 2023 and 2024, the profits of currently active credit institutions remained generally higher than in 2018–2022 (Chart 2.25). The financial operating income of credit institutions consisted mainly of net interest income (almost three quarters of the financial operating income). Although the share of net interest income has slightly decreased compared to 2023 and 2024, its share in financial operating income is higher than in 2018–2022.

Due to the ECB's interest rate cuts, market interest rates and, consequently, the net interest income of credit institutions decreased. In 2025, the average 3-month and 6-month EURIBOR rates were 1.4 and 1.2 percentage points lower respectively than in 2024. However, they remained higher than in 2022 (i.e. before the start of the ECB's monetary policy tightening), by 1.8 and 1.5 percentage points respectively. In Latvian credit institutions, interest rates on loans and deposits are mainly linked to market rates[56], which led to a decrease in both interest income on loans and interest expense on deposits in 2025 (Chart 2.26).

[56] The loans issued by Latvian credit institutions are mostly variable rate loans linked to market interest rates, primarily EURIBOR. By the end of 2025, nearly 90% of the loans to households and NFCs were variable rate loans.

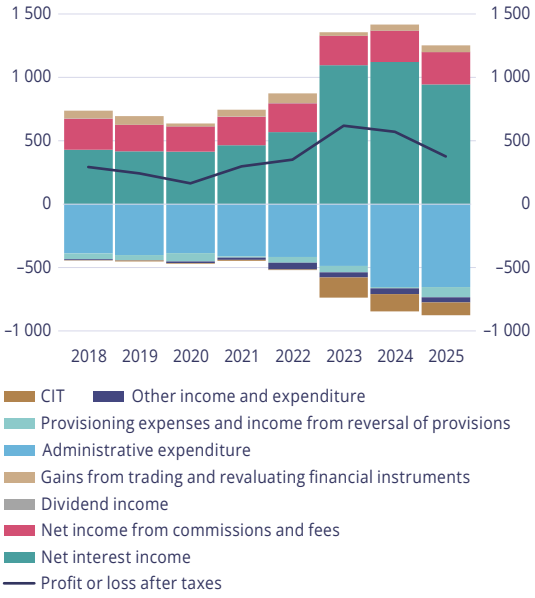
Chart 2.24
Credit institutions' retained earnings in the reporting year and the contribution of their components to changes in profits in 2025 (million euro)



* Only currently active credit institutions (adjusted for the merger between Signet Bank AS and AS Expobank in 2022).

Source: Latvijas Banka (FINREP data).

Chart 2.25
Credit institutions' retained earnings in the reporting year and their components (million euro)



* Only currently active credit institutions (adjusted for the merger between Signet Bank AS and AS Expobank in 2022).

Source: Latvijas Banka (FINREP data).

Outstanding loans grew faster in 2025 than in previous years (see the Section "Lending development"). This partly offset the impact of interest rate decrease on interest income. Interest income also increased slightly due to higher income from debt securities and debt derivatives, but this was modest compared with a decline in loan income.

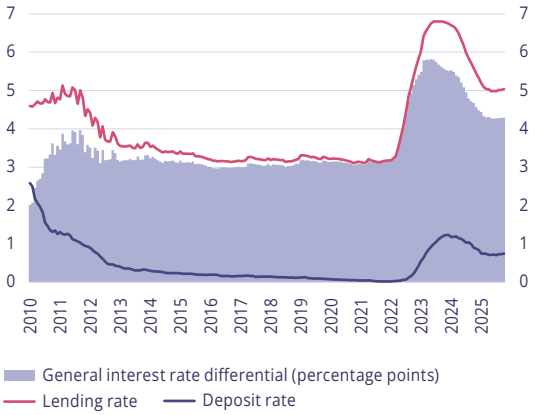
In 2025, net interest income decreased by 15.7% in comparison with 2024. At the same time, as average interest rates are still higher than before the start of the ECB's monetary policy tightening, net interest income in 2025 **was overall around twice as high as the average for 2018-2022** (Chart 2.27). It was generated primarily from households, NFCs, and deposits with the central bank.

Commission and fee income and expenses remained broadly unchanged in 2025, while net commission and fee income rose by 2.7%. Net commission and fee income from payment services decreased slightly, mainly due to higher commissions and fees for payment card servicing. In turn, commission and fee income for securities issuance and other intermediation services rose. The decline in income from transactions in financial instruments was more than offset by gains from exchange rate fluctuations. Thus, income of credit institutions from financial instrument and currency trading rose by 13.0%.

The administrative expenses of credit institutions remained virtually unchanged, with an increase of only 0.4% compared to 2024. **However**, as the income of credit institutions fell, **its ratio to the financial operating income of credit institutions increased**. With the growth rate of wages in the economy slowing, the rise in staff costs of credit institutions also moderated. Staff costs increased by 5.5% in 2025 (compared to 16.1% in 2024). Expenses on information technology rose slightly, while expenses on advertising, marketing, and consultancy services decreased.

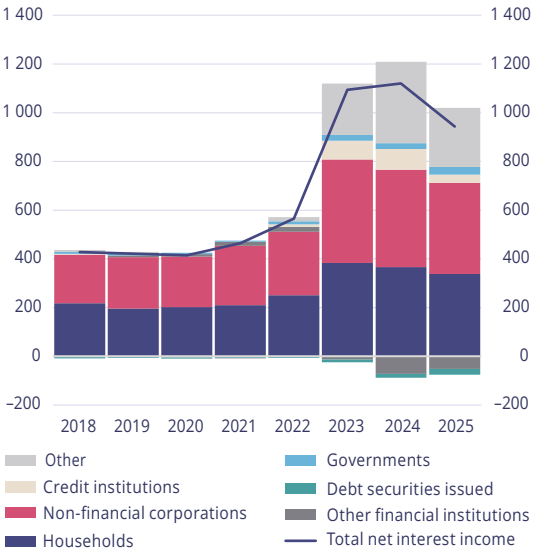
From 2025 onwards, credit institutions are required to pay a solidarity contribution[57]. Its advance payments led to a slight increase in the tax and fee burden on credit institutions (by 9.5%), even though most credit institutions required to make advance payments of the solidarity contribution qualified for at least a partial

Chart 2.26
Average interest rates on outstanding loans and deposits (including demand) granted by credit institutions to domestic households and NFCs (%) **and their differential** (percentage points)



Source: Latvijas Banka (MFI interest rate statistics).

Chart 2.27
Net interest income of credit institutions by type of counterparty (million euro)



* Only currently active credit institutions (adjusted for the merger between Signet Bank AS and AS Expobank in 2022).

Source: Latvijas Banka (FINREP data).

reduction in the solidarity contribution[58]. It should be noted that, also in 2024, credit institutions were subject to an additional levy – the mortgage borrower protection fee. Thus, the administrative expenses of credit institutions were already elevated in 2024, and the introduction of the solidarity contribution effectively replaces the mortgage borrower protection fee. The two fiscal measures differ in scope. The mortgage borrower protection fee applied to loans for house

[57] See Box 2.3 "Solidarity Contribution Law" of Financial Stability Report 2025.

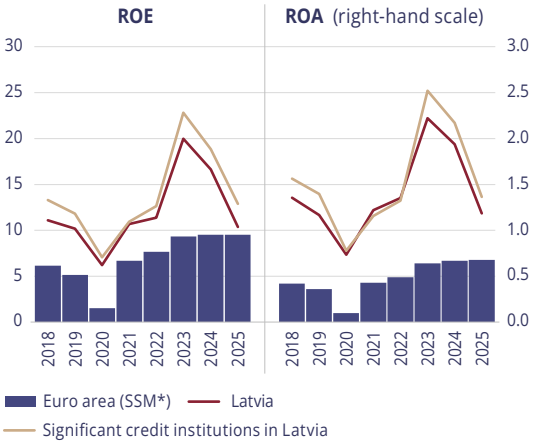
[58] The Solidarity Contribution Law provides that the solidarity contribution payer has the opportunity to receive a reduction in the solidarity contribution if it significantly increases lending.

purchase, whereas the basis for the solidarity contribution is the net interest income of credit institutions that exceeds the 2018–2022 average by more than 50%.

Although net provisioning expenses rose in 2025, this was attributable to individual cases and does not, overall, indicate a weakening in the debt servicing capacity among customers of credit institutions (see also the Section "Credit risk"). The majority (around two-thirds) of the increase in provisioning expenses is associated with legal proceedings brought by the Russian authorities against AS Rietumu Banka (the fifth largest credit institution in Latvia by assets), which may result in it losing its subsidiary's property in Russia[59]. In view of the preventive capital adjustment, the impact of those additional provisions on the fulfilment of the credit institution's supervisory capital requirements is minor[60]. Meanwhile, the remaining increase in provisioning expenses is primarily attributable to a slight deterioration in loan quality in the NFC sector (driven by the effect of a few borrowers).

Overall, the profitability ratios of credit institutions declined in 2025, but from relatively high levels. They remain good, including when compared with the averages of the largest credit institutions in the euro area. The average ROE for credit institutions decreased to 10.4% (from 16.6% in 2024), while the average ROA reached 1.2% (1.9% in 2024). As mentioned above, in 2025, the profitability ratios of credit institutions were strongly influenced by the solidarity contribution: if its direct impact were excluded, the average ROE and ROA of credit institutions would be around 13.2% and 1.5% respectively. The ROE and ROA of the three largest credit institutions reached 12.9% and 1.4% respectively (Chart 2.28). The gap between the overall average and the average for the three largest credit institutions is primarily attributable to the aforementioned exceptional provisioning expenses recorded by one credit institution. At the same time, the average cost-to-income ratio deteriorated, increasing from 49.5% to 55.8%.

Chart 2.28
Average ROE and ROA for credit institutions in Latvia and the euro area



* Euro area averages are calculated based on the data on credit institutions under direct supervision of the ECB's SSM, covering all euro area countries.

Sources: Latvijas Banka and ECB (FINREP data).

The outlook for future profitability of credit institutions depends to a large extent on the impact of geopolitical instability on the economy. Prior to the war in the Middle East, the profitability outlook for credit institutions was sound, with interest rates stabilising and lending showing significant increases that would ensure a good income base. Despite the solidarity contribution, the profits of credit institutions would remain good overall. However, the war in the Middle East has created significant uncertainty and, depending on the spread of its future impact, the profitability of credit institutions may either deteriorate or improve. If the ECB pursues a monetary policy aimed at curbing inflation, credit institutions will benefit from higher interest rates in the short term. At the same time, part of the increase in interest income will have to be directed towards the solidarity contribution. In addition, increased uncertainty and interest rates will reduce demand for loans, making it more difficult for credit institutions to meet the criterion for the solidarity contribution reduction. If, on the other hand, borrowers' solvency weakens due to faster price increases and slower economic growth, provisioning expenses of credit institutions will rise. Thus, the profitability of credit institutions in 2026 will depend on the evolution and balance of the factors mentioned above.

[59] See the information published on the website of AS Rietumu Banka on 03.12.2025 "Rietumu Banka may lose property worth EUR 16 million in unfair court proceedings in Russia".

[60] See Note 4 Risk management to the financial statements in "Group's consolidated and Bank's Separate Annual Report for the year ended 31 December 2025" of AS Rietumu Banka.

Capitalisation

Prepared by Ilze Vilka

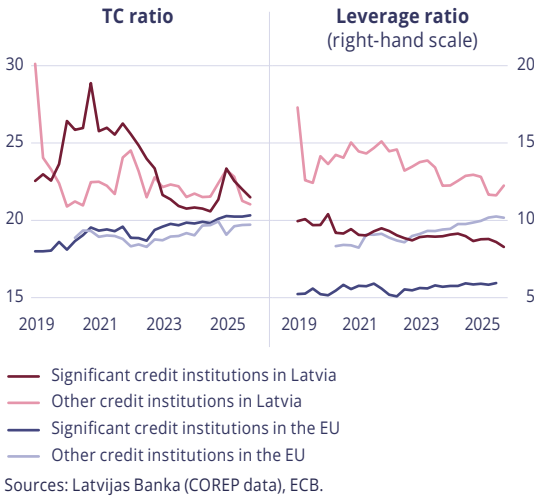
Overall, the capital buffers of credit institutions are sufficient to absorb potential losses in the event of financial shocks. In 2025, as lending growth resumed, exposure increase was accompanied by rising risk weights in the portfolios of small credit institutions, reflecting increasing risk tolerance. At the same time, as the profits of credit institutions shrink, their profit distribution plans become more moderate and the remuneration paid to shareholders decreases.

In 2025, the capital ratios of credit institutions declined slightly overall, reflecting stronger lending activity in the economy. At the end of 2025, the average TC ratio of credit institutions was 21.5% on a consolidated basis[61], the CET1 capital ratio – 19.2%, and the leverage ratio – 9.0% (at the end of 2024 – 21.6%, 19.5%, and 9.3% respectively). To compare, the EU significant credit institutions had an average TC ratio of 20.3%, a CET1 capital ratio of 16.2%, and a leverage ratio of 6.0% at the end of 2025[62]. The differences in risk-weighted capital ratios between Latvian and EU credit institutions are gradually narrowing. At the same time, the gap between the average leverage ratios in Latvia and the EU suggests substantial differences in average risk weights, including a broader use of internal models among significant EU credit institutions (Chart 2.29).

With the implementation of the Basel III reform, the amended Capital Requirements Regulation (CRR), which introduced significant changes to the capital requirements framework, is to be applied in the EU from 2025 onwards. The amendments concern requirements for credit risk, credit valuation adjustment risk, operational risk, market risk, and the output floor. In the area of credit risk, a more granular and risk-sensitive breakdown of exposures has been introduced for institutions using the standardised approach to determine capital.

On the other hand, an output floor has been introduced for IRB credit institutions. Accordingly, credit institutions that calculate their capital adequacy based on internal models are required, gradually by 2030, to ensure own funds requirements of at least 72.5% of the capital requirements that would apply if they were using the standardised approach. This innovation affects credit institutions using internal models for the calculation of credit risk capital requirements and the risk weights resulting from these models are significantly lower than those under the standardised approach. For Latvian IRB credit institutions, this output floor is not restrictive as, according to their models, relatively high risk weights are already being used for the calculation of credit risk capital requirements. For operational risk, a common calculation method has been introduced, making the risk assessment simpler and more comparable between institutions.

Chart 2.29
Capitalisation ratios of credit institutions (% of TREA, % of LREA)



Sources: Latvijas Banka (COREP data), ECB.

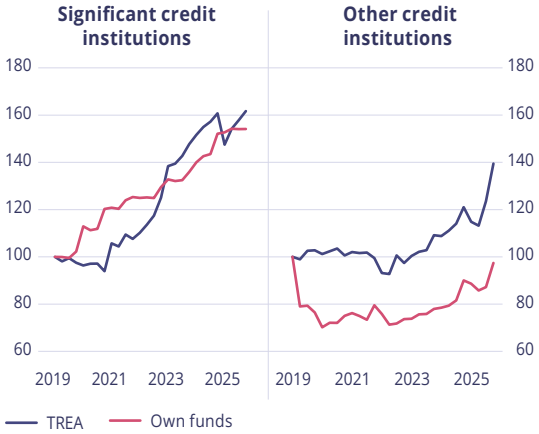
Owing to regulatory changes, the total risk exposure amount of Latvian credit institutions decreased significantly at the beginning of 2025, improving the risk-weighted capitalisation ratios of credit institutions and releasing own funds for most credit institutions. **However**, this effect was temporary, as **in the second half of the year, stronger lending activity led to an increase in the risk exposures of credit institutions, and the share of higher-risk loans** in portfolios of some institutions **also rose** (Chart 2.30), marking divergent developments in risk profiles. Average risk weights[63] in the portfolios of significant credit institutions have remained broadly unchanged, whereas

[61] Capitalisation calculations and figures only include currently active credit institutions at the consolidated level.
[62] ECB's Supervisory Banking Statistics for significant institutions. Fourth quarter 2025.
[63] The risk weight of an exposure is calculated as the ratio of the risk-weighted exposure measure to the total exposure measure within a credit institution.

in the group of other credit institutions, they have increased in certain portfolio segments, as these credit institutions issued more higher-risk loans. Average risk weights have increased for exposures secured by real estate and for acquisition, development, and construction exposures[64]. For this exposure class, the average risk weights of other credit institutions rose during 2025 – from 63% at the beginning of the year to 94% at the end of the year. For comparison, for the same exposure class, the average risk weight was 64% for other EU credit institutions using the standardised approach for capital requirement calculations, and 48% for significant EU credit institutions. Risk weights for exposures to commercial companies, individuals, as well as small and medium enterprises have remained broadly unchanged.

The voluntary capital buffers of credit institutions remained broadly unchanged in 2025, standing at 5.3% at the end of the year. Overall, they are sufficient to absorb potential losses due to borrowers' solvency and other shocks (see the Section "Credit risk and market risk shock absorption capacity stress tests"). At the end of 2025, significant institutions' buffers above total capital requirements stood at 5.1%, while the voluntary capital buffers of other credit institutions reached an average of 5.7%. The level of voluntary capital buffers varies across credit institutions, with some smaller credit institutions maintaining buffers well below the sector average.

Chart 2.30
Capital ratio numerator and denominator
(Q1 2019 = 100)



Source: Latvijas Banka (COREP data).

Overall, credit institutions envisage retaining a larger share of profits in capital than in previous years. In 2026, credit institutions plan to distribute, on average, 63% of the profit earned in the previous year, and several institutions that paid dividends in the past have decided to refrain from doing so this year. With the profits of credit institutions declining, the remuneration of shareholders also decreases. The total amount of dividends announced for 2026 is EUR 199 million, half the amount announced in the previous year.

[64] Acquisition, development, and construction exposures or ADC exposures are exposures to commercial companies or special purpose vehicles that finance any land acquisition for development and construction purposes or finance the development and construction of any housing or commercial real estate. These exposures are assigned a risk weight of 150% or a risk weight of 100% if certain risk-mitigating criteria are met.

3. Stress tests of credit institutions

Credit risk and market risk shock absorption capacity stress tests

Prepared by Nadežda Siņenko, Ilze Vilka, Jānis Strazdiņš, and Mikus Āriņš

The results of the macroeconomic stress test suggest that the resilience of Latvian banks to potential shocks is good. The shock absorption capacity of the banking sector is expected to improve further in 2026, as projected profits[65] will strengthen the resilience of banks.

The sensitivity analysis shows that all credit institutions would be able to meet the minimum TC requirement of 8% at the end of 2025, even in a scenario where the share of loans past due over 90 days would rise by more than 5 percentage points. In turn, significant credit institutions would be able to absorb an even larger deterioration in credit risk, such that the share of loans past due over 90 days would rise by up to 17 percentage points. Thus, even without considering the materialisation of a more complex macroeconomic stress scenario, the current results of the sensitivity analysis already indicate a good level of resilience against the potential loss burden among credit institutions (see the Section "Capitalisation").

The macroeconomic stress test has been carried out to assess the capability of credit institutions to absorb a potential increase in credit risk and market risk caused by a deterioration of the macrofinancial environment. In the stress scenario, the most important risks comprise high uncertainty and geopolitical shocks, including in the Middle East. They may lead to higher energy and food prices and supply chain disruptions, negatively affecting bank customers and asset quality.

Methodology

Latvijas Banka conducts a sensitivity analysis[66] and macroeconomic stress tests[67] of credit institutions on a regular basis. The calculations of the macroeconomic stress test are based on the consolidated data of credit institutions as at the end of 2025, and the assessment covers the period until the end of 2026. The thresholds used for the stress tests are as follows: meeting the minimum capital requirement – a TC ratio of 8.0%, T1 capital ratio of 6.0%, and CET1 capital ratio of 4.5%[68]. Failure to meet any of the minimum capital requirements is considered failure to meet the overall capital requirements.

Given the high share of secured loans in the loan portfolio of Latvian credit institutions, from 2022 onwards, the weighted average loss given default (LGD_i) of each credit institution is used instead of a single provisioning rate. The weighted average LGD is calculated for each group of resident loans presented separately from other loans in the stress test description, as well as for the largest sectors. Its calculation is based on the loan-level collateral data available in the Credit Register of Latvijas Banka. In the calculation, state guarantees and cash are recognised in full, for real estate, a differentiated haircut is applied depending on scenario assumptions, while for physical collateral a haircut of 30% is applied.

As of 2023, **the stress test** of Latvijas Banka's credit institutions **includes a profit projection before taxes**

[65] Even if the profit projection is not included in the calculations, the shock absorption capacity of credit institutions remains good.

[66] A credit risk sensitivity analysis provides an indication of the magnitude of an increase in loans past due over 90 days a credit institution would be able to absorb before its capital adequacy ratios fall below the minimum capital requirements. The sensitivity analysis assumes that a credit institution has to build provisions in the amount of at least 50% for its portfolio of loans past due over 90 days and build additional provisions totalling 50% of the increase in the loans past due over 90 days; unlikely-to-pay loans must be provisioned by at least 35%. The credit institution capital and TREA are reduced by the amount of the additional provisions.

[67] Macroeconomic stress tests measure the resilience of Latvian credit institutions to strong adverse macroeconomic shocks whose materialisation is plausible, yet their probability is low. The results of the credit risk and market risk stress tests allow for the assessment of whether credit institutions have sufficient capital for absorbing losses in particularly severe and even extreme macroeconomic stress circumstances without additional capital injections.

[68] A characteristic feature of the capital structure of Latvian credit institutions is the fact that the T1 requirement is met with CET1; therefore, compliance with the T1 requirement automatically means compliance with the CET1 requirement as well. As a result, a relatively high stress test threshold is applied to high quality capital.

and before provisioning expenses for loans and securities (according to the share of NPLs projected in each scenario and its impact on the profits of credit institutions).

The market risk component of the stress test uses the data on each credit institution's securities portfolio, including the securities measured at fair value through profit or loss, securities measured at fair value through other comprehensive income, and securities measured at amortised cost (AC). This stress test methodology applies market shocks to all securities in order to assess the overall economic effect of the changes in the market value of the securities portfolio on capital, assuming that changes in the value of securities will need to be recognised regardless of their accounting treatment.

Since data on the securities portfolios of individual credit institutions are available at the highest level of granularity, the analysis was based on these data, while the group-level securities portfolio was extrapolated assuming it was structurally similar to that of a credit institution's level.

The securities of each credit institution's bond portfolio are grouped by major risk factors (euro area and US bond yields of different maturities, credit rating, and sector) according to the assessment of experts. Given their share in the portfolio, the bonds of the three largest issuers have been reported separately. The modified duration of each bond is set using Refinitiv data or, in the absence of data, using the residual maturity of the bond as a proxy. The modified duration is used to calculate the impact of the interest rate shock scenario. The foreign exchange risk has been reported separately from the revaluation effect, and the shock scenario is applied to the open foreign exchange position.

Stress test scenarios

Tables 3.1–3.6 summarise the parameters of the stress test scenarios.

The baseline scenario uses Latvijas Banka's forecasts of June 2026 for the domestic loan portfolio, which projects Latvia's GDP growth to be 2.0% in 2026 (seasonally adjusted data).

Table 3.1
Credit risk parameters of the macroeconomic stress test (%, percentage points)

Macroeconomic and credit risk parameters	Baseline scenario	Stress scenario
Latvia		
Annual changes in Latvia's GDP in 2026	2.0	–5.4
3-month EURIBOR forecast[69]	2.6	2.6[70]
Probability for a performing loan or a loan that is past due less than 90 days and not forborne to become a loan past due over 90 days within a year	0.9	5.6[71]
Probability for an unlikely-to-pay loan to become a loan past due over 90 days within a year	3.6	22.4
Probability for a performing loan or a loan that is past due less than 90 days to become an unlikely-to-pay loan within a year	0.9	5.6[71]
Share (%) of forborne loans other than NPLs that will migrate to the category of loans past due over 90 days within a year	0.9	100
Increase in the share of loans past due over 90 days in the loan portfolio of domestic customers at the end of 2026[72] (percentage points)[73]	1.0	8.8
Haircut applied to commercial real estate	20%	40%
Haircut applied to residential real estate	10%	30%

[69] 3-month EURIBOR annual average by the end of 2026; Eurex Exchange, 30.03.2026.
[70] Monetary policy responses to the shocks would likely result in a different level of EURIBOR under the stress scenario compared to the baseline scenario. However, the precise monetary policy response in the euro area – and, consequently, the level of EURIBOR – would depend on a wide range of factors affecting the euro area economy that are beyond the scope of this analysis. Accordingly, no monetary policy response is projected.
[71] Concerning groups of loans without any specific assumptions about the PD.
[72] Loans that have migrated from the categories "a performing loan or loan that is past due less than 90 days", "unlikely-to-pay loans", and "forborne loans other than NPLs" to the category "loans past due over 90 days" have been added up.
[73] This increase cannot be regarded as a forecast because of a static balance sheet and other conservative assumptions.

Under the baseline scenario, when calculating the loss given default, a haircut applied to real estate collateral reflects a depreciation in the value of the collateral as a result of a fire sale[74]. Under the stress scenario, the haircuts applied to the real estate values are higher than under the baseline scenario, as they reflect the risk of impairment due to both the fire sale and the decrease in the real estate prices. Under both scenarios, the haircuts applied to commercial real estate are larger than those applied to the residential segment (Table 3.1).

The total rise in NPLs in the stress test (Table 3.1) is assessed using a credit risk model. However, the assessment of NPL growth varies across loan groups according to expert assumptions about the credit risk of each loan group or sector based on the increase in credit risk due to the energy shock observed in 2022–2023 (Tables 3.2 and 3.4).

- The PD remains elevated in the agricultural sector: the financial resilience of the grain sub-sector has been weakened over the past three years by adverse weather conditions, while increases in fertiliser prices and production costs will reduce the solvency of companies operating in the sector (see the Sub-section "NFC solvency").
- The rise in energy and fuel prices triggered by the war in the Middle East could adversely affect manufacturing, the transport sector, and the rental and leasing activities sub-sector, as well as trade.
- Potential disruptions to the supply of construction materials and rising construction costs could weaken the construction sector.

[74] Under the baseline scenario, a haircut is not a forecast of price dynamics in the real estate market.

While the outstanding forborne loans accumulated on bank balance sheets in previous years continued to decrease in 2025 (at the end of 2025, they accounted for around half of the amount accumulated during the pandemic), a further deterioration in the quality of forborne loans is possible under macroeconomic stress. To reflect this risk, the stress scenario envisages a migration of these loans to the category of loans past due over 90 days. **The increase in NPLs foreseen in the stress scenario is applied after the migration.**

Assumptions regarding credit risk parameters for borrowers from other countries are presented in Table 3.3. The stress test scenarios assume that the PD for loans extended to borrowers from the Baltic States is the same as that of loans to domestic borrowers, while the provisioning rate is 60%. The PD on loans to borrowers from other EU and OECD countries is larger than to borrowers of the Baltic States, whereby the LGD has been set at 75%. For borrowers from all other countries, a higher PD is assumed, while the LGD is determined individually for each bank with such exposures, taking into account only the real estate collateral located in Latvia or other EU countries, to which a haircut is applied in accordance with scenario assumptions.

To ensure a more accurate reflection of the potential losses arising from foreign exposures, the amount of cross-border exposures have been adjusted based on Credit Register data on country risk transfer, taking into account all risk transfers of exposures to jurisdictions with a higher level of risk.

Table 3.2
Credit risk parameters by loan group under the baseline scenario (%)

Loans to Latvian residents	Loans to households	Loans to NFCs	
		Agriculture, manufacturing, transportation and storage, rental and leasing activities, construction, trade	Other sectors
Probability for a performing loan or a loan that is past due less than 90 days to become a loan past due over 90 days within a year (PD)	0.5	2.0	0.8
Probability for an unlikely-to-pay loan to become a loan past due over 90 days within a year	2.0	8.0	3.2
Probability for a performing loan or a loan that is past due less than 90 days to become an unlikely-to-pay loan within a year	0.5	2.0	0.8

Table 3.3
Assumptions regarding loans to foreign borrowers under the baseline scenario (%)

Loans to foreign borrowers	PD	LGD (or the provisioning ratio applicable to the loan volume)
Customers from Lithuania and Estonia	0.9	60
Customers from other EU and OECD countries	5	75
Customers from other countries[75]	20	LGD_i

In the **market risk component** of the baseline scenario, no significant shocks or losses from changes in the securities portfolio are assumed, based on the premise that even if there are disruptions in securities markets, they will return to their previous state during the stress test horizon.

From 2023 onwards, the stress scenario has been developed using the forecasts of the GaR model, which reflect **the 5th percentile** of the future probability distribution of GDP growth rates, based on the latest available GDP data and the value of deflated CCRI developed by Latvijas Banka. **According to the calculations, in the stress scenario, GDP would contract by 5.4% in 2026.**

Under the adverse scenario, the assessed increase in NPLs also differs across loan segments, reflecting expert assumptions regarding the credit risk of each loan segment or sector, as presented in Table 3.4. The differentiation in sectoral vulnerabilities is maintained under the stress scenario. Larger macroeconomic shocks aggravate the situation across sectors, particularly in vulnerable sectors.

The assumptions made for foreign investment in the stress scenario are presented in Table 3.5.

Table 3.4
Credit risk parameters by loan group under the stress scenario (%)

Loans to residents of Latvia	Loans to households	Loans to NFCs	
		Agriculture, manufacturing, transportation and storage, rental and leasing activities, construction, trade	Other sectors
Probability for a performing loan or a loan that is past due less than 90 days to become a loan past due over 90 days within a year (PD)	5.6	8	5.6
Probability for an unlikely-to-pay loan to become a loan past due over 90 days within a year	22.4	32	22.4
Probability for a performing loan or a loan that is past due less than 90 days to become an unlikely-to-pay loan within a year	5.6	8	5.6

Overall, **the assumptions made in the baseline scenario are quite conservative, thus the stress test results in this scenario should not be interpreted as a forecast of capital ratios.**

Table 3.5
Assumptions regarding loans to foreign borrowers under the stress scenario (%)

Loans to foreign borrowers	PD	LGD
Customers from Lithuania and Estonia	6.3	60
Customers from other EU and OECD countries	10	75
Customers from other countries	40	LGD_i

[75] Both the baseline and stress scenarios assume that all loans to residents of Russia, Belarus, and Ukraine, as well as all loans, for which Russia, Belarus, and Ukraine are identified as risk transfer countries, are written off. However, when recognising these as losses, previously accumulated provisions and real estate collateral located in Latvia or in other EU countries are taken into account, with the value of the collateral adjusted in line with the scenario assumptions (Table 3.1). Credit exposures of significant credit institutions in Russia, Belarus, and Ukraine are generally low, and their write-offs have no material impact on the institutions' capitalisation.

The stress scenario for the **market risk component** is based on the securities portfolio as at the end of December 2025. For market risk, **a stress scenario simulates a global market shock scenario[76] (Table 3.6) where significant shocks are applied to government and corporate securities through a rise in the benchmark yield**. The selection of this stress scenario, based on the unchanged methodology described in the footnote, identifies one historical 12-month period in this stress test exercise – the increase in interest rates in 2022 – as the period that would have the most significant impact on the value of the existing securities portfolio given its structure. The impact calculation assumes constant initial amounts of securities. Financial derivatives which comprise a wide range of financial assets, characterised by a lack of market price and liquidity, as well as relatively high risk, were subject to an in-depth review[77] during the previous year. It was based on EMIR data and aimed to assess the presence of any concentration risks, including for off-balance-sheet exposures of such instruments, but no such heightened risks were identified for these instruments. Accordingly, without changing the methodology, a plain percentage value shock of 50% has been applied to the carrying value of these instruments on the asset side of the balance sheet, based on expert judgement.

[76] Under the stress scenario, shock parameters have been set for the debt securities portfolio, mostly using the historic monthly changes in indices corresponding to each risk factor (market data since 2006 have been used) and assuming that the current investments in securities remain unchanged. Then, the sum of changes over the previous 12 months is calculated for each month, resulting in the total changes from the previous year. Finally, 1% of cases or months with the largest estimated hypothetical 12-month losses accumulated in the aggregate portfolio of credit institutions are calculated. The average values of the identified cases are used in the scenario. Given that the stock and funds portfolio of Latvian credit institutions is rather small and notably lacks market data, the shock scenario applied to this portfolio uses a simple parameter of a percentage fall in the portfolio value, corresponding to 1% of the most adverse changes in the STOXX EUROPE 600 stock index value since 2006.

[77] Full analysis: Strazdiņš, J., "Application of financial derivatives in the financial system and beyond: based on EMIR data", makroekonomika.lv, 22.01.2026.

Table 3.6
Parameters of market risk stress test under the stress scenario

Instrument	**Original value** (%)	**Changes under the stress scenario** (in basis points)
Benchmark yield curve		
Securities in euro (1 month–10 years)	1.9 to 2.7	226 to 343
Securities in US dollars (1 month–10 years)	3.6 to 4.1	160 to 448
Risk premium of the key categories[78]		
Investment class (government, corporate sector)	0.5 to 1.1	–20 to 50
High yield class (government, corporate sector)	2.8 to 3.5	–102 to 146
Risk premium of the three major issuers	–0.6 to 1.9	127 to 167
Other significant market shocks		**Changes under the stress scenario** (%, compared to the baseline value)
Equities, funds, and other instruments (excluding financial derivatives)		–3
Financial derivatives		–50

[78] The difference between the yield on a security and the benchmark rate of the respective currency. No risk premium shock is applied to German and US government bonds.

Stress test results

Table 3.7 summarises **the results of the stress test**.

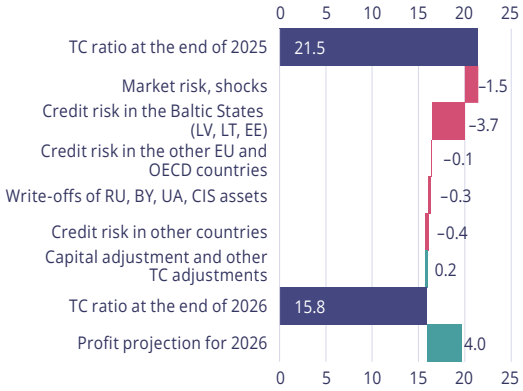
Under the conservative assumptions of the baseline scenario, it is expected that the estimated total losses could reach EUR 170.9 million or 0.6% of credit institutions' total assets. Losses in the baseline scenario are mainly driven by losses arising from investments in the countries affected by warfare[79] (24.7%). These losses are concentrated in individual non-significant credit institutions, and the write-off of these assets from balance sheets would not pose problems in meeting capital requirements even in a stress scenario. The remaining losses are determined by the necessary additional provisions for the loan portfolio of residents and non-residents.

Under the stress scenario, the share of loans past due over 90 days in the domestic loan portfolio would increase by 8.8 percentage points by the end of 2026. In the event of the stress scenario materialising, the estimated total losses could reach EUR 906.4 million or 3.3% of credit institutions' total assets. Losses arising from market risk would constitute 25.9% of the total losses, while losses arising from investments in the countries affected by warfare would amount to 4.9%[80]. Meanwhile, losses from loans to domestic borrowers and borrowers from other countries would account for 69.2% of total losses. The results of the stress scenario suggest that no credit institution experiences capital deficit that would prevent it from meeting the minimum capital requirements. Chart 3.1 shows changes in the TC ratio of the banking sector under the stress scenario. Chart 3.2 reflects stress test results in significant and other credit institutions.

Table 3.7
Aggregated macroeconomic stress test results

Results	Baseline scenario	Stress scenario
Estimated losses[81] (million euro)	170.9	906.4
Estimated losses (% of total assets of credit institutions)	0.6	3.3
TC ratio		
Number of credit institutions with the TC ratio below 8%	0	0
T1 capital ratio		
Number of credit institutions with T1 capital ratio below 6%	0	0
CET1 capital ratio		
Number of credit institutions with CET1 capital ratio below 4.5%	0	0

Chart 3.1
Changes in the TC ratio under the stress scenario by loss component and other corrections, and the expected profit for 2026 (% of TREA)

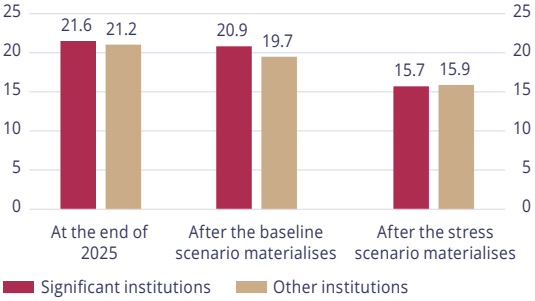


* The profit projection before taxes and before provisioning expenses for loans and securities.

*The profit projection before taxes and before provisioning expenses for loans and securities.

Source: Latvijas Banka (COREP data) and its calculations.

Chart 3.2
TC ratios under stress test scenarios (% of TREA)



Source: Latvijas Banka (COREP data) and its calculations.

[79] The results of the stress test in the baseline scenario cannot be considered a capital ratio projection for 2026. First, the stress test was conducted under the assumption of a constant balance sheet of banks. Second, the assumption that customers from Russia and Belarus, as well as those whose country risk has been transferred to Russia and Belarus, will fail to fulfil their obligations in full is rather conservative. Direct investments in Russia and Belarus do not take into account the transfer of country risk to other countries, e.g. there are many loans whose country risk is transferred to Latvia (e.g. a company's economic activity takes place in Latvia), thus reducing the risk of default. It has also been assumed that all loans, whose country risk has been transferred to Russia and Belarus, are not repaid either. The country risk has been transferred while also taking account of factors such as the country where the collateral is registered and the country where the guarantor is situated. Indeed, the location of the collateral or guarantor in Russia or Belarus increases the risk of losses, but the PD may turn out to be lower than 100%.

[80] Includes losses arising from investments in securities and shares of these countries.

[81] Additional provisions required under the scenarios are indicated, but the expected bank profits are not taken into account.

Liquidity stress test of credit institutions

Prepared by Mārcis Risbergs

The results of the liquidity stress test of credit institutions conducted by Latvijas Banka suggest that their capacity to absorb the shocks caused by potential funding outflows has improved slightly further, while remaining strong overall.

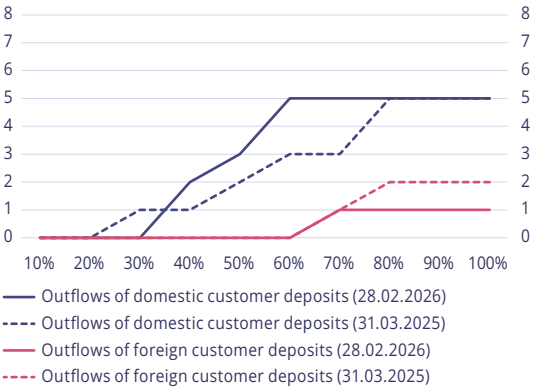
The liquidity stress test is used to evaluate the significance of the potential consequences of funding outflows. It is based on the data available at the end of February 2026[82] and uses consolidated supervisory reporting data on liquid assets and liabilities up to 30 days[83]. The test aims to calculate the liquidity ratio[84], which would be equivalent to the liquidity ratio previously used for banking supervision in Latvia, with a minimum requirement of 30% binding on all credit institutions until the LCR requirements became fully effective.

The methodology from the previous years is used to conduct this short-term liquidity stress test. It helps to obtain an indicator of the resilience of banks to liquidity risks, which is more easily understood[85].

The results of the stress test indicate the tolerance of credit institutions to the outflows of domestic non-MFI customer deposits or of foreign non-MFI customer deposits before their liquidity ratio (and thus the amount of their liquid assets) would decrease to 0, assuming that credit institutions have no access to additional resources to offset the funding outflows.

According to the stress test results (Chart 3.3), **all credit institutions would be able to withstand the outflows of up to 30% of domestic customer deposits or the outflows of more than 60% of foreign customer deposits.** The stress test results have slightly improved compared to March 2025. This was driven by a slight increase in the liquidity ratio of the three largest banks

Chart 3.3
Results of liquidity stress tests (number of illiquid credit institutions[86])



Source: Latvijas Banka (MBP, COREP, and securities statistics data) and its calculations.

due to structural changes in liquid assets at the banking group level. The ability of the largest credit institutions, mainly subsidiaries of Nordic banks with centralised liquidity management and good possibilities to obtain, if necessary, additional liquidity from their parent banks, to withstand the outflows of domestic customer deposits remains lower.

In addition, two particularly adverse scenarios were analysed.

According to the assumptions of the first adverse scenario, it is impossible to pledge or sell the securities portfolio, except euro area government securities with a credit rating no lower than A– and those issued by countries' governments where at least one of the long-term ratings by three international credit rating agencies is AAA. Regarding euro area government securities, it is assumed that they would lose 15% of their value under the first adverse scenario and could be used in Eurosystem's monetary policy operations with a haircut of 3%.

Under the second adverse scenario, in addition to the assumptions of the first, no credit institution has access to overnight claims on credit institutions in the country where it holds the largest volume of such claims, including intra-group claims[87].

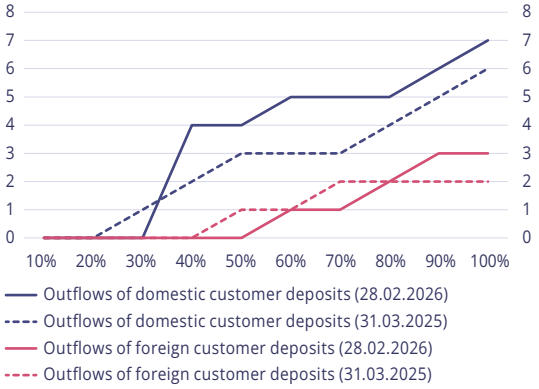
The application of the first adverse scenario does not yield significantly worse results than the standard stress

[82] Data for two small banks are for the end of 2025, as they submit supervisory reports on a quarterly basis.
[83] According to the requirements of the common reporting framework (COREP), a report on additional liquidity monitoring metrics (ALMM) has been prepared on a consolidated basis or, if a bank does not provide reports on a consolidated basis, on an individual bank level.
[84] The ratio of unencumbered liquid assets to the total current liabilities of credit institutions with residual maturity of no more than 30 days.
[85] For a description of the methodology, see Financial Stability Report 2023.

[86] Credit institutions active at the end of February 2026 (nine in total).
[87] For example, if the value of the security portfolio decreases substantially due to turmoil in the global financial markets, the repayment of overnight claims to a credit institution from another foreign credit institution is delayed.

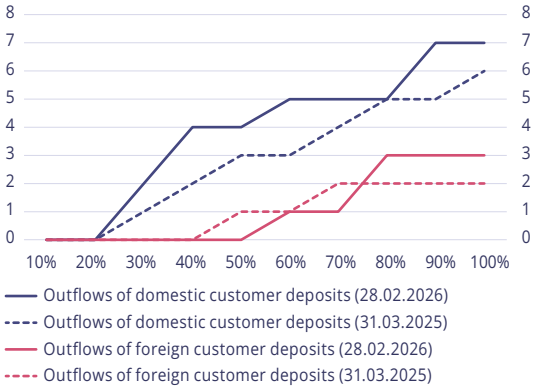
test, and credit institutions **would be able to withstand the outflows of up to 30% of domestic customer deposits or 50% of foreign non-MFI customer deposits** (Chart 3.4). In turn, **the application of the second scenario slightly reduces the ability to withstand outflows of domestic customer deposits – up to 20%** (Chart 3.5). Compared to the previous year, the capacity to absorb outflows of foreign deposits has improved in both adverse scenarios. This is explained by the increasing share of domestic deposits also in banks other than the four largest ones. By contrast, the minimum absorption capacity of domestic deposits has been slightly improved by an increase in the liquidity ratios of the three largest banks, driven mainly by structural changes in liquid assets at the banking group level. **Thus, it can be concluded that the capacity of banks to absorb the shocks caused by potential funding outflows has improved slightly further, while remaining strong overall.**

Chart 3.4
Results of the stress test for the first adverse scenario (number of illiquid credit institutions)



Source: Latvijas Banka (MBP, COREP, and securities statistics data) and its calculations.

Chart 3.5
Results of the stress test for the second adverse scenario (number of illiquid credit institutions)



Source: Latvijas Banka (MBP, COREP, and securities statistics data) and its calculations.

Climate risk stress tests: windstorm risks

Prepared by Jānis Strazdiņš, Nadežda Siņenko, Velga Ozoliņa

Similar to the flood risk stress test conducted in 2023, the assessment of windstorm risk in the Latvian banking sector was carried out at the individual loan and collateral level, with the primary focus on the impact transmitted through the loan collateral channel. Overall, under the stress scenario considered (corresponding to a windstorm with a 200-year return period), approximately 3% of loans secured by real estate collateral are exposed to windstorm risk. However, the potential extent of damage is limited. Consequently, the estimated losses for the resident loan portfolio are modest, amounting to approximately EUR 3.3 million. This represents 0.02% of banks' total resident loan portfolio and 0.01% of banks' total assets.

Selection of wind speed data and scenarios

To identify real estate exposed to windstorm risk, the study used synthetic winter[88] windstorm data for Europe[89] developed by the Copernicus Climate Change Service's Climate Data Store. The decision to use synthetic windstorm data was based on several considerations:

- the dataset covers a much larger number of windstorm events than datasets based on historical observations of actual windstorms, allowing for a more robust estimation of the characteristics of rare but highly destructive windstorms;
- the dataset is generated using a quality, high-resolution climate model that represents physically plausible atmospheric conditions;
- similar datasets are used by insurers in risk analysis.

To assess the impact of a severe yet plausible shock on the loan portfolio of credit institutions, the stress

[88] In Latvia, cyclone activity is more pronounced during the winter months, and severe windstorms occur more frequently and typically affect larger areas (see "Latvija. Zeme, daba, tauta, valsts" (Latvia. Land, Nature, People, State). Riga: University of Latvia Press, 2018).

[89] Copernicus Climate Change Service, Climate Data Store (2022): Synthetic windstorm events for Europe from 1986 to 2011. Copernicus Climate Change Service (C3S) Climate Data Store.

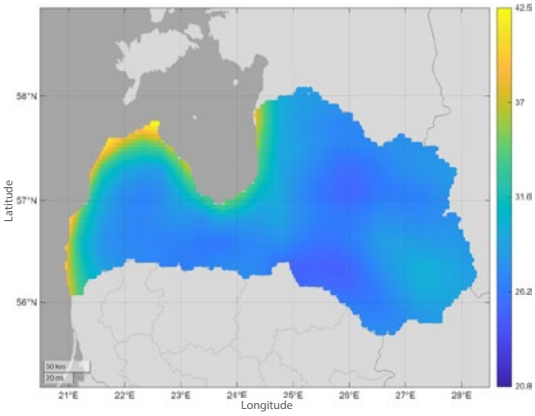
test scenario was calibrated very conservatively: it was assumed that a windstorm with a 200-year return period would occur within the next year (Chart 3.6). To estimate the associated wind speeds, synthetic windstorm events with wind speeds of at least 20.8 m/s were selected according to the Beaufort scale classification of a windstorm[90]. The selected period is 2006–2010, covering 1237 windstorm events and 5946 points at a spatial resolution of 4.4 km. At each observation point, extreme wind gust values were estimated using a non-parametric kernel density approach. According to the Beaufort scale, wind speeds in very severe windstorms exceed 28.5 m/s. Wind speeds of this magnitude, corresponding to a 200-year return period, are expected to affect approximately 25% of Latvia's territory.

Linking buildings and loan collateral to windstorm risk

Within the methodology, an open dataset of real estate cadastral textual data is used to identify buildings and assess their exposure to windstorm risk. This dataset provides information on building cadastral identifiers, associated real estate cadastral numbers, corresponding codes from the State Address Register (VARIS), and the primary load-bearing construction material of buildings. In addition, data from the State Address Register, where geographic coordinates are assigned to each address code, are used. By combining these two datasets, structured information is obtained for each building, including its construction material and location. This data layer is essential, as the wind gust intensity varies spatially, while potential losses in real estate value depend both on wind intensity at the specific point and on the type of building construction material.

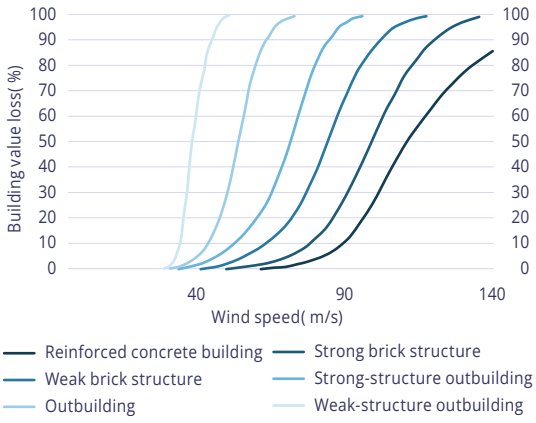
To integrate building data into the windstorm impact assessment model, the nearest point of the windstorm intensity model is assigned to each building based on its coordinates, thereby linking it to the projected wind gust intensity. Loss functions used in the methodology (Feuerstein et al. (2011)) are defined for six standardised building material categories (e.g. concrete buildings, strong brick structure, outbuilding, etc.), whereas the cadastral database contains a significantly more detailed and granular material classification.

Chart 3.6.
Wind gust speeds reached across the territory of Latvia with a 200-year return period (m/s)



Sources: Climate Data Store, Latvijas Banka's calculations.

Chart 3.7
Building value loss (%) **as a function of wind speed** (m/s) **by building material category**



Source: adapted from Feuerstein et al. (2011)[91].

To ensure a consistent mapping to the categories used in the loss functions, an LLM-based approach was used for the automated classification of non-residential buildings, while residential buildings were classified by an expert, taking into account a narrower and well-defined set of materials.

For the estimation of potential losses, functions linking wind speed to the share of real estate value loss were applied (Chart 3.7). These functions are calibrated for Central Europe and are also used by the ECB[92].

The linking of building data with credit institutions' collateral is based on the approach used as part of the

[90] Beaufort scale, Latvian Environment, Geology and Meteorology Centre.

[91] Feuerstein et al. (2011). Towards an improved wind speed scale and damage description adapted for Central Europe. *Atmospheric Research*, 100, pp. 547–564.

[92] See *Climate change-related statistical indicators*.

flood risk stress test[93]. The cadastral number serving as the collateral identifier in the Credit Register of Latvijas Banka is used to identify loan collateral and retrieve the corresponding buildings from the cadastral database. In cases where only non-residential buildings are linked to a given collateral, real estate value losses are calculated as a floor-area-weighted average based on the total floor area of each building. Thus, the significant heterogeneity (diversity) within the non-residential building group is taken into account, as a single location may include production facilities, warehouses, sheds, greenhouses, and other lightweight structures exposed to substantially different levels of damage risk under windstorm conditions.

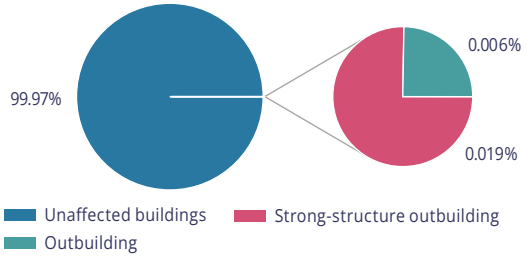
The results show that, within the analysed wind speed categories, the projected wind gusts are not sufficient to cause significant damage to concrete and well-constructed brick buildings; consequently, the projected share of potentially affected residential buildings is very small (Chart 3.8). In the segment of non-residential buildings, the number of potentially affected objects is significantly higher (Chart 3.9), as a substantial share of this stock consists of structurally weaker buildings. However, when translating these results into bank balance sheets and capital adequacy assessment, the overall impact on the financial sector is limited, and the estimated losses do not exceed conservative risk tolerance thresholds.

Windstorm risk in bank loan portfolios

To assess the risk in the loan portfolios of Latvian banks arising from damage to loan collateral caused by windstorms, cadastral numbers of all real estate collateral items recorded in the Credit Register of Latvijas Banka were extracted. These were linked to the corresponding real estate objects and their locations on windstorm exposure maps, and a value loss of each property was estimated in accordance with the methodology described above.

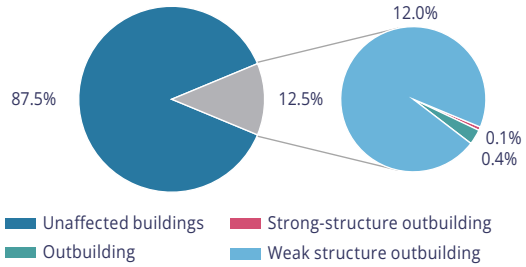
Where a single non-residential real estate object comprises more than one building (i.e. where multiple buildings share the same cadastral number) and these buildings belong to different construction material categories, the assigned damage intensity is aggregated into a single value for the entire real estate object by calculating an area-weighted average across the buildings within the object. As cadastral data are sufficiently detailed and also include small, lightweight structures, there are relatively many cases where large real estate objects (e.g. warehouse or industrial complexes) contain such minor lightweight structures. As a result, the object is included in the list of windstorm-exposed buildings, but the resulting damage intensity for the property as a whole is negligible.

Chart 3.8
Distribution of residential buildings in Latvia (a total of 390 thousand buildings in the cadastre) by building material type category and exposure to damages under the selected scenario



Sources: Cadastre Information System, Latvijas Banka's calculations.

Chart 3.9
Distribution of Latvian non-residential buildings (total in the cadastre exceeding 1.2 million) by material categories and exposure to damage under the selected scenario



Sources: Cadastre Information System, Latvijas Banka's calculations.

The share of windstorm-exposed objects[94] (Chart 3.10) **among all loans secured by real estate collateral recorded in the Credit Register of Latvijas Banka is uneven. In the segment of non-residential buildings securing loans to non-financial corporations (NFCs), the share of exposed properties exceeds the national average and is close to 20%, while properties with substantial damage intensity (i.e. exceeding 5%) account for less than 2% of all collateral items. In the residential building segment, the share of windstorm-exposed objects**

[93] Strazdiņš, J., Siņenko N., "Climate risk stress tests: focus on flood risk", macroeconomics.lv, 03.04.2023. (available in Latvian only); see Financial Stability Report 2023 pp. 46-49 for English translation [https://datnes.latvijasbanka.lv/fsp/FSP_2023_EN.pdf]

[94] Windstorm-exposed objects are real estate properties for which a storm with a 200-year return period would cause damage and a full or partial loss of value.

is considerably lower than the national average, amounting to only 0.016%. Even when considering all buildings together, including those not serving as loan collateral, it can be concluded that the share of windstorm-exposed buildings in the residential building segment is very low.

The impact of windstorm risk materialises primarily through two channels: loss given default (LGD) in the event of the borrower's default, and an increase in the probability of default (PD). LGD rises due to a decline in the value of collateral located in the affected area. The damage is determined by the intensity of wind gusts and the construction material of the building. Damages may be expressed either in terms of property reconstruction costs or as a damage factor. The amount of losses is also influenced by insurance coverage. In turn, PD increases when a borrower's ability (if the borrower incurs losses as a result of the windstorm) and/or willingness (if the collateral value falls below the loan amount) to repay the loan deteriorate.

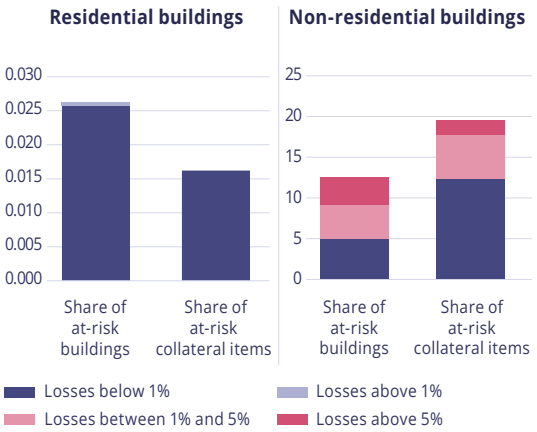
Calculation of banks' losses

After applying the damage factor to collateral items located in windstorm-affected areas, the overall LGD value for a loan is calculated by aggregating the total value of all collateral securing the loan[95] (including also collateral items located outside windstorm-affected areas) and relating the resulting collateral value to the outstanding loan balance. If the collateral value has declined by at least 20%, an additional 30% haircut is applied, reflecting the reduction in the collateral value in the event of a forced sale.

It is then assumed that all loans for which the total collateral value has declined by at least 20% are assigned a PD of 1, i.e. all borrowers whose loans are significantly affected by windstorm risk are assumed to be unable to meet their obligations and to default, with the outstanding exposures being recovered through the available collateral. Furthermore, **it is assumed that windstorm-related losses are not covered by insurance**; i.e. insurance does not reduce borrowers' expected losses. The same approach is applied to both NFCs and households. The calculations are based on data as of December 2025, to facilitate comparison with the results of the regular banks' stress test.

[95] In calculating the collateral value, the allocated collateral value is also taken into account. The allocated value differs from the full collateral value where the same collateral has been pledged against multiple obligations.

Chart 3.10
The total share of buildings and loan collateral items exposed to windstorm damage among all buildings of the respective type (residential and non-residential) recorded in the cadastral register, and among the corresponding types of collateral[96], broken down by damage intensity (% of the total value)



Sources: Data from the Credit Register of Latvijas Banka, the Cadastre Information System and the State Address Register, and Latvijas Banka's calculations.

The estimated direct losses arising from windstorms through the collateral channel are low, amounting to EUR 0.48 million. **They represent only 0.005% of banks' total portfolio of resident real estate-secured loans.** Of these losses, 69% arise from residential mortgage loans to households, while the remaining 31% relate to real estate-secured loans to non-financial corporations (NFCs).

The residential building stock is not materially exposed to windstorm risk in any way that would have a systemic impact on collateral values. Although the risk of damage is higher for non-residential buildings, the decline in value of the majority of real estate properties does not exceed 1% of their total value. Furthermore, corporate loans are typically backed by multiple collateral assets. As a result, only a small number of loans exceed the loss threshold of a 20% decline in the total collateral value.

To capture, to the extent possible, **the indirect losses arising from windstorms**, it is assumed that, for corporate borrowers, default on at least one real

[96] A collateral object may include multiple buildings, including both residential and non-residential ones (e.g. a private house with a garage, shed, or greenhouse). If at least one residential building is included, the entire collateral value is allocated to residential buildings. There may be cases where a real estate property consists of multiple structures and only part of them is exposed to windstorm damage; in such cases, the proportion of value loss for the real estate object is calculated as a floor-area-weighted average across all buildings.

estate-secured loan triggers default on all of the borrower's remaining obligations, including both unsecured loans and real estate-secured loans whose collateral has not been directly affected by windstorm damage. While the number of such loans is limited, the associated losses (EUR 2.8 million) exceed the direct losses from mortgage loans by nearly an order of magnitude (Chart 3.11).

Overall, the estimated storm-induced losses are limited, amounting to approximately EUR 3.3 million. They account for only 0.03% of banks' total portfolio of resident real estate-secured loans (0.02% of banks' total resident loan portfolio and 0.01% of banks' total assets). Thus, the impact of windstorm risk can be assessed as relatively immaterial, given the conservative nature of the scenario.

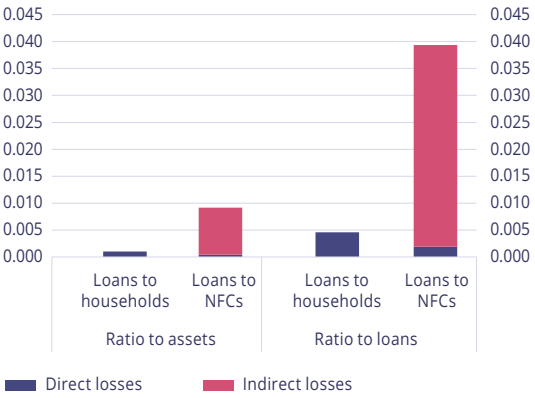
Conclusions

The impact of windstorm risk can be assessed as relatively[97] immaterial: under the scenario considered, total losses would amount to only 0.03% of banks' total portfolio of resident real estate-secured loans and 0.01% of banks' total assets.

In the residential building segment, the number of buildings exposed to windstorm damage is negligible. This is attributable to the modelled wind intensity and the fact that the residential building stock is predominantly constructed of brick or concrete-equivalent materials, which would not be significantly affected by the respective wind intensity. Although the results are affected by nuances in wind intensity modelling, and and in some locations wind gusts may occasionally be stronger and affect even more resilient buildings, an assessment of Latvian residential buildings as a whole allows to conclude that **the residential housing stock is not materially exposed to windstorm risk in a way that would lead to a significant systemic impact on collateral values**.

Meanwhile, non-residential buildings comprise a much broader range of structures, including many outbuildings and auxiliary structures (including very small facilities like guard huts, greenhouses, and wooden sheds), whose construction materials are is significantly more vulnerable to windstorm damage.

Chart 3.11
Potential windstorm-related losses in the banking sector (as a percentage of the total banking sector assets; as a percentage of the corresponding loan portfolio)



Accordingly, the number of non-residential buildings exposed to damage is larger. However, given that such small structures often account for only a minor share of the total floor area within a real estate property, the group of non-residential buildings exposed to damage also includes a substantial number of collateral items for which the proportion of value loss in the real estate property is negligible (below 1% of its total value).

As corporate loans are typically secured by multiple collateral items, the total direct losses from windstorm damage remain low. Although indirect losses arising from other loans to affected corporate borrowers are higher than direct losses, they are also limited.

The accuracy of the loss estimates could be further improved by identifying the location[98] of the main production facilities of borrower companies.

[97] For comparison, losses estimated in the 2023 flood risk assessment amounted to 0.1% of banks' total assets, whereas losses projected in the 2026 macroeconomic stress test reached 3.3% (see the Section "Credit risk and market risk shock absorption capacity stress tests").

[98] Data on the location of companies' main production facilities are not available to Latvijas Banka.

4. Macroprudential policy

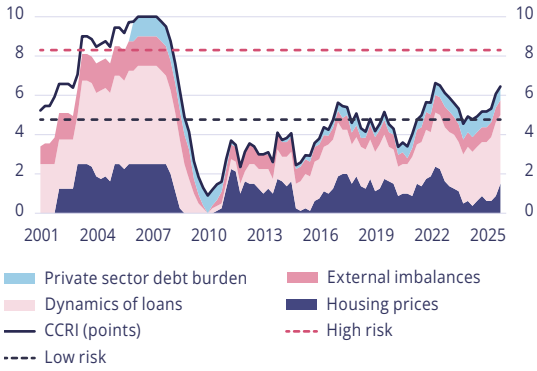
Prepared by Dace Antuža

Latvijas Banka's macroprudential policy stance is aligned with its assessment of financial stability risks and the resilience of the financial sector. As part of a positive neutral CCyB approach, the CCyB rate further strengthens credit institutions' resilience and creates macroprudential space, which is particularly important amid heightened external uncertainty. In 2025, Latvijas Banka reviewed its analytical framework for identifying O-SIIs and for calibrating the O-SII capital buffer rate. This enables a more appropriate identification and designation as O-SIIs of those institutions that are systemically important to the Latvian economy (the number of O-SIIs has decreased from five to three institutions), as well as a broader application of proportionality in the supervision and resolution of financial market participants. Borrower-based measures enforce sustainable lending standards.

Overall, Latvijas Banka's macroprudential policy is aimed at maintaining resilience. This policy is in line with the ECB Governing Council statement on macroprudential policies of 7 July 2025, in which the ECB indicated that, in light of geopolitical and macro-financial uncertainties, maintaining the resilience of the banking sector remains the primary objective of macroprudential policy. Accordingly, Member States are encouraged to maintain existing capital buffer requirements, while those with lower levels of effectively usable capital buffers are advised to strengthen them. A targeted review of capital buffer rates is possible if sufficient macroprudential space is preserved. Borrower-based measures should be maintained, while Member States that have not yet introduced such measures are encouraged to implement them as permanent structural safeguards.

As part of a positive neutral CCyB approach, the 1% CCyB rate requirement took effect on 18 June 2025[99]**.** According to this approach[100], the CCyB rate is maintained at a positive base level of 1%. This already applies under standard risk conditions or at the neutral stage of the financial cycle when the cyclical systemic risk is neither elevated nor significantly low. In the event of increasing cyclical systemic risk, the CCyB rate is raised proportionately to its intensity, starting from a base rate.

Chart 4.1
Composite cyclical risk indicator



Sources: CSB, Latvijas Banka (MBP data, balance of payments data, Credit Register, financial accounts data, and MFI interest rate statistics), and its calculations.

According to Latvijas Banka's assessment, **the cyclical risk is gradually increasing; at this stage, however, the CCyB cyc-lical component should not be increased.** In the fourth quarter of 2025, the CCRI reached 6.5 points (1.3 points higher than a year earlier) and remained within the medium-risk range (Chart 4.1). The increase in the CCRI was driven by growth in lending and housing prices. Lending activity was supported by the materialisation of the pent-up demand as interest rates became more attractive, as well as by stronger economic growth. However, the recovery in lending is taking place from a persistently low base and is partly influenced, among other things, by the temporary solidarity contribution. It cannot be ruled out that lending growth may moderate once the period of application of the solidarity contribution has ended. Moreover, further lending and economic development may be constrained by external factors, including the ongoing war in the Middle East and other geopolitical risks. The credit-to-GDP ratio of the private non-financial sector remains low, while the financial resilience of borrowers remains good. Banks' balance sheet resilience indicators – capitalisation, profitability, and asset quality – are also very strong. The real estate market as a whole is in a phase of moderate growth.

[99] On 18 December 2023, Latvijas Banka decided to start implementing a positive neutral CCyB approach and gradually increase the CCyB rate (General Administrative Act No 444/10 of Latvijas Banka "On setting the countercyclical capital buffer rate for exposures to residents of the Republic of Latvia at 1%" of 18 December 2023).

[100] Latvijas Banka's approach to the application of the countercyclical capital buffer rate.

In 2025, **Latvijas Banka reviewed and enhanced its analytical framework for identifying and designating O-SIIs and for calibrating the O-SII capital buffer rate** (Appendix 4 "Latvijas Banka has reviewed its analytical framework for identifying and designating O-SIIs and for setting the O-SII capital buffer rate). The O-SII identification methodology has been refined to better reflect the specific characteristics of countries with relatively smaller financial sectors and to reduce the sensitivity of the methodology to individual systemically insignificant financial transactions of credit institutions, which, in the context of a small financial market, may have a disproportionately large impact on assessment results.

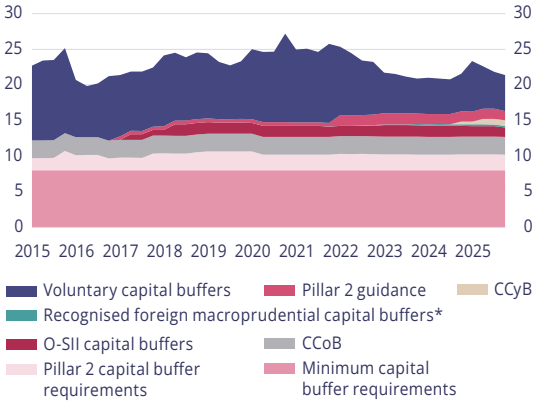
In accordance with Latvijas Banka's new approach, the 10 000 basis points used in the O-SII identification calculation, as recommended in the EBA Guidelines[101] and allocated for the distribution of systemic importance scores among banks, are weighted (normalised) using a coefficient derived from a ratio of the Latvian banking sector assets-to-GDP ratio to the EU average.[102] Latvijas Banka considers that the normalised total number of basis points allows for a more appropriate identification of systemically important institutions in the Latvian financial sector.

On 15 December 2025, **Latvijas Banka identified and designated three institutions – Swedbank Baltics AS[103], AS SEB banka, and AS Citadele banka – as O-SIIs.** AS Rietumu Banka and BluOr Bank AS are no longer identified and designated as O-SIIs. The effect of no longer applying O-SII requirements to these two institutions amounts to 0.06% of the banking sector's TREA and does not reduce the overall resilience of the banking sector.

The improvement of the O-SII identification and designation methodology enables:

- a better alignment of the practical implementation of the EU regulatory framework with the specific characteristics of Latvia's financial system;
- the identification and designation as O-SIIs of only those credit institutions that are systemically important to the Latvian economy;
- the simplification of regulation where appropriate, without reducing the overall level of resilience of the financial system, while providing additional scope for a broader application of proportionality in the supervision and resolution of financial market participants.

Chart 4.2
The capital requirements for Latvian credit institutions and their voluntary capital buffers (% of TREA)



* Credit institutions are also subject to CCyB requirements set in foreign jurisdictions and to other capital buffer requirements that are reciprocally recognised by Latvijas Banka, provided that they have exposures falling within the scope of those requirements.

Source: Latvijas Banka (COREP data) and its calculations.

In 2025, **Latvijas Banka also changed the methodology for setting the O-SII capital buffer rate, transitioning from the model of equal expected impact to an interval approach**. Most other EU countries have adopted this approach, and it offers greater transparency and comparability across EU countries.

Taking into account changes in the relative systemic importance of credit institutions, as well as the revision of the methodology for setting the O-SII capital buffer rate, **AS SEB banka and AS Citadele banka have been subject, since 22 December 2025, to an O-SII capital buffer rate that is 0.25 percentage points lower (1.50% and 1.25% respectively), while for Swedbank Baltics AS (and, at the individual level, for Swedbank AS) it has remained at 2.0% of TREA**.

The range of macroprudential measures in place in Latvia is summarised in Table 4.1, while the set of capital requirements is shown in Chart 4.2.

[101] EBA Guidelines (EBA/GL/2014/10) of 16 December 2014 EBA Guidelines (EBA/GL/2014/10) of 16 December 2014 on the criteria to determine the conditions of application of Article 131(3) of Directive 2013/36/EU (CRD) in relation to the assessment of other systemically important institutions (O-SIIs).

[102] The number of points of the systemic importance score of Latvian credit institutions was normalised by multiplying the 10 000 points specified in the EBA Guidelines by a coefficient of 45.9%, calculated as the ratio of Latvia's financial sector assets-to-GDP ratio to the corresponding EU average (Eurostat data for 2024). As a result, the aggregate normalised systemic importance score of all Latvian credit institutions amounts to 4589 points.

[103] The O-SII capital buffer requirement applies to Swedbank Baltics AS at the level of the prudential consolidation group, and to Swedbank AS at the sub-consolidated and individual levels.

Borrower-based measures remain unchanged. Data from the Credit Register of Latvijas Banka on the maturity, LTV, DSTI and DTI breakdown of new housing loans indicate that the overall trends in credit institutions' lending standards have remained broadly unchanged. **Maturities on new housing loans have been gradually increasing**; however, the pace of increase has slowed compared with the period of elevated interest rates. In 2025, the average maturity of new housing loans was 21.9 years (Chart 4.3).

Data on DSTI and DTI values at the individual loan level that have been available in the Credit Register of Latvijas Banka since November 2025 indicate that **housing loans are being granted at rather prudent DSTI and DTI values** – in the first quarter of 2026, the average DSTI for new housing loans was 30.0%, while the average DTI was 3.8. The share of loans with a DSTI value exceeding 45% in new housing loans stood below 1%, while the share of loans with a DTI value exceeding 8 stood below 0.3% (Chart 4.4).

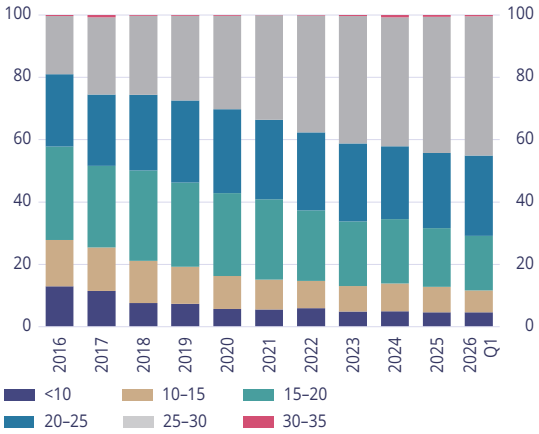
At the same time, **the distribution of LTV values shows an increasing share of loans with higher LTV values**. In 2025, the average LTV value for new housing loans was 79.9%, and one third of new housing loans had an LTV ratio above 90%. Changes in the distribution of LTV values continue to correlate with the intensity of state support programme usage for house purchase[104]. The share of loans granted in 2025 under the state support programme in new housing loans reached 46.9% (Chart 4.5).

The implementation of macroprudential policy in Latvia and other Member States is taking place against the backdrop of an increasingly active debate on the simplification of EU banking regulation. The EC has launched a consultation on the competitiveness of the EU banking sector and the single market. In late 2025, the ECB High-Level Task Force published a report setting out proposals for regulatory changes.

Since the middle of 2025, **macroprudential decisions in other EEA countries have primarily involved increases in the CCyB rate** (e.g. in Croatia, Bulgaria, and Belgium) and **revisions to borrower-based measures.** These included the introduction of LTV and DTI limits for buy-to-let housing loans in Czechia; the relaxation

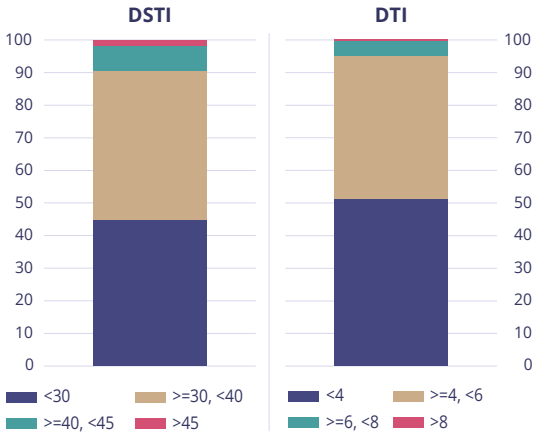
[104] The maximum LTV value for loans secured by a mortgage on real estate and a state guarantee in accordance with the Law on Assistance in Solving Apartment Matters is set at 95%.

Chart 4.3
Maturity breakdown of new housing loans (in years)



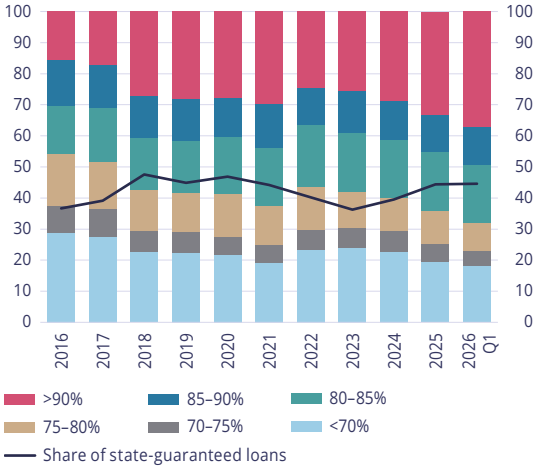
Source: Latvijas Banka (Credit Register data) and its calculations.

Chart 4.4
DSTI and DTI breakdown of new housing loans in the first quarter of 2026 (%)



Source: Latvijas Banka (Credit Register data) and its calculations.

Chart 4.5
LTV breakdown of new housing loans and share of loans granted under the state support programme in new housing loans (%)



Source: Latvijas Banka (Credit Register data) and its calculations.

of the LTV limit and the review of loan amortisation requirements in Sweden; revisions to certain aspects of the DSTI limit and the differentiation of the LTV requirement between first-time and repeat mortgage borrowers in Lithuania; an increase in the LTV limit and in the tolerance margin for borrower-based measures in Iceland; and refinements to the borrower-based measures framework in Hungary.

Table 4.1
The macroprudential policy measures that are currently in place in Latvia

Measure	Rate	Effective and decision dates
Countercyclical capital buffer; CCyB	1%	18.06.2025 (decision taken on 18.12.2023)
O-SII (other systemically important institutions) capital buffer	Swedbank Baltics AS – 2% Swedbank AS – 2% AS SEB banka – 1.50% AS Citadele banka – 1.25%	22.10.2025 (decision taken on 15.12.2025) Reviewed on an annual basis
Loan-to-value (LTV) ratio	90% for all consumer credits exceeding 100 minimum wages and secured by a mortgage on real estate	12.06.2007 (amendments to the law were adopted on 17.05.2007)
	95% for loans secured by a mortgage on real estate and a state guarantee in accordance with the Law on Assistance in Solving Apartment Matters	25.09.2014 (amendments to the law were adopted on 18.09.2014)
	70% for buy-to-let housing loans or other housing loans generating income*	01.06.2020 (regulatory amendments were adopted on 27.11.2019) (regulatory amendments introducing higher DSTI and DTI limits for loans granted for the purchase of energy-efficient housing were adopted on 18.12.2023 and took effect as of 01.01.2024)
Debt service-to-income (DSTI) (the total monthly amount of loan payments to financial institutions to the borrower's monthly net income)*	40% 45% for loans for the purchase of energy efficient housing	
Debt-to-income (DTI) ratio*	6 times 8 times to loans issued for the purchase of energy efficient housing	
Loan maturity limits*	30 years for mortgage loans 7 years for consumer credits	

*the tolerance margin may not exceed 10% of new loans granted to natural persons in a given quarter.

5. Developments and risks in the non-bank financial sector

Prepared by Kārlis Ločmelis and Kristīne Petrovska

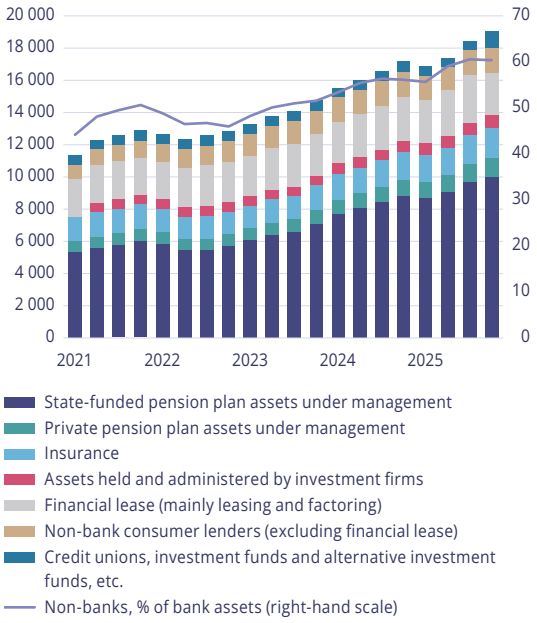
In 2026, against the backdrop of elevated uncertainty and the war in the Middle East, weak economic growth and expected inflation will present further challenges for savings service providers and for the profitability of the non-life insurance sector. High costs further strain the sustainability of investment firms' business. Divergence between the supervision of the crypto-industry in the EU and the rest of the world, closer ties between the crypto-industry and the financial sector, as well as consumer optimism regarding crypto-assets may create vulnerabilities to financial stability in the future.

In 2025, the non-bank financial sector experienced moderate growth. The assets of this sector increased overall by 11.2% compared to 16.7% in 2024 (Chart 5.1). Higher contributions to pension funds, increased optimism in financial markets driven by developments in AI, and rising yields contributed to the growth of the non-bank savings service sub-sectors. In 2025, the assets of the non-bank consumer credit service providers increased by 3.4%, while those of financial leasing companies decreased by 5.8% (for more information, see the Section "Lending development").

Investments by the Latvian credit institution sector in the non-bank financial sector remain moderate. According to Latvijas Banka's financial accounts statistics, in 2025 the assets of the participants of Latvia's non-bank financial sector accounted for 12.4% of the total assets in the structure of assets of credit institutions (10.5% in 2024), while their liabilities made up 10.8% of the total liabilities (10.5% in 2024)[105].

The continuity in the availability of non-bank financial sector services in Latvia's financial system is high, since the exit of a market participant would be offset by other participants providing similar services necessary for the functioning of the financial system, as market concentration is relatively low. The role of Latvia's non-bank financial sector in the financial industry and economy remains considerably less significant compared to other euro area countries. This is primarily due to the low level of long-term savings of the population, as Latvians have accumulated savings over a shorter period compared to many other euro area countries. Nevertheless, household investment has continued to grow in recent years, including in riskier assets such as securitised credit claims placed with investment firms. However, the average financial literacy of the Latvian population and companies (which, for the population, is below the OECD average[106]) is also an important consideration.

Chart 5.1
Assets of the non-bank financial sector by sub-sector (billion euro) **and in relation to credit institutions' assets** (%)



Source: Latvijas Banka's statistics (1-fp quarterly report, MBP and supervisory reports) and calculations.

[105] Although credit institutions have limited exposures to the non-bank sectors in their consolidated assets, they own the majority of pension managers and financial leasing companies. While credit institutions have limited direct exposure to the risk of a decline in the value of the non-bank financial sector's assets – since this sector does not represent a significant share of the credit institutions' income – the profitability of the non-bank financial sector still affects them indirectly.

[106] For Latvia, 59 points on a 100-point scale, OECD average of 63 points. See OECD (2023), OECD/INFE 2023 International Survey of Adult Financial Literacy, OECD Business and Finance Policy Papers, No 39, OECD Publishing, Paris.

Savings service providers

Household savings for retirement purposes account for the largest share of the non-bank financial sector's assets. At the end of 2025, the funds accumulated under the state funded pension scheme amounted to 53.4%, while the assets of the 3rd pillar pension scheme made up 6.2% of the total assets of the non-bank financial sector.

2025 was a volatile year for stock markets. The main fluctuations were driven by US trade policy and tariffs announced by the US administration. The US government reduced tariffs during the year. This, together with other factors, allowed stock prices to recover and rise. In 2025, the returns on investment plans of the state funded pension scheme and private pension plans reached 5.86% and 5.42% respectively.

Global uncertainty across a number of key areas will continue to have a significant impact on the global economy and the returns on pension investments. Potential trade tensions, de-globalisation, increased investment in defence, concerns about the sustainability of sovereign debt, military conflicts, and other factors may significantly alter the level of investment risk, reprice risk premiums, change the level of benchmark rates, and reduce the value of investments.

The ongoing war in the Middle East caused an energy price shock. **Such an energy price shock simultaneously increases the risk of both recession and inflation and creates a particularly unfavourable environment in financial markets, where the stock price risk is difficult to diversify with bonds and vice versa.**

At the beginning of 2026, the discussion on the introduction of voluntary participation in the state funded pension scheme was re-launched in Latvia. Such a decision would substantially increase the risk of poverty among the population in old age, the long-term risk of poverty in the country, as well as economic inequality in society. This, in turn, would increase public social expenditure and, consequently, also the tax burden required to finance it. In the short term, this would contribute to an increase in inflation, which would, in turn, adversely affect the purchasing power of all savings. The withdrawal of funds from the state funded pension scheme would also increase economic imbalances due to faster consumption growth followed by a slowdown in economic activity.

Insurance corporations

The recovery in the purchasing power of the economy and consumers supported the development of the insurance sector. Although in 2025 the solvency capital ratio (SCR)[107] of insurance corporations slightly decreased, it remains high and provides a buffer for insurance corporations to adjust to higher inflation and financial market volatility caused by the war in the Middle East.

In 2025, the recovery in economic growth, improving household wealth, as well as favourable financial market conditions allowed insurance corporations to achieve positive returns on both assets and investments[108] (Table 5.1).

Table 5.1
Key indicators of insurance corporations

Indicator	2023	2024	2025
Assets (million euro)	1 546.1	1 715.8	1 829.8
ROA of life insurers (%)	0.8	2.2	2.0
ROA of non-life insurers (%)	4.9	4.9	4.5
ROE of life insurers (%)	5.3	16.3	14.8
ROE of non-life insurers (%)	17.5	16.8	15.7
Return on investments of life insurers (%)	5.0	5.5	3.0
Return on investments of non-life insurers (%)	1.6	2.2	2.6

Source: Latvijas Banka's supervisory statistics and calculations.

Life insurance premiums written saw moderate growth in 2025, increasing by 7.5% compared to 2024 (Chart 5.2, panel (a)). By comparison, life insurance premiums written in the EEA rose by an average of 5.7% in the first half of 2025[109]. Life annuities as a pension product remain unattractive from the consumer perspective, and the volume of their premiums declined by 4% compared to 2024. At the same time, life insurance premiums

[107] The available ratio of equity to the solvency capital requirement. The calculation of the solvency capital requirement is based on the assessment of all the risks an insurance corporation is exposed to, including the assessment of the insurance underwriting risk, market risk, credit risk, and operational risk. Each risk module is calibrated according to the VaR method, using a 99.5% confidence level over a one-year time horizon; see Latvijas Banka's Regulation No 376 "Regulation on calculating the insolvency capital requirement and own funds of insurance undertakings, reinsurance undertakings and branches of foreign insurance undertakings".

[108] Investments are all financial assets controlled by an insurer that qualify as financial instruments and are used to cover liabilities, generate income, and manage risk, regardless of whether the investment risk is borne by the insurer or the policyholder.

[109] *Financial Stability Report*, European Insurance and Occupational Pensions Authority, 15 December 2025.

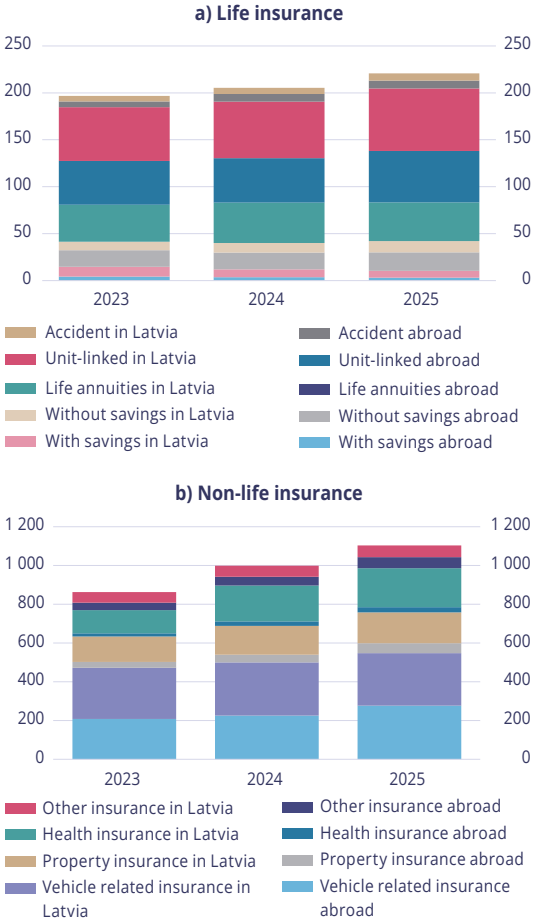
exceed claims by 47% on average (with the exception of life insurance with savings, where claims are 1.4 times higher than premiums written). The potential impact of the war in the Middle East on the life insurance sector is likely to materialise primarily through a decline in the value of investments. These consequences will primarily affect life insurance customers, while the profitability of life insurance corporations themselves will be affected to a lesser extent.

In 2025, the amount of non-life insurance premiums written continued to increase (by 10.5%; Chart 5.2, panel (b)), **as higher costs continued to be passed on to consumers**. In 2025, property insurance premiums continued to grow rapidly (by 28%) due to both the revaluation of coverage amounts and the pricing-in of flood risk following the July 2024 floods. Transport-related insurance stagnated in Latvia (declining by 1% compared to 2024), while increasing by 23% abroad.

The potential impact of the war in the Middle East on the non-life insurance sector may take the form of higher insurance claims if driven by higher inflation-related restoration costs, as well as a decline in the value of the investment portfolio.

The non-life insurance sector is negatively and directly affected by climate change and natural catastrophes. Although the insurance protection gap in Latvia, as currently assessed by EIOPA, is lower than its historical average, it remains higher than the current EEA average[110]. This is partly due to low property insurance coverage levels, with only 31% of the Latvian population having housing insurance, according to Eurobarometer data[111].

Chart 5.2
Annual premiums written by Latvian insurance corporations and branches of foreign insurance corporations[112] (million euro)



Source: Latvijas Banka's supervisory statistics and calculations.

Cross-border activities are important to Latvian insurance corporations, as is the case for insurance corporations in other small markets, since they help diversify and manage risks and promote profitability. In 2025, the share of non-life insurance premiums written abroad in the total amount of premiums written was 37.3% (a year-on-year increase of 3.8 percentage points), while that of life insurance premiums written abroad made up 35.2%, reflecting a rise of 1.8 percentage points.

According to EIOPA's assessment, the main **systemic risks for the insurance sector at the EU level include weak economic growth, fiscal sustainability at the national level, geopolitical tensions, the risk of investment revaluation (including in less liquid**

[110] For EEA floods, the current insurance protection gap is estimated at 1.5 (on a 5-point scale), while for Latvia it is 2 (historically 2.5 for Latvia). EIOPA notes that scores below 3 indicate an insignificant gap. However, unlike the EEA, where historically 20% of losses have been insured, Latvia's data show that only 7% of losses have been insured. This reduces risks for insurers but exerts pressure on national and local budgets. *Dashboard on insurance protection gap for natural catastrophes*, European Insurance and Occupational Pensions Authority, 5 December 2025.

[111] *Latvia: Flash Eurobarometer Consumer trends in insurance services*, European Insurance and Occupational Pensions Authority.

[112] Premiums written abroad include both premiums written by foreign branches of Latvian insurance corporations and those written according to the principle of freedom to provide services.

assets), cyber risk, and the insurance underwriting profitability risk[113, 114].

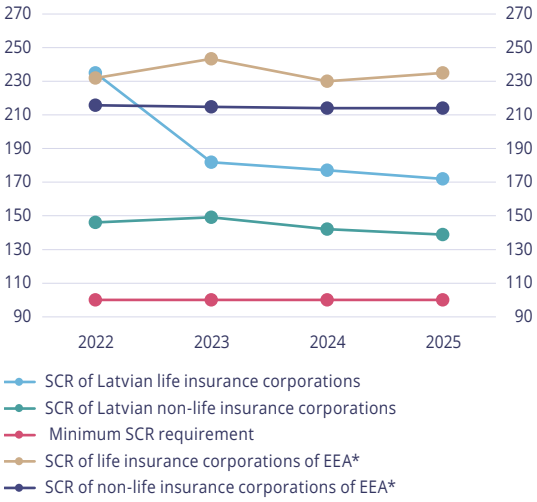
The ability of Latvian insurance corporations to absorb potential shocks remains good, as their **solvency capital ratios remain high** (Chart 5.3), with none of the insurance corporations using exemptions under the regulation[115] to improve the solvency capital ratios. In addition, the share of capital in assets reached 13.5% for life insurance corporations and 28.8% for non-life insurance corporations at the end of 2025.

The risks, particularly those related to climate catastrophes, are alleviated by using reinsurance. In 2025, the proportion of reinsurance in gross premiums written averaged 13% in non-life insurance and 1.9% in life insurance[116]. In the longer term, the availability of reinsurance for Latvia as a small market may become increasingly challenging (and costly), especially if investments in climate change adaptation are not made.

Investment firms offering securitised credit claims (investment platforms)

The value of assets managed by investment firms[117] amounts to EUR 844.3 million, representing a year-on-year increase of 25.1%. The growth was supported by profitability, investor demand, and the financing needs of lenders using these platforms. However, in 2026, the negative sentiment and uncertainty in financial markets may deter investors from reinvesting in alternative, high-risk investments offered by Latvian investment firms. While investment platforms continue to rapidly scale up their business and increase the diversification of their income sources, high personnel costs, among other factors, continue to weigh on business profitability: the average return on equity of the investment firm sector remained negative in 2025 (–30.8%; –22.9% in 2024). High costs pose additional challenges to the business sustainability of a sector that is already dependent on economic and financial cycles.

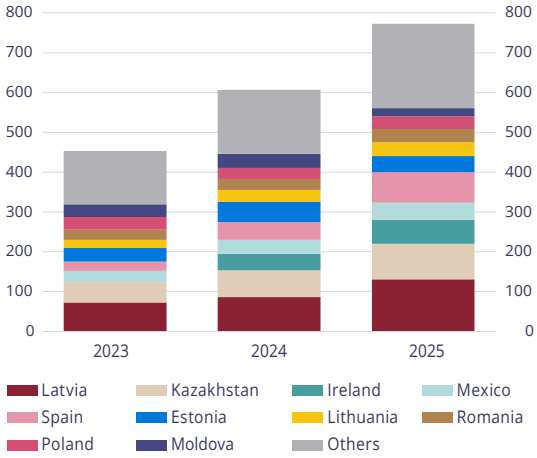
Chart 5.3
Solvency capital ratio of Latvian and EEA insurance corporations (%)



* Data at the end of the second quarter of 2025.

Sources: Latvijas Banka's supervisory statistics and calculations, EIOPA data.

Chart 5.4
Country breakdown of the initial credit risk of securitised credit claims at the end of 2023–2025 (million euro)



Source: Latvijas Banka's data and calculations on the financial position of financial vehicle corporations.

Securities from Latvia, Kazakhstan, Ireland, Mexico, and Spain account for the largest share of credit claims (loans) securitised in Latvia (Chart 5.4). The majority (64.6%) of securitised loans are consumer loans to households. In addition to the risk of not fully

[113] The insurance underwriting profitability risk refers to the risk that an insurer sets premiums improperly, resulting in compensation payouts exceeding the premiums written. For example, inflation is leading to an unpredictable rise in the compensation costs, while the revision of premiums is constrained by competition and the duration of the contracts concluded.

[114] *Financial Stability Report*, European Insurance and Occupational Pensions Authority, 15 December 2025.

[115] Exemptions cover, for example, the long-term guarantee assessment and the term premium applied to the long-term risk-free interest rate used to discount the technical reserves. These exemptions are frequently used by insurers in Germany and, to a lesser extent, in France. For more information, see *Use of limitations and exemptions in Solvency II reporting in the EEA*, European Insurance and Occupational Pensions Authority , October 2025.

[116] The low proportion of reinsurance in life insurance is attributable to the fact that investment risks are primarily borne by the insured person rather than the insurance corporation.

[117] The section only covers those investment firms that are investment platforms, given that they account for 99.7% of the total assets managed by all investment firms.

recovering investments, there is also a risk arising from the unpredictability of the consumer protection framework in the countries of origin of individual credit claims.

The quality of securitised loans is gradually declining. At the end of 2025, 10.5% of the outstanding securitised loan portfolio was more than 30 days past due (7.0% at the end of 2024). Of the loans past due over 30 days, 45.7% did not have a buyback guarantee provided by the original lender (30.5% at the end of 2024). Investors should assess the limited likelihood of fully recovering their initial –if, for example, the original borrowers face significant solvency problems during a downturn in the economic cycle, this may subsequently lead to solvency problems for the original lender that issued the guarantee.

The high investment risk of securitised credit claims stems from their exposure to a broad range of risks: the guarantee risk, the liquidity risk, the credit risk, the risk of legal loopholes, particularly in cross-border (non-EU) activities, the currency risk, the servicer risk related to the management of the securitised loan portfolio, and the originate-to-distribute risk. The sanctions risk also cannot be ruled out.

In Latvia, securitised credit claims have been acquired mainly[118] by private (household) investors from Germany, Latvia, Spain, Czechia, and the Netherlands (the concentration of investors from these five largest investor countries accounted for 64.6% of the total outstanding amount at the end of 2025). The high concentration of investors has remained unchanged in recent years. If the sentiment of investors in a particular country shifts, it poses a potential vulnerability to the business model of the platforms.

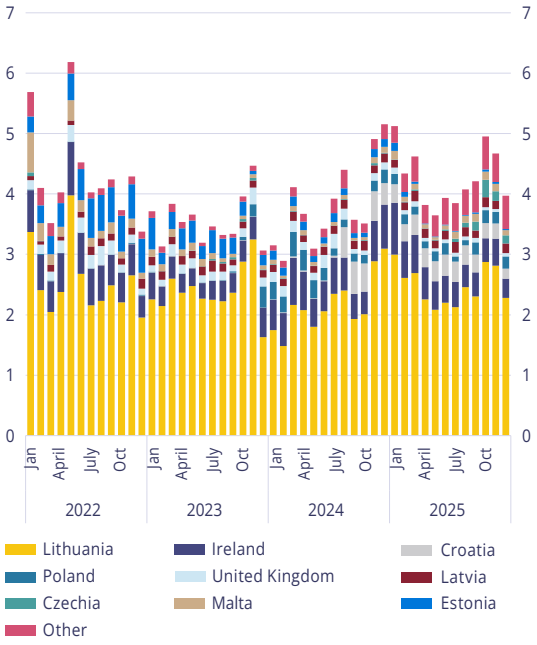
Crypto-assets

Latvian households moderately increased their transfers to crypto-asset wallets, following the growth of the crypto-asset market in 2025. As crypto-asset companies expand globally, their integration into the traditional financial system is becoming increasingly pronounced.

Data from a survey conducted in February 2026 show that the share of people investing in crypto-assets is

[118] Households hold 84% of the investment portfolio (data as at the end of 2025).

Chart 5.5
Payments made with payment cards issued by Latvian credit institutions by country of the crypto-wallet holder's account (amount; million euro)



Source: Latvijas Banka's payment card statistics and calculations.

stable (8%)[119]. The continued popularity is driven both by the new US government's initially positive stance on crypto-assets, including the adoption of stablecoin regulation, which contributed to an increase in their market capitalisation, and by the entry into force of the EU Regulation on crypto-assets and the provision of a new supervisory framework for the EU market.

This is also reflected in the data on payments made by Latvia's residents to holders of crypto-asset wallets with payment cards issued-by Latvian credit institutions[120]. In 2025, the total value of such payments was 11.3% higher than in 2024, reaching EUR 51.2 million (Chart 5.5). The share of on-site payments remains low (1.6%), suggesting that the use of crypto-asset ATMs is not popular in Latvia. The average payment amount also continues to decline: 50% of payments are up to EUR 50 (EUR 60 in 2024), while 77% are up to EUR 100.

Monitoring the extent to which households and other **Latvian economic sectors invest in crypto-assets**

[119] Data from a survey conducted by Latvijas Banka and SIA Latvijas Fakti (9% in 2025). Investments are made primarily by young people with higher incomes.

[120] For more information on the methodology and calculations, see K. Petrovska's article entitled "Prevalence of crypto-assets in Latvia: the first steps of evaluation", www.macroeconomics.lv, 30.12.2021.

through financial instruments[121] – such as exchange traded funds and other types of securities – allows for the assessment of links between traditional financial markets and high-risk assets. Such links may amplify the transmission of volatility to the financial system and influence the behaviour of investors, particularly in the event of rapid market adjustments.

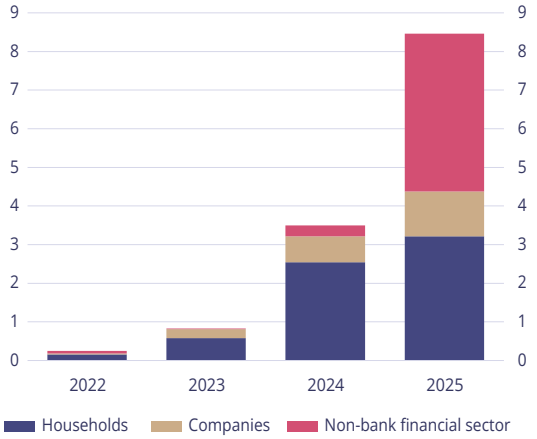
Although such investments are becoming increasingly popular in Latvia, including in the non-bank financial sector, their balance remained insignificant, reaching EUR 8.5 million at the end of 2025 (Chart 5.6). The increase is largely attributable to the non-bank financial sector, including pension funds that track the composition of companies in the S&P 500[122].

A more detailed look at the investments suggests that direct holdings of crypto-assets through trusts, shares in crypto-asset mining companies, and investments in other crypto-asset companies are the most common. **It is households that are more likely to choose to invest through EU financial institutions:** the outstanding amount of investments stood at 55.2% at the end of 2025 (48.3% at the end of 2024), while other sectors more frequently chose Latvian financial institutions.

Although the crypto-asset sector in Europe is becoming more mature, Chainalysis estimates[123] suggest that the global volume of criminal proceeds continues to increase, reaching USD 154 billion in 2025 (a 2.6-fold increase) amid the growing prevalence of sanctions and improved detection of fraudulent payments.

The main risks in the crypto-asset market include ill-considered consumer investments in risky or fraudulent assets, growing links between crypto-asset companies and supervised financial sector participants, high concentration among service providers (leading to potential abuse of market power), and involvement in money laundering and other illegal activities.

Chart 5.6
Investments by Latvian economic sectors through EU[124] financial institutions in securities of crypto-asset companies from 2022 to 2025 (balance; million euro)



Sources: Latvijas Banka's statistics on securities held by Latvian financial institutions and calculations.

[121] For more information on the methodology, see K. Petrovska's article entitled "How common are financial products that provide investment in crypto-assets in Latvia?", www.macroeconomics.lv, 22.01.2025.
[122] In 2025, the S&P 500 included three companies from the crypto-asset sector (Coinbase, Block and RobinHood). Pension fund strategies include replicating the portfolio of S&P 500 companies.
[123] Crypto Crime in 2025 Was Primarily Driven by 694% Surge in State-Driven Sanctions Evasion Volume, chainanalysis.com, 5 March 2026.
[124] Countries that identify Latvian investors: Latvia, Lithuania, Estonia, Ireland, Luxembourg, Italy, Belgium, Croatia, Greece, Germany, Portugal, Czechia, the Netherlands, Bulgaria, Finland, Slovenia, Slovakia, and Spain.

Appendix 1. Extraction of unstructured financial data from appendices to annual reports with artificial intelligence models

Prepared by Jānis Strazdiņš

Latvijas Banka has developed a locally hosted, LLM-based tool that automatically extracts depreciation and amortisation data from the appendices to annual reports at the Register of Enterprises, converting them into a single structured format to be used for empirical analyses. It enables the consistent calculation of EBITDA and the related financial indicators, significantly expanding the availability of detailed financial data to the entire corporate sector and achieving more than 90% accuracy during tests. The developed method is scalable and enables the extraction of other unstructured financial data, enhancing the use of the information made public by companies in financial stability analysis.

Why more detailed data are needed

During the last few years, approximately 36 000 companies have been actively borrowing in Latvia. It means that approximately 250 000 annual reports that contain information on the financial standing and risk profile of these companies can be potentially used for the financial stability analysis (a large part has financial indicators for time series analysis spanning several years).

To assess the **sector-specific credit risks** of the economy both in general and by company size groups and other parameters, **sufficiently detailed financial data are required**. They include various financial indicators (for example, profitability, lever, and liquidity indicators) and their development during various shock periods. The aim is to improve the understanding of:

- the ability of companies to generate sufficient cash flow to cover their liabilities;
- the sensitivity of companies to interest rate, cost, and demand shocks as well as other economic fluctuations, in particular, sector-specific changes.

Such analysis is traditionally based on regression models and other empirical methods that require input data that are as comprehensive as possible. However, the structured financial data that are available in the standard section of the financial statements submitted by companies to the State Revenue Service in the EDS forms do not reflect significant information that is included in appendices to annual reports.

The role of EBITDA and depreciation in assessing credit risk

One of the practical examples that motivated the development of the data extraction tool was the collection of data on the depreciation of the initial value of long-term intangible assets and fixed assets of companies (amortisation). In most cases, depreciation is not separately indicated in the standard P&Ls submitted in the structured EDS format, and cash flow statements that contain information on depreciation are mandatory only for the largest companies. Currently, these data, in a structured format, are available on 4.3 thousand companies, with annual reports of another 32 000 companies available at the Register of Enterprises, allowing for additional information to be extracted. Though their absolute number is smaller, the companies with available detailed information, i.e. the largest companies, constitute 60% of the economically significant borrowers (62% of the total borrower turnover and 66% of the total borrower assets in 2024).

To analyse credit risk, DSCR, ICR, and debt-to-EBITDA ratios are important – EBITDA is one of the calculation components, and its calculation requires information on depreciation. Thus, the availability of depreciation data is a pre-condition for the reliable calculation of EBITDA in the entire corporate sector, comparison of companies and sectors by relying on uniform criteria, as well as the development of models that are more accurate in predicting insolvency and credit risk increases.

Depreciation items are often detailed in the appendices to annual reports, in fixed asset and intangible asset movement tables, segments, or explanatory notes that are not available in the standardised EDS structure.

Structured and unstructured data: a challenge and an opportunity

In the Latvian practice, annual reports of companies consist of two conceptually different types of information.

1. Structured data: P&Ls, balance sheets, and, occasionally, cash flow statements. In the EDS environment, these data are submitted in standardised forms: numbers in fixed columns and formats, one structure for all companies.
2. Unstructured information: appendices to annual reports and explanatory notes that may contain:

- freely worded text (a description prepared by the management, an accountant, or a financial director);
- tables with different structures (for example, on asset movements, segment data, maturity structure of loans, etc.);
- information on depreciation and other important indicators – not in the number fields, but in the text, explanations, or alternative tables.

Moreover, the technical format of these documents varies: e-documents, PDFs, archives (ZIP), and occasionally scanned images. This hinders the automated large-scale extraction of data. The latest AI tools can help in this procedure. Additionally, LLMs are able to process:

- freely composed text with varied structure;
- tables and descriptions, whose form differs from one company to another;
- documents in various formats (by combining the recognition of optical characters (OCR) with semantic understanding).

This gives an opportunity to systematically and automatically extract unstructured financial data from a large number of annual reports.

Solution: an LLM-based data extraction tool to identify depreciation

The tool developed at Latvijas Banka is the first step towards more extensive use of unstructured financial data in analysing financial stability. To prepare the foundation for the automatic extraction of financial indicators, testing the practical efficiency of the LLM technology, and assessing the ability to adjust this tool to large-scale data processing, during its initial stage, the project focussed on one significant data item – depreciation.

The underlying concept and steps in this method:

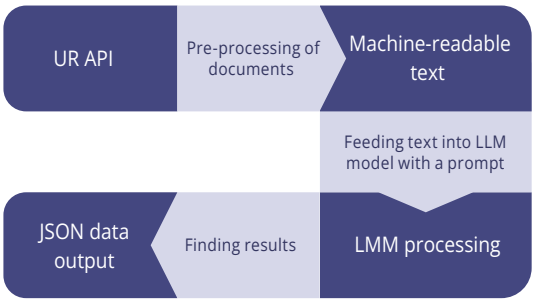
- reading of documents from publicly available data bases;
- extraction of text and tables from various formats with OCR and structuring algorithms;
- use of LLM to semantically identify depreciation and amortisation indicators irrespective of their specific formatting;
- generation of structured outputs (for example, in JSON) that can be directly used during the empirical analysis.

The solution is based on an LLM hosted in the cloud service provided by Azure and used by Latvijas Banka (modified GPT type model) that is adjusted to the depreciation identification task by means of examples and special prompts.

Technical process: from the Register of Enterprises API to structured data

To ensure the repeatability and scalability of the process, a single technical data flow was developed (Chart A1.1).

Chart A 1.1
Schematic diagram of the process



1. **Reading data from the Register of Enterprises API:**

- open data provided by the Register and software API were used;
- annual reports of respective companies were acquired in their original formats (eDoc, PDF, ZIP, etc.).

2. **Technical processing of documents and OCR**

- if the document is available as text, it is converted into structured Markdown, maintaining the structure, headers, and sections;
- if the document is an image (scanned documents), OCR is used to produce a machine-readable text.

3. **Use of LLM to interpret unstructured information:**

a) an LLM hosted in the cloud service provided by Azure and used by Latvijas Banka (modified ChatGPT, model 5.1) was deployed.

b) the model was fed structured document content (text and tables in Markdown);

c) the model was instructed by means of a specialised task description;

   i) depreciation and amortisation items were identified;

   ii) they were identified in various potential locations (P&L explanations, asset movement tables, intangible asset tables, sections of appendices, etc.);

   iii) if these data were not directly marked but could be inferred from the structure of a table, there was an attempt to consolidate them and solve various potential nuances (numbers indicated in thousands, numbers to be summed).

4. Structuring and saving the outputs:

d) LLM outputs are generated in standardized JSON and include:

   i) the identified amount of depreciation (or amounts if categorisation is required);

   ii) financial year of the data;

   iii) a reference (section, page, table) to enable manual verification by an analyst, if needed;

e) data are stored in the data warehouses of Latvijas Banka, supporting their further use in subsequent analyses (for example, in models, aggregations, statistical reports).

5. Testing and accuracy

To assess the reliability of the developed tool several testing stages were completed.

- Comparison with cases, when depreciation is known:
  - o large companies that have clearly stated depreciation in their public cash flow reports were used;
  - o LLM outputs were compared with the manually verified data.
- Random selection tests:
  - o a random selection of companies was made from various sectors and size groups;
  - o depreciation data were manually reviewed and compared with the information extracted by the LLM.

In both testing directions, the achieved accuracy was above 90%, i.e.:

- approximately 94% in the random test;
- approximately 93% in the company test.

In addition, the accuracy was assessed by calculating the approximate accuracy of the achievable final indicator (DSCR) by economic sectors. A selection of known depreciation items was used for the calculation, as a larger number was needed to have a sufficient number of observations in the largest sectors. The accuracy of this method in sectors with at least 10 observations was 94% (when calculating the sectoral weighted average and weighting by the value of liabilities) and 97% (when calculating the arithmetic average in sectors). This level of accuracy allows for the practical use of this tool in macro-level analysis, where a small number of individual deviations do not significantly change the results collected.

Benefits for the financial stability analysis and opportunities for further development

The developed tool allows users to practically achieve the above objective – to use more detailed financial data to eliminate credit risk in the entire corporate sector.

It is important that the tool can be conceptually scaled, and the depreciation data are just the first example. Technologically, a similar approach can be used to extract other data from appendices to financial statements – these data cannot be acquired elsewhere without additional resources. Thus, LLM-based methods give an opportunity to use information that companies already publish in annual reports more comprehensively – until now, this information was almost never available for large-scale quantitative analysis.

This project became possible mostly due to the Register of Enterprises opening the data. It allowed these data to be used with high added value, and the software interfaces provided by the Register and the approach to annual reports allowed for the data to be extracted efficiently.

Latvijas Banka will continue to improve LLM-based methods for processing unstructured data to improve the risk assessment of the financial sector and the corporate sector, strengthening financial stability in Latvia.

Appendix 2. Assessment of long-term effects of capital requirements change on GDP

Prepared by Velga Ozoliņa and Ilze Vilka

Latvijas Banka has assessed the long-term effects of changes in capital requirements on GDP. It demonstrates that in standard risk conditions the long-term benefits of increasing capital requirements are, on average, four times higher than the related initial implementation costs. Furthermore, during the capital risk build-up phase, there is a positive long-term impact on GDP development.

In addition, it was concluded that the optimum level of T1 capital requirements for Latvian banks that would ensure a balance between risk mitigation and capital costs is approximately 15–16%. At the end of 2025, no Latvian bank had a prescribed Tier 1 capital requirement exceeding 15%. This means that the further increase of releasable capital buffers could provide additional long-term benefits for the economy.

Bank capital buffers are similar to a safety net, established to absorb losses. In 2020, with the onset of COVID-19, most countries with CCyB requirements either decreased the rate or waived entirely to prevent a decline in lending and to boost lender confidence. This was the first such case since the creation of these requirements that clearly demonstrated the potential of releasable capital buffers during crises[125]. Since June 2025, Latvia has also introduced a 1% CCyB rate that can be released during a crisis.

The study mostly focussed on two issues:

1) What is the optimum capital requirements level for the Latvian banking sector to ensure that the sector has a sufficient resilience buffer and that the requirements do not have a negative effect on long-term GDP growth?
2) What is the impact of changes in capital requirements on GDP growth in various phases of the financial cycle?

These questions are essential for further decisions on the size of the CCyB rate and the adequacy of the total amount of capitalization for the absorption of potential shocks.

Assessment of the optimum capitalization's level

The usefulness of increasing the capital requirements is often analysed in the context of the optimum capitalization level for the bank sector. From the point of view of regulatory institutions, this is a balance between the objective of creating sufficient resilience buffers and mitigating risks, while avoiding disproportionate capital maintenance costs for the bank sector.

The optimum capital level can be assessed as the net marginal benefit that is calculated by subtracting the costs of increasing and maintaining the capital level from long-term benefits. By applying the *McInerney et al.* (2022)[126] approach, the net marginal benefit of increasing the capital requirements is calculated according to the following equation:

$$NMB = (\Delta Pr_{crisis} \cdot Cost_{crisis}) - \Delta Cost_{cap},$$

where NMB is the net marginal benefit, ΔPr_{crisis} is the reduction of crisis probability, $Cost_{crisis}$ is the potential loss of GDP due to a crisis, while $\Delta Cost_{cap}$ is the decrease in GDP growth attributable to banks maintaining higher capital levels and, consequently, more expensive loans. The first two terms in the equation represent marginal benefits, while the third term – marginal costs.

To assess the probability of a crisis, crises probability assessments from the *McInerney et al.* (2022) study that apply to small, open economies and countries with a high ratio of foreign direct investments were used. The crisis probability assessment that is the most relevant for the Latvian economy (i.e. small, open economy) was used as the baseline scenario, while the other selected scenarios were used as the assessment range. The higher the capital level, the lower the probability of a crisis. As a result, the decrease in the probability of a crisis is calculated as the difference in the probability

[125] At the beginning of the COVID-19 pandemic, some national supervisors also reduced the systemic risk buffer and the O-SII capital buffer. For its part the ECB allowed the credit institutions under its supervision to use the capital conservation buffer and Pillar 2 Guidance to absorb potential losses.

[126] McInerney, N., O'Brien, M., Wosser, M., & Zavalloni, L. (2022), Rightsizing Bank Capital for Small, Open Economies, *Research Technical Paper*, Central Bank of Ireland, Vol. 2022, No. 4.

of a crisis, when the capital level increases by 1 percentage point.

To assess the potential GDP losses in Latvia caused by a crisis, data on the real GDP during the global financial crisis and the post-crisis period, as well as data on the GDP trend from the third quarter of 1996 to the fourth quarter of 2004 (Chart A2.1) were used. This is the period between the 1995 banking crisis[127] and the rapid growth before the global financial crisis. The trend assessed is similar to the Polish GDP dynamic that boasted stable growth during this period.

The following equation is used to calculate GDP loss:

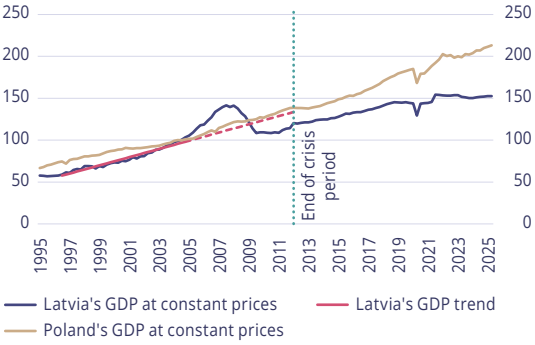
$$Cost_{crisis} = \frac{1}{4}\sum_{qt=1}^{12}\left(\frac{\widetilde{GDP}_{qt}-GDP_{qt}}{\widetilde{GDP}_{qt}}\right)\cdot 100\ \% +$$

$$+\left(\frac{\widetilde{GDP}_{12}-GDP_{12}}{\widetilde{GDP}_{12}}\right)\left(\frac{1-(1+r)^{-t}}{r}\right)\cdot 100\ \%\ ,$$

where $Cost_{crisis}$ is the potential GDP loss due to a crisis, $\widetilde{GDP}$ is the GDP trend, GDP is the GDP in constant prices (seasonally and calendar adjusted data), qt is the time period (sequential quarter) from the moment the real GDP becomes smaller than the GDP trend, r is the discount factor (3%), while t is the timing of the post-crisis effect in years. It is assumed that the length of the post-crisis period is 26 years, i.e. the period until the moment, when the post-crisis GDP trend reaches the pre-crisis trend. After the assessment of the impact of the crisis in Latvia, it was concluded that the total GDP losses of the global financial crisis[128] and the post-crisis period amounted to 215%. According to the practice accepted in publications, the assessed GDP losses are to be considered the maximum limit of crisis costs.

As two of the most important financial institutions in Latvia are subsidiaries of Swedish banks, Swedish data were used in the assessment of marginal costs of increasing the capital. The assessment of *Sveriges Riksbank* was used as the baseline. According to it, any increase of the capital requirements by 1% may result in a long-term decrease of GDP by 0.09%[129] – compared to studies from other countries, this is a conservative estimate[130]. However, to determine the slope and range of the margin costs line, data on the financing costs of Latvian banks in the period from 2006 to 2025 were used.

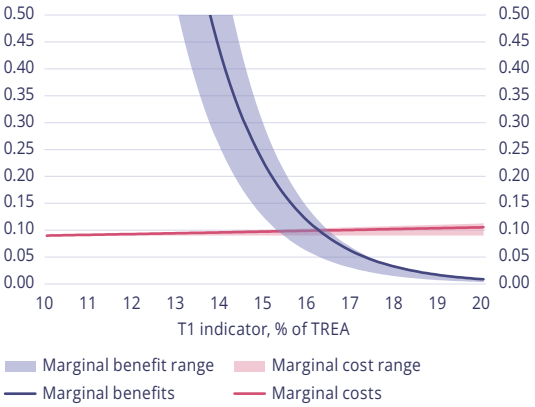
Chart A2.1
GDP of Latvia and Poland in constant prices
(2004 = 100), (%)



Sources: CSP, Eurostat, and Latvijas Banka's calculations.

After a review of marginal benefits and marginal costs, it can be concluded that the optimum T1 ratio in Latvia is 16.2% (in a range from 15.3% to 16.4%, Chart A3.2). At the end of 2025, the average T1 requirement in the banking sector was 13.7%, and for no bank did the capital requirements to be met by T1 exceed 15%. At the same time, the actual T1 ratio for the banking sector is voluntarily maintained at 19.7%. Thus, if needed, there is a capacity to efficiently increase the resilience buffer by 1.6–2.7 percentage points. Such an increase in the capital requirements could still ensure long-term benefits that are higher than the related long-term costs.

Chart A2.2
Assessment of the T1 capital ratio (impact on the GDP; %)



Source: Latvijas Banka's estimates.

[127] Latvijas Banka: 1995 Annual Report: the protracted critical state of execution of the national budget and the banking crisis that started in May 1995 caused the financial crisis. Latvijas Banka limited or suspended the operations of several banks (including, AS Banka Baltija), and during the next few months revoked the licences of several banks.

[128] According to information in the ESRK European financial crises database, the global financial crisis hit Latvia in November 2008 when the government took over AS Parex banka and ended in March 2012.

[129] Almenberg et al. (2017), Appropriate capital ratios in major Swedish banks – new perspectives, *Staff Memo*, Sveriges Riksbank, May 2017.

[130] Data collected by McInerney et al. (2022) demonstrate that in most studies the long-term decrease in GDP was assessed to be 0.02–0.08%.

Assessment of the long-term effects of higher capital buffers

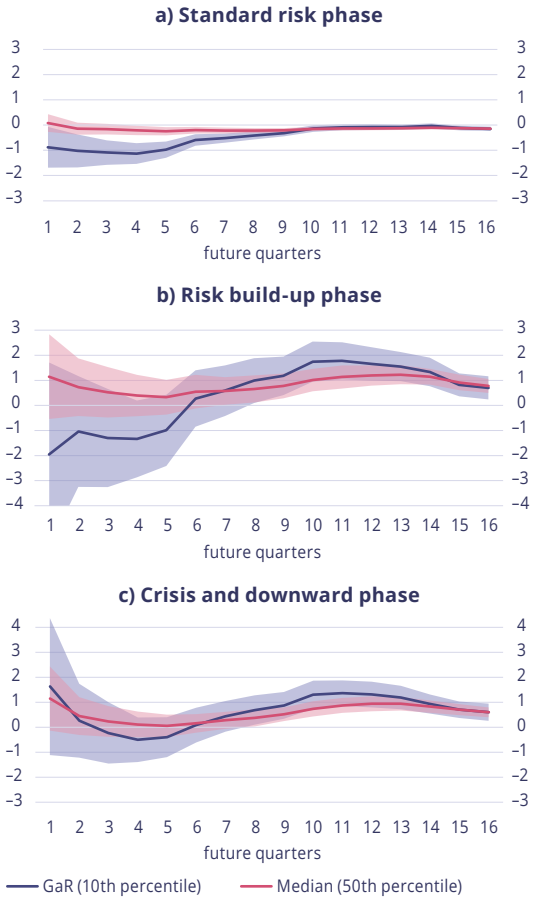
The GaR panel approach was used to assess the long-term effect of changes in capital requirements – it allows for the analysis of these effects during various phases of the financial cycle. This approach was selected in accordance with the basic principles guiding the CCyB rate[131]. The GaR was used in Estrada et al. (2024), Galan and Rodríguez-Moreno (2020)[132] studies. The following equation was used for the assessment:

$$\hat{Q}_{y_{i,t+h}|\alpha_i}(\tau|X_{i,t},\alpha_i) = \hat{\alpha}_{it} + \hat{\beta}_{1t}y_{it} +$$
$$+ \hat{\beta}_{2t}CCI_{it} + \hat{\beta}_{3t}CLIFS_{it} + \hat{\beta}_{4t}CBR_{it} +$$
$$+ \hat{\beta}_{5t}CCI_{it} \times CBR_{it} + \hat{\beta}_{6t}CLIFS_{it} \times CBR_{it} +$$
$$\hat{\beta}_{7t}y_{it} \times CBR_{it}; \quad \tau = 10,50;\ h = 1,\dots,16,$$

where: $y_{i,t+h}$ is the annualised GDP changes during the $t+h$ period in the country i; α_i are the country fixed effects; y_{it} is the GDP changes during the t period in the country i; CCI_{it} is the Common Composite Indicator during the t period in the country i[133]; $CLIFS_{it}$ is the Country-Level Indicator of Financial Stress (developed by Duprey and Klaus)[132] during the t period in the country i; CBR_{it} is the combined capital buffer requirement during the t period in the country i; τ is the assessment percentile. In this case, the 10th percentile equals GaR that represents the development rate during shocks, while the 50th percentile – the median that equals the development rate in normal conditions[134]. Data from EU Member States (except Cyprus, Denmark, Greece, and Ireland) for the period from the first quarter of 2013 to the first quarter of 2025 were used in the assessment.

Three phases of the financial cycle are considered in the cost-benefit analysis: the standard risk phase, the risk build-up phase, and the crisis and downward phase (Chart A2.3). In the context of this study, it is assumed that the standard risk is characterised by the average rate of changes in GDP and a moderate level of systemic risks and financial stress[135]. The risk build-up phase has a higher rate of change in the GDP, increasing systemic risks and low financial stress[136]. While the crisis and downward phase is characterized by decreasing GDP, materialization of risks, and high financial stress[137].

Chart A2.3
Impact of changes in capital requirements* (for 1 percentage point) on the annual GDP growth rate
(percentage points)



Note. The 10th percentile is GaR that represents the growth rate during shocks, while the 50th percentile is the median that equals the growth rate in normal conditions. The coloured areas represent the 95% confidence interval of the assessment. If the coloured area in the respective quarter includes a zero value, the effect on GDP during this quarter is not statistically significant.

* In the standard and the risk build-up phases, the charts represent the impact of increasing capital requirements, while in the crisis and downward phase, the impact of decreasing capital requirements is represented (changes in the capital requirements without a transition period, fully implemented in the zero period).

Source: Latvijas Banka.

[131] The CCyB rate is first increased in the early stages of the cycle, when the cyclical systemic risk is not yet elevated, but is neither significantly low. In the risk build-up phase, when the cyclical risks accumulate, the CCyB rate is increased above the CCyB base rate of 1% depending on the risk intensity. While in the crisis and financial cycle downward phase, the CCyB rate can be reduced or fully released.

[132] Galan, J. E. & Rodríguez-Moreno, M. (2020), At-risk measures and financial stability, *Financial Stability Review*, Issue 39, Banco de España.

[133] CCI is similar to Systemic Risk Indicator (SRI) developed by Lang et al. (2019) without the equity price element (see also 132). To adjust the assessment for Latvia, CCRI was used. For more information on the CCRI see Latvijas Banka's 2025 Financial Stability Report.

[134] In the probability distribution of GDP growth rates, the bottom 10% consists of periods with the lowest GDP growth rates (in Latvia's case, the largest GDP declines), which characterise economic development under conditions of turmoil. Sk. Ozoliņa, V., Siņenko, N., "Mathematical GaRa preparation for shocks: a new model for developing stress test scenarios of credit institutions", makroekonomika.lv, 29.02.2024.

[135] The medians of the GDP growth rate, CCI, and CLIFS.

[136] The 95th percentile of the GDP growth rate and CCI, and the 5th percentile of CLIFS.

[137] The 5th percentile of the GDP growth rate and CCI, and the 95th percentile of CLIFS.

The results indicate that **during a crisis, long-term benefits from releasing capital buffers are higher than short-term costs incurred by increasing the capital requirements during periods of standard risk** (Table A2.1)[138].

- If the capital requirements are increased during the standard risk phase[139], the median GDP growth rate can decrease by 14–25 basis points, while during sudden shocks (characterised by GaR) the annual GDP growth rate would be lower by 41–113 basis points.
- If the capital requirements are increased during the risk build-up phase in the medium term[140], a neutral or positive impact is expected on GDP. The median GDP growth rate could improve to +122 basis points, while during sudden shocks – to +178 basis points. The positive impact can be explained by higher risk absorption capacity, lower ability to accumulate risks, and the smaller probability of a crisis.
- When a crisis and downward phase of the financial cycle starts, and the capital buffers are released, the assessed long-term benefits are significant: the median GDP growth rate is 52–94 basis points higher, while during further shocks it could increase by 60–136 basis points.

Table A2.1.
Impact of changes in capital requirements* (for 1 percentage point) on the annual real GDP growth rates (basis points)

	Impact on the median (50th percentile)		**Impact on the GaR** (10th percentile)	
	short-term	medium-term	short-term	medium-term
Standard risk phase	–16.6	–14.1	–82.7	–12.5
Risk build-up phase	61.3**	102.2	–59.7**	134.6
Crisis and downward phase	35.0**	76.6	24.6**	103.3

Note. The 10th percentile is GaR that represents the growth rate during shocks, while the 50th percentile – the median that equals the growth rate in normal conditions. The table includes the average short term (the first two years) and the medium term (the third and the fourth year) impact values.

* In the standard and the risk build-up phases, the charts represent the impact of increasing capital requirements, while in the crisis and downward phase – the impact of decreasing capital requirements (changes in the capital requirements without a transition period, fully implemented in the zero period).

** These results are not statistically significant.

Source: Latvijas Banka.

The findings regarding the long-term benefits of raising capital requirements in Latvia are consistent with the assessments of other studies. Studies by other authors confirm the usefulness of releasable capital buffers during a crisis. Herrera et al. (2024)[141] have assessed that the total benefit of releasing the CCyB is more than two times higher than the costs related to increasing the requirement. Similarly, the study by Estrada et al. (2024)[142] has confirmed that raising CCyB rates during periods of economic growth result in a comparatively smaller drop in GDP growth, while their release during downward periods yields benefits that are 3–4 times higher, particularly at the lower end of the distribution of GDP growth rates.

[138] After reviewing the implementation of the CCyB rate in Latvia, it was concluded that in 2025–2028 the average impact on the median GDP growth rate is positive, but not statistically significant.
[139] For up to two years.
[140] A period of three to four years.
[141] Herrera, L., Scalone, V., Pirovano, M. (2024), The importance of being positive: costs and benefits of a positive neutral rate for the countercyclical capital buffer, Macroprudential Bulletin 24, ECB, June 2024.
[142] Estrada, A. et al. (2024), Analysis of cyclical systemic risks in Spain and of their mitigation through countercyclical bank capital requirements, *Documentos Ocasionales*, N.º 2414, Banco de España.

Appendix 3. Latvijas Banka has reviewed the analytical framework for identifying and recognising O-SIIs and setting the O-SII capital buffer rate

Prepared by Kristīna Bojāre

In 2025, Latvijas Banka reviewed the analytical framework for identifying and recognising O-SIIs and for setting the O-SII capital buffer rate. The approach to identifying and recognising the O-SIIs has been refined to better reflect the specific characteristics of countries with relatively smaller financial sectors and to reduce the sensitivity of the methodology towards individual systemically insignificant financial transactions of credit institutions, which, in the context of a small financial market, may have a disproportionately large impact on assessment results. Latvijas Banka also improved the method for setting the O-SII capital buffer rate, transitioning from the Equal Expected Impact model to an interval approach.

O-SII identification and recognition

Latvijas Banka, as an institution that according to the Credit Institution Law is responsible for identifying and recognising O-SIIs in Latvia, performs the annual assessment of systemic importance of credit institutions to determine those credit institutions that should be identified and recognised as O-SIIs or institutions that could create a systemic risk should they cease their operations or any disruptions occur. Sufficient assessment of the systemic importance of credit institutions is essential, as O-SIIs have a higher intensity of regulatory requirements and supervision.

In Latvia, the assessment of the systemic importance of credit institutions is performed pursuant to the requirements of the Credit Institution Law that have transposed the harmonised EU framework and the criteria, indicators and weightings set out in the EBA guidelines[143] (Table A3.1). According to the EBA methodology, 10 000 basis points are allocated among all credit institutions (including branches of foreign credit institutions that have the right to provide financial services in the respective country) considering the weight of each credit institution in these indicators.

[143] EBA Guidelines (EBA/GL/2014/10) of 16 December 2014 on the criteria to determine the conditions of application of Article 131(3) of Directive 2013/36/EU (CRD) in relation to the assessment of other systemically important institutions (O-SIIs).

Table A3.1.
Quantitative criteria of EBA guidelines for identification of O-SIIs

Criterion	Indicator	Weight
Size	Total assets	25%
Importance (including substitutability/financial system infrastructure)	Value of domestic payment transactions	8.33 %
	Private sector deposits from depositors in the EU	8.33 %
	Private sector loans to recipients in the EU	8.33 %
Complexity/cross-border activity	Value of OTC derivatives (notional)	8.33 %
	Cross-jurisdictional liabilities	8.33 %
	Cross-jurisdictional claims	8.33 %
Interconnectedness	Intra financial system liabilities	8.33%
	Intra financial system assets	8.33%
	Debt securities outstanding	8.33%
	Total	**100%**

Source: EBA guidelines EBA/GL/2014/10.

In the opinion of Latvijas Banka, the methodology outlined in the EBA guidelines[144] does not fully consider the specificities of the comparatively smaller and simpler financial sector of Latvia and returns disproportionate results of the systemic importance assessment of credit institutions, namely:

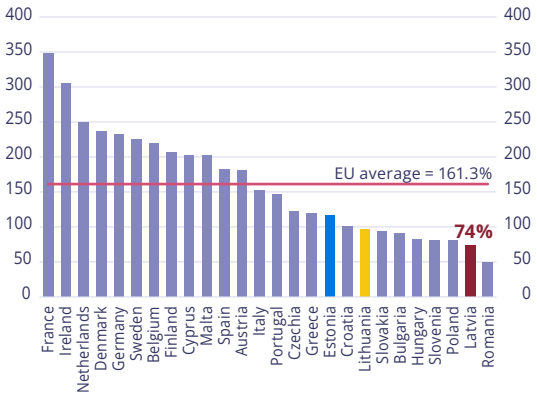
1) the requirement for all EU Member States to uniformly apply the respective indicators and their weighting does not consider the level of complexity of various financial sectors. For example, in countries with relatively less developed financial markets, some transactions of credit institutions are recognised as important contributors to the respective indicator. As a result, the assessed systemic importance of these credit institutions is not correct (overvalued);
2) the requirement for all EU Member States to allocate 10 000 basis points in the local bank sector does not fully consider the fact that the financial sectors of EU Member States significantly differ as to the number of market participants and the total contribution of the sector to the economy.

To adequately consider the national specificities and produce more accurate systemic importance assessments of credit institutions, as of 2025, Latvijas Banka identifies and recognises O-SIIs in three stages:

1) during the first stage, O-SIIs are identified according to the EBA guidelines;
2) during the second stage, the amount of 10 000 basis points is adjusted to the specific features of the Latvian financial sector: the 10 000 basis points are weighted with a ratio that is calculated as the ratio between the size of the Latvian bank sector and the size of an average EU bank sector to ensure that disproportionately small credit institutions are not identified and recognised as O-SIIs;
3) during the third stage, an additional in-depth quantitative and qualitative analysis is performed to verify the true systemic importance of credit institutions.

The ratio between the assets of the Latvian financial sector and GDP was 45.89% of the EU average in 2024 (Chart A3.1). Thus, the 10,000 basis points recommended in the EBA guidelines that each EU Member State should allocate for the assessment of systemic importance are weighted with the ratio of 45.89%. **As a result of this adjustment, or normalisation, 4589 basis points (and not 10 000 basis points) are used to perform the adjusted assessment of the systemic importance of Latvian credit institutions. These points are allocated among credit institutions depending on their systemic importance.** This normalisation allows for a better understanding of the relevance of the Latvian financial sector in the economy, as it differs considerably from the EU average. This, *inter alia*, ensures that the systemic importance of credit institutions (calculated as per EBA guidelines) is less sensitive to separate non-systemic financial transactions of those institutions. During the annual identification and recognition of O-SIIs, Latvijas Banka will use the most recent information on the ratio between the assets of the Latvian financial sector and GDP, and the EU average of this indicator.

Chart A3.1
Size of the financial sector in EU Member States compared to GDP in 2024 (%)



Source: Eurostat[145].

To ensure that in less complex financial sectors where credit institutions have some non-systemic financial transactions (for example, issued debt securities), only truly systemically important credit institutions are identified as an O-SII, Latvijas Banka uses the highest threshold[146] (425 basis points) allowed in EBA guidelines to automatically identify O-SIIs. This threshold is applied to the normalised assessment of the systemic importance of credit institutions (in total, 4589 basis points).

[144] The methodology in EBA guidelines, to a large extent, relies on the GSIB identification methodology that was developed by the Basel Committee on Banking Supervision without proper adjustments for its application at a national (not global) level.

[145] Eurostat data on MFIs that are not central banks (ratio between assets and GDP in 2024). Luxembourg is excluded for the purposes of data quality.

[146] According to EBA guidelines, the threshold for automatic identification of O-SIIs can be set in the range from 275 to 425 basis points.

Finally, **Latvijas Banka analyses the results obtained in the previous stages in greater detail to ensure that the normalised systemic importance assessment identify and recognise as O-SIIs only those credit institutions whose discontinuation or significant disruption of operations could give rise to systemic risk.** This analysis covers several aspects that are significant, considering the specific features of the Latvian financial sector, for example, the share of each credit institution in the total assets of the sector, in the total deposits of the Latvian private sector residents, in loans to the Latvian private sector residents, in the volume of domestic payment transactions, and in the total number of customers of the credit institution sector.

Due to the new approach to identifying and recognising O-SIIs, Latvijas Banka did not identified and recognised AS Rietumu Banka or BluOr Bank AS as O-SIIs[147] in 2025. According to the available information, in terms of assets, these two credit institutions were the smallest O-SIIs in EEA countries.

While proposals on the competitiveness of the EU banking sector are drafted in Europe[148], including on the need to improve the current O-SII framework, Latvijas Banka has amended the methodological deficiencies of the EBA guidelines in practice by introducing adjustments in the national framework. Latvijas Banka will adjust its approach considering changes in the EU regulatory requirements.

Setting the O-SII capital buffer rate

O-SII capital buffer aims to increase the ability of O-SIIs to absorb potential losses, reducing potential systemic risks to the financial system and costs to the economy. This rate should be proportionate and commensurate to the size, importance, and complexity of O-SIIs, as well as their connection with the financial system.

Unlike identification and recognition of O-SIIs, the method for calculating O-SII capital buffer rates can be freely selected by the responsible authorities. It is only important to follow the general principles for setting a O-SII capital buffer rate that are derived from the CRD[149] requirements.

Initially, more comprehensive and complex model-based methods were used by the EEA countries to set the O-SII capital buffer rate. However, currently, most countries use simpler methods such as the interval method where the result of the systemic importance of O-SIIs in basis points is related to the pre-determined O-SII capital buffer rate. This trend is partially reflected in the approaches and conclusions of EU institutions, for example, the interval approach that the ECB uses to determine the minimum capital buffers for O-SIIs[150], as well as the EBA conclusions[151], where the initial interval approach of the ECB[152] was found to be a suitable reference point to harmonise practices used to set the O-SII capital buffers. It is possible that in some cases, EEA countries have selected the interval approach, as it is also used to determine additional capital buffer requirements for globally systemically important banks (GSIB)[153].

Since 2016, Latvijas Banka has used the Equal Expected Impact (EEI) model to calibrate the O-SII capital buffer rates, considering the historic losses of the banking sector[154] and the systemic importance indicators of credit institutions. In essence, the EEI required an O-SII capital buffer rate where the expected potential loss of O-SII would not exceed the expected loss of a credit

[147] As of 22 December 2025, AS Rietumu Banka and BluOr Bank AS are no longer identified or recognised as O-SII, and they are no longer subject to the O-SII capital buffer rate.

[148] EC consultation on the competitiveness of the EU banking sector.

[149] Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC. See EUR-Lex - 02013L0036-20260111 - LV - EUR-Lex.

[150] The ECB approach to setting the minimum O-SII capital buffer rates requires the consideration of not only the systemic importance assessments calculated according to the EBA guidelines, but also to gradually (by 1 January 2028) incorporate the Banking Union perspective. All O-SIIs identified in the euro area countries should maintain an appropriate O-SII capital buffer rate that equals at least 0.25% of TREA.

[151] In 2020, the EBA published a report, concluding that the approaches of EU Member States to calculating the O-SII capital buffer rates differ not only methodologically, but also in terms of economic indicators and supervisory practices. This could significantly hinder the introduction of uniform standards at the EU level.

[152] The initial ECB approach described in the respective EBA report (see footnote 151) was developed in 2016 (and updated in 2020). However, it has been significantly amended by introducing the Banking Union dimension.

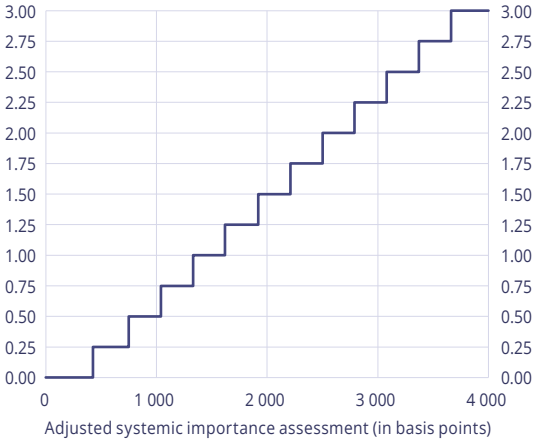
[153] The Financial Stability Board (FSB), in cooperation with the Basel Committee on Banking Supervision and the national responsible authorities, identify the G-SIB on annual basis and set additional requirements for them, including a higher respective capital buffer that is calibrated by applying the linear interval approach.

[154] According to the EEI model, the Return on Risk-Weighted Assets (RORWA) of the Latvian banking sector for the period since 2004 were used. However, considering the extensive structural changes of the Latvian banking sector since 2004, the relevance of the historic RORWA values included in the model has decreased for the current banking sector of Latvia.

institution that has not been identified and recognised as an O-SII. Relatively high-risk sensitivity is one of the advantages of this method, while poorer transparency and comparability – one of its most significant drawbacks.

As the interval method is not only simpler and more transparent, but also becoming more popular internationally, **as of 2025, Latvijas Banka has started using the interval approach to set the O-SII capital buffer rate**. According to the interval approach, the respective O-SII capital buffer rate should be set, considering pre-determined, clear, and simple interval thresholds (Chart A3.2). Lower risk sensitivity of this approach in comparison to other more complex methods is partially offset by narrower intervals (by setting the lowest possible interval step of 0.25 percentage points according to CRD requirements), as well as a regular review of interval thresholds. In standard situations[155] and according to CRD requirements, the O-SII capital buffer rate can be set up to 3% of a credit institution's TREA.

Chart A3.2
Latvijas Banka's interval approach to setting the O-SII capital buffer rate (O-SIIS capital buffer rate, % of TREA)



Source: Latvijas Banka.

Thresholds of the interval approach were calibrated by applying the linear regression method and by relying on practices of countries that are equivalent in terms of the nature of their financial sector[156] to ensure that the respective O-SII capital buffer rates O-SIIs identified and recognised in Latvia are internationally comparable and competitive in similar financial markets.

The ECB interval approach was also considered in setting the minimum O-SII capital buffers, as well as the information gathered by the EBA on the practices of EEA countries regarding the respective systemic importance assessments of credit institutions and their O-SII capital buffer rates. The results were verified considering the average historic results of the EEI model applied by Latvijas Banka for the period since 2020.

According to Latvijas Banka's interval approach, credit institutions with higher systemic importance should apply proportionally higher O-SII capital buffer rates. The respective thresholds of O-SII capital buffer rates increase linearly with a step of 290 basis points, except the lowest threshold that has a larger step (425–750 basis points), considering the limits of the lowest intervals used in setting the minimum O-SII capital buffers according to the ECB interval approach[157].

As previously stated, for the purposes of calculating the O-SII capital buffer rate, Latvijas Banka carries out an adjusted[158] assessment of systemic importance of credit institutions by employing indicators and weightings that, in the opinion of Latvijas Banka, are the most suitable for the specificities of the Latvian financial sector. In this assessment, each credit institution receives an adjusted systemic importance score (on a scale from 0 to 10 000 basis points), while the respective O-SII capital buffer rate is set only for the identified and recognised O-SIIs.

[155] After approval from the EC, the responsible authorities can set the O-SII capital buffer rate that is higher than 3%.

[156] Equivalent countries were selected by applying several criteria: the number of banks in the sector (< 25), assets of the banking sector (< 100 billion EUR), average assets of a bank (< 5 billion EUR), as well as the qualitative comparison and expert assessments. As a result, the following countries were selected as equivalent: Bulgaria, Cyprus, Estonia, Croatia, Lithuania, Malta, and Slovenia.

[157] Unlike the linear or gradual increase concept, the ECB approach in essence provides for exponential (every step of the next interval is larger than the previous step) setting of the respective O-SII capital buffer rates, considering the systemic importance of credit institutions. This approach is more suitable to determine the harmonized minimum O-SII capital buffer rates. However, countries may still calibrate higher O-SII capital buffer rates that are more suitable considering the specificities of their financial sector and their systemic risks.

[158] In essence, the adjusted systemic importance assessment is based on the EBA guideline methodology and also includes several optional indicators listed in Appendix 2 of these guidelines – respective indicators are more appropriate for the specificities of the Latvian financial sector, such as weighted assets, loans to Latvian private sector residents, and deposits of Latvian private sector residents. This assessment assigns greater weight to the indicator that represents the loans and deposits of Latvian residents, and lesser weight to indicators in the interconnectedness criterion.

In 2025, Latvijas Banka reviewed the indicators used in the adjusted systemic importance assessment and their weighting and excluded the results of the stress test but increased the weighting of deposits of the Latvian private sector residents to reflect the deposit growth trend observed since 2016.

For identified and recognised O-SIIs, as of 2025, Latvijas Banka has imposed the requirement to maintain the O-SII capital buffer rate not only at the highest level of the prudential consolidation group, as it has been applied since, but also (where possible) individually to, *inter alia*, ensure alignment with the application of the combined buffer requirement at the individual level.

Impact assessment of reviewing the O-SII framework

Improving the approach to identifying and recognising O-SIIs provides an opportunity to:

1) better align the practical implementation of the EU regulatory framework with the specificities of the Latvian financial system;
2) identify and recognise as O-SIIs, only those credit institutions that are truly and systemically important to the Latvian economy;
3) simplify the framework where possible, while preserving the overall resilience of the financial system and providing potential for a more comprehensive application of the principle of proportionality in the supervision and resolution frameworks.

Latvijas Banka assessed that the resilience of the Latvian financial sector would not be significantly affected by changing the approach regarding setting the O-SII capital buffer rates, as the respective O-SII capital buffer rates obtained according to the interval approach do not significantly differ from those that would be calculated with the previously used EEI model (Table A3.2).

Table A3.2
Assessment of the O-SII capital buffer rate according to the interval approach and the historic EEI model (2025)

O-SII	Interval approach	EEI model	Difference between the interval approach and the EEI model
Swedbank Baltics AS	2.50%	2.00%	+0.50 pp
AS SEB banka	1.50%	1.50%	–
AS Citadele banka	1.25%	1.50%	–0.25 pp

Source: Latvijas Banka.

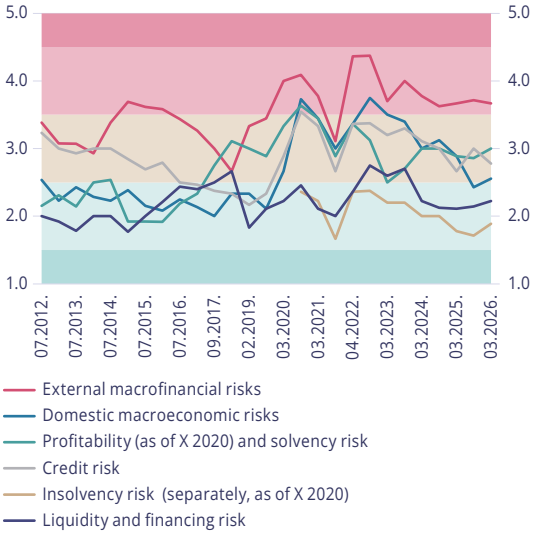
The largest differences in the O-SII capital buffer rates affect Swedbank Baltics AS, considering not only changes in the adjusted systemic importance assessment methodology, but also the nature of the interval approach that requires setting the respective rate for all O-SIIs by applying uniform principles, i.e. by relying only on the assessed adjusted systemic importance and irrespective of the O-SII capital buffer rate applicable to the EU parent company of these credit institutions. Though according to the new interval approach, Swedbank Baltics AS would have to apply a higher O-SII capital buffer rate, i.e. 2.5% of TREA, considering the current limits of the CRD requirements[159], it is not possible to apply an O-SII capital buffer rate exceeding 2% to Swedbank Baltics AS, as its EU parent company Swedbank AB has a respective rate of 1%.

According to the assessment of Latvijas Banka, the decrease of capital requirements related to the new approach to identifying O-SIIs and setting the O-SII capital requirements amounts to only 0.16% of the banking sector's TREA[160] and, consequently, does not significantly undermine the resilience of the credit institution sector.

[159] The cap of the CRD requirements that apply to the O-SIIs, whose EU parent company already has an O-SII capital buffer rate.
[160] According to the data from the second quarter of 2025.

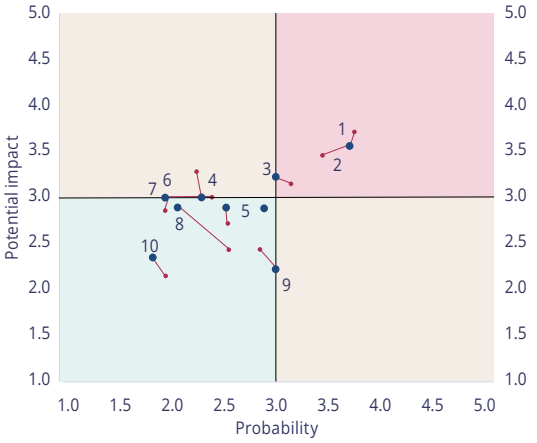
Appendix 4. Results of the credit institution survey on risks

Chart A4.1
Assessment of the key risk categories by credit institutions[161] in terms of risk level over the coming year (taking account of the expected likelihood of a risk and the potential negative impact)



Assessment of credit institutions' risk categories did not significantly change, though the credit risk slightly decreased compared to a survey conducted in autumn 2025. In terms of individual risk factors, the assessment of most factors changed only slightly, though the respondents had the opinion that the probability of AML/CFTP reputational risks marginally decreased.

Chart A4.2
Assessment of the risk factors provided by credit institutions in March 2026 over the coming year

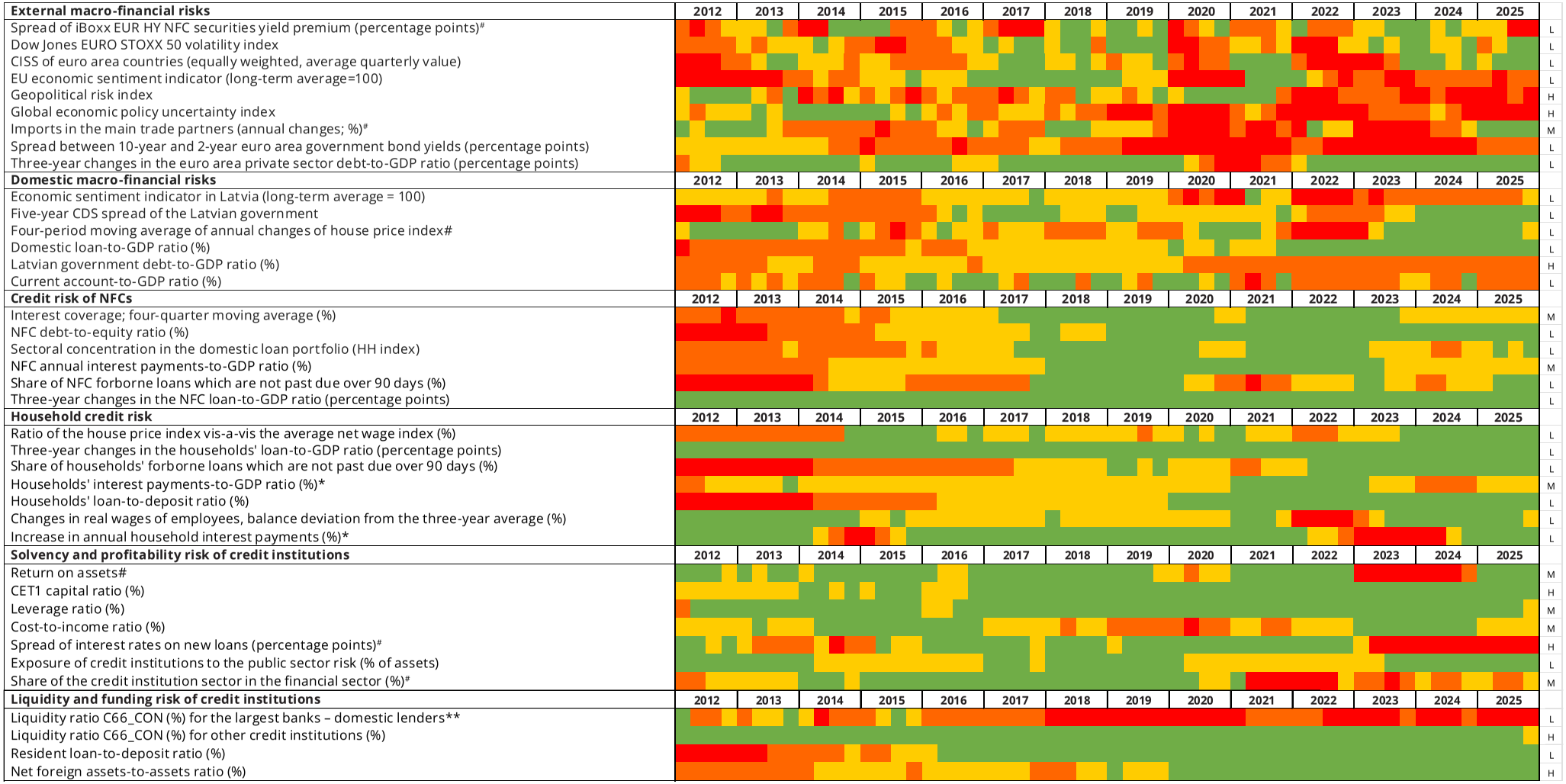


Risk factors (in descending order)

1. Negative impact of significant deterioration of the external macro-financial environment on the Latvian economy
2. IT security risk to Latvia's financial system (it is recommended to be filled by IT specialists)
3. Deterioration of NFC solvency
4. Deterioration of Latvia's economic situation due to domestic factors
5. A significant fall in demand in the commercial real estate market
6. Deterioration of household solvency
7. Substantial changes in residential real estate prices
8. Reputation risk and other risks related to financial crime (including fraud, AML/CFTP and circumvention of sanctions) in Latvia and the Baltics
9. Effect of climate change physical and transitional risks on Latvia's financial system (unlike other risks, it would be preferable to assess this risk over a medium term – 5 to 7 years – horizon).
10. Rising risks in parent banks of the largest Latvian banks or in their home countries (including rising macro-financial risks in their economies or an increase in funding risks in the parent banks)

[161] In February 2026 (before the war in the Middle East), Latvijas Banka conducted a credit institution survey regarding their assessment of risks to Latvia's financial system. The survey respondents were Swedbank AS, AS SEB banka, Latvian branch of Luminor Bank AS, AS Citadele banka, BlueOr Bank AS, AS Reģionālā investīciju banka, AS Rietumu Banka, AS INDEXO Banka, and AS Industra Bank.

Appendix 5. Heatmap of early warning indicators



Notes.

For each indicator, the letter added at the end of the row in the table represents the level of last reading ("L" for low, "M" for medium, "H" for high).

Bilateral indicator

* Since 2014, non-bank interest payments as well.

** Data until 2019 and those for 2019 include the four and three largest credit institutions respectively, since branches are excluded from the calculation of liquidity ratio. The liquidity ratio of this credit institution group is relatively lower, as liquidity of subsidiaries is managed at the group level. The liquidity ratio is not compulsory for these credit institutions from a supervisory standpoint; it serves as a tool for monitoring risks.

The heatmap is only one of the tools used by Latvijas Banka for the analysis of systemic financial stability risks. The assigned risk level should not be interpreted in absolute terms. Instead, it should be viewed in comparison with the historical benchmarks of the chosen indicators, warning of the build-up of risks. For the explanation of the heatmap methodology, see Appendix "Heatmap: analytical tool for the analysis of systemic financial stability risks in Latvia" to Latvijas Banka's "Financial Stability Report 2018".

The risk level is indicated by colour:

Appendix 6. Performance indicators of credit institutions

Table A6
Overall performance indicators of credit institutions

Indicator	2020	2021	2022	2023	2024	2025	March 2026
Balance sheet indicators							
Number of credit institutions and branches of foreign credit institutions	16	16	14	13	14	14	14
Total assets (million euro)	24 029.2	24 754.6	26 986.7	27 831.2	29 871.1	31 642.2	32 238.6
Share of loans in assets (%)	51.6	55.4	54.0	52.9	51.0	54.1	53.6
Annual growth rate of domestic loans (%)[162]	–3.3	11.8	7.6	1.4	3.4	12.7	12.1
Share of deposits in total liabilities (%)	75.1	77.9	77.6	76.4	78.1	77.3	78.7
Annual growth rate of domestic deposits (%)	10.3	10.3	11.8	0.7	9.9	8.1	12.6
Share of liabilities to MFIs in total liabilities (%)	3.9	3.0	4.5	5.7	5.9	5.8	6.7
Domestic loan-to-deposit ratio (%)	73.8	74.8	72.0	72.6	68.2	71.1	70.4
Profitability[163]							
ROE (%)[164]	5.2	10.0	10.0	20.0	16.6	10.4	–
ROA (%)[165]	0.7	1.2	1.2	2.2	1.9	1.2	–
Cost-to-income ratio (%)[166]	64.9	64.9	56.0	39.3	49.5	55.8	–
Capital adequacy[167]							
TC (million euro)	2 316.1	2 335.5	2 310.5	2 397.3	2 699.9	2 791.8	–
CET1 (million euro)	2 219.7	2 241.6	2 206.9	2 299.4	2 448.1	2 486.0	–
TREA (million euro)	8 624.5	9 266.5	10 055.6	11 468.2	12 524.5	12 969.4	–
TC ratio	26.9	25.3	23.0	20.9	21.6	21.5	–
CET1 capital ratio (%)	25.7	24.3	21.9	20.1	19.5	19.2	–
Leverage ratio (%)	10.5	10.3	9.3	9.5	9.3	9.0	–
Liquidity[168]							
Liquid assets to total assets ratio (%)[169]	36.5	36.4	38.8	40.9	43.6	38.4	37.5
LSK (%)[167]	373.7	319.3	221.8	251.7	248.0	206.7	–
NSFR (%)[167,170]	155.9	173.1	157.7	167.5	172.6	154.3	–
Asset quality[171]							
Ratio of provisions for non-performing loans in the loan portfolio (%)	1.9	1.6	1.6	1.7	1.5	1.8	1.5
Share of loans past due over 90 days in the loan portfolio (%)	2.3	1.5	1.1	1.2	1.2	1.3	1.2
Share of NPLs in loan portfolios (%)	4.7	3.6	2.7	2.7	2.7	2.8	2.7

[162] The indicator has been calculated using individual-level data and incorporates all one-off effects referred to in Chapter 2: Development and Risks of the Credit Institution Sector.
[163] Indicators for 2019–2021 have been calculated based on Latvijas Banka's consolidated-level data.
[164] Annualised profit/loss ratio to average capital and reserves of the reporting period (excluding data of foreign credit institution subsidiaries).
[165] Annualised profit/loss ratio to average assets of the reporting period.
[166] Cost-to-income ratio = (administrative expenses + intangible and fixed asset depreciation and disposal + cash contributions to resolution funds and deposit guarantee schemes)/(net total operating inome) × 100.
[167] Data are shown at the consolidated level.
[168] Data are presented at the level of individual credit institutions.
[169] Liquid assets = vault cash + claims on central banks and other credit institutions + central government fixed income debt securities (those having a regular, unlimited market, i.e. they can be sold in a short period of time without considerable loss or used as loan collateral).
[170] Until 2021 – Latvijas Banka's estimate.
[171] The loan quality indicators for 2019-2024 have been calculated based on consolidated-level data for the credit institutions subject to consolidated supervision and on individual-level data for other credit institutions and branches of foreign banks (for the first quarter of 2025 – at the level of individual credit institutions). Credit risk ratios have been presented without excluding the one-off effects referred to in Chapter 2: Development and Risks of the Credit Institution Sector.