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ECONOMIC DEVELOPMENT TRENDS

Until 2019, Latvia's economic growth remained stable, exceeding the EU average. From 2011-2019, GDP on average increased by 3.3% annually. In 2019, economic growth moderated. GDP increased by 2.1%. The slight economic slowdown was driven by both internal factors (investments from EU funds have peaked, developments in the financial sector, etc.) and external factors (review of global trade tensions, Brexit, slower growth in other EU countries).

The Covid-19 pandemic has a significant impact on the global and Latvian economies. In the 2nd quarter of 2020, GDP in Latvia decreased by 8.9% annually. However, this appears to be a comparatively mild decline, as the EU-27 GDP contracted by 11.7% over the same period. According to the Ministry of Economics, GDP in Latvia in 2020 could shrink by as much as 4-5%, compared to 2019. However, if the exposure to the virus in the world will not be ceased, then the negative impact on the Latvian economy could be greater and the economy risks a deeper recession.

Key Economic Development Indicators

	2014	2015	2016	2017	2018	2019	2020e
Gross domestic product, at current prices, billion euro	23.6	24.6	25.4	27.0	29.1	30.5	29.1
changes as per cent							
Gross domestic product	1.1	4.0	2.4	3.3	4.0	2.1	-4.4
Private consumption	0.6	2.2	2.4	3.0	2.6	2.2	-6.8
Public consumption	3.5	2.7	2.5	3.4	1.6	2.6	2.0
Gross fixed capital formation	0.6	-2.0	-8.2	11.4	11.8	2.1	-1.3
Exports	6.2	3.0	4.0	6.4	4.3	2.1	-4.8
Imports	2.9	1.6	3.6	8.6	6.4	3.0	-5.2
Consumer prices	0.6	0.2	0.1	2.9	2.5	2.8	0.4
as per cent							
Changes in the number of employed	-1.3	1.4	-0.0	1.5	1.5	0.1	-2.5
Employment rate	59.1	60.8	61.6	62.9	64.5	65.0	64.0
Unemployment rate	10.8	9.9	9.6	8.7	7.4	6.3	8.4
as per cent of GDP							
General government balance	-1.6	-1.4	0.2	-0.8	-0.8	-0.5	-7.5
General government debt	41.6	37.1	40.4	39.1	37.1	36.9	49.0
Net exports	-2.9	-1.7	0.3	-0.6	-0.8	-0.8	0.1

e – estimation

The Covid-19 crisis has had a significant impact on consumption. With rising employment and wages, private consumption has grown steadily in recent years. The growth rate of private consumption in 2019 (2.2%) was close to the overall economic growth rate. In 2020, the increase in unemployment and the fall in income caused by the Covid-19 crisis have significantly reduced household consumption. In the first half of 2020, private consumption was 12.6% less than a year ago. The government's support measures to mitigate the negative effects of Covid-19, which have been largely financed at the expense of increasing the general government deficit, have maintained positive growth in government consumption. In the first half of 2020, it was 2.4% higher than a year ago.

The Covid-19 crisis has had a relatively more moderate impact on investment. In previous years, the increase in investment was largely due to the acquisition of EU funds. In 2019, when the investments of the EU funds reached the maximum within the current planning period, the investment rate declined, increasing only by 2.1% (for comparison in 2018 - by 11.8%). In the first half of 2020, the gross fixed capital formation declined by 0.6%, compared to H1 of 2019. Investment in dwellings, buildings, and structures decreased by 7.4%; in machinery and equipment - by 6.6%. However, investment in intellectual property products increased by 1.2%.

The Covid-19 crisis is having a negative impact on exports of goods and services. In recent years, export growth rates have exceeded the overall economic growth. In 2015-2019, exports of goods on average increased by 3.1% annually. However, exports of services increased at a higher rate of 5.7%, indicating that the services sector continue to be increasingly integrated into world markets. However, in 2019. the growth rate of exports began to slow down, reaching only 2.1%. In 2020, export development will continue to be significantly affected by Covid-19 restrictions in Latvian export markets and delays in raw material supply chains. In the first half of 2020, export volumes decreased by 5.3%, compared H1 of 2019. Exports of goods declined more moderately (by 0.1%), while exports of services were 18.2% lower than a year ago. The decline can primarily be attributed to the downturn in exports of tourism and transport services.

Since 2011, Latvia has experienced a low current account deficit, thus indicating the external sustainability of the Latvian economy. In 2019, the current account deficit of 0.6% of GDP was observed. Despite the negative impact of Covid-19 pandemic on economic development, it is anticipated that in the coming years the current account will remain with a small deficit, not comprising the external sustainability of Latvia's economy.

Development trends are highly variant across sectors. In 2019, the most significant contribution to economic growth was provided by the trade sector (an increase of 4.2%). Rapid growth was also observed in the agricultural and forestry (12.3%), catering services (11.2%), computer programming and consulting services (7.9%), and commercial services (6.3%). As a result of the Covid-19 crisis, the most significant decline in the first half of 2020 was observed in the accommodation and food service activities, as well as in the arts, entertainment, and leisure sectors, where the annual decrease of 38.7% and 27.9% respectively was recorded. The restrictions imposed on Covid-19 also had a significant impact on aviation, land transport, and railway companies. In the first half of 2020, the decline in the transportation and storage reached 15.2%. A decline in financial and insurance activities, trade, information and communication services, and commercial services was also observed. However, in the first half of 2020, an increase of 5.3% was recorded in construction.

The decline in H1 of 2020 was also observed in manufacturing (by 4.2%). Although overall the decline was observed in most sub-sectors, the monthly data shows signs of growth. For example, compared to May, when the only sector that made a significant positive contribution to manufacturing was the chemical industry, several sectors already showed positive trends in June-August. Also, an overall growth in manufacturing in June and July 2020.

Since 2011, when Latvia returned to economic growth, significant improvements in the fiscal position have been achieved. In recent years, the budget has had a small deficit. According to the assessment, in 2019, the budget deficit reached 0.5% of GDP. In 2020, the general government budget deficit is planned at 0.3% of GDP. However, the COVID-19 epidemic could significantly increase the deficit. According to the Ministry of Finance, the deficit could reach 7-8% of GDP.

In 2019, the average annual inflation reached 2.8%. The rise in prices for services had a significant impact on the consumer price level. In 2020, average annual inflation is expected to be significantly lower than in 2019, determined by the negative impact of the COVID-19 epidemic.

The introduction of Covid-19 restrictive measures has a significant impact on the labour market. In previous years, the increase in economic activity has contributed to a decrease in unemployment and an increase in employment. Also, the increase in the number of employees was moderate due to the overall decline in the working age population. In 2019, the unemployment rate was 6.3%, thus approaching the pre-crisis unemployment rate of 2007. Also, the employment rate increased to 65%.

The situation in the labour market has changed dramatically since mid-March 2020, as restrictive measures were introduced. The most negatively affected are labour-intensive sectors: transport services / passenger transport, travel agency and tour operator reservation services, accommodation and food services, arts, cultural sectors, sports centres, and other sectors requiring human interaction. In 2019, the number of jobs in the directly affected sectors reached nearly 60 thousand, constituting nearly 7% of the total number of jobs in the economy.

The impact of the COVID-19 epidemic on the labour market will largely depend on how long the restrictions associated with the spread of the coronavirus will last. According to the methodology of the Labour Force Survey, the number of employees could decrease by 2.5% -3% in 2020. Also, the unemployment rate could increase to 8.4% (82 thousand jobseekers).

Wage growth has remained above 7% annually over the last three years. In 2019, the average gross wage reached EUR 1 076 (i.e., an increase by 7.2%, compared to 2018). In Q2 of 2020, the annual gross wage growth rate declined to 3.9%. In May 2020, compared to May 2019, the average gross wage increased by 2.5%, which was the slowest growth during the year since July 2016. In Q2 of 2020, the average gross wage reached EUR 1 118.

The further development of the economy in the medium term depends on the situation in the external environment and the pace of reforms. The further development of the Latvian economy will be closely related to export opportunities; therefore, the largest risk to Latvia's growth is related to the development of the global economy, especially the expansion of the COVID-19 epidemic. Also, the further development of the EU's common economic space is vitally important. Latvia's medium-term economic benefits will be mainly based on the macroeconomic stability (as a result of which Latvia's credit ratings have improved), the efficiency of the planned EU support programs, and improvements in the business environment. The competitive advantages of the Latvian economy mainly rely on technological factors, improvements in production efficiency and innovations; however, to a lesser extent on low labour and resource prices. In the medium term, Latvia's growth rates may reach 4-5% annually. On the other hand, if growth in Europe weakens and the geopolitical situation does not improve, the growth rates of the Latvian economy may be much slower.

2020 | 2 WORLD ECONOMIC OUTLOOK

In the first half of 2020, the world economy entered a sudden downturn with the sharpest decline in output since the Second World War. To prevent the spread of COVID-19, strict containment measures were put in place around the world, significantly suppressing much of the economy. The outlook for global growth remains highly uncertain. Global growth is projected to reach 5% in 2021 (OECD Interim Economic Outlook, September 2020; hereinafter - OECD, 2020).

GDP Growth Rate
as per cent

	2019	2020p	2021p
World	2.6	-4.5	5.0
G20	2.9	-4.1	5.7
Euro Area	1.3	-7.9	5.1
USA	2.2	-3.8	4.0
Russia	1.4	-7.3	5.0
China	6.1	1.8	8.0

Source: OECD Interim Economic Outlook Forecasts, March 2020;
f – forecast

In China, which is on its way to recovery after the sharp decline in the first quarter of 2020, growth is projected to reach 1.8% in 2020 (OECD, 2020). India's economy is projected to shrink by 4.5%. The two largest Latin American economies, Brazil and Mexico, are projected to contract by 9.1% and 10.5% respectively in 2020. (IMF, World Economic Outlook, June 2020).

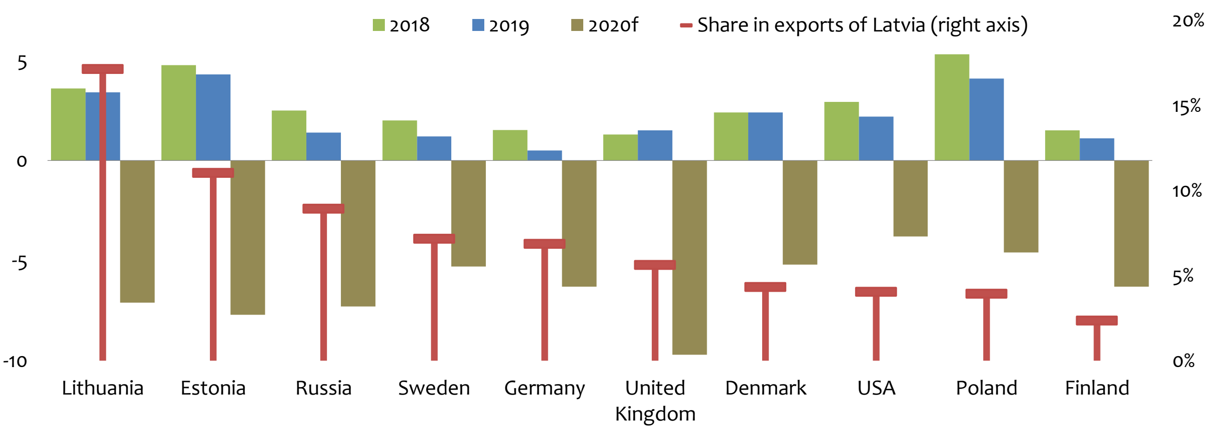
In the United States, economic growth is anticipated to slow by 3.8% in 2020. However, in 2021, it is expected that GDP growth rate will reach 4% (OECD, 2020).

A series of indicators show that the eurozone economy has operated between 25% and 30% below its capacity during the tightest constraints (European Commission, European Economic Forecast, Summer 2020; hereinafter - EC, 2020). In 2020, the Eurozone economy is projected to shrink by 7.3%. However, in 2021, it is anticipated that an annual growth rate of 5.1% will be reached (OECD, 2020).

The nominal GDP of the United Kingdom decreased by 6.2% year-on-year in the first half of 2020. In 2020, GDP is projected to decline by 9.7%. However, in 2021, it is anticipated to reach a growth rate of 6% (EC, 2020).

Germany's nominal GDP in the first half of 2020 decreased by 4.3%, compared to the first half of 2019. Although the relatively favourable epidemiological situation allowed Germany to be among the first EU countries to start relaxing restrictive measures in the second quarter of 2020, an unprecedented decline in economic activity is still anticipated. Sweden's nominal GDP contracted by 3.1% in the first half of 2020. In 2020, economic growth is expected to decline by 5.3%. However, in 2021, the economy is expected to recover, with real GDP growth reaching 3.1%. Estonia's GDP at current prices declined by 4% in the first half of the year. In 2020, GDP is projected to decline by more than 7.5%. GDP is projected to grow by more than 6% in 2021, reflecting the base effect and the stimulus measures already taken to boost investment and overall confidence. In Lithuania, in the first half of 2020, compared to the first half of 2019, nominal GDP decreased by only 0.8%. GDP in Lithuania is projected to decline by around 7% in 2020. However, in 2021, real GDP will grow by 6.7% (EC, 2020).

Growth of Latvia's Largest Trade Partners
GDP changes against the corresponding period last year, as per cent – left axis; share as per cent in 2019 – right axis



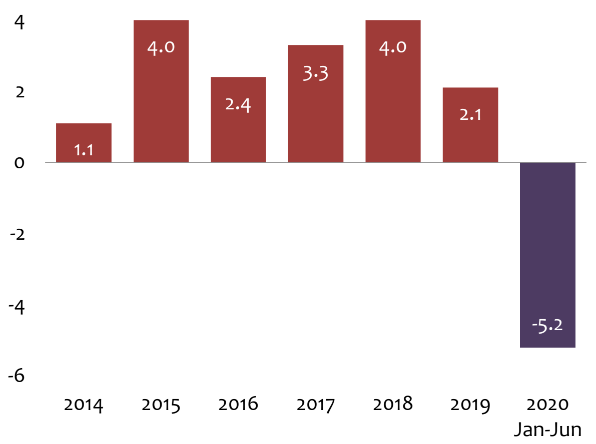
Source: CSB, OECD 2020, EC 2020, f – forecast

2020 | 2 GROSS DOMESTIC PRODUCT AND AGGREGATE DEMAND

GROSS DOMESTIC PRODUCT

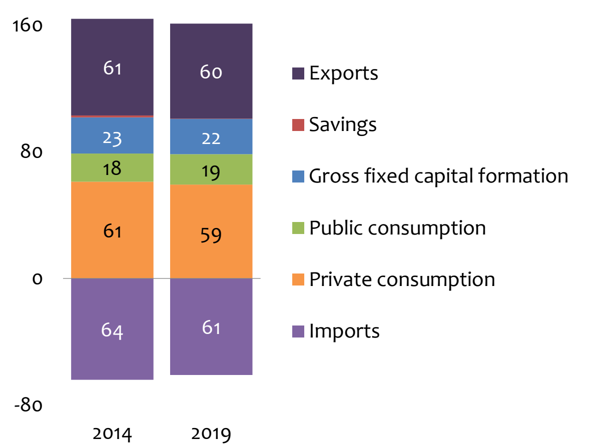
In 2020, an economic downturn will be observed. In the first half of 2020, GDP decreased by 5.2%. which was the sharpest decline in a decade.

Gross Domestic Product
changes against the corresponding period last year, as per cent



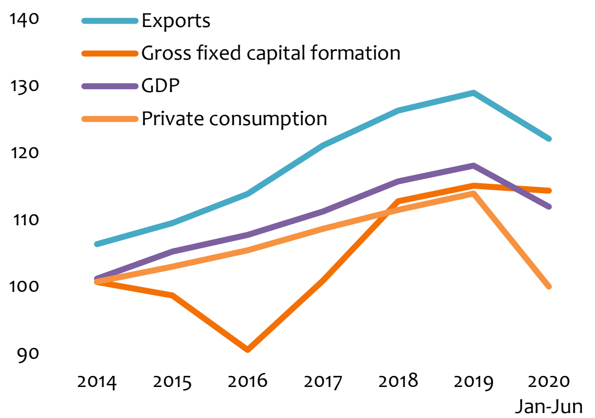
In 2020, economic development trends are primarily determined by the negative impact of Covid-19. Although the worst months of the Covid-19 crisis remain behind us, uncertainty remains high. The decline in private consumption, driven by rising unemployment and falling incomes, had the largest impact on the decline in GDP in the first half of the year.

Gross Domestic Product from Expenditure Approach
as per cent of GDP

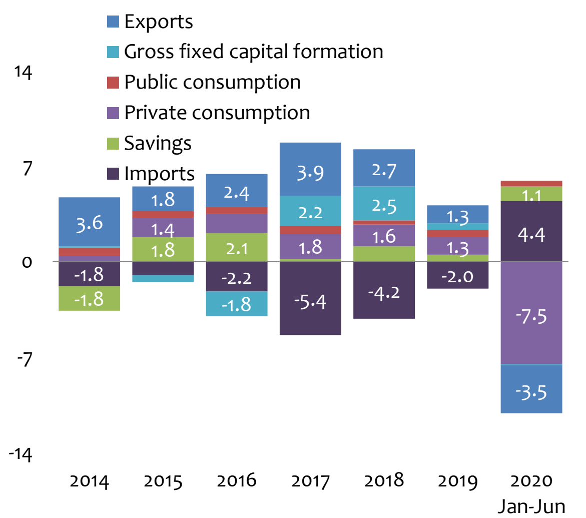


Restrictions on Covid-19 in Latvia's export markets and delays in raw material supply chains have affected exports of goods and services. Exports of goods declined more moderately, while exports of services declined very sharply. The decline can mainly be attributed to a significant downturn in exports of tourism and transport services. In the first half of the year, a relatively more moderate decline was observed in investment. Government consumption, on the other hand, continued to grow, driven mainly by government support measures to mitigate the negative effects of Covid-19.

Gross Domestic Product by Expenditure Items
2013 = 100



Gross Domestic Product by Expenditure Items
contribution to growth as percentage points

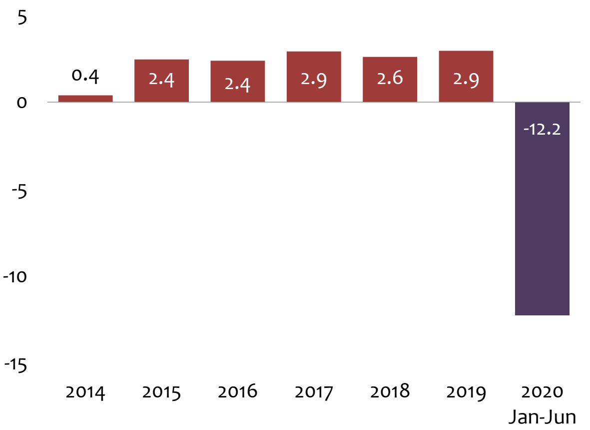


CONSUMPTION

Private consumption is declining significantly as a result of the Covid-19 crisis. From 2014-2019, private consumption increased on average by 2.3% annually, primarily due to rise in employment and wages. However, in the first half of 2020, due to Covid-19 constraints, private consumption declined sharply, driven by declining expenditures, rising unemployment and falling incomes.

Private Consumption

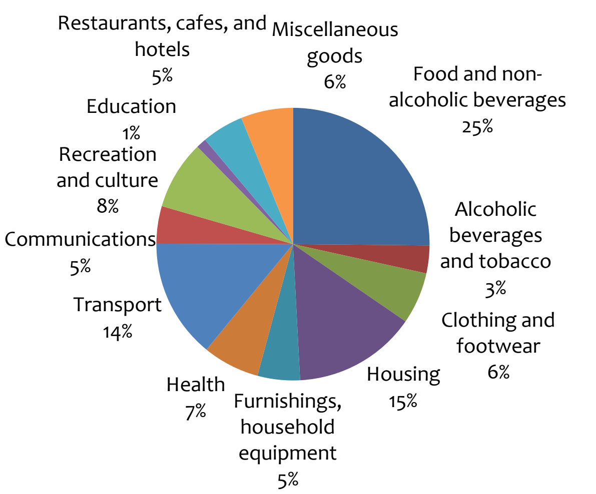
changes against the corresponding period last year, as per cent



Expenditures on food and non-alcoholic beverages account for the majority of household consumption. In 2019, spending on food and non-alcoholic beverages, compared to 2018, increased only by 0.9%. Spending on housing, the second largest consumer spending group, rose slightly – by 2%. The largest increase was observed for transport expenditure, the third largest expenditure group, where expenditures rose by 9.6%. This was mainly due to higher expenditure on the operation of personal vehicles and the purchase of cars. The fourth priority in household spending is on recreation and culture, where spending increased by 6.9 percent.

Structure of Household Expenditures

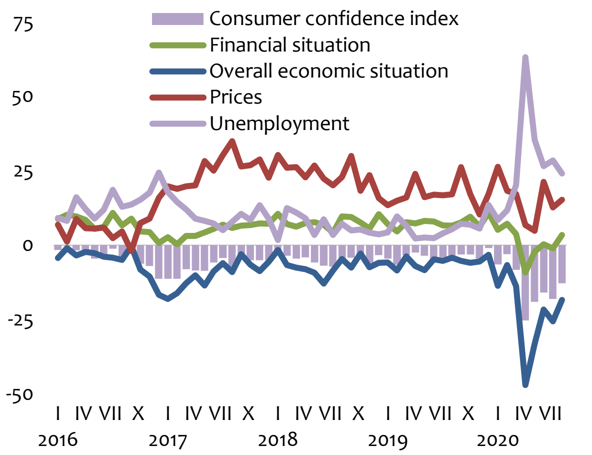
2019, as per cent



Consumer sentiment on a decline in 2020. If at the beginning of the year consumer sentiment continued to improve as a result of trends in 2019, then with the declaration of a state of emergency in the country due to the Covid-19 outbreak, it began to deteriorate. Almost all CCI positions (i.e., family financial situation, general economic situation in the country, unemployment expectations) experienced a marked decline, reaching their record lows in April and May 2020. Meanwhile, inflation expectations reached their lowest level over the last three years. Consumer sentiment has been gradually improving since August 2020; nonetheless, it could change at any time, given the uncertainty in the world with Covid-19.

Consumer Confidence Index

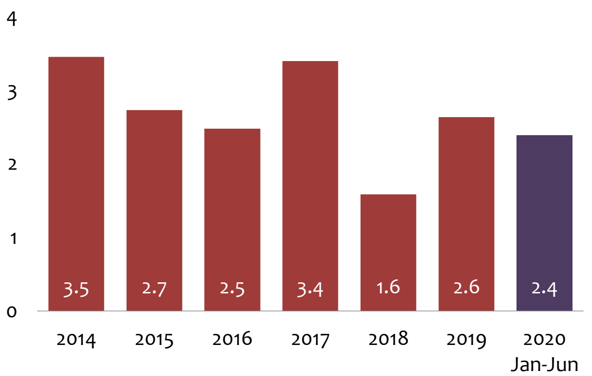
consumer assessment for the next 12 months, response balance, seasonally adjusted data



Public consumption gradually increases. Since 2014, along with an increase in budget revenues, public consumption has risen expeditiously. Between 2014-2019, public consumption has increased by 2.7% annually. Also, in the first half of 2020, public consumption continued to grow, primarily due to the measures introduced by the government to mitigate the negative effects of Covid-19.

Public Consumption

changes against the corresponding period last year, as per cent

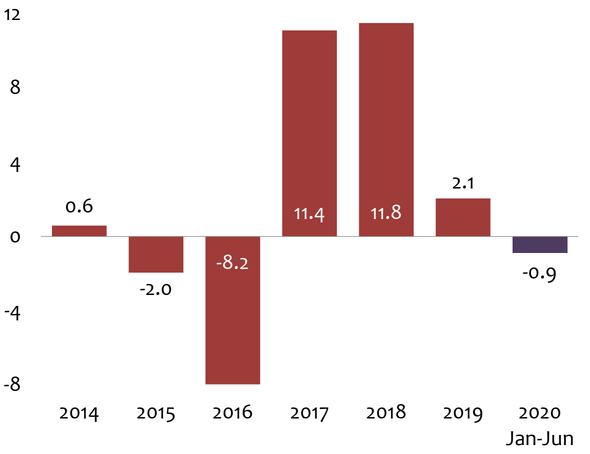


INVESTMENT

As a result of the Covid-19 crisis, investment is declining and trends for the coming years remain highly uncertain. Investment growth is an important pillar of Latvia's economic growth. Between 2016-2019, real investment growth reached almost 33%; in particular, in 2017 and 2018, investment grew by 11.4% and 11.8% (i.e., a notably higher growth rate than in most EU Member States), respectively. EU-funded public investment accounted for a large share of investment. As the absorption of the EU structural funds approaches the maximum level, the growth rate of investment activities moderates. In 2019, expenditure on gross fixed capital formation was only 2.1% higher than a year ago, amounting to 22.2% of GDP.

Gross Fixed Capital Formation

changes against the corresponding period last year, as per cent



Due to the Covid-19 pandemic, in the first half of 2020, the volume of investments declined by 0.6% annually, which is a relatively minor decline in investment activities.

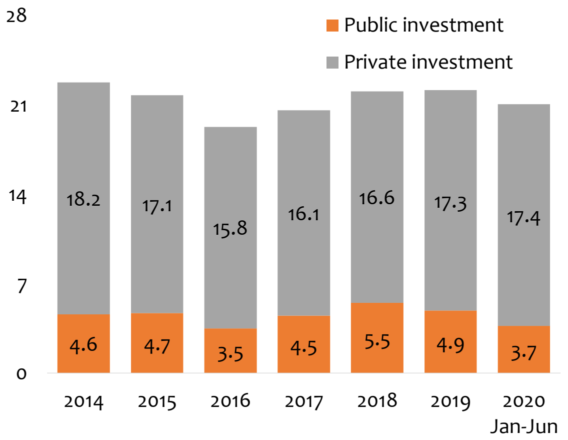
Private investment increased; however, the overall investment level remains low. The recovery of private investment after the crisis was long-lasting. Since 2017, positive dynamics, albeit volatile, have been observed. Between 2017-2019, investments increased on average by 6.5% annually. In 2019, investments rose by 6% (accounting for 17.3% of GDP), which is lower than in the years of rapid economic expansion. Investment financing was mainly provided by entrepreneurs' own funds. In the first half of 2020, private investment was 1.4% higher than a year ago.

In the long run, low levels of private investment are largely driven by weak crediting, low demand, and high uncertainty. The negative impact of these factors on investment has been exacerbated by the Covid-19 crisis.

In Latvia, public investment remains at a high level. In recent years, public investment constitutes 1/5 of total investment in the Latvian economy, and its dynamics largely rely on the cyclicality of the absorption of EU structural funds. Between 2017-2018, along with the recovery of EU structural funds, public investment has increased on average by 35% annually. As EU structural funds reached its peak, public investment growth slowed. In 2019, government expenditure on fixed capital formation did not exceed the previous year's level; however, in the first half of 2020, public investment was nearly 9% lower than a year ago.

Public and Private Investment

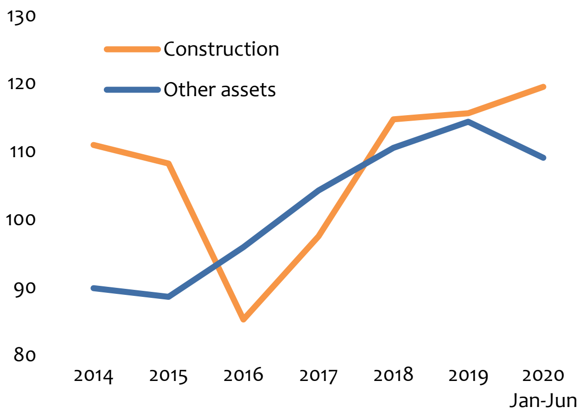
as per cent of GDP



The largest share of investments has been made in construction. Primarily these constituted investments in buildings and structures, which during the last three years accounted for 45% of total fixed capital formation expenditure. However, investments in machinery and equipment has been slower to recover from the crisis than other asset classes, not exceed 30% in the total investment structure. Investment in intellectual property products remained at an average level of 1.6% of GDP (including investment in R&D – 0.6% of GDP).

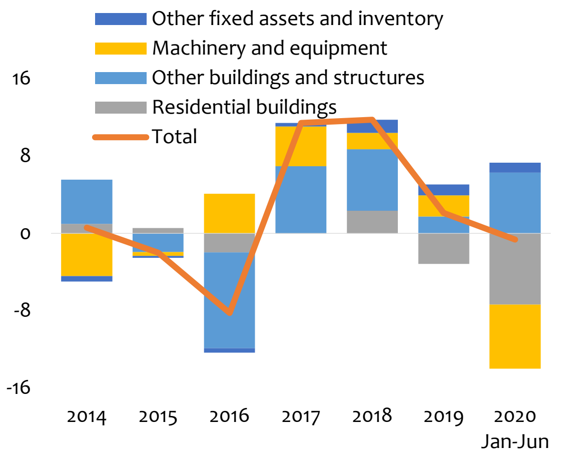
Gross Fixed Capital Formation by Type of Assets

2013 = 100



In the first half of 2020, investments in construction assets were by 3.1% higher than a year ago and their share in the total investment reached almost 56.2%. Investment in housing was 7.1% lower than a year ago, while investment in civil engineering and buildings increased by 6.3%. Entrepreneurs invested 6.6% less in machinery and equipment than a year ago; however, the volume of investments in vehicles declined significantly – by 22.1%. Investments in intellectual property products were 1.3% higher, compared to the corresponding period last year.

Gross Fixed Capital Formation by Type of Asset
changes against the last year, as per cent; asset type investment, as percentage points

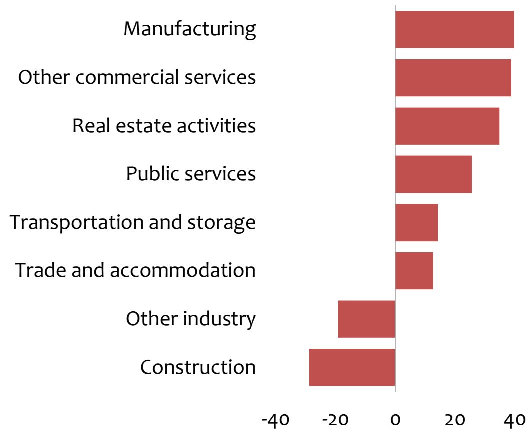


In the first half of 2020, capital investment in tangible assets grew faster in the goods manufacturing sectors. Investment in the manufacturing sector was almost 6% higher than a year ago. In the service sectors, on the other hand, capital investment declined by nearly 25 percent.

Investment in the manufacturing sector (an increase of 29%) and the electricity, gas and heat supply sector (an increase of 75%) constituted the largest share of investment growth. Capital investment in tangible assets in the public administration and real estate sectors was almost 35% lower than a year ago. Also, investment in the construction declined.

The survey results of top executives and managers in the industry reveal that the demand remains the most significant factor for investment decisions. In recent years, the role of finance accessibility has increased. Also, in 2020, financial conditions (also technical factors such as technological developments and access to skilled labour, etc.) are deemed highly important in fostering investment.

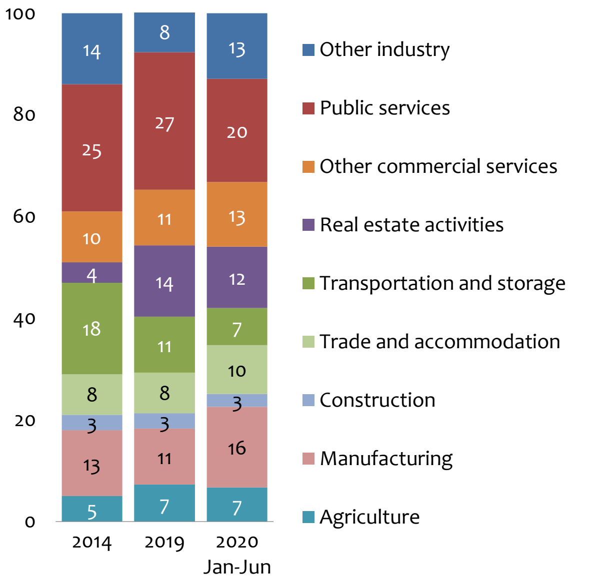
Non-financial Investment Dynamics
2019, changes as per cent*



* – calculated using quarterly data

Investment dynamics will be further affected by uncertainty regarding the external environment, incl. the impact of the coronavirus outbreak, as well as significant reductions in capacity utilization. Investment dynamics have also weakened due to lacklustre lending. The implementation of state support programs will positively impact investment dynamics. It is anticipated that investment activities will expand along with the launch of the Rail Baltica project.

Gross capital investment Structure
*by sectors, as per cent**

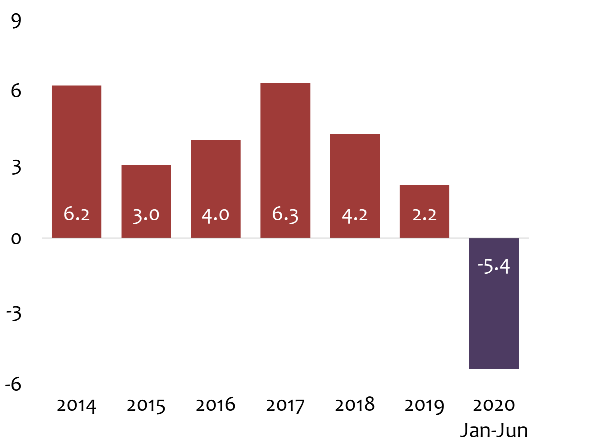


* Gross capital investment in tangible assets (calculated using quarterly data)

EXPORTS

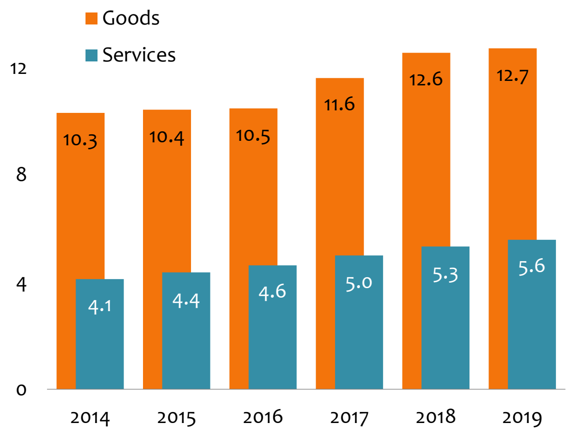
Export growth is one of the main drivers of economic development. It is closely linked to external demand and economic development of key partner countries.

Exports of Goods and Services
changes against the corresponding period last year, as per cent



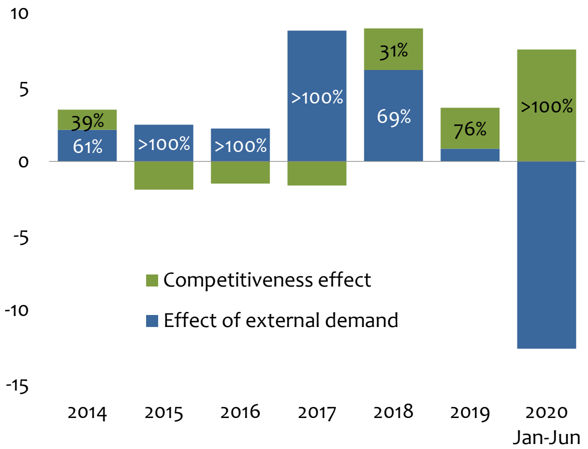
In 2019, exports of goods and services, albeit more moderately than in the previous year, increased steadily. The growth was mainly facilitated by economic development in Lithuania and Estonia and the stabilization of economic situation in Russia and other CIS countries. In Q1 of 2020, export growth was higher than in 2019; however, due to the spread of Covid-19, a sharp decline in exports was observed in Q2 of 2020.

Exports of Goods and Services
at current prices, billion euro



Between 2014-2018, export growth was mainly driven by external demand. The role of price competitiveness was negligible. On the other hand, in 2019, the growth of exports was more influenced by the competitiveness effect, which is related to the successful acquisition of new markets. However, in 2020, due to the spread of Covid-19, external demand is rapidly declining, which is partially offset by the increase in competitiveness in certain sectors.

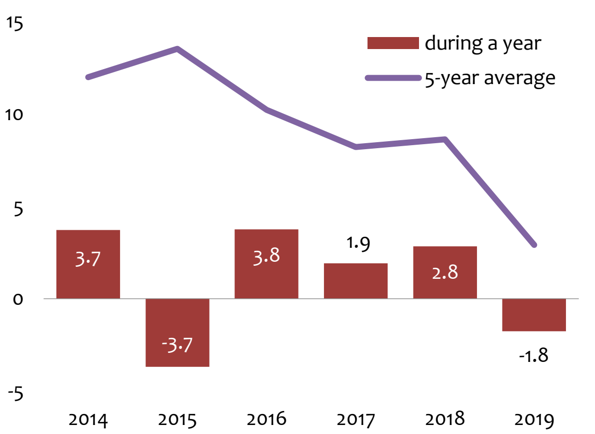
Changes of Exports by the Constant Market Share
structure of exports' changes to the EU countries, as per cent



During years of economic expansion, a few large exports of goods categories (e.g. wood and its products, metals) constituted a large share of total exports. Amidst the crisis, export volumes declined across all export classes; however, the most substantial downturn was observed for the largest exports of goods categories. In the aftermath of crisis, as the economic growth resumed, exports of goods growth across product classes has become more similar, implying a higher degree of diversification for exports. In recent years, the export diversification rate of Latvia corresponds to the EU-15 average.

Between 2016-2018, the share of Latvia's exports in the world market increased, illustrating our competitiveness despite rapidly rising labour costs. In 2019, export growth was lower than the global average; therefore, the share of Latvia's exports in the world slightly declined.

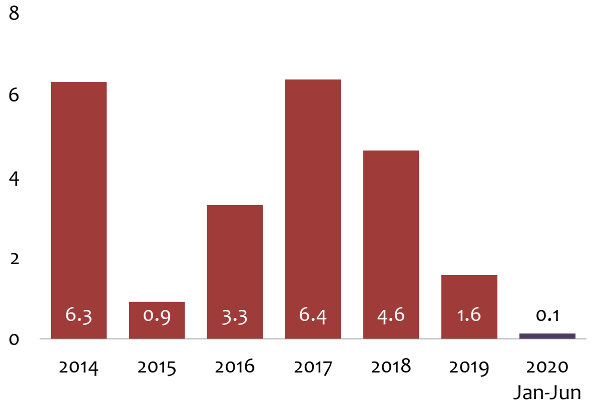
Share of Exports In World Trade
changes as per cent



Exports of Goods

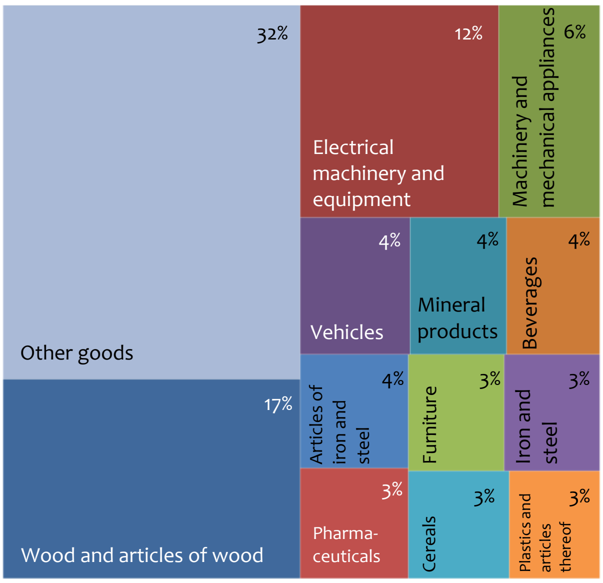
Exports of goods have remained stable, constituting around 70% of total Latvia's exports. Also, its share has not changed significantly in recent years.

Exports of Goods
at constant prices, changes against the corresponding period last year, as per cent



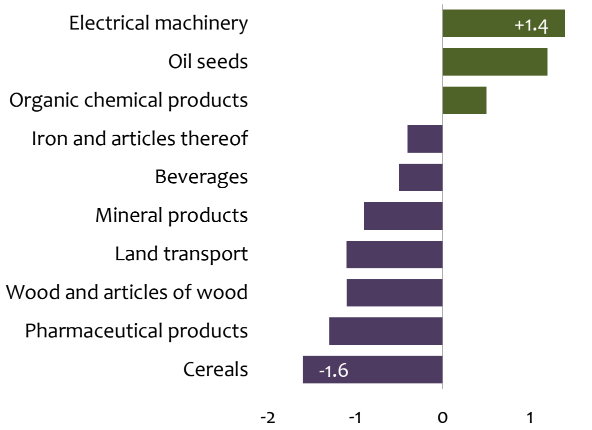
In 2019, exports of goods increased moderately (by 1.5% at current prices; 1.7% at constant prices). In the first half of 2020, exports at current prices decreased by 3.7% (at constant prices – by 2%).

Exports of Goods
January-August 2020, structure, as per cent



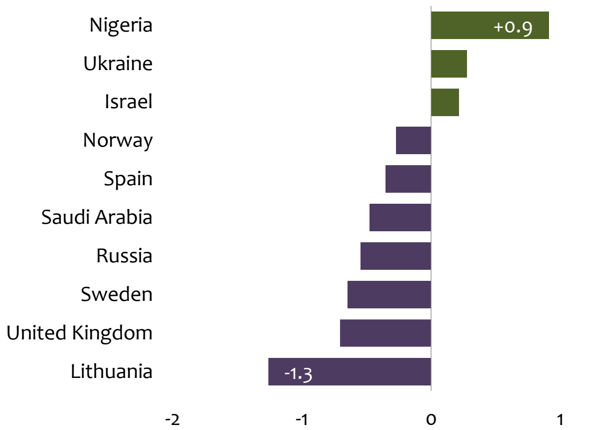
In January-August 2020, the value of exports increased due to the expansion in the exports of electrical machinery and equipment, oilseeds and organic chemical compounds; the export dynamics were negatively affected by reductions in exports of cereals, pharmaceuticals, wood and articles of wood, and vehicles.

Exports of Goods
contribution to growth in January-August 2020, changes as per cent



In the eight months of 2020, exports to Estonia slightly declined; however, a more marked decline was observed to Lithuania and other EU countries (EU – by 3.4%). Exports also decreased to the CIS countries (-4.5%). On the other hand, exports to other countries rose by 2.6%.

Exports of Goods by Country
contribution to growth in January-August 2020, changes as per cent



In January-August 2020, the largest export partner countries of Latvia were Lithuania, Estonia, Russia, Germany, Sweden, the United Kingdom, Denmark, Poland, and Finland. Latvia exported 2/3 to these countries.

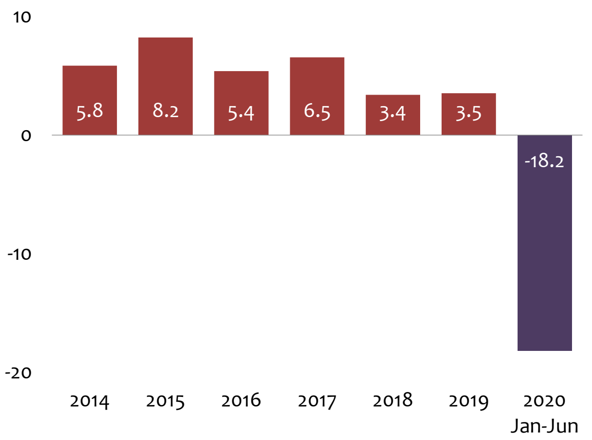
In January-August 2020, the main exports to the EU countries were wood products, electrical machinery and equipment. Alcoholic beverages, electronic machinery and equipment were mostly exported to the CIS countries. Exports to other countries constituted primarily wood and articles of wood, cereals, and electrical machinery and equipment.

Exports of Services

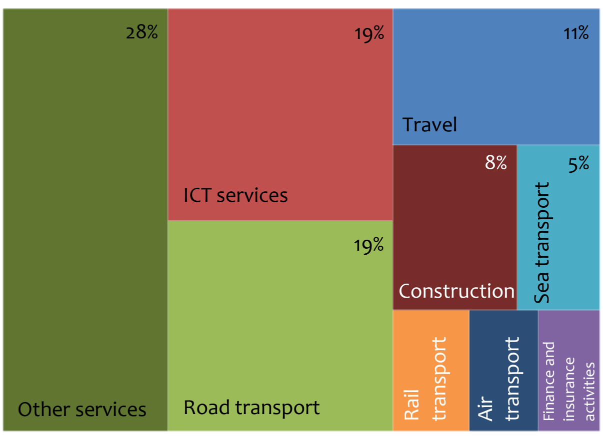
Until 2019, exports of services have increased at a higher rate than exports of goods. Transport services, ICT, trade intermediation, and travel services provide a major contribution to export growth. However, since 2016, the share of finance and insurance activities in exports is declining.

After stable growth in exports of services in 2019, due to the spread of Covid-19, in the first half of 2020, the value of exports was 18.2% lower than a year ago.

Exports of Services
at constant prices, changes against the corresponding period last year, as per cent



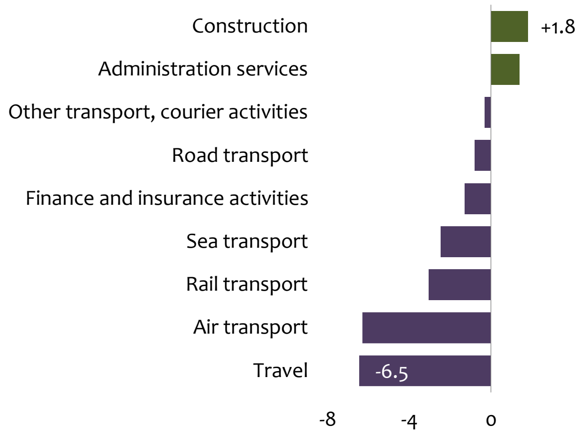
Exports of Services
January-August 2020, structure as per cent



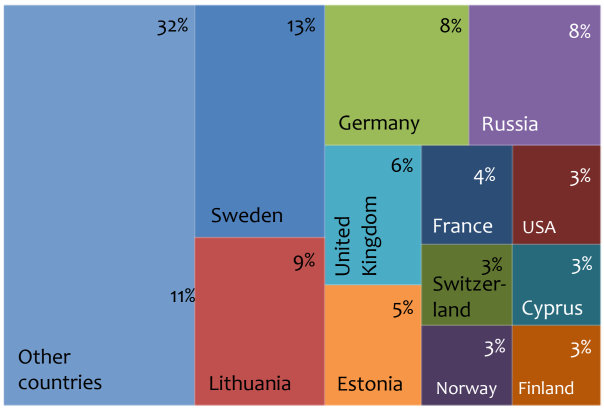
In the first half of 2020, only exports of construction and other services increased. On the other hand, exports of transport services declined significantly, especially in air and rail transport. Also, a decline in travel, finance and insurance activities, and ICT services was observed.

Each year the share of exports of services to EU countries has increased. Exports of services to CIS countries (mainly transit services) still comprise a significant share of total export volume. It should be noted that exports of services to CIS countries in recent years have slightly declined.

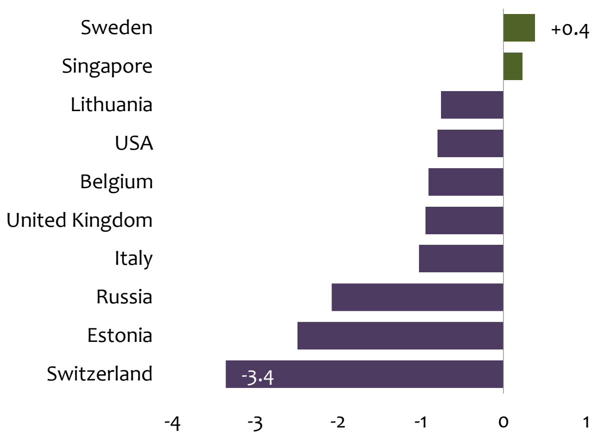
Exports of Services
contribution to growth in January-June 2020, changes as per cent



Structure of Exports of Services by Country
January-June 2020, structure as per cent



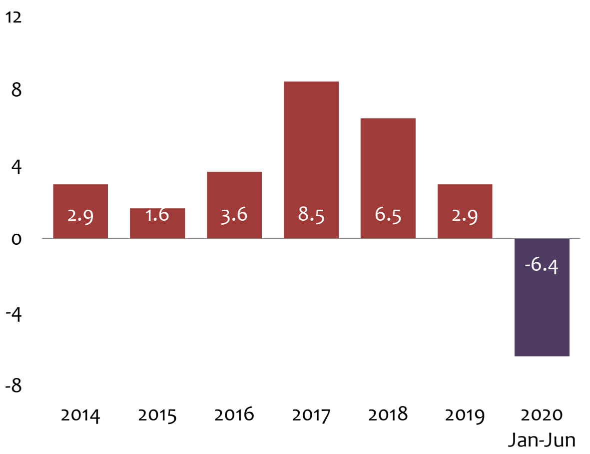
Exports of Services by Country
January-June 2020, changes as per cent



IMPORTS

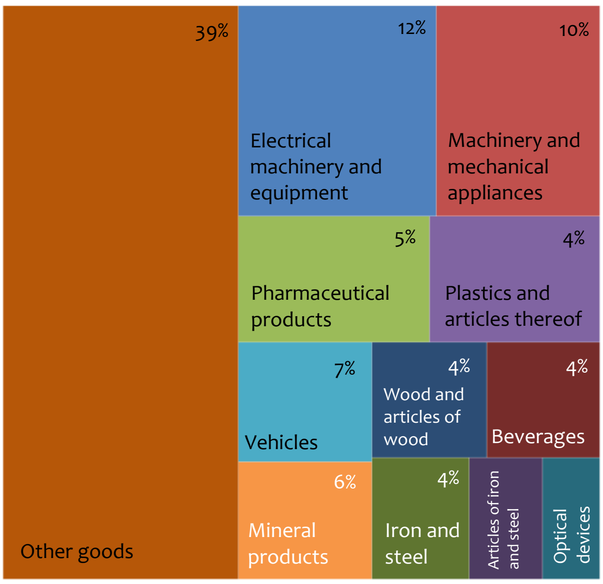
In recent years, imports of goods and services experience a similar growth as exports. Since 2017, imports of goods increased at a higher rate than imports of services. However, in the first half of 2020, imports of services will experience a more pronounced decline, whereas imports of goods will decline moderately.

Imports of Goods and Services
at constant prices, changes against the corresponding period last year, as per cent



In 2019, imports of goods at current prices increased by 0.8% (at constant prices – by 1.9%). However, in the eight months of 2020, imports of goods at current prices, due to the spread of Covid-19, decreased by 9.8%. It was significantly affected by a decrease in imports of aircraft and parts thereof, mineral products, and land vehicles. However, imports of electrical machinery and equipment, weapons and ammunition, and textiles increased.

Structure of Imports of Goods
January-June 2020, as per cent



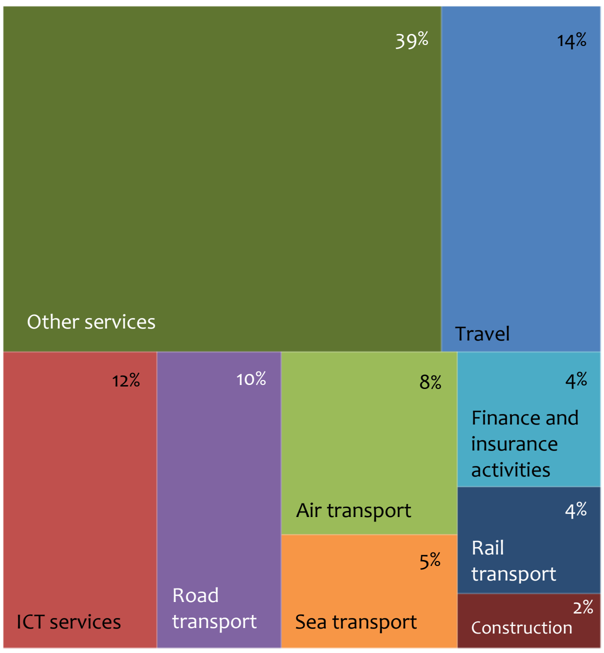
The main Latvia's imports of goods partner countries are Lithuania, Germany, Poland, Estonia, Russia, Finland, the Netherlands, and China. In January-August 2020, the production of these countries accounted for more than 2/3 of the imports of Latvia.

Since 2012, the import structure by the end use of goods has not significantly changed. Due to a decline in the value of fuel imports, the share of intermediate consumption goods has slightly declined. Similarly, the share of fuel in intermediate consumption has decreased from 34% in 2012 to 21% in 2019. The drop to a large extent can be explained by declining world prices for oil. In the first half of 2020, imports of capital goods experienced a marked decline; however, imports of consumer goods decreased moderately. Therefore, the share of capital goods in imports has decreased from 19.7% to 15.3% during the year. Consequently, the share of imports of consumer goods has increased.

In recent years, imports of services have grown at a relatively higher rate than imports of goods. Between 2017-2019, imports of services increased by 8.5% annually.

However, in the first half of 2020, when, due to the spread of Covid-19, imports of services at current prices decreased by 18.1% (in Q1 by 3.6%; in Q2 by 31.5%). The decline in imports of services in January-June 2020 was significantly influenced by the downturn in travel and transport, especially air transport, services sectors. Imports of ICT services, finance and insurance activities also declined. At the same time, imports of construction and other services increased slightly.

Structure of Imports of Services
January-June 2020, as per cent



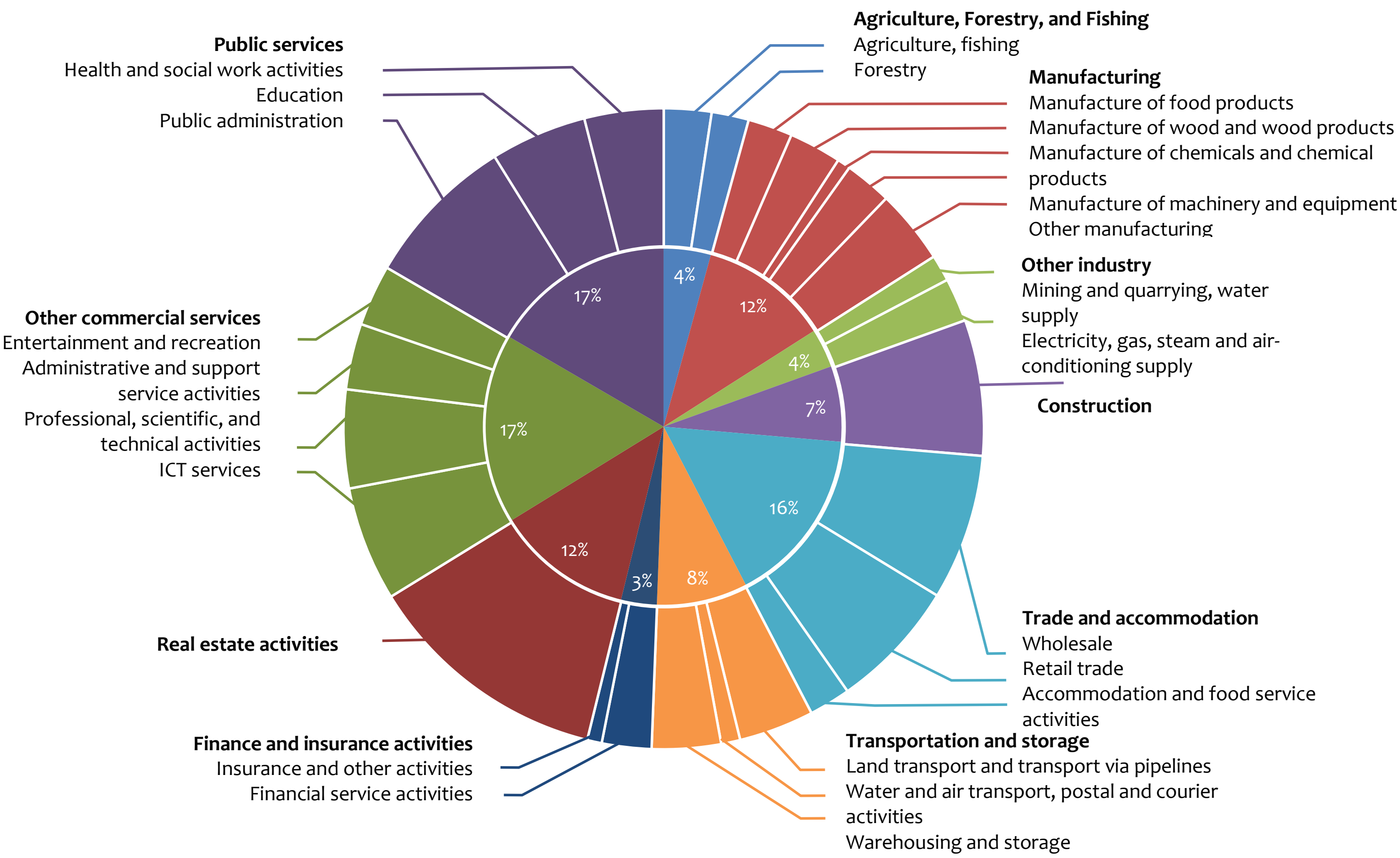
2020 | 2 SECTORAL DEVELOPMENT

In 2009-2010, as labour costs declined, the competitiveness of Latvian producers improved, which significantly stimulated export growth and hence the development of tradable sectors. The structure of the economy changed. In 2008, tradable sectors (agriculture, forestry, manufacturing, and transportation and storage) constituted 26.6% of the total value added. However, in 2010, the share for these sectors reached 33.1%. In 2019, it slightly declined to 27.4%. In 2019, compared to 2010, the share has dropped in practically all sectors, except construction, commercial services, and public service sectors. In 2014-2016, the growth continued in all sectors, except construction and transport, while in 2017 and 2019, the increase in construction volumes had one of the largest effects on growth. In the first half of 2020, the Covid-19 crisis has negatively affected practically all sectors of the economy. Growth was observed only in construction and public administration and defence.

In 2019, goods accounted for 27% and services for 73% of total value added.

Structure of Value Added

2019, as per cent*



* calculations by the Ministry of Economics

Development of Sectors
changes against the corresponding period last year, as per cent

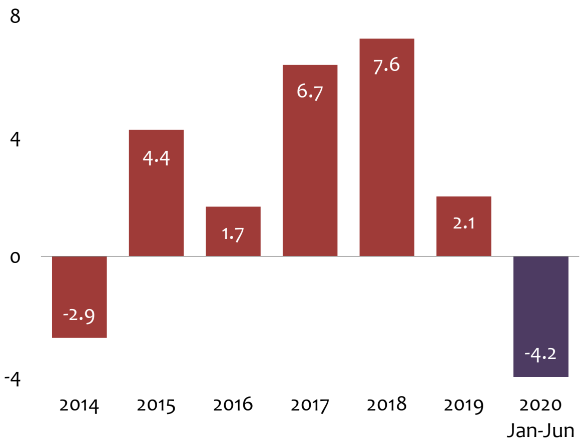
	2014	2015	2016	2017	2018	2019	2020 January-June
Gross domestic product	**1.1**	**4.0**	**2.4**	**3.3**	**4.0**	**2.1**	**-5.2**
Agriculture, forestry, and fishing	8.0	2.7	-4.3	1.8	-3.6	12.3	-1.1
Mining and quarrying	-13.1	14.8	-2.8	9.1	9.1	-4.6	3.5
Manufacturing	-2.9	4.4	1.7	6.7	7.6	2.1	-4.2
Manufacture of food products	0.1	-4.6	1.8	5.2	-2.9	-0.7	-2.2
Light industry	-13.6	-13.2	2.1	7.6	-0.8	-2.6	-15.7
Manufacture of wood and articles of wood	6.9	7.1	8.0	2.1	4.5	0.0	-1.8
Manufacture of paper and paper products	-0.6	0.0	3.6	4.5	-3.7	5.7	2.3
Manufacture of chemicals and chemical products	-2.6	-4.1	10.7	11.4	7.0	3.9	0.7
Manufacture of non-metallic mineral products	1.2	-9.8	11.6	11.1	1.3	-2.1	-1.1
Manufacture of basic metals	-10.5	34.8	5.4	12.0	3.6	13.5	-6.3
Manufacture of computer, electronic and optical products	32.3	16.7	12.6	15.8	12.1	11.3	4.4
Manufacture of machinery and equipment	2.4	7.9	8.5	21.5	7.0	-1.9	-13.2
Manufacture of motor vehicles	-15.2	3.5	-2.9	22.8	7.3	-7.7	-22.8
Other manufacturing	-12.0	3.5	0.8	4.3	-1.8	2.8	-16.7
Electricity, gas, steam, and air-conditioning supply	-13.3	22.1	17.5	-2.1	-38.7	-4.4	0.3
Construction	-2.6	-0.4	-9.6	14.6	12.5	2.2	5.3
Construction of buildings	28.2	-8.2	-11.1	22.4	25.6	7.8	4.0
Civil engineering	-6.8	0.4	-25.7	30.0	11.6	1.0	-0.9
Trade	3.7	7.0	4.5	2.5	4.0	4.2	-5.5
Retail trade	3.5	4.9	2.3	4.3	3.8	2.4	0.4
Transportation and storage	-3.6	1.2	1.7	6.4	4.0	-2.7	-15.2
Freight rail transport	2.2	-2.4	-14.1	-8.4	12.5	-15.8	-47.2
Cargo handling	5.2	-6.2	-9.3	-2.0	6.9	-5.7	-30.1
Freight transport by road	2.7	0.5	1.3	7.0	12.8	-3.8	1.9
Accommodation and food service activities	-2.2	8.9	4.4	9.3	7.6	8.3	-38.7
Information and communication services	-2.7	2.3	5.0	8.6	9.7	1.0	-7.4
Finance and insurance activities	5.5	13.3	-0.2	-17.1	-3.1	-15.2	-0.9
Real estate activities	4.9	-2.4	1.6	-1.6	2.4	1.4	-1.3
Other service activities	-1.2	1.9	3.9	4.5	2.8	6.3	-2.7
Public administration and defence; compulsory social security	2.4	2.4	1.5	3.8	2.8	2.0	1.4
Education	1.9	3.2	1.1	4.3	3.0	2.9	-0.1
Health and social work activities	14.5	5.2	1.2	4.3	9.3	9.6	-1.3
Arts, entertainment, and recreation	-7.7	8.2	5.0	5.1	6.1	5.7	-27.9

MANUFACTURING

The development of manufacturing is driven by improvements in the competitiveness of Latvian producers and the favourable demand dynamics in export markets. In 2017, a rapid growth in production volumes was observed. In 2018 and 2019, the growth rates have moderated.

In 2019, the growth in manufacturing was positively influenced by manufacture of basic metals and manufacture of computer, electrical and optical equipment. The production volumes of the largest sub-sector (i.e., wood products and articles of wood) experienced a similar growth than a year ago. At the same time, the second largest sub-sector (i.e., manufacture of food products) slightly declined.

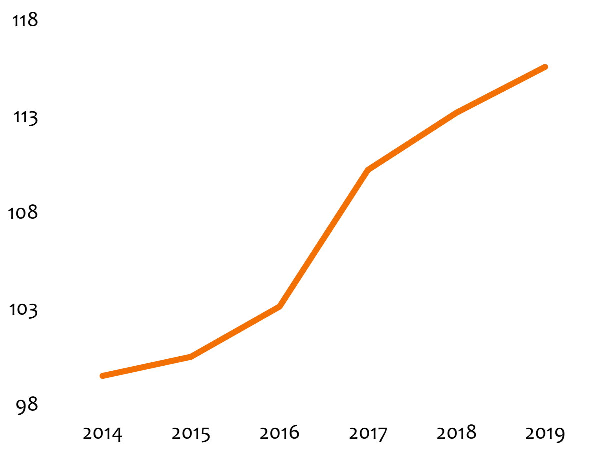
Manufacturing
changes in value added, as per cent



In June-August 2020, manufacturing volumes were 3.5% lower than a year ago. Vehicles and metal processing declined markedly; however, the manufacture of electronic and optical products, wood and wood products increased.

In June-August 2020, the manufacturing turnover at current prices declined. Sales on the domestic market decreased; the volumes of exported products increased.

Manufacturing
value added, 2013 = 100



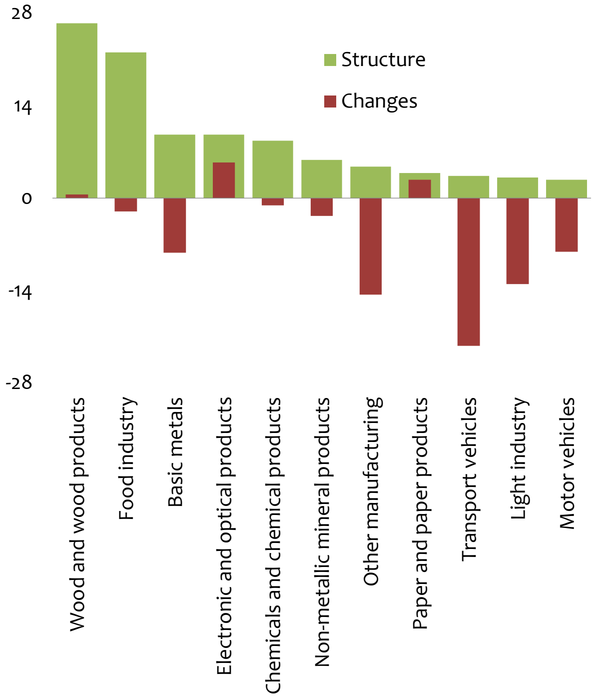
In 2018 and 2019, the number of occupied posts in manufacturing remained practically unchanged. In the first half of 2020, the number of occupied posts declined (light industry and wood processing sharply declined); occupied posts increased in metal processing, the manufacture of electronic and optical equipment, and food industry.

Structure of Manufacturing and Development Trends by Field
as per cent

	Structure in 2019			Changes in production volumes			
	Output	Occupied posts	Exports in total sales	2017	2018	2019	2020 January-August
Manufacturing	**100**	**100**	**64.9**	**8.0**	**2.7**	**2.1**	**-3.5**
Food industry	21.8	19.4	37.6	5.2	-2.9	-0.7	-2.0
Light industry	3.7	9.2	85.8	7.6	-0.8	-2.6	-13.0
Manufacture of wood and wood products	26.7	19.8	70.9	2.1	4.5	0.0	0.6
Manufacture of paper and paper products	4.0	4.3	64.3	4.5	-3.7	5.7	2.8
Manufacture of chemicals and chemical products	8.3	7.1	75.2	11.4	7.0	3.9	-1.1
Manufacture of non-metallic mineral products	5.8	5.2	49.4	11.1	1.3	-2.1	-2.7
Manufacture of basic metals	9.2	10.6	67.5	12.0	3.6	13.5	-8.2
Manufacture of electronic and optical products	8.9	5.0	89.8	15.8	12.1	11.3	5.4
Manufacture of machinery and equipment	2.7	3.3	83.5	21.5	7.0	-1.9	-8.1
Manufacture of motor vehicles	3.8	3.2	90.2	22.8	7.3	-7.7	-22.4
Other manufacturing	5.1	12.6	62.5	4.3	-1.8	2.8	-14.6

Growth of Manufacturing

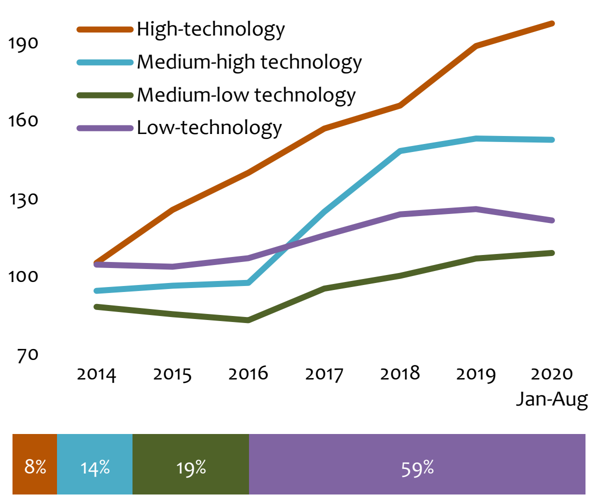
structure and changes in January-August 2020, as per cent



The outlook for manufacturing remains highly uncertain. Although increasingly more sectors will return to growth in the second half of the year, growth will continue to be limited by external demand.

Manufacturing Volume Index and Structure by Levels of Technology

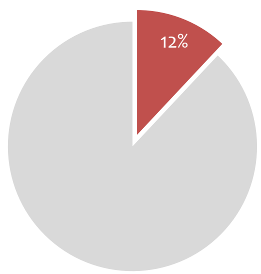
2013 = 100, structure in January-July 2020, as per cent



Main Indicators of Manufacturing[1]

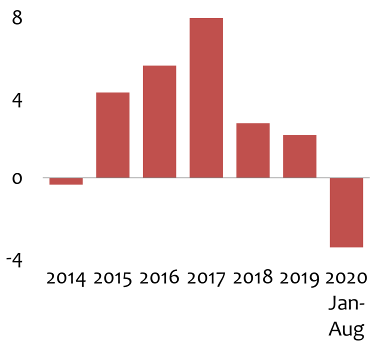
Share in total value added

2019, as per cent



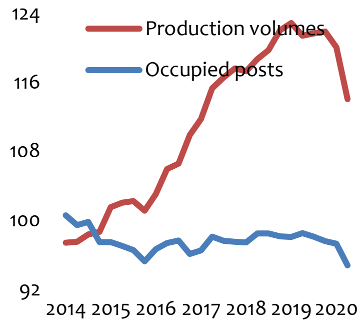
Changes in production volumes

as per cent



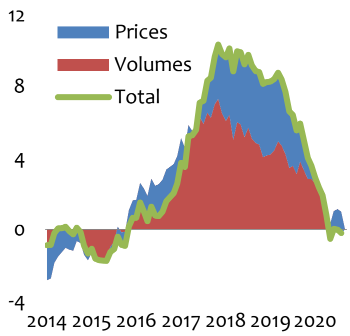
Production volumes and occupied posts

Q4 2013 = 100



Changes in sales of production

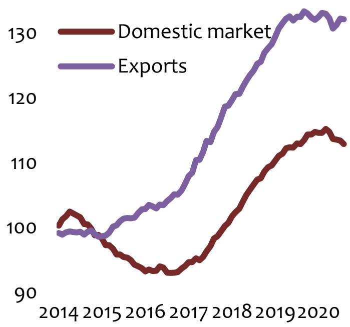
12-month moving average



Production sales

December 2013 = 100,

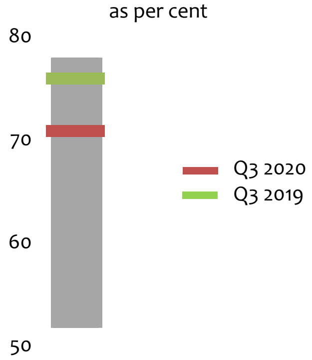
12-month moving average



Capacity utilization rate

Historically highest/ lowest level,

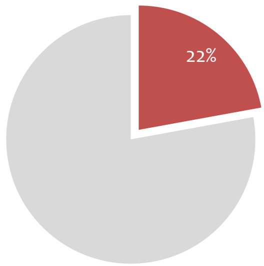
as per cent



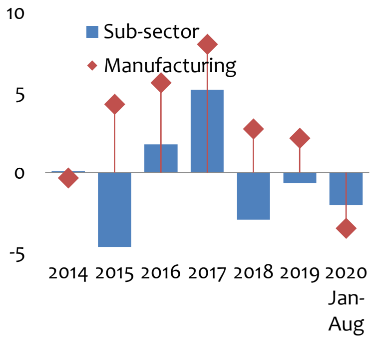
[1] Sales data available until August 2020

Manufacture of food products and beverages

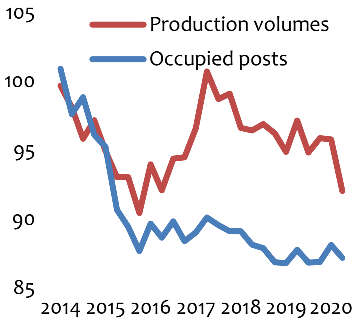
Share in total value added
2019, as per cent



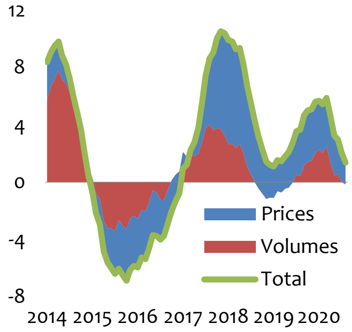
Changes in production volumes
as per cent



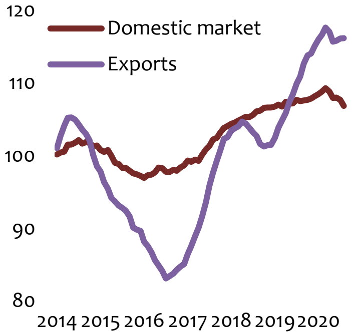
Production volumes and occupied posts
Q4 2013 = 100



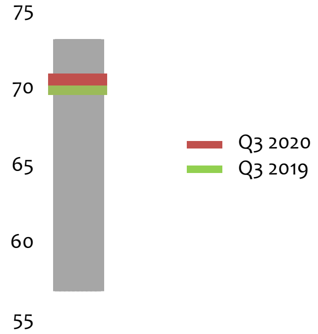
Changes in sales of production
12-month moving average



Production sales
December 2013 = 100,
12-month moving average

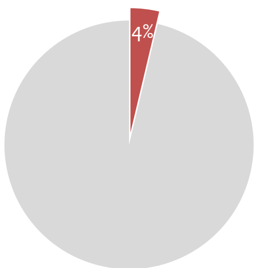


Capacity utilization rate
Historically highest/ lowest level,
as per cent

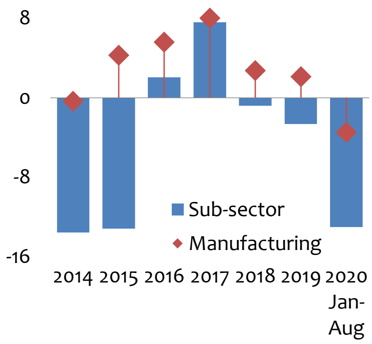


Light industry

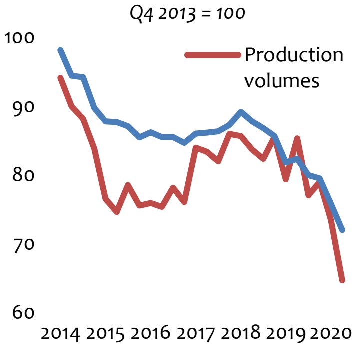
Share in total value added
2019, as per cent



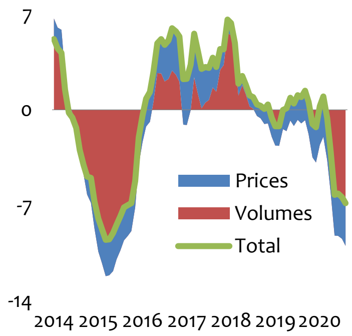
Changes in production volumes
as per cent



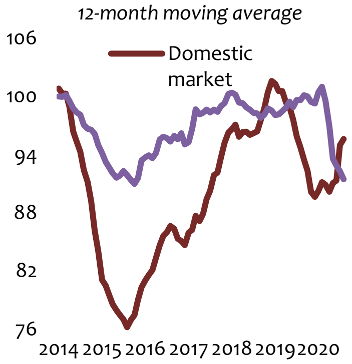
Production volumes and occupied posts
Q4 2013 = 100



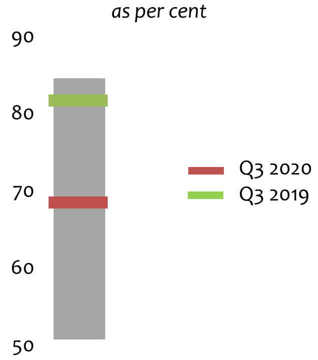
Changes in sales of production
12-month moving average



Production sales
December 2013 = 100,
12-month moving average

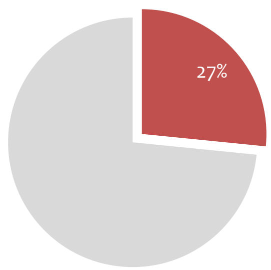


Capacity utilization rate
Historically highest/ lowest level,
as per cent

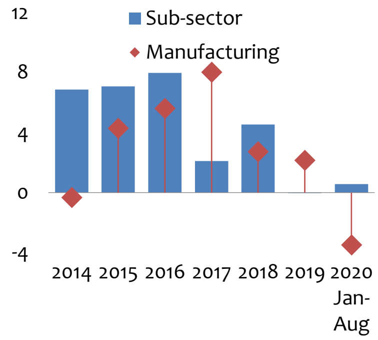


Manufacture of wood and articles of wood

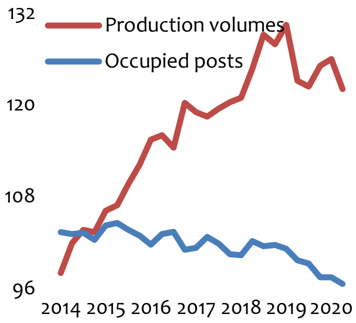
Share in total value added
2019, as per cent



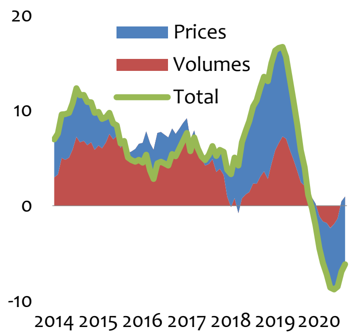
Changes in production volumes
as per cent



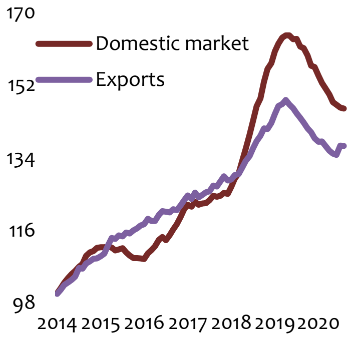
Production volumes and occupied posts
Q4 2013 = 100



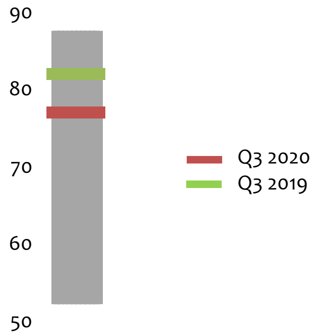
Changes in sales of production
12-month moving average



Production sales
December 2013 = 100,
12-month moving average

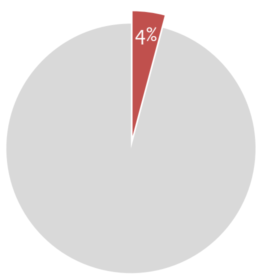


Capacity utilization rate
Historically highest/ lowest level,
as per cent

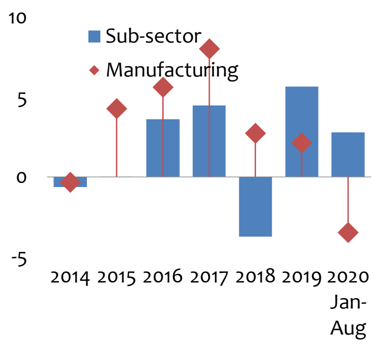


Manufacture of paper and paper products

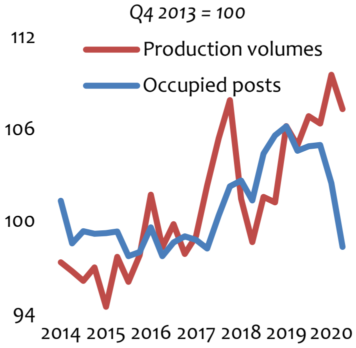
Share in total value added
2019, as per cent



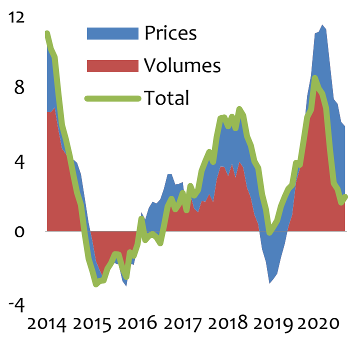
Changes in production volumes
as per cent



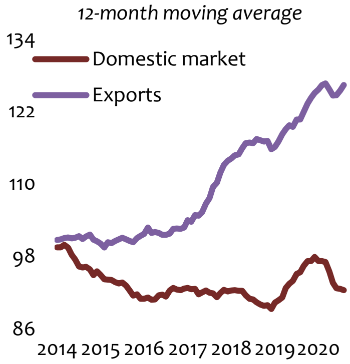
Production volumes and occupied posts
Q4 2013 = 100



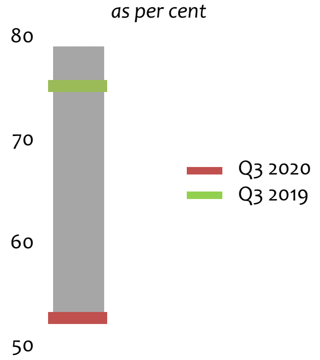
Changes in sales of production
12-month moving average



Production sales
December 2013 = 100,
12-month moving average

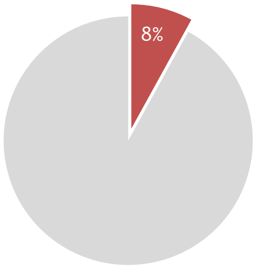


Capacity utilization rate
Historically highest/ lowest level,
as per cent

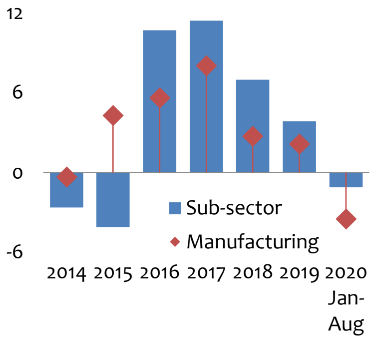


Manufacture of chemicals and chemical products

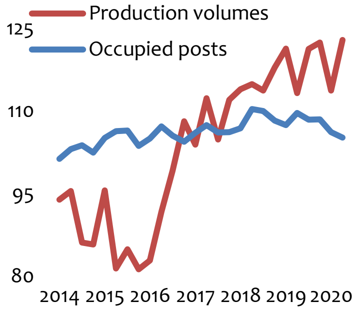
Share in total value added
2019, as per cent



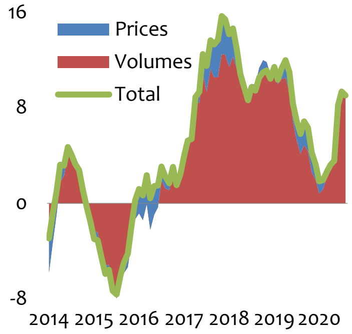
Changes in production volumes
as per cent



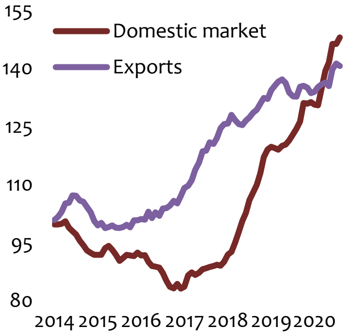
Production volumes and occupied posts
Q4 2013 = 100



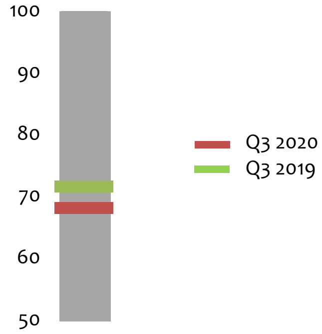
Changes in sales of production
12-month moving average



Production sales
December 2013 = 100, 12-month moving average

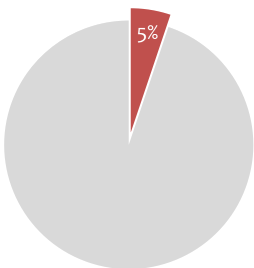


Capacity utilization rate
Historically highest/ lowest level, as per cent

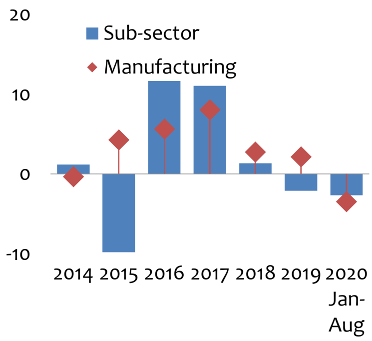


Manufacture of non-metallic mineral products

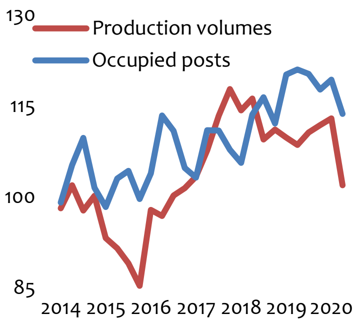
Share in total value added
2019, as per cent



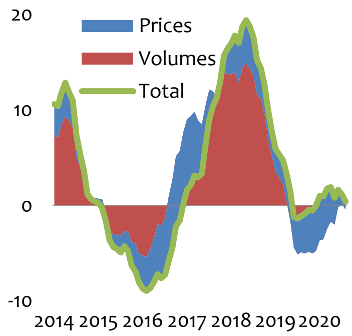
Changes in production volumes
as per cent



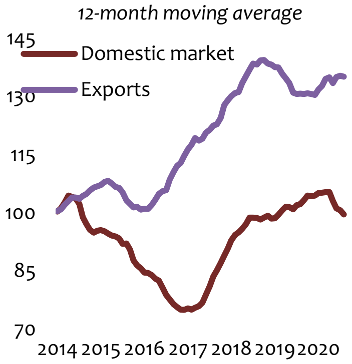
Production volumes and occupied posts
Q4 2013 = 100



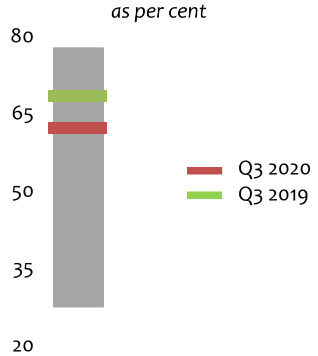
Changes in sales of production
12-month moving average



Production sales
December 2013 = 100, 12-month moving average

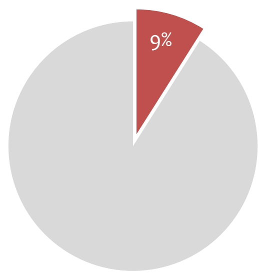


Capacity utilization rate
Historically highest/ lowest level, as per cent

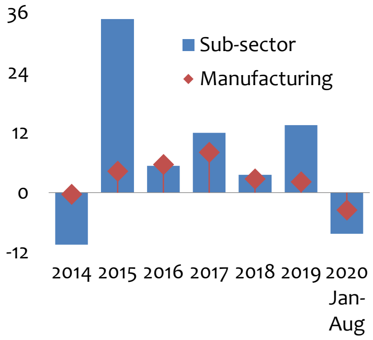


Manufacture of basic metals and fabricated metal products

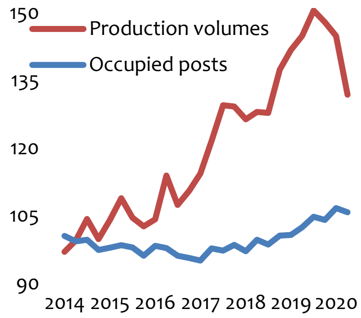
Share in total value added
2019, as per cent



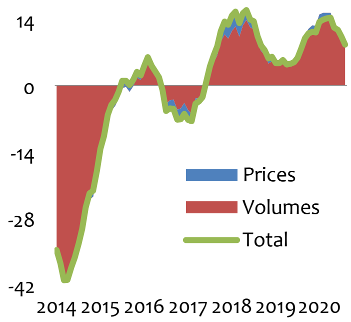
Changes in production volumes
as per cent



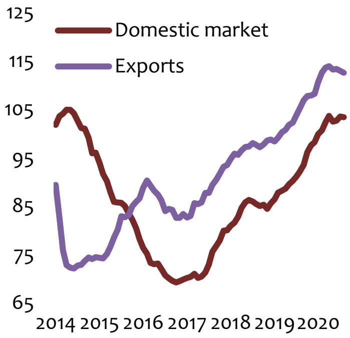
Production volumes and occupied posts
Q4 2013 = 100



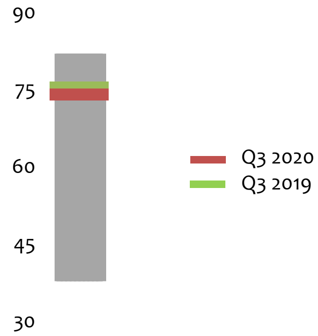
Changes in sales of production
12-month moving average



Production sales
December 2013 = 100,
12-month moving average

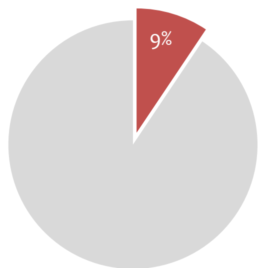


Capacity utilization rate
Historically highest/ lowest level,
as per cent

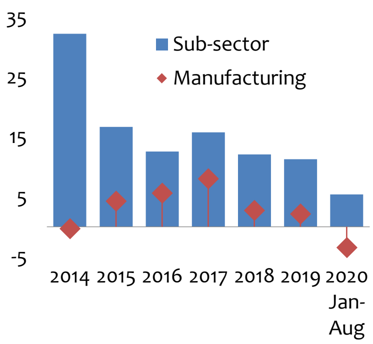


Manufacture of electronic and optical products

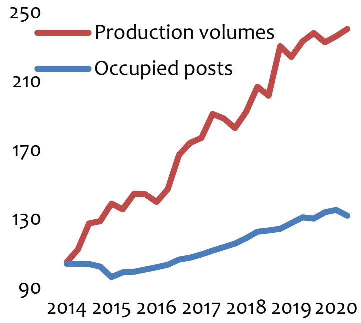
Share in total value added
2019, as per cent



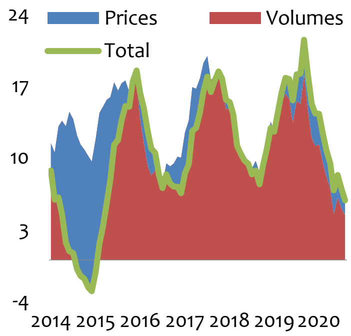
Changes in production volumes
as per cent



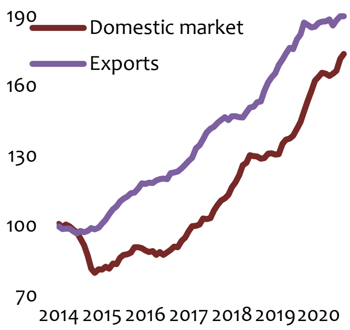
Production volumes and occupied posts
Q4 2013 = 100



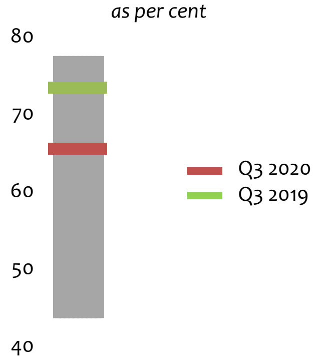
Changes in sales of production
12-month moving average



Production sales
December 2013 = 100,
12-month moving average

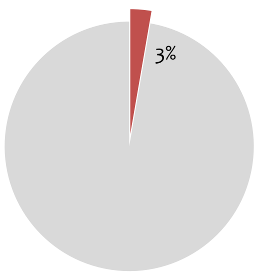


Capacity utilization rate
Historically highest/ lowest level,
as per cent

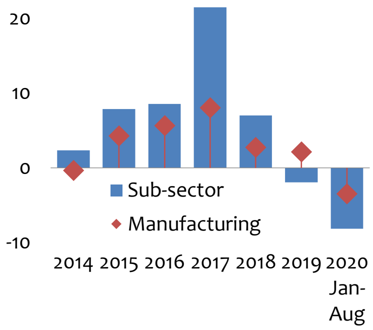


Manufacture of machinery and equipment

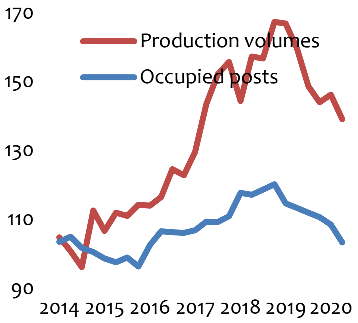
Share in total value added
2019, as per cent



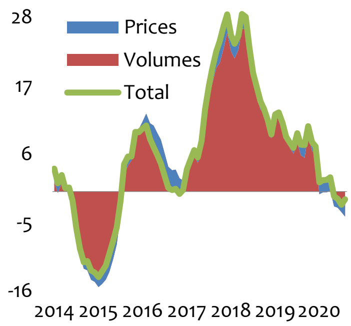
Changes in production volumes
as per cent



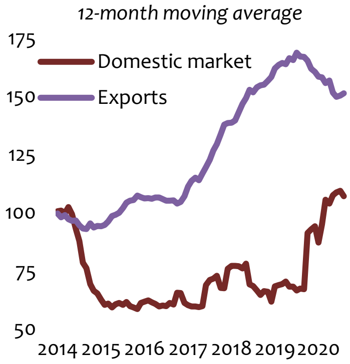
Production volumes and occupied posts
Q4 2013 = 100



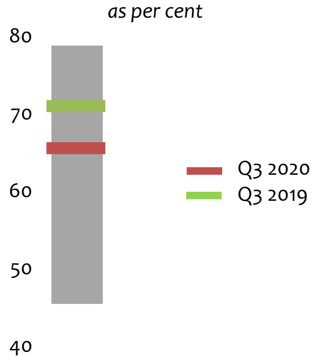
Changes in sales of production
12-month moving average



Production sales
December 2013 = 100,
12-month moving average

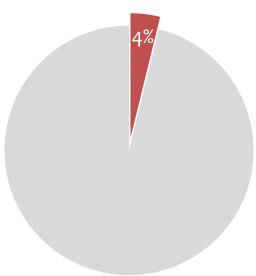


Capacity utilization rate
Historically highest/ lowest level,
as per cent

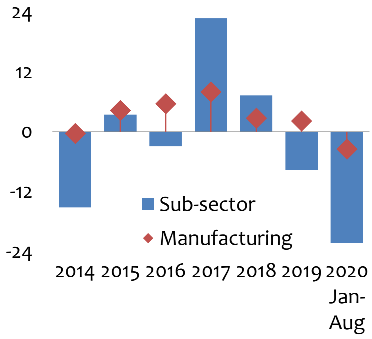


Manufacture of motor vehicles

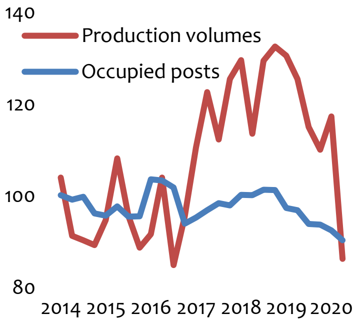
Share in total value added
2019, as per cent



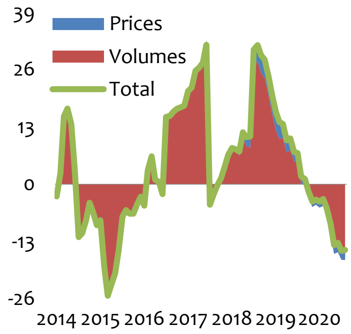
Changes in production volumes
as per cent



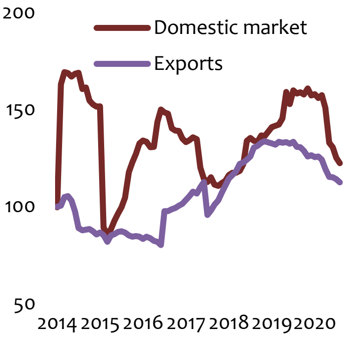
Production volumes and occupied posts
Q4 2013 = 100



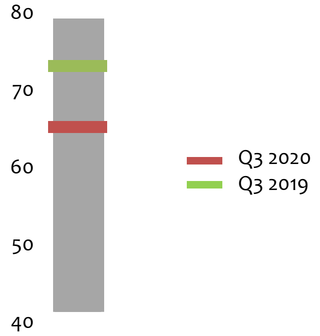
Changes in production sales
12-month moving average



Production sales
December 2013 = 100,
12-month moving average

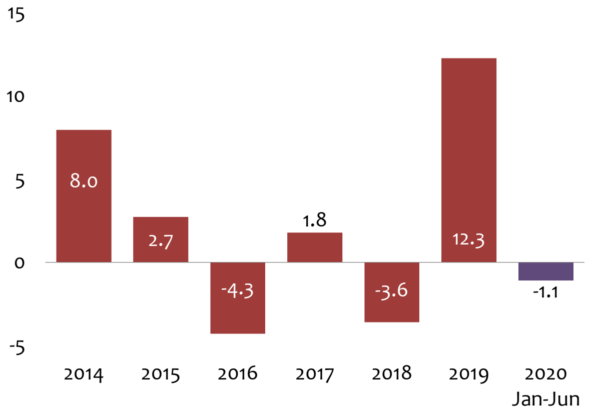


Capacity utilization rate
Historically highest/ lowest level,
as per cent



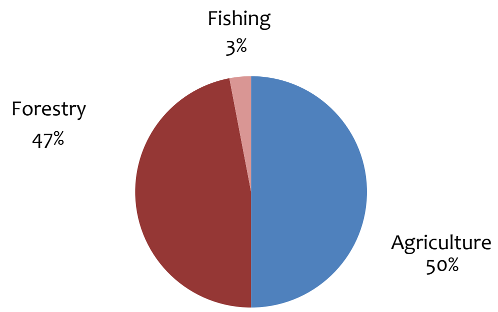
AGRICULTURE, FORESTRY, AND FISHING

Agriculture, Forestry, and Fishing
value added, changes against the corresponding period last year, as per cent



Agriculture and forestry provide the largest contribution to growth within the sector. The economic activity of the sector is closely tied to weather conditions. Thus, volatile growth within the sector can be observed. In 2019, a rapid increase in production volumes was observed due to favourable weather conditions and rapid growth in crop production. However, in the first half of 2020, the volumes in the sector have declined. In agriculture, production volumes increased in crop production; however, a decline was observed in livestock production. Also, production volumes in forestry and fisheries decreased. In recent years, the number of employees and occupied posts have been on the rise, already exceeding the pre-crisis levels. Occupied posts grew at a higher rate, indicating that the sector is increasingly using paid labour. In the first half of 2020, the number of occupied posts declined, especially in the forestry sector, due to Covid-19 outbreak.

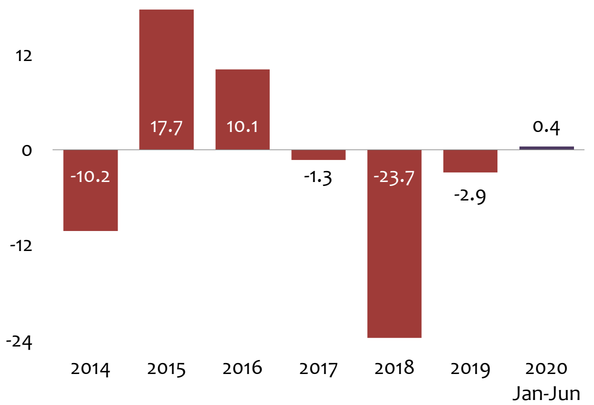
Structure of Agriculture, Forestry, and Fishing
2019, as per cent*



* – forecast by the Ministry of Economics

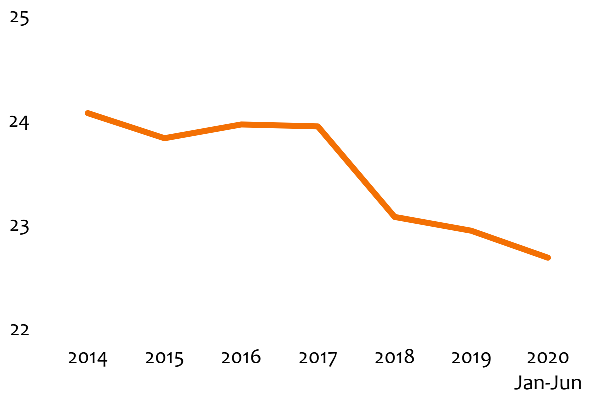
OTHER MANUFACTURING

Other Manufacturing
value added, changes against the corresponding period last year, as per cent



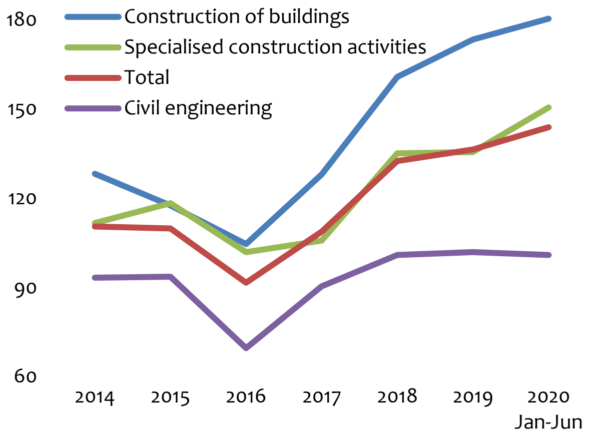
The largest share of added value in other manufacturing (incl. mining and quarrying, electricity, gas, steam, and air-conditioning supply, water supply, and waste management) provide electricity and gas supply sub-sectors. In 2017-2019, the volumes of other manufacturing decreased, primarily determined by the decline in the electricity and gas supply due to warm weather conditions. In the first half of 2020, the volumes of other manufacturing remained essentially unchanged. Favourable weather conditions contributed to the development of the mining and quarrying. However, non-seasonal warm weather significantly reduced the supply of natural gas. The number of occupied posts declined in the electricity, gas, steam, and air conditioning supply, the water supply, and waste management sectors.

Occupied Posts in Other Manufacturing
in thousands

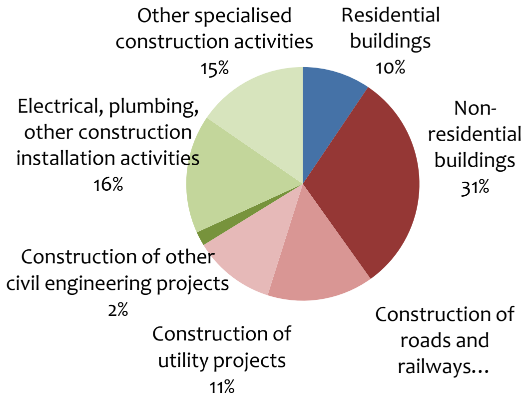


CONSTRUCTION

Development of Construction
2013 = 100



Structure of Construction
January-June 2020, as per cent

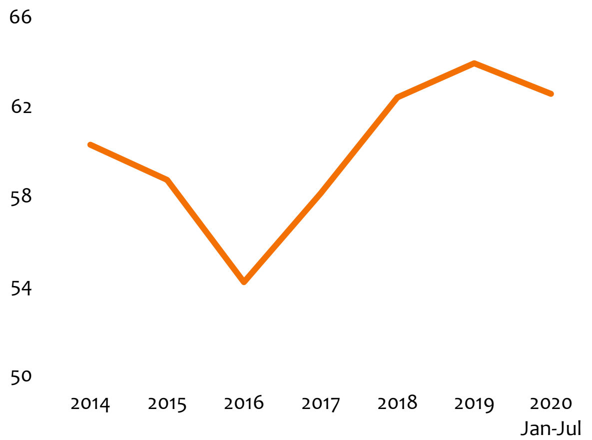


Despite the restrictions imposed due to the spread of the coronavirus, construction output increased by 5.5% in the first half of the year, compared to the corresponding period last year. However, in Q2 of 2020, the impact was more noticeable, as the volumes of construction output were 0.6% lower than in Q2 of 2019.

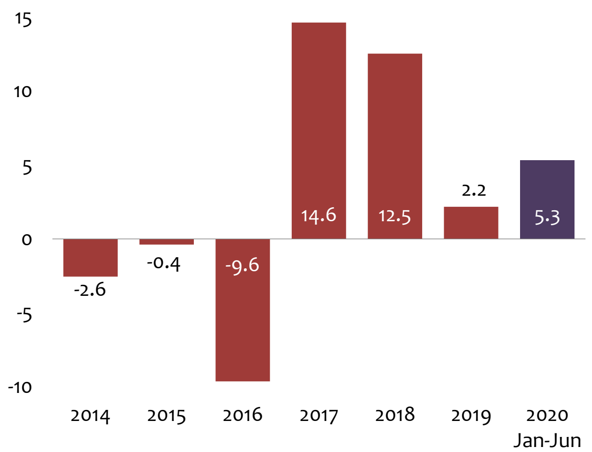
In Q2 of 2020, specialized construction works increased, compared to the corresponding period last year; however, the volumes of construction of buildings and civil engineering declined.

In the first half of 2020, the number of building permits granted reached 2199, representing a 11.4% decline, compared to the corresponding period last year. It can primarily be attributed to a decrease in the number of building permits granted for the construction of residential buildings.

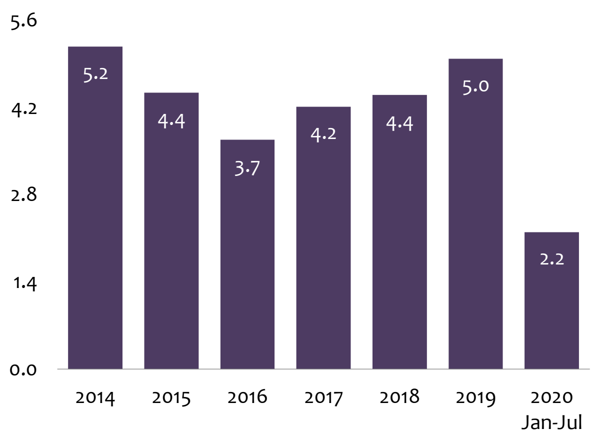
Occupied Posts in Construction
in thousands



Construction
value added, changes against the corresponding period last year, as per cent

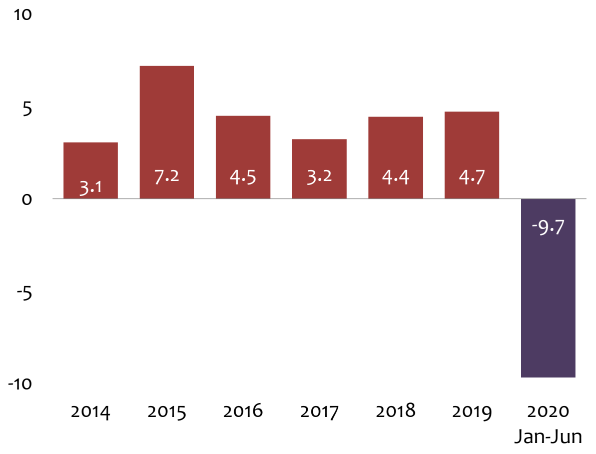


Building Permits Granted
in thousands



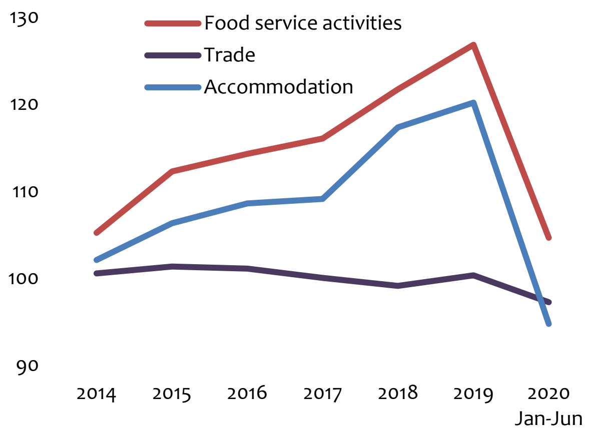
TRADE, ACCOMMODATION, AND FOOD SERVICE ACTIVITIES

Trade, Accommodation, and Food Service Activities
value added, changes against the corresponding period last year, as per cent

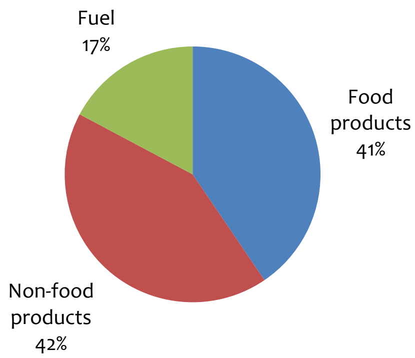


In the first half of 2020, the volumes of services provided in the trade, accommodation, and food service activities decreased sharply. Trade was negatively affected by the fall in private consumption, rising unemployment and declining incomes. In the first half of 2020, it decreased by 5.5%. In the first half of 2020, retail turnover experienced similar growth patterns as in Q1 of 2019, increasing by only 0.4%. Retail sales of food products and fuel increased, whereas sales of non-food products declined. The turnover of the wholesale sector at current prices decreased by 12.1%. The accommodation and food service activities were negatively affected by the strict measures put in place to limit the spread of the virus. In the first half of 2020, the sector volumes declined by 38.7%. The largest share of occupied posts prevails in trade. In the first half of 2020, due to the Covid-19 outbreak, the number of occupied posts decreased in both sectors; however, an especially abrupt decline was observed in the accommodation and food service activities.

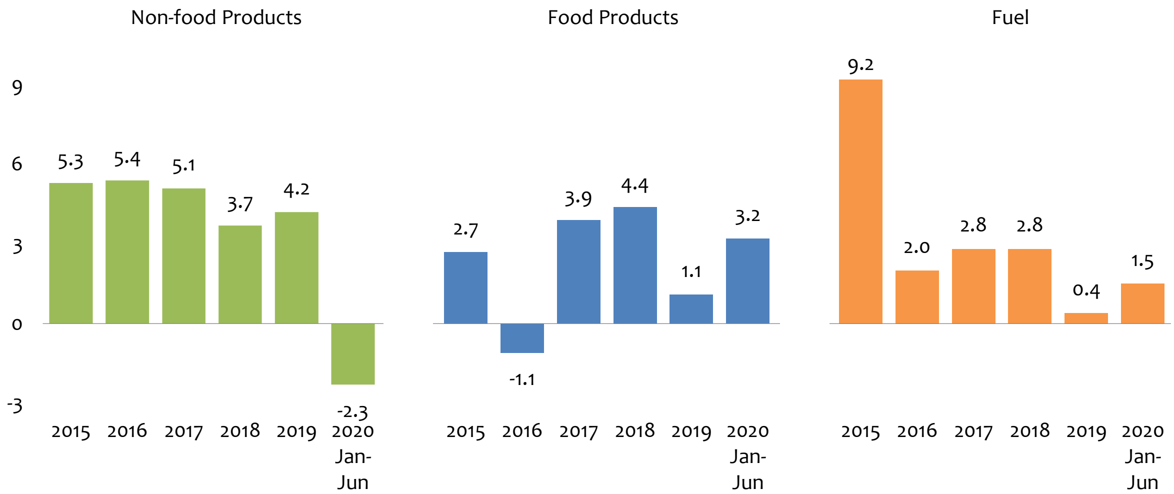
Occupied Posts In Trade, Accommodation, and Food Service Activities
2013 = 100



Structure of Retail Turnover
2019, as per cent

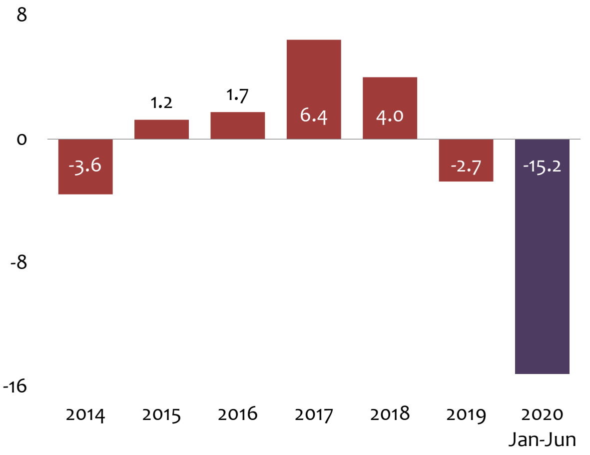


Retail Turnover
changes as per cent



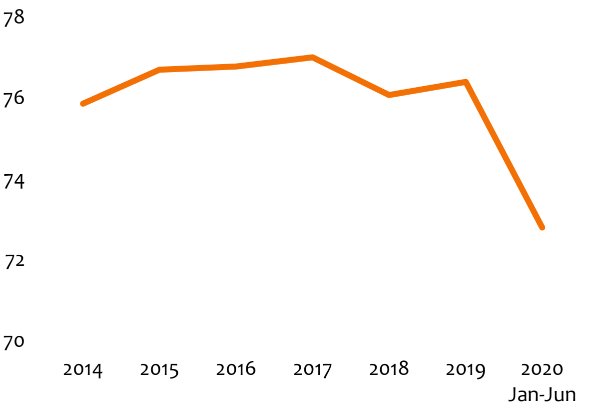
TRANSPORTATION AND STORAGE

Transportation and Storage
value added, changes against the corresponding period last year, as per cent

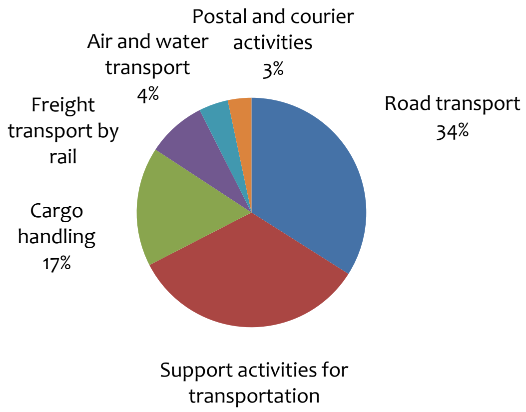


The transportation and storage sector is closely linked to international transportation. Between 2014-2019, the sector's volumes increased only by 1.1% annually, reflecting a decline in freight transport caused by Russia's transport policies and increased competition. In the first half of 2020, the volumes of the sector decreased rapidly. The restrictions on Covid-19 had a significant impact on air transport, land transport, and transport by rail. A sharp decline in freight transport by rail and at ports was observed; however, volumes of freight transport by road increased slightly due to an increase in volumes domestically. Passenger traffic decreased across all modes of transportation. The sharpest decline in the number of passengers was observed in air transport - by 62.9%. At ports the number of passengers decreased by 57.2%; whereas in land transport - by 38.9%.

Occupied Posts In Transportation and Storage
in thousands

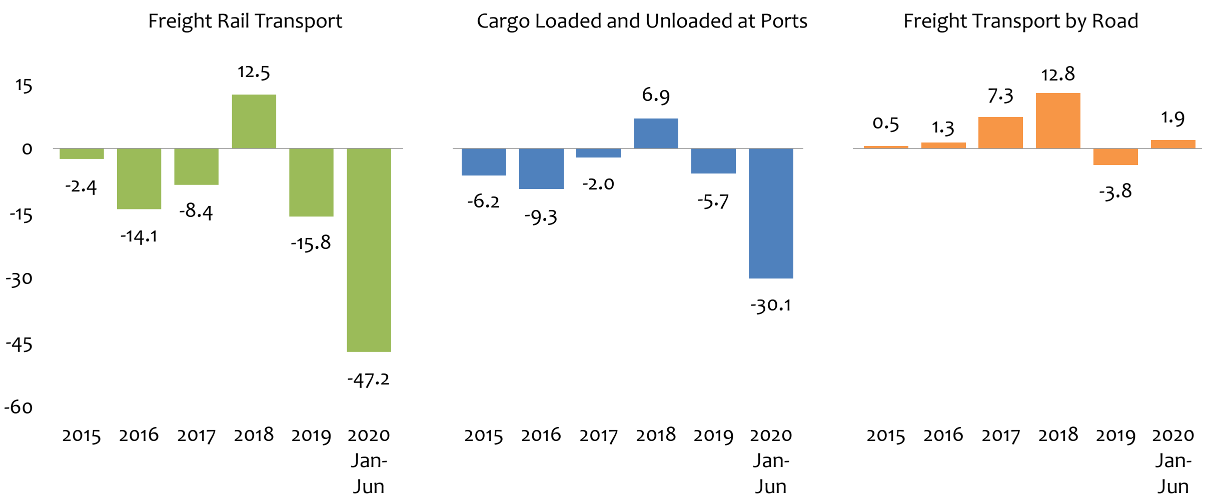


Structure of Transportation and Storage
2019, as per cent



* – forecast by the Ministry of Economics

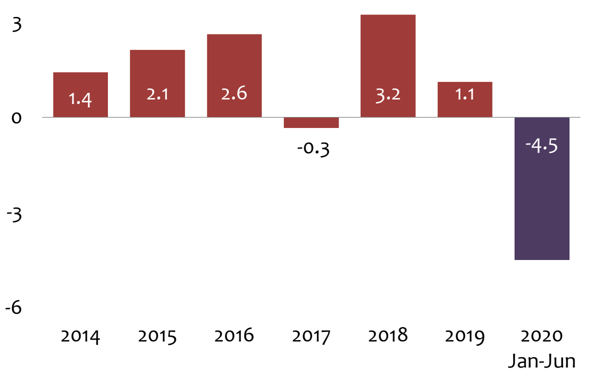
Freight Traffic
changes as per cent



COMMERCIAL SERVICES

Commercial Services

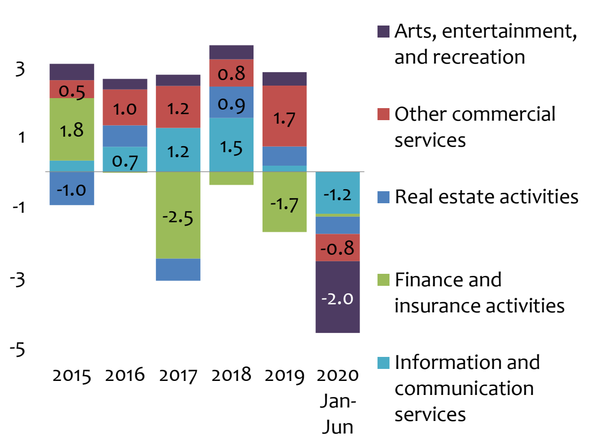
value added, changes against the corresponding period last year, as per cent



The largest share of added value in commercial services (incl. information and communication services, financial and insurance activities, real estate activities, professional, scientific, and technical services, administrative and support service activities, arts, entertainment, and recreation) provide real estate activities. In the first half of 2020, due to the Covid-19 crisis, the volume of commercial services decreased rapidly in all sectors. The largest impact was due to the decline in the arts, entertainment, and recreation, which was negatively affected by the strict measures put in place to contain the Covid-19 pandemic. In other sectors, the effects of volume reductions were similar. The largest share of occupied posts remains in professional, scientific, and technical services, administrative and support service activities, and ICT services. In the first half of 2020, the number of occupied posts decreased rapidly in the arts, entertainment, and recreation; however, an increase was observed in ICT services.

Contribution of Commercial Services

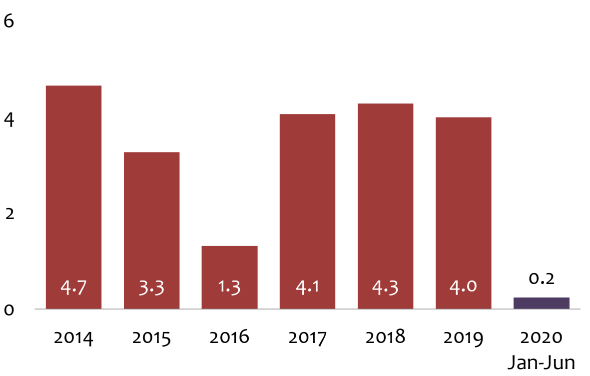
changes as per cent



PUBLIC SERVICES

Public Services

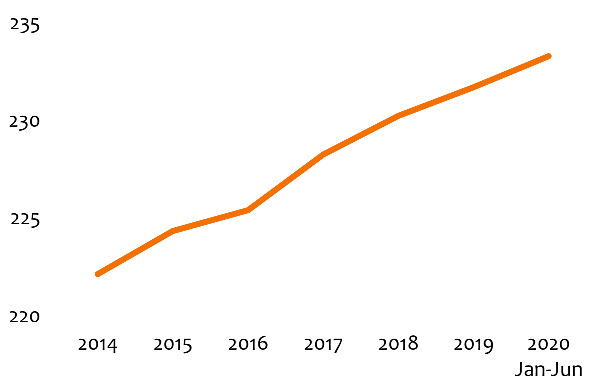
value added, changes against the corresponding period last year, as per cent



The largest share of value added in public services (incl. public administration and defence, education, health and social work activities) provide public administration and defence. In the first half of 2020, the public service sector was also negatively affected by the Covid-19 crisis. The volume of services remained essentially unchanged, compared to the corresponding period last year. The volume of public administration and defence increased by 1.4%; however, the volume of health and social care services decreased by 1.3%, whereas the volumes of education services remained unchanged. The largest share of occupied jobs is in education. The fastest job growth in recent years has been in healthcare. Also, in the first half of 2020, a rapid increase in the number of occupied posts was observed in health care; nonetheless, the number of occupied posts in public administration continued to decline.

Occupied Posts in Public Services

in thousands



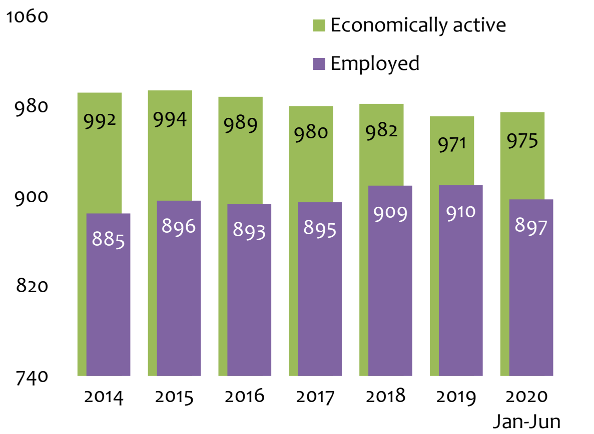
2020 | 2 LABOUR MARKET

EMPLOYMENT AND UNEMPLOYMENT

The Covid-19 crisis has contributed to the growing structural imbalances in the labour market. The Covid-19 pandemic has had a negative impact on the labour market, especially in sectors such as tourism, accommodation, and catering, transport (i.e., passenger transport), the arts, entertainment, and recreation.

However, despite the rise in unemployment, the number of vacancies in the labour market remained high, indicating an increase in the risks of structural unemployment. Differences between changes in the employed population and the number of occupied posts in the second quarter of 2020 indicate an increase in the share of unregistered employment in the economy during the Covid-19 pandemic.

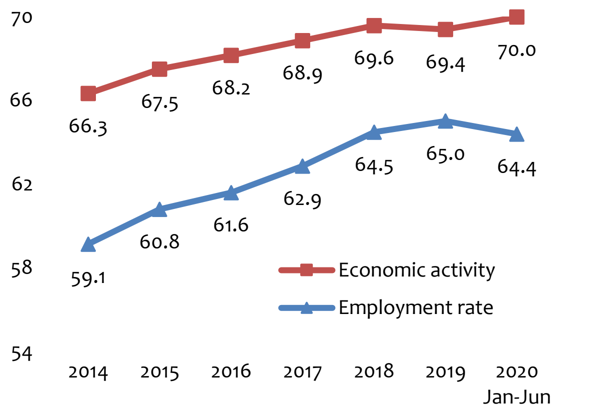
Employed and Economically Active
aged 15-74, in thousands



A moderate decline in the number of employees, can be observed; however, the economic activity is rising. In Q2 of 2020, the number of employees decreased by 13.5 thousand (i.e., by 1.5%), representing a sharper decline in employment, compared to the last year. In Q2 of 2020, the number of employees decreased to 892.1 thousand; however, its level among the population aged 15-74 declined to 64.1% (i.e. by 0.6 percentage points lower than a year ago).

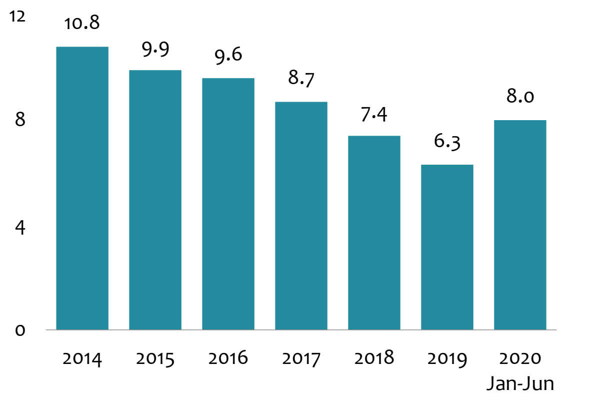
The negative impact of Covid-19 on the employment was mitigated by the introduction of allowances for idle time, which partially ensured the preservation of jobs and personal income during the emergency period. However, the average decrease in the number of employees in normal time units by 7%, compared to the Q2 of 2019, indicates that the decline in workload and real employment of the population has been significantly higher.

Employment and Economic Activity
aged 15-74, as per cent



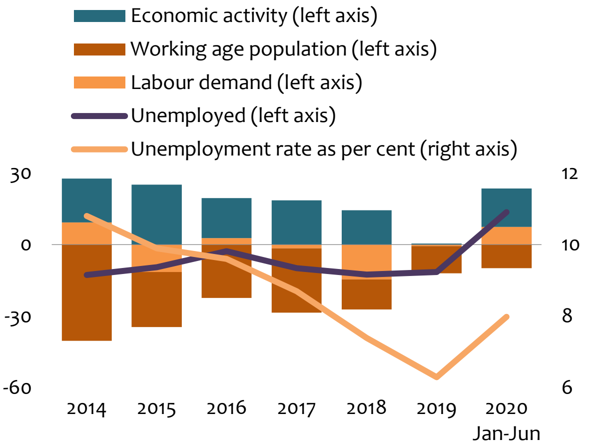
The negative effects of Covid-19 crisis are vividly reflected in the dynamics of unemployment. In Q2 of 2020, the number of jobseekers increased by 22 thousand, reaching 72.2 thousand, which is the highest level since tQ3 of 2017. In Q2 of 2020, the unemployment rate approached the average level of 2017, reaching 8.6%, which is 2.2 percentage points higher than in Q2 of 2019.

Unemployment Rate
aged 15-74, as per cent



Higher growth rate of the number of jobseekers, in comparison to the decline in the number of employees, has been promoted by the growth in economic activity, which increased to 70.1% in the 2nd quarter of 2020, representing a 1.1 percentage point increase, compared to 2019.

Unemployment Rate and Its Determinants
changes against the last year, in thousands

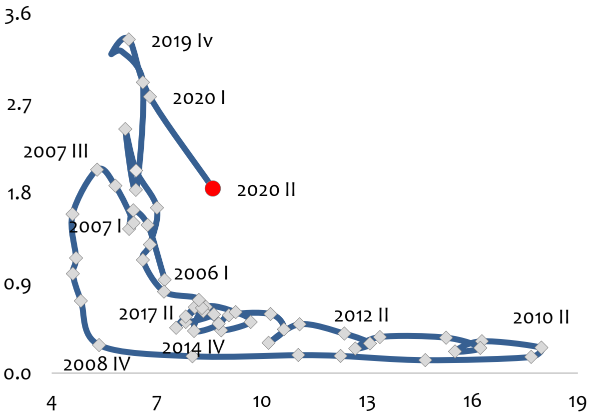


Overall, in Q2 of 2020, the number of economically active population increased by 8.5 thousand, reaching 975.6 thousand.

It should be noted that along with the decline in economic activity, the labour market is also affected by the negative demographic trends. Therefore, both the dynamics of the total number of employees and unemployment rate are negatively affected.

Risks of structural unemployment are rising. The current crisis has accelerated the digitalisation of the economy and the automation of jobs increasing labour productivity potential on the one hand and changing the structure of skills demand in the labour market on the other.

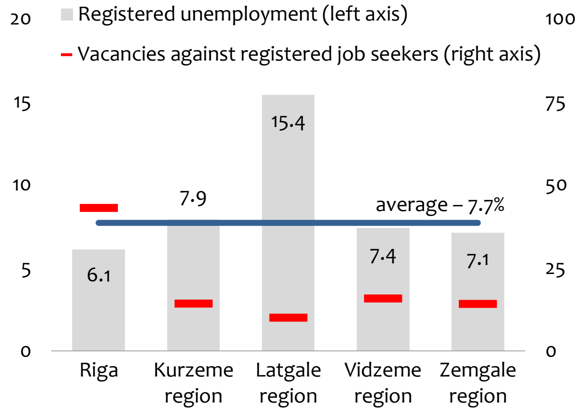
Beveridge Curve
by quarters as per cent; horizontal axis – unemployment rate; vertical axis – vacancies against the economically active population



In Q2 of 2020, the increase in the number of jobseekers has been significantly outpaced the decrease in vacancies compared to the total labour supply / economically active population (see Beveridge curve). Therefore, despite the increase in vacancies, a large share of occupied posts / vacancies remains vacant.

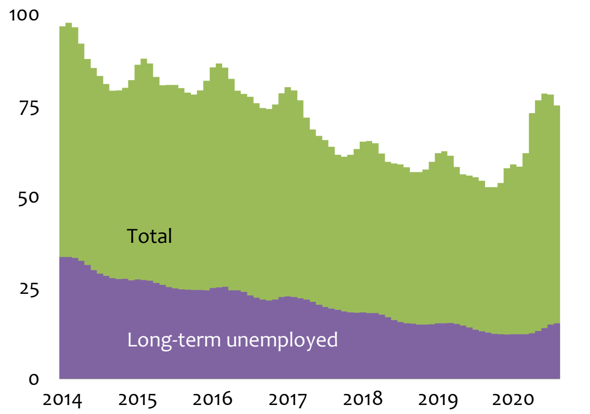
Structural problems may also be exacerbated by significant regional disparities in the labour market, as well as rising long-term unemployment, which may hamper future labour market recovery.

Registered Unemployment by Region
at the end of September 2020, as per cent



Although regional disparities in the labour market have levelled off somewhat during the crisis, the unemployment rate in Latgale region still remains twice the average in the economy and almost 3 times higher than in Riga region, which combined with low labour mobility pose the risks of structural unemployment.

Registered Unemployed
in thousands



The relatively high share of long-term unemployed also poses risks to the increase in structural unemployment - about 1/5 of registered jobseekers are still unemployed for more than a year.

Overall, in Q2 of 2020, the unemployment rate was the fifth highest among the EU27 countries (i.e., 1.9 percentage points higher than the EU27 average), ranking close to

Lithuania (8.6%) and lagging behind Estonia by 1.7 percentage points (7.1%).

Half of the job losses have been in the sectors directly affected by the Covid-19 crisis. At the end of Q2 of 2020, the number of occupied posts decreased by 4.5% (or by 41.6 thousand), thus amounting to 882.6 thousand occupied posts.

Approximately half (i.e., 22.4 thousand) of the total job losses were in the sectors directly affected by the Covid-19 crisis (accommodation and food services; transport; the arts, entertainment, and recreation, and administrative and support service activities). The most severely was affected the accommodation and food service activities. During the year, the number of occupied posts declined by 10.1 thousand (or by 26.6%).

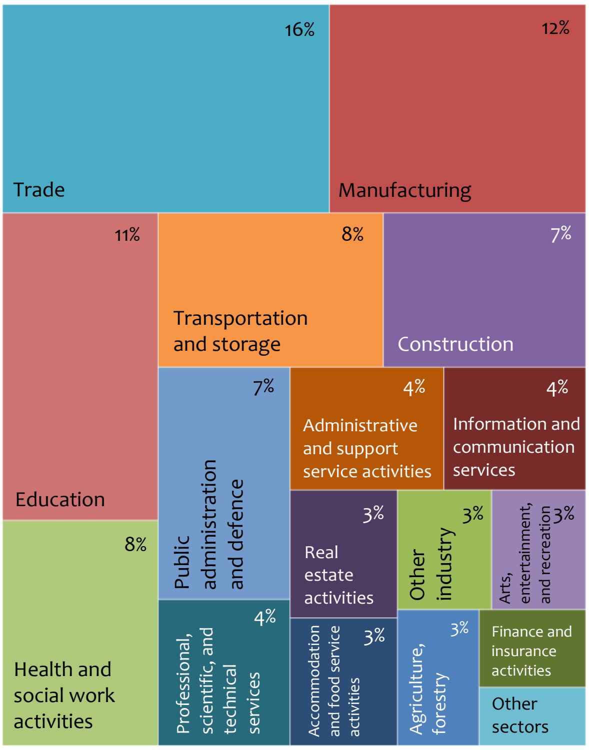
In some sectors, the demand for labour continued to grow in Q2 of 2020. The number of occupied posts increased in the ICT services (i.e., by 656 jobs or 1.9%, compared to Q2 of 2019). The increase primarily occurred in the computer programming and information services segments. Also, a significant increase in occupied posts in the health care sector (i.e., by 1,441 jobs or 2.1%) was observed.

In Q2 of 2020, the largest decline in occupied posts was observed in the private sector - by 35.7 thousand or 5.6%. Therefore, the number of occupied posts in the private sector has now returned to the level of 2014-2015.

Overall, the public sector has been less affected by the Covid-19 crisis - the number of occupied posts has decreased by 5.9 thousand or 2%. The largest job losses in the public sector have been in the transportation and storage, public administration, the arts, entertainment, and recreation.

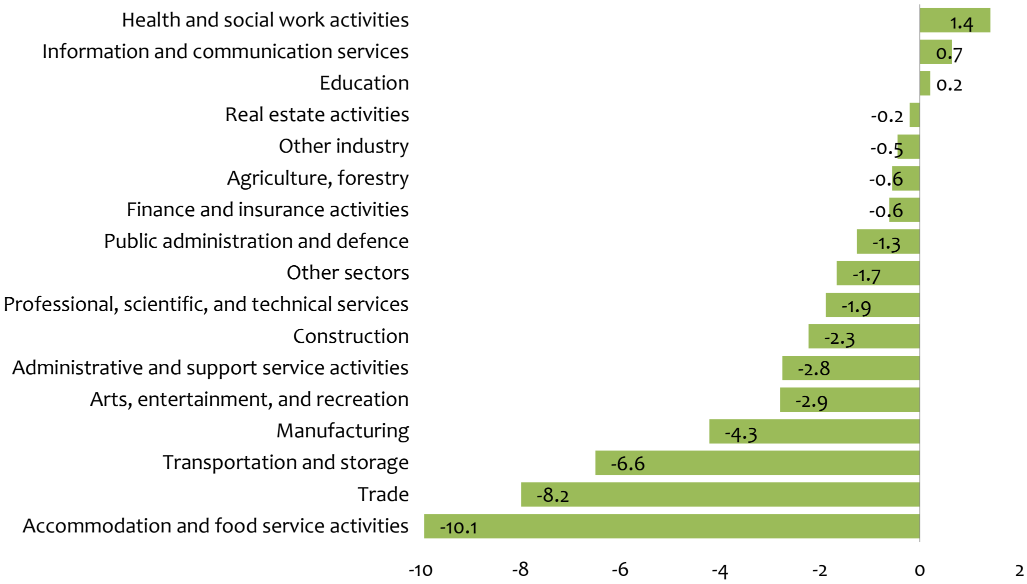
At the same time, it should be noted that the statistics on the number of occupied posts consider only medium-sized and large enterprises. Therefore, the overall job losses in the economy could be even higher.

Occupied Posts by Sector
structure in 2019, as per cent



Meanwhile, the differences in the number of occupied posts with the dynamics of the number of employees, according to the Labour Force Survey data, which also considers unregistered employment, indicate an increase in the shadow economy / unregistered employment during the Covid-19 crisis.

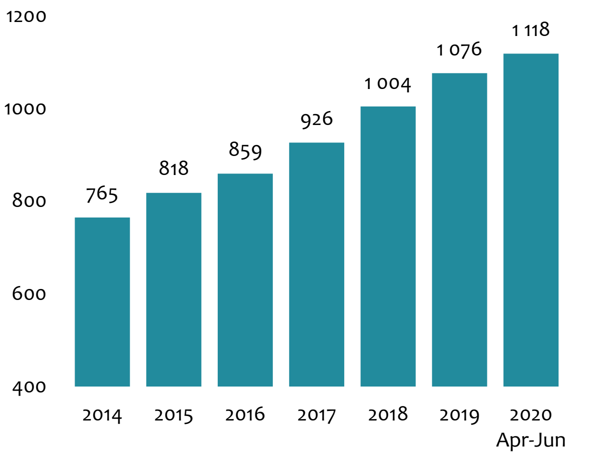
Changes In Occupied Posts
Q2 of 2020, compared to Q2 of 2019, in thousands



WAGES AND SALARIES

The average wage in the economy continues to grow; however, along with a decline in activity, the growth rates have moderated. In Q2 of 2020, the average monthly gross wage increased by 3.9%, thus reaching EUR 1 118. Although in Q2 of 2018 and 2019 the average gross wage increased by 7.1% and 8.4%, respectively, it still represents a notable increase. Wage growth on average has remained above 5% annually over the last four years. In 2018 and 2019, the average gross wage rose by 7.2% and 8.4%, respectively.

Average Monthly Gross Wage
euro

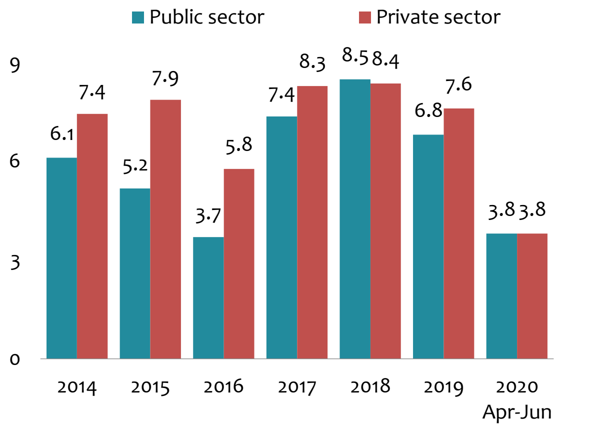


A large part of the wage growth was determined by the relatively high base effect at the end of 2019 and in Q1 of 2020 (EUR 1 100), when the activity in the labour market remained high. In Q1 of 2020, compared to Q2 of 2020, the average monthly gross wage increased by 1.6%.

Wage growth has been driven in part by a decline in the share of lower-paid jobs, given the significant decline in both the accommodation and food service activities, and the retail sector, where average wages have so far been significantly below the economy average.

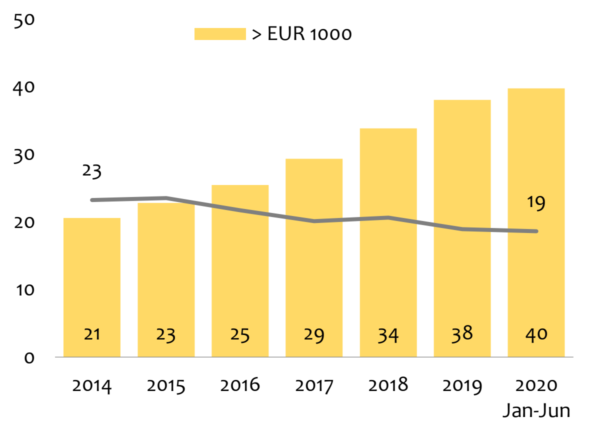
Wage growth has slowed equally in both the private and public sectors. In Q2 of 2020, the average monthly gross wage in both the private and public sectors was 3.8% higher than a year ago. Since 2010, wages have risen in both the private and public sectors. At the same time, growth in the private sector has been significantly higher. This can largely be attributed to the different dynamics of labour demand between sectors. Between 2011-2019, the number of occupied posts in the private sector and the public sector has increased by 20.2% and 1.3%, respectively.

Average Monthly Gross Wage
changes as per cent



In recent years, the share of minimum wage earners has been gradually declining. At the same time, the number of employees receiving a monthly gross wage above EUR 1 000 has increased. In Q2 of 2020, approximately 2/5 received a gross salary above EUR 1 000.

Employee Gross Wage
as per cent of total number employed



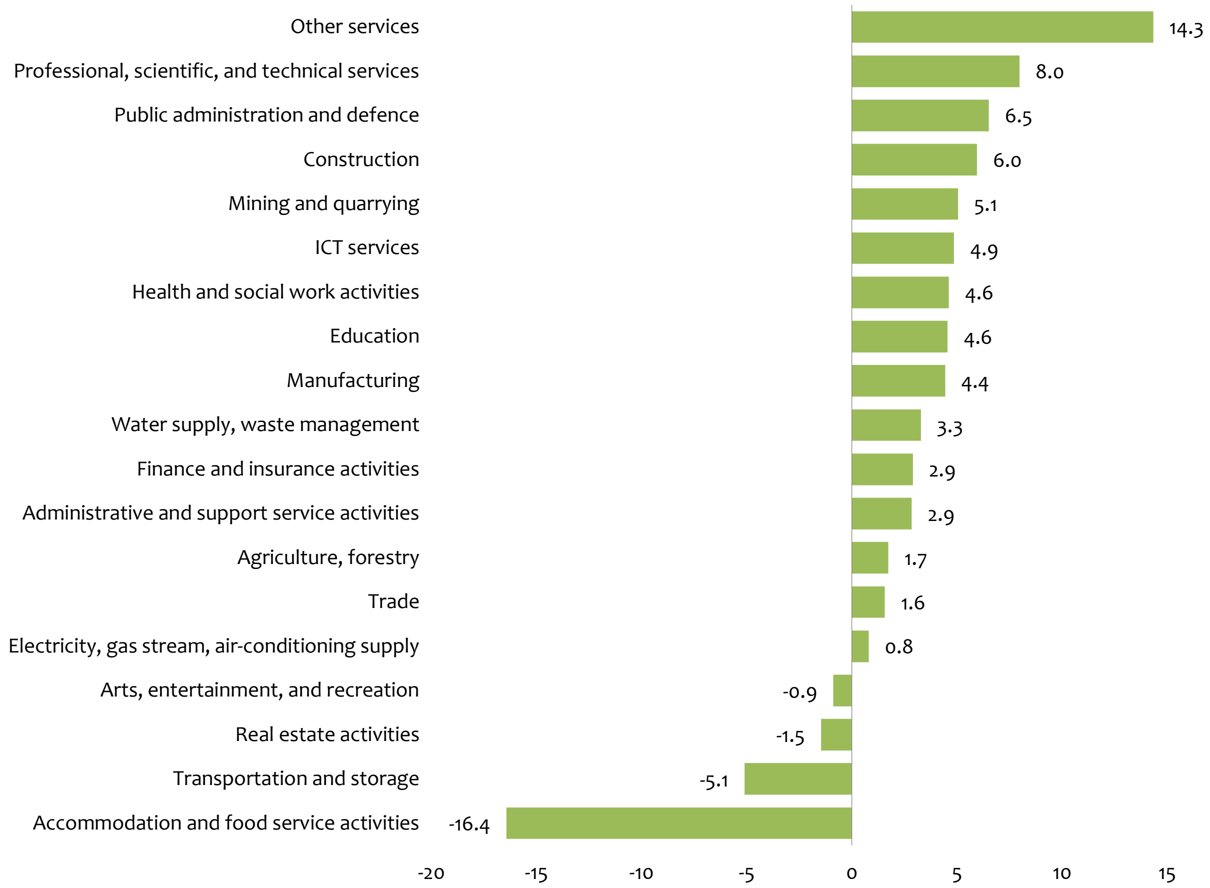
In Q2 of 2020, the highest wage growth was observed in other services, primarily in the repair of computers and personal and household goods (by 11.5%), public, political, and other organizations (by 14.2%), and professional, scientific, and technical services, wherein an increase was largely determined by wage rises in advertising and market research services (by 17.1%) and scientific research (by 10.8%).

The largest decline was observed in the accommodation and food service activities, wherein the average gross wage decreased by 16.4%; also, in the transportation and storage the average gross wage declined by 5.1%.

Meanwhile, in Q2 of 2002, the highest level of remuneration still remained in finance and insurance activities - the average gross monthly wage reached EUR 2 160.

Changes In Gross Wage

Q2 of 2020, compared to Q2 of 2019, as per cent



2020 | 2

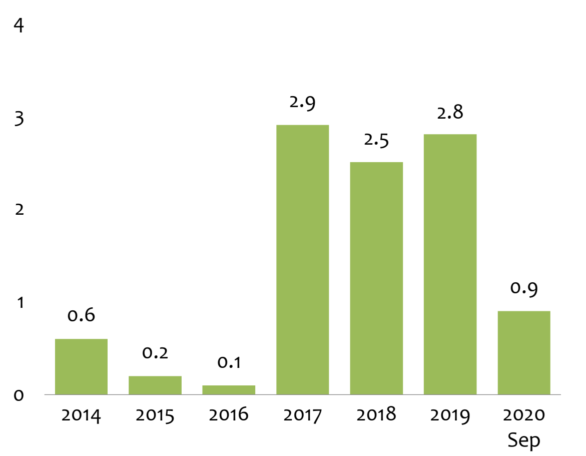
ECONOMIC STABILITY AND COMPETITIVENES

PRICES

In 2019, one of the largest price increases in recent years was observed. Consumer prices rose by 2.3%, but annual inflation rate was 2.8%. Rising prices for services and world price trends had a significant impact on consumer price levels.

In January-September 2020, prices fell due to Covid-19. In September 2020, compared to December 2019, consumer prices decreased by 0.1%. However, in comparison to September 2019, a decrease of 0.3% was observed. The average annual inflation in September 2020 was 0.9%.

Consumer Price Changes
annual average, as per cent



Key factors affecting overall price level in January-September 2020:

(1) falling prices for heat and natural gas due to tariff reductions caused by falling world oil prices. Electricity prices also fell due to higher hydropower development and falling demand due to the Covid-19 crisis;

(2) falling fuel prices due to falling world oil prices. Overall, in January-September 2020, oil prices decreased by 36%. The fall in oil prices was driven by falling oil demand and increasing restrictions on oil production due to the Covid-19 crisis;

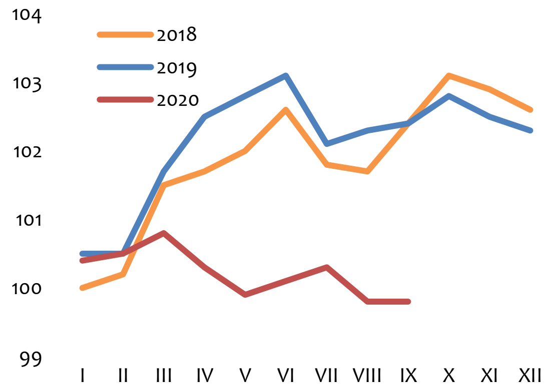
(3) rise in prices for services – in particular, the rise in prices for complex leisure services, outpatient services, food services, and cultural services;

(4) rising food prices, which were affected by rapid price rises at the beginning of the year and an uncharacteristic rise in July. The largest upward effect yielded the rise in prices for fresh fruit. World food prices fell by 3%. A decline was observed for meat, sugar, and dairy products; however, an increase was recorded for cereals and vegetable oils;

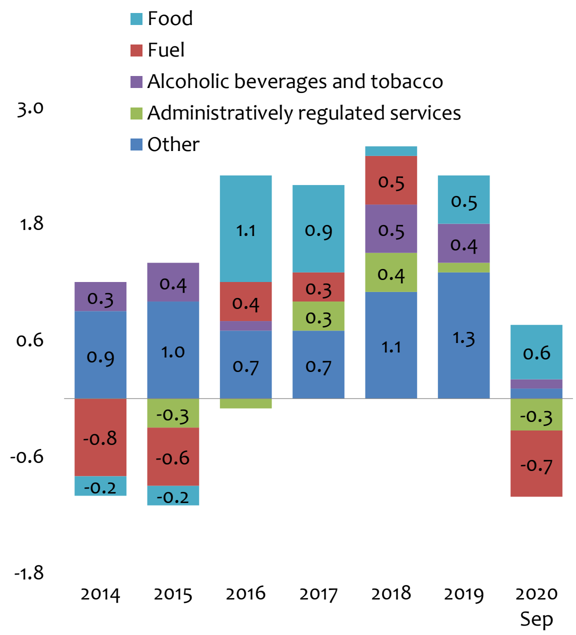
(5) increase in prices for alcoholic beverages and tobacco products due to increase in excise duty;

(6) price increase for footwear.

Consumer Price Index
December 2019 = 100

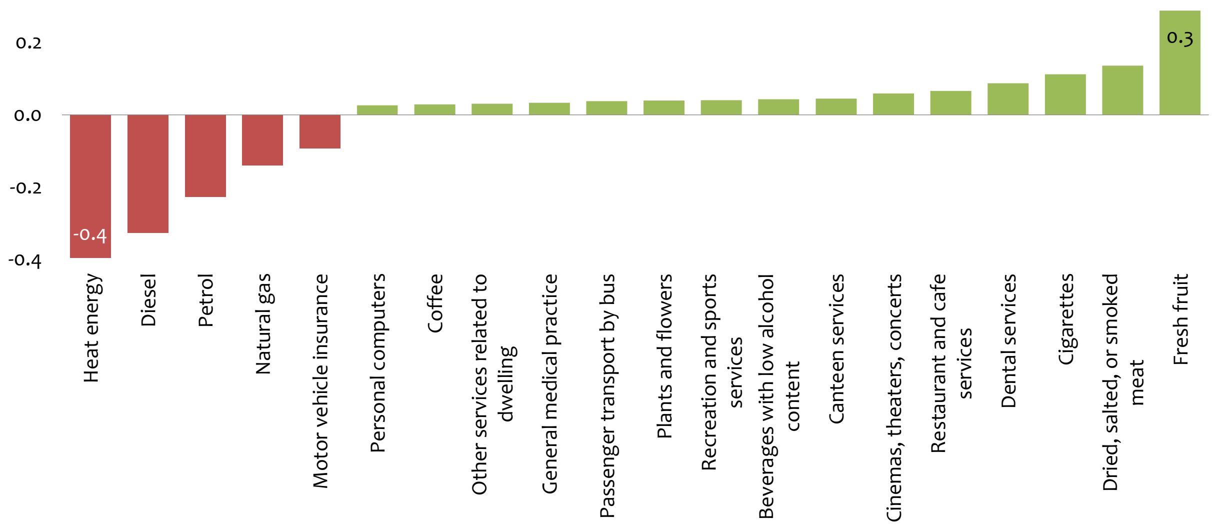


Consumer Prices by Goods and Services
contribution to 12-month changes, as per cent



Consumer Price Changes by Goods and Services

September 2020, contribution to 12-month changes, as per cent

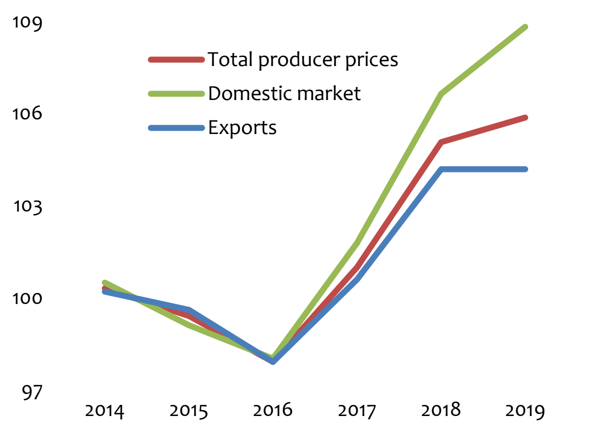


Overall, in 2020, the average annual inflation will be lower than in 2019. These will be determined by the impact of the Covid-19 pandemic on the development of the global economy, as well as the associated fluctuations in world prices. Supply and demand shocks will work contrarily and concurrently; therefore, inflation will remain volatile.

In 2019, producer prices increased much more slowly than in 2018, producer prices in manufacturing in 2019 rose moderately.

Producer Prices in Manufacturing

2013 = 100

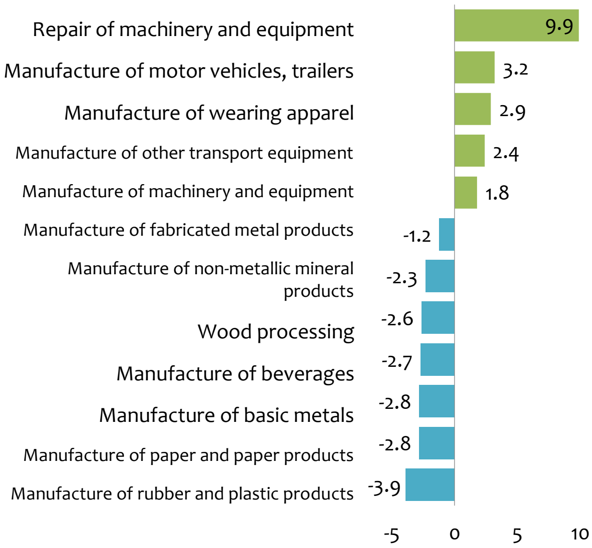


In 2020, a slight decline in producer prices in manufacturing was observed. In January-August 2020, producer prices in manufacturing decreased by 0.2%. Overall, in January-August 2020, producer prices in manufacturing for products sold domestically and exported products decreased by 0.1% and 0.3%, respectively. In January-August 2020, the most significant fall in prices was observed in the manufacture of non-metallic mineral products; on the other hand, the largest upward effect produced the of machinery and equipment and the manufacture of wood and wood products.

In 2020, manufacturing producer prices, compared to 2019, are prone to rise slowly or even decline. The level of producer prices is largely influenced by fluctuations in the producer prices of exported products, which are mainly determined by the dynamics of world raw material prices. It should be noted that world energy and raw material prices fell sharply in January-April 2020; however, since May 2020, prices have been rising. Fluctuations in raw material supply and demand in the context of the Covid-19 pandemic will also have a significant impact on producer prices. At the same time, the dynamics of producer prices for products sold on the domestic market will continue to be influenced by growth rates.

Producer Price Changes In Manufacturing in August 2020

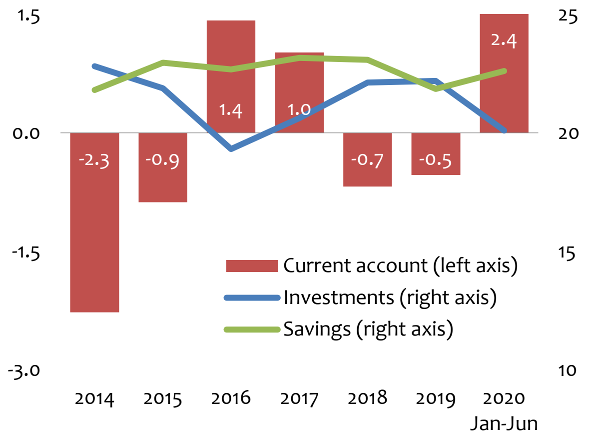
against the corresponding period last year, as per cent



BALANCE OF PAYMENTS

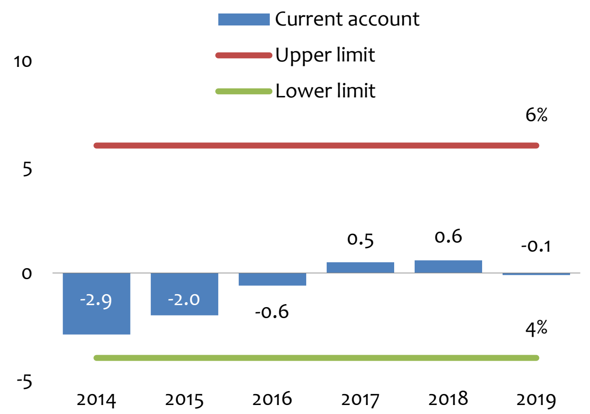
As a small open economy, Latvia is susceptible to external shocks, as demonstrated by the current account situation. In recent years, the current account has been close to balance, indicating that the Latvian economy has become more resilient since the financial crisis. The current account position in the first half of 2020 was determined by the shock caused by the COVID-19 pandemic, which affected cross-border flows of goods, services, and income. Thus, the current account surplus reached 2.4% of GDP.

Current Account, Savings, and Investment
as per cent of GDO



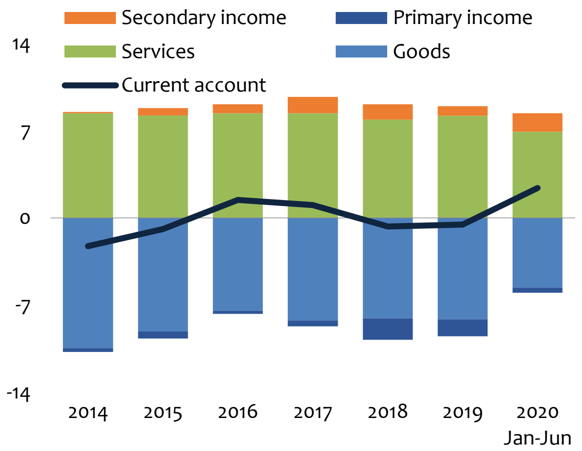
Between 2017-2019, the current account on average did not exceed the indicative thresholds set by the EU alert mechanism and thus is considered sustainable.

EU Alert System Indicative Threshold and Current Account
three-year average, as per cent of GDP



In recent years, external trade flows have weakened. It can primarily be attributed to the uncertainty in the external environment and declining external demand. In 2020, measures to limit the spread of the COVID-19 pandemic negatively affected trade. Latvia has a foreign trade deficit in goods. Over the last three years, the deficit on average constituted 8.2% of GDP (in 2019 - 8.1% of GDP). In H1 of 2020, the value of exports and imports of goods, compared to the corresponding period last year, was 1.5% and 8% lower, respectively. Also, the trade deficit declined to 5.6% of GDP (in the first half of 2019 - 8.7% of GDP).

Current Account
as per cent of GDP



Cross-border trade in services is more strongly affected by the Covid-19 shock than trade in goods. The services balance is positive, averaging 8.2% of GDP over the last three years and almost covering the foreign trade deficit. In 2020, the balance of services declined. In the first half of 2019, exports and imports of services at current prices decreased by 18.2% and 18.1%, respectively. Therefore, the surplus of the services balance decreased, reaching 6.9% of GDP (-8% in H1 of 2019). The decline in cross-border flows of services was due to restrictions on movement and the decline in leisure and business travel, which led to a decline in air travel and road transport services.

Changes in income and capital accounts are primarily due to variations in the absorption activities of EU funds. The capital account surplus has averaged 1.5% of GDP over the last three years. In H1 of 2020, it reached 2.8% of GDP.

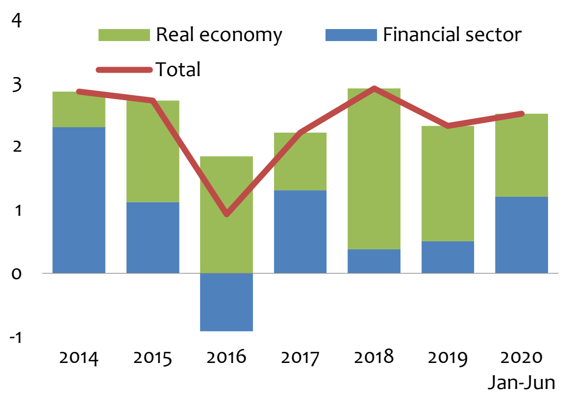
In recent years, the financial account balance was primarily determined by the public sector (i.e. the financial sector stabilisation measures and other measures adopted by the Bank of Latvia for the restructuring of public debt within the framework of the extended asset purchase programme). Fluctuations in the financial account were affected by the decline in non-resident deposits in credit institutions of Latvia. In the first half of 2020, financial account assets increased more than liabilities; the financial account balance (with reserve assets) reached 6% of GDP.

The state of balance of payments in the near future will be largely determined by the extent and duration of the spread of the COVID-19 pandemic and the restrictions imposed to combat it.

FOREIGN DIRECT INVESTMENT

The dynamics of foreign direct investment (FDI) flows in Latvia, as well as in other Baltic countries, remain moderate. This can mainly be attributed to the instability in the global economy and rising geopolitical tensions.

FDI in Latvia
flows, as per cent of GDP

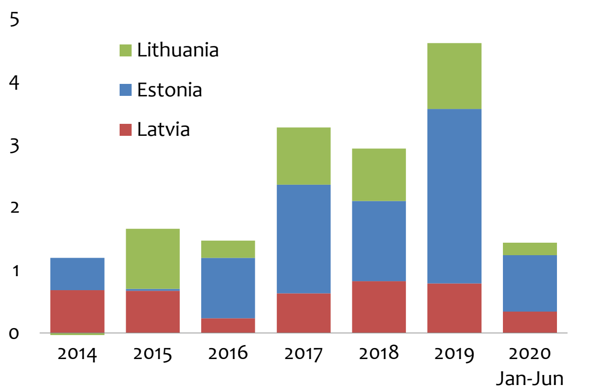


In the Baltic States, cross-border direct investment flows in the first half of 2020 were more moderate than a year ago.

Between 2017-2019, the inflows of FDI in the Baltic States averaged almost 3% of GDP; however, most of the FDI flows were in the Estonian economy.

In the first half of 2020, the total net inflow of FDI in the Baltic States reached nearly 1.4 billion euros; Latvia attracted 24% of all FDI (Estonia - 63%; Lithuania - 14%).

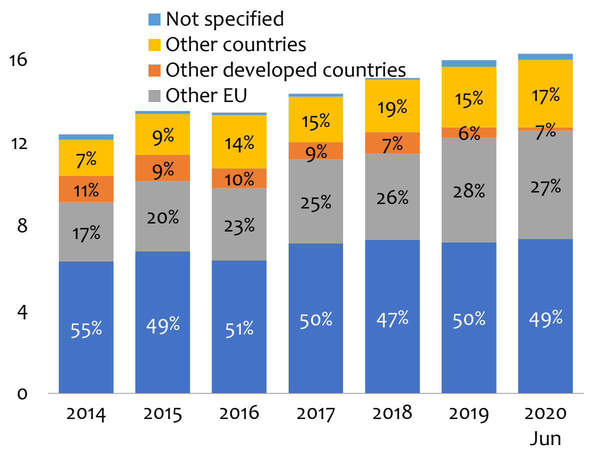
FDI In the Baltic States
flows, billion euro



The intensity of attracted FDI flows is higher than a year ago. In the first half of 2020, the volume of FDI transactions reached 341 million. euro. Most of them constituted non-residents' investments in the equity of companies registered in Latvia. The liabilities to direct investors increased by 223 million euro. On the other hand, reinvested earnings flows were more moderate than a year ago. It should be noted that in the first half of 2020, compared to the first half of 2019, net FDI inflows were nearly twice as high, accounting for 2.5% of GDP.

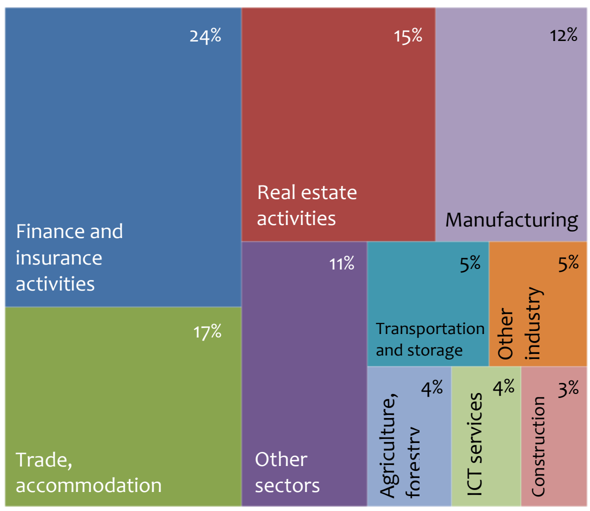
In June 2020, accumulated FDI in Latvia's economy reached EUR 16.2 billion (55% of GDP). In 2020, an increase of 6.5% was observed. Currently, the largest investor in Latvia's economy is Sweden. In June 2020, accumulated FDI from Sweden (mainly financial intermediation services) amounted to 15.4% of total FDI in Latvia. Also, significant FDI flows have come from Estonia, Russia, the Netherlands, Cyprus, Lithuania, and Germany. In June 2020, the investment of these countries represented 66.3% of FDI in the Latvian economy.

FDI Stock in Latvia By Groups of Countries
closing balance at then end of the year, billion euro and per cent



The largest share of accumulated FDI represent investments in financial intermediation services (24.4% of accumulated FDI), trade (16.2%), real estate activities (16.2%), and manufacturing (11.5%).

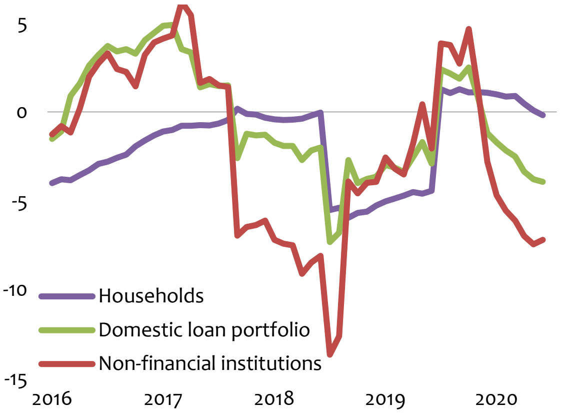
FDI by Sector
closing balance at the end of June 2020



MONETARY INDICATORS

As in other areas, future credit developments and the quality of the loan portfolio will be greatly affected by changes in the Covid-19 situation. Despite the uncertainty, the banking sector is currently operating at a profit.

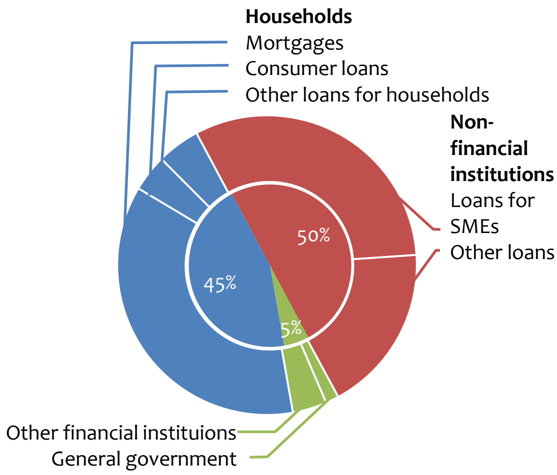
Domestic Credit Balances
against the corresponding period last year, as per cent



Source: Bank of Latvia

In June 2020, the domestic loan portfolio shrank by almost 4% annually. The loan portfolio of non-financial corporations declined by 7.2%. However, no significant changes in household lending (i.e., a decline of 0.2%) can be observed.

Non-Bank Resident Loan Portfolio
at the end of June 2020, as per cent

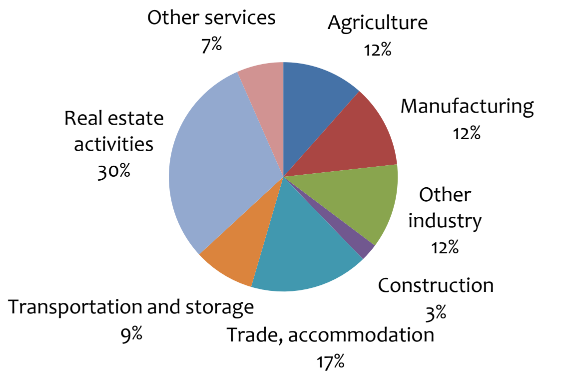


Source: Financial and Capital Market Commission

The breakdown of loans by sector has not significantly changed - at the end of June 2020, the largest loan volumes were issued in real estate activities (30% of total loans), trade and accommodation (17%), and manufacturing (12%).

However, since 2019, a steady rise in interest rates has been observed. In June 2020, interest rates on long-term and short-term loans were 2.45% and 3.34%, respectively. Also, interest rates on short-term mortgage loans to households have declined, reaching 3.18% in June 2020 (4.51% in June 2019). Interest rates on long-term loans also have risen slightly, reaching 2.36%; however, their volatility remains low.

Lending Portfolio of Non-Financial Institutions by Sector
at the end of June 2020, as per cent



Source: Financial and Capital Market Commission

In June 2020, deposit volumes increased to 19.5 billion euro. At the of June 2020, deposits were by 6% higher than a year ago. The represents a largest increase in the last two years. At the end of June 2020, non-resident deposits were by 19% lower than a year ago, constituting 1/5 of total non-bank deposits (at the end of June 2015 – 53% of non-bank deposits). At the same time, domestic deposits increased by 16%. Banks working with non-resident deposits are subject to more stringent liquidity and capital requirements.

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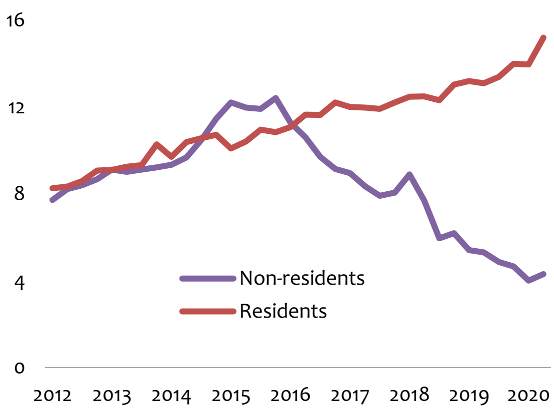
Non-Bank Deposits in Banks
billion euro



Source: Financial and Capital Market Commission

BUDGET AND GOVERNMENT DEBT

Since 2011, as Latvia returned to economic growth, significant improvements in the fiscal position have been achieved. The general government budget deficit, in accordance with European System of Accounts (ESA), has been reduced from 9.6% of GDP in 2009 to 1.4% of GDP in 2015. In 2016, for the first time since 1998, a budget surplus of 0.2% was observed. However, in 2017-2019, budget was at a small deficit, not exceeding 1%. The Saeima approved the 2020 budget with a deficit of 0.3% of GDP.

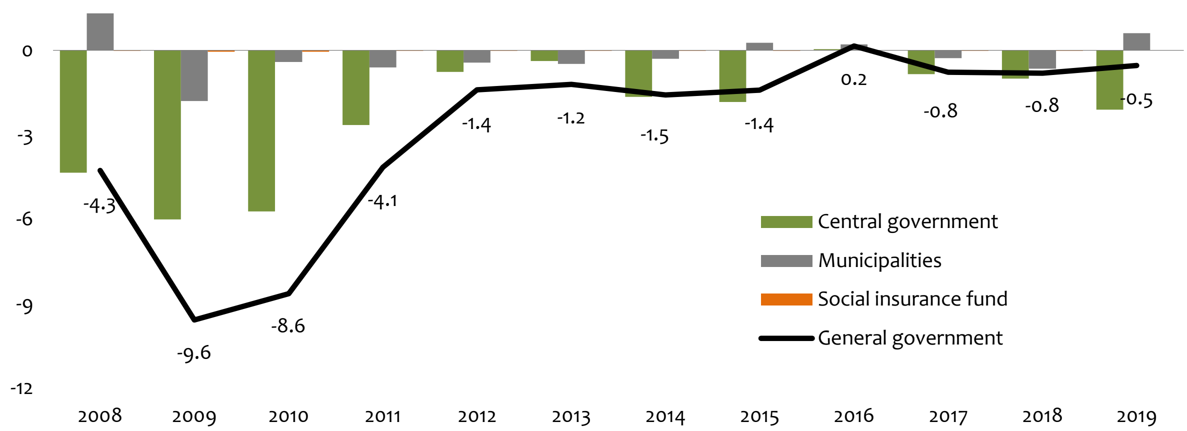
However, under the influence of the Covid-19 pandemic in 2020 the budget deficit could increase significantly.

According to the Ministry of Finance estimates, budget deficit could decline to about 7-8% of GDP.

General Government Budget

	2015	2016	2017	2018	2019
Revenues. bn euro	9.1	9.5	10.2	11.2	11.5
% of GDP	37.2	37.5	37.9	38.5	37.9
Expenditures. bn euro	9.5	9.5	10.4	11.5	11.7
% of GDP	38.7	37.4	38.7	39.4	37.9
Net. bn euro	-0.35	0.04	-0.02	-0.24	-0.17
% of GDP	-1.4	0.2	-0.8	-0.8	-0.5

General Government Budget Balance by Sector
as per cent of GDP

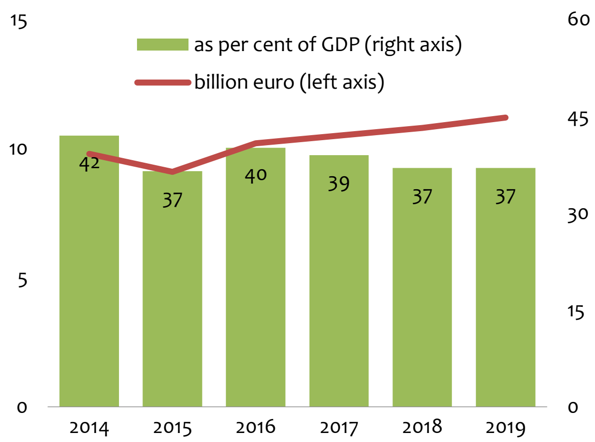


In Latvia, general government debt level remains one of the lowest amongst EU. Until 2007, it increased moderately. To finance state financial obligations, from 2008-2010, however, general government debt increased more rapidly. At the end of 2010, it reached EUR 8.6 billion or 47.9% of GDP. Since the end of 2011, general government debt on average has declined. In 2019, it reached EUR 11.2 billion or 36.9% of GDP.

Due to the COVID-19 pandemic, in 2020, the level of public debt could increase significantly.

By borrowing in a timely manner in line with the medium-term strategy and pursuing a sustainable fiscal policy, it is possible to refinance current central government debt liabilities on favourable terms; reduce and stabilize general government debt in the long run, meeting the general government debt criterion set out in the Maastricht Treaty.

General Government Consolidated Gross Debt nominal value at the year end

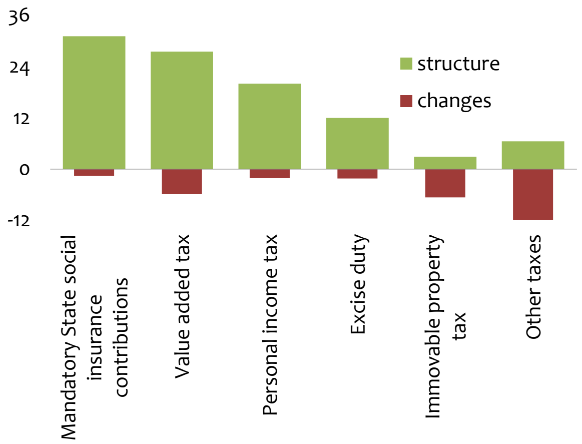


BUDGET REVENUES AND EXPENDITURES

Since 2011, general government budget revenues have increased. At the beginning of 2020, budget revenues continued to increase; however, with the declaration of a state of emergency in the country, revenues began to decline. Budget revenues in May and June 2020 sharply declined by 17.4% and 24.3%, respectively, compared to the corresponding period last year. Overall, in January-August 2020, budget revenues fell by 1.1%.

Tax Revenues

structure as per cent, changes in million euro, January-August 2020



In January-August 2020, tax revenues decreased in almost all tax categories Revenues from personal income tax and mandatory state social insurance contributions decreased by 2.1% and 1.6%, respectively.

Consolidated General Government Budget

	2018	2019	2020 January-August	2020 January-August
	Billion euro			*Changes as per cent*
Revenues:	10.9	11.4	7.6	-1.1
Tax revenues:	8.6	9.1	5.7	-1.1
Mandatory State Social Insurance Contributions	2.6	2.8	1.8	-1.6
Value added tax	2.5	2.6	1.6	-5.9
Personal Income Tax	1.7	1.9	1.1	-2.1
Corporate Income Tax	0.3	0.0	0.1	707.0
Excise Duty	1.0	1.1	0.0	-2.2
Immovable Property Tax	0.2	0.2	0.2	-6.6
Other taxes	0.3	0.2	0.2	-51.1
Other revenues	2.2	2.4	1.8	-0.9
Expenditures	11.1	11.5	7.6	7.9

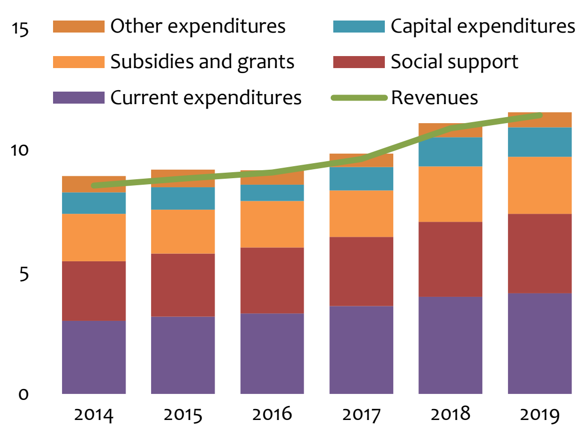
Consumption taxes also decline. In particular, value added tax decreased by 5.9%, whereas excise duty declined by 2.2%. However, revenues for natural resources tax increased by 11.2%.

Capital tax revenues are growing rapidly, primarily determined by the abrupt increase in corporate income tax revenues - by almost 707%, which is related to the changes made in the procedure of paying this tax within the framework of the 2019 tax reform.

In 2019, consolidated government budget expenditure increased by 4.0%, reaching EUR 11.5 billion. Also, in 2020, expenditures continue to rise. In January-August 2020, an increase of 7.9% was observed. Current expenditures grew by 10.4%; also, subsidies and grants and capital expenditures decreased by 2.8% and 6%, respectively.

Consolidated General Government Budget Expenditures

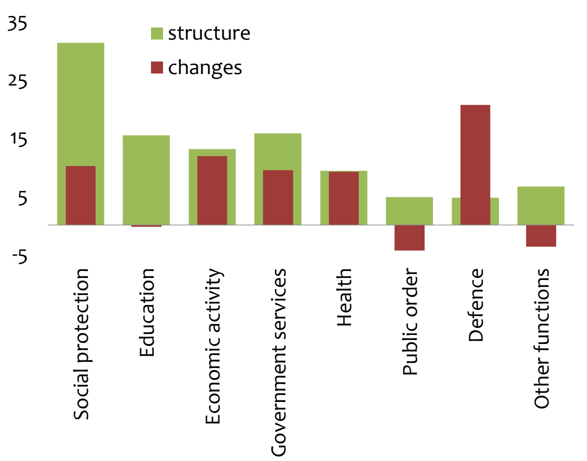
billion euro



In January-August 2020, expenditure on defence grew rapidly; however, expenditures decreased for public order and security.

Consolidated General Government Budget Expenditures by Functions

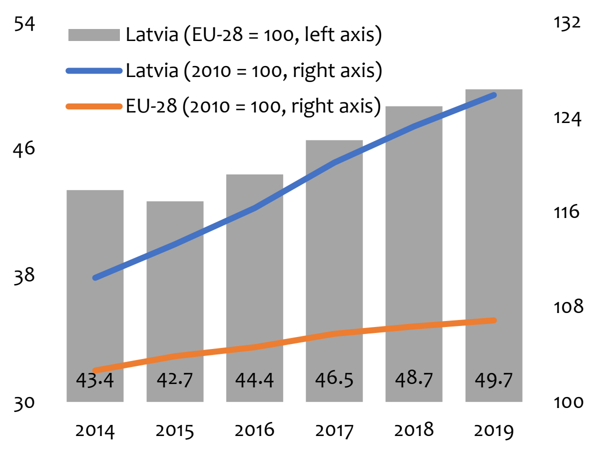
structure and changes in January-August 2020, as per cent



PRODUCTIVITY AND COMPETITIVENESS

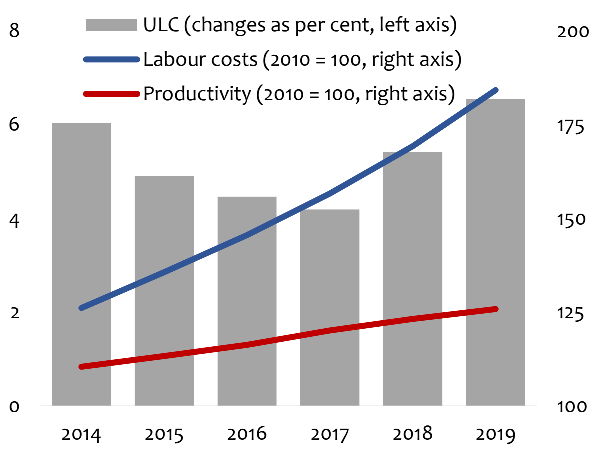
Latvia's economic growth is mainly supported by productivity growth. Productivity has increased on average by 2.7% annually over the last three years (2017-2019), i.e. almost 3.5 times faster than the EU average. In 2019, GDP per person employed (productivity) in the Latvian economy reached 49.8% (almost 70% by PPS) of the EU average. Since 2017, the productivity gap with the EU average level decreased by 6 percentage points. However, it should be noted that productivity dynamics are becoming more moderate, which is slowing down the pace of convergence.

Productivity Dynamics



Labour costs are growing at a higher rate than productivity. In 2019, labour costs increased by 8.8% (i.e., at a 6% higher rate than productivity. Thus, nominal unit labour costs (ULC) increased significantly. This indicates growing risks of declining competitiveness of Latvian entrepreneurs.

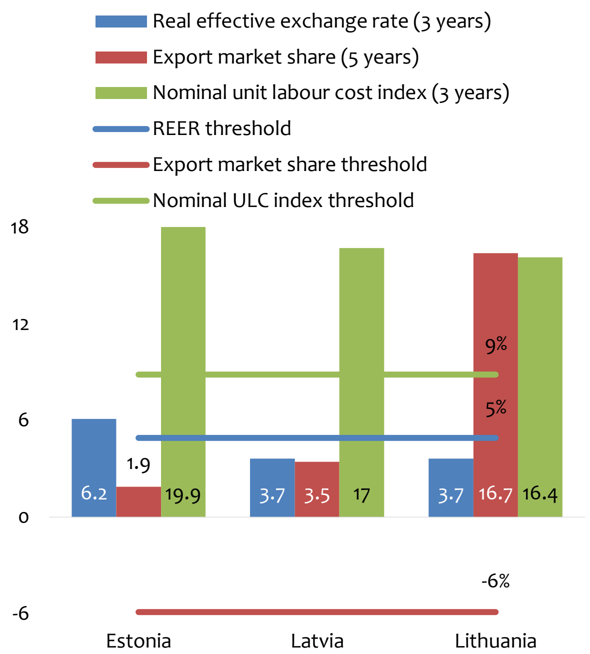
Labour Costs and Productivity



The strong increase in labour costs is affected by wage convergence processes in the EU labour market and rising labour market tensions domestically. Recently, a strong increase in nominal ULC can be observed in the Baltics. In 2019, compared to 2015, nominal ULC in Latvia, Estonia, and Lithuania increased by 22.2%, 19.1%, and 23.5%, respectively, i.e., higher than the EU average (2.8%), exceeding EU Alert Mechanism (MIP) threshold (9%).

Competitiveness Indicators

changes as per cent



REER dynamics have been positive. Between 2016-2018, the consumer price index (CPI) (based on REER against 42 trading partners) has increased by 3.7% (against Euro Area partner countries by 2.8%). The indicator is close to the threshold set by the EU Alert Mechanism.

The negative trends in cost competitiveness indicators are reflected in the dynamics of Latvia's export market share. Although the average share of Latvia's exports in world markets increased by 3.5% over the last 5 years, annual growth rates reveal the growth has moderated. In 2019, the share of Latvia's exports in world markets decreased by 1.58%. On the other hand, the share for Estonia and Lithuania increased by 2.53% and 6.8%, respectively.

The Covid-19 shock has a stronger impact on the goods market than on the labour market. In the first half of 2020, labour costs rose by 6.2%, whereas productivity decreased by 6.1%. Thus, nominal ULC increased by 13%. In the near future, the dynamics of productivity and labour costs will be largely determined by measures to combat the Covid-19 pandemic and to stimulate economic activity.

EU ALERT MECHANISM

In line with the economic and fiscal policy surveillance rules adopted in 2011, a macroeconomic imbalances procedure was also established in the EU alongside the Excessive Deficit Procedure, aimed at identifying (through the Alert Mechanism Scoreboard) and correcting macroeconomic imbalances.

The Alert Mechanism Report for 2019 did not identify Latvia amongst those 13 EU Member States, where macroeconomic imbalances were present, and further in-depth study – required. However, Latvia violates thresholds set by the Alert Mechanism for some indicators (see the table below). Although improvements in the net international investment position were achieved, as Latvia's external debt to the rest of the world grew more slowly than gross domestic product, the indicator exceeded the threshold set by the EU Alert Mechanism. Also, nominal unit labour costs index (similarly to Lithuania, Bulgaria, and Estonia) exceeded the threshold. In Latvia, the increase can mainly be attributed to the rise in wages in private non-tradable sectors. Wages have risen at a higher rate than productivity. It is anticipated that wages will continue to increase due to strong demand in the labour market. In addition, the housing price index slightly exceeded the threshold, reflecting the high demand in the housing market. The real effective exchange rate (REER) against 42 trading partners was close to the threshold. However, all employment indicators significantly improved – employment rate has increased, and long-term unemployment and youth unemployment rates have declined.

List of Indicators for the Macroeconomic Imbalances Procedure for Latvia

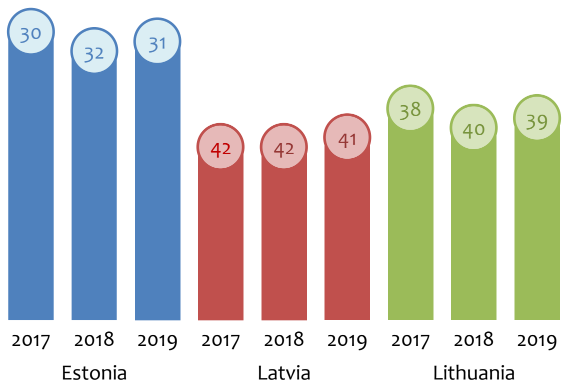
	Threshold	2014	2015	2016	2017	2018	2019
External imbalances and competitiveness							
Current account (% of GDP. 3-year average)	-4%/6%	-2.7	-1.7	-0.2	0.7	0.9	0.1
Net international investment position (% of GDP)	-35%	-65.5	-61.7	-55.8	-53.1	-46.5	-41.7
Real effective exchange rate – 42 partner countries. HICP deflator (% changes over the last 3 years)	±5%* & ±11%	0.4	2.5	4.8	1.7	4.9	3.7
Export market share – % of world export (% changes over the last 5 years)	-6%	11.7	13.2	9.3	7.6	8.8	3.5
Nominal unit labour costs index (% changes over the last 3 years)	9%* & 12%	17.0	17.3	16.2	14.2	14.7	17.0
Internal imbalances							
House price index (% annual changes)	6%	4.6	-2.8	6.3	5.6	6.4	5.8
Private sector credit flow (% of GDP. consolidated)	14%	-4.6	-0.8	2.5	2.7	-0.2	1.5
Private sector debt (% of GDP. consolidated)	133%	82.3	78.4	78.4	75.7	69.8	67.1
General government debt (% of GDP)	60%	41.6	37.3	40.9	39.3	37.2	36.9
Unemployment rate (3-year average)	10%	12.6	10.9	10.1	9.4	8.6	7.5
Financial sector liabilities (% annual changes)	16.5%	10.9	13.3	4.7	6.2	-3.5	4.6
Employment indicators							
Economically active population – % of population aged 15-64 (% over the last 3 years)	-0.2 percentage points	1.8	1.3	2.3	2.4	2.0	1.0
Long-term unemployment rate – % economically active population (% changes over the last three years)	0.5 percentage points	-4.2	-3.3	-1.7	-1.3	-1.4	-1.6
Youth unemployment rate – % of economically active population (% over the last 3 years)	2 percentage points	-11.4	-12.2	-5.9	-2.6	-4.1	-4.9

* – Euro area countries.
Note: highlighted numbers exceed the thresholds set out in the Early Alert Mechanism Report 2019.
Source: List of Indicators for the Macroeconomic Imbalances Procedure for Latvia, *Eurostat*

2020 | 2 LATVIA IN INTERNATIONAL RANKINGS

Ratings from the United Nations, the World Bank Group, the World Economic Forum, and other organisations described Latvia as a country that makes a lot of reforms to improve its competitiveness by improving e-government, the business environment, ICT infrastructure, and other areas, while providing free press and not militarily endangering other countries of the world. In World Economic Forum report and the Global Competitiveness Index (GCI 4.0) for 2019 Latvia is ranked 41st between 141 surveyed countries.

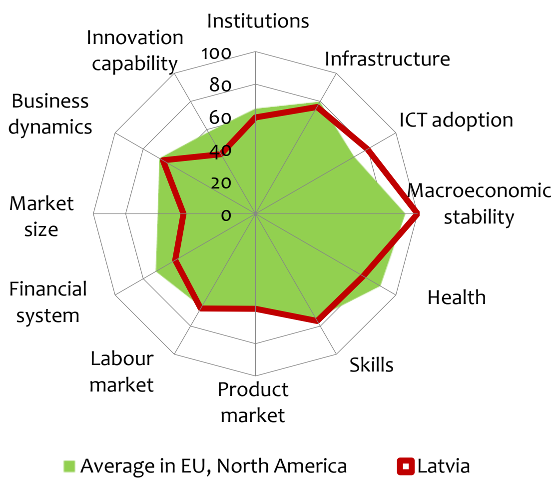
Baltic Countries In Global Competitiveness Index 4.0



Source: *World Economic Forum, The Global Competitiveness Report 2019*

In 2019, Latvia has ranked one place higher, compared to 2018. Improvements can be observed in 8 out of 12 pillars.

Latvia GCI 4.0 2019
in scale from 0 to 100

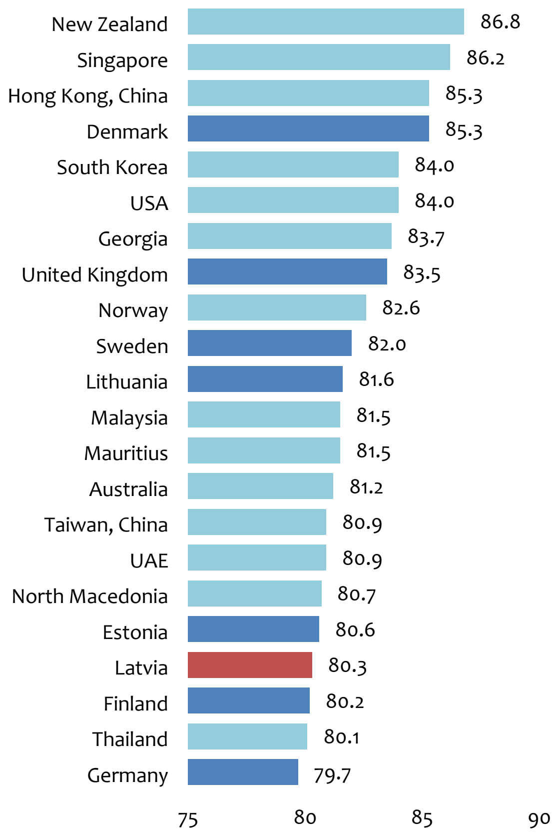


Source: *World Economic Forum, The Global Competitiveness Report 2019*

In terms of macroeconomic stability, Latvia ranks 1st (along with other 33 countries). Based on well-developed infrastructure and a larger share of internet users, Latvia ranks 15th in the ICT adoption index. Latvia also ranks high in skills and labour market indexes – 22nd and 28th place, respectively. An average performance can be observed in business dynamism (40th), infrastructure (43rd), institutions (47th), product market (47th), and innovation capability (54th) indexes. However, the worst assessment has been received for health (84th), financial system (85th), and market size (95th) indicators.

In the World Bank Group *Doing Business* Latvia ranks 19th amongst 190 countries. However, between EU countries Latvia has been ranked in the 6th place. Compared to the assessment in 2019, improvements for 2 groups indicators have been achieved. A decline has been observed in one indicator group, and 7 indicator groups have remained the same. Overall, Latvia, compared to 2019, has remained in the same position, ranking 19th.

Doing Business 2020
in scale from 0 to 100



Source: *Doing Business 2020, International Bank for Reconstruction and Development, The World Bank*

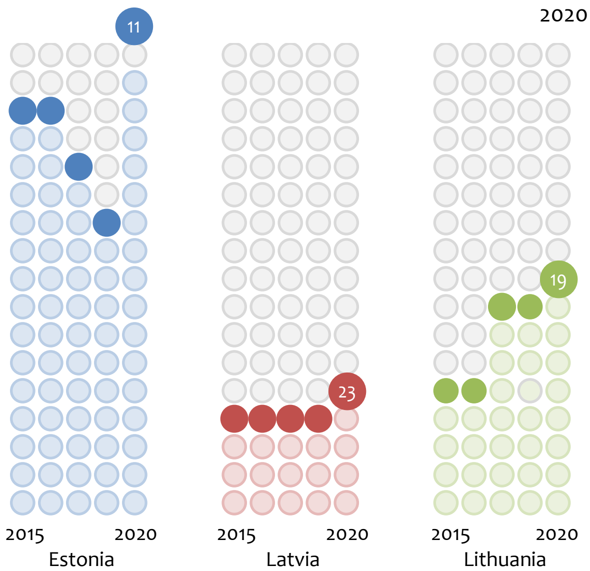
Baltic Country Assessment, Doing Business 2020

	Latvia			Lithuania		Estonia	
	place	*score*	*changes. compared to Doing Business 2019**	*place*	*score*	*place*	*score*
Index. total	**19**	**80.3**	**0**	**11**	**81.6**	**18**	**80.6**
Starting a business	24	94.1	0	34	93.3	14	95.4
Dealing with construction permits	56	73.5	0	10	84.9	19	82.6
Getting electricity	61	82.3	+0.1	15	92.9	53	83.3
Registering property	25	82.3	0	4	93.0	6	91.0
Getting credit	15	85.0	0	48	70.0	48	70.0
Protecting minority investors	45	68.0	0	37	70.0	79	58.0
Paying taxes	16	89.0	-0.7	18	88.8	12	89.9
Trading across borders	28	95.3	0	19	97.8	17	99.9
Enforcing contracts	15	73.5	0	7	78.8	8	76.1
Resolving insolvency	55	59.6	+0.2	89	46.7	54	60.1

* *Doing Business 2019* results have been recalculated based on *Doing Business 2020* methodology
Source: *Doing Business 2020, International Bank for Reconstruction and Development, The World Bank*

In the European Innovation Scoreboard 2020, published annually by the European Commission, Latvia ranks 23th among the 27 EU countries, and has been included in the group of moderate innovators for the fourth consecutive year. Finance and support, the impact on employment and an innovation-friendly environment are Latvia's strongest dimensions of innovation. However, innovators, research systems and business investment are the weakest dimensions of innovation.

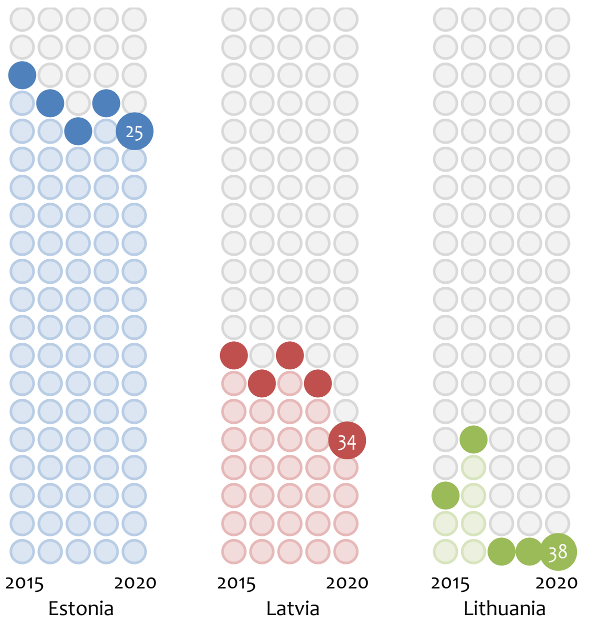
Baltic Countries In the European Innovation Scoreboard 2020



Source: *European Commission, European Innovation Scoreboard 2020*

In turn, in Global Innovation Index 2020 Latvia is ranked 36th between 131 surveyed countries. The strengths of Latvia are highlighted: the ratio of students and teachers in secondary education institutions, the share of secondary school graduates, compliance with environmental management system standards, ease of obtaining credit, the share of women with higher education, total domestic R&D expenditure financed by foreign, domestic increase in gross domestic product per employee by purchasing power parity, as well as increase in the volume of products of creative industries.

Baltic Countries In Global Innovation Index



Source: *Cornell University, INSEAD, WIPO, The Global Innovation Index 2020: Who Will Finance Innovation?*

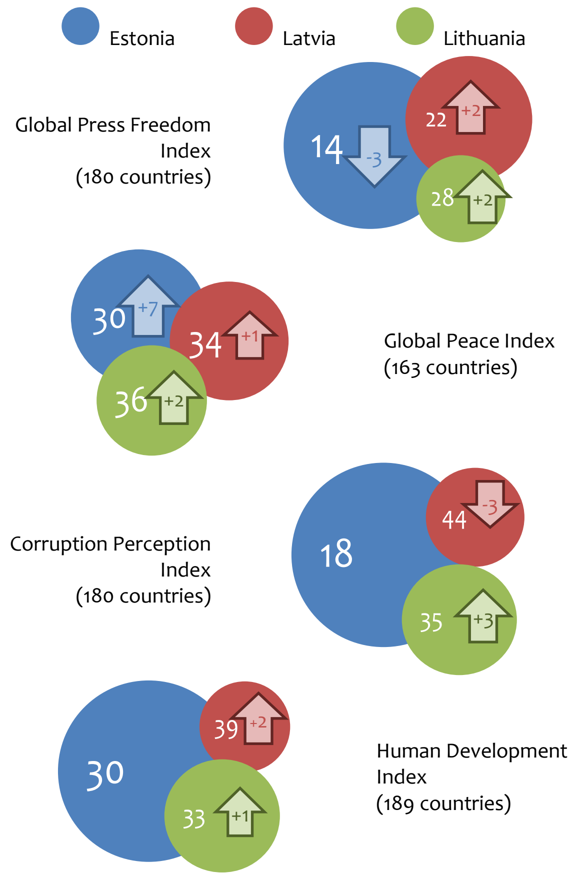
In World Press Freedom Index by Reporters Without Borders (RWB) Latvia ranks 22nd (amongst 180 countries), improving its position by two positions, compared to 2019.

In Global Peace Index (GPI) produced by the Institute for Economics and Peace (IEP) Latvia was ranked 34th (amongst 163 countries) in 2020. Compared to 2019, Latvia's position has ranked one position higher due to improvements in social security and defence.

In Corruption Perceptions Index 2019 produced by The Global Anti-Corruption Organisation *Transparency International* Latvia ranked 44th (among 180 countries), worsening its position by 3 places, compared to 2018.

In the Human Development Index (HDI) produced by the United Nations Organization Latvia ranks 39th (amongst 189 countries) in 2019, thus achieving by two places higher position than in 2017.

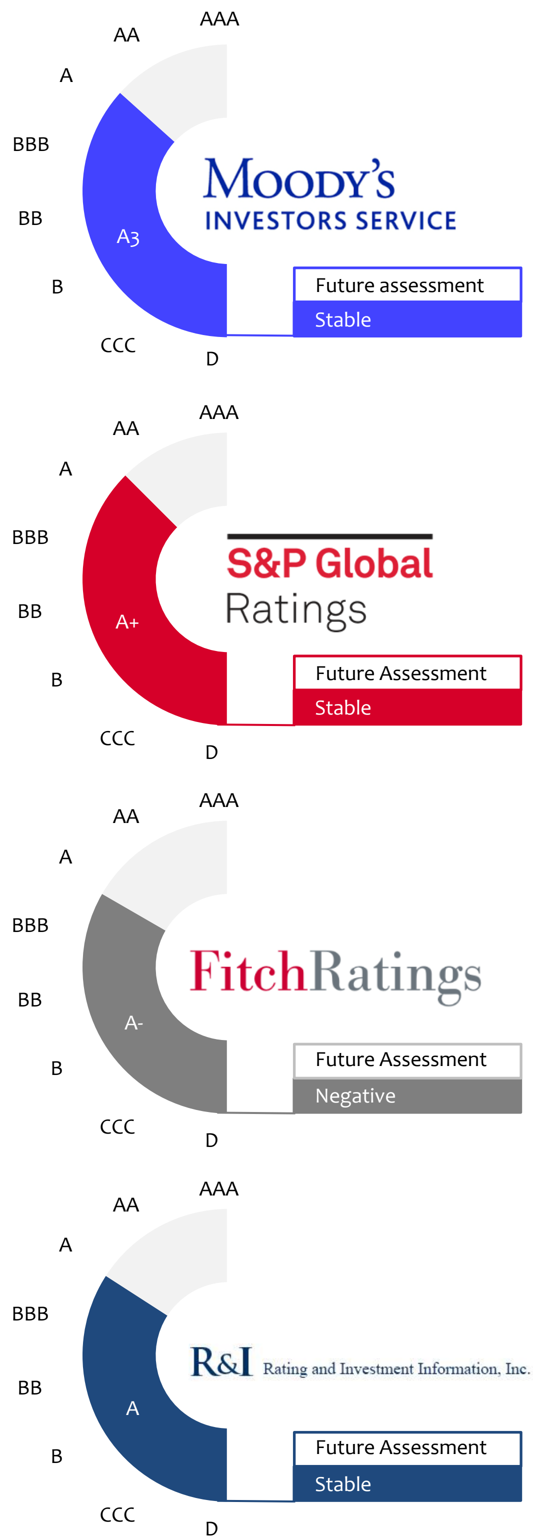
Baltic Countries In International Rankings
place and changes during a year



Source: Reporters Without Borders, *2020 World Press Freedom Index; The Institute for Economics and Peace, Global Peace Index 2020; Transparency International, Corruption Perceptions Index 2019; United Nations Development Programme, Human Development Report 2019.*

In 2020, the *international credit rating agency Moody's Investors Service and S&P Global Ratings* did not change the rating of Latvia, but *R&I* raised Latvia's credit rating from "A-" to "A". Only Fitch Ratings downgraded the outlook from "Stable" to "Negative". Latvia's high credit rating is ensured by low government debt and strong institutional capacity. However, due to the Covid-19, there is a temporary deterioration of economic indicators (i.e., a decrease in budget revenues and an increase in state budget expenditures), which worsens Latvia's fiscal forecasts for 2020-2021. Meanwhile, the stimulus measures taken by the government to support companies and employees do not raise concerns regarding Latvia's ability to reduce public debt in the medium term.

Credit Rating of Latvia for Long-Term Liabilities in Foreign Currency



Source: Treasury Republic of Latvia