

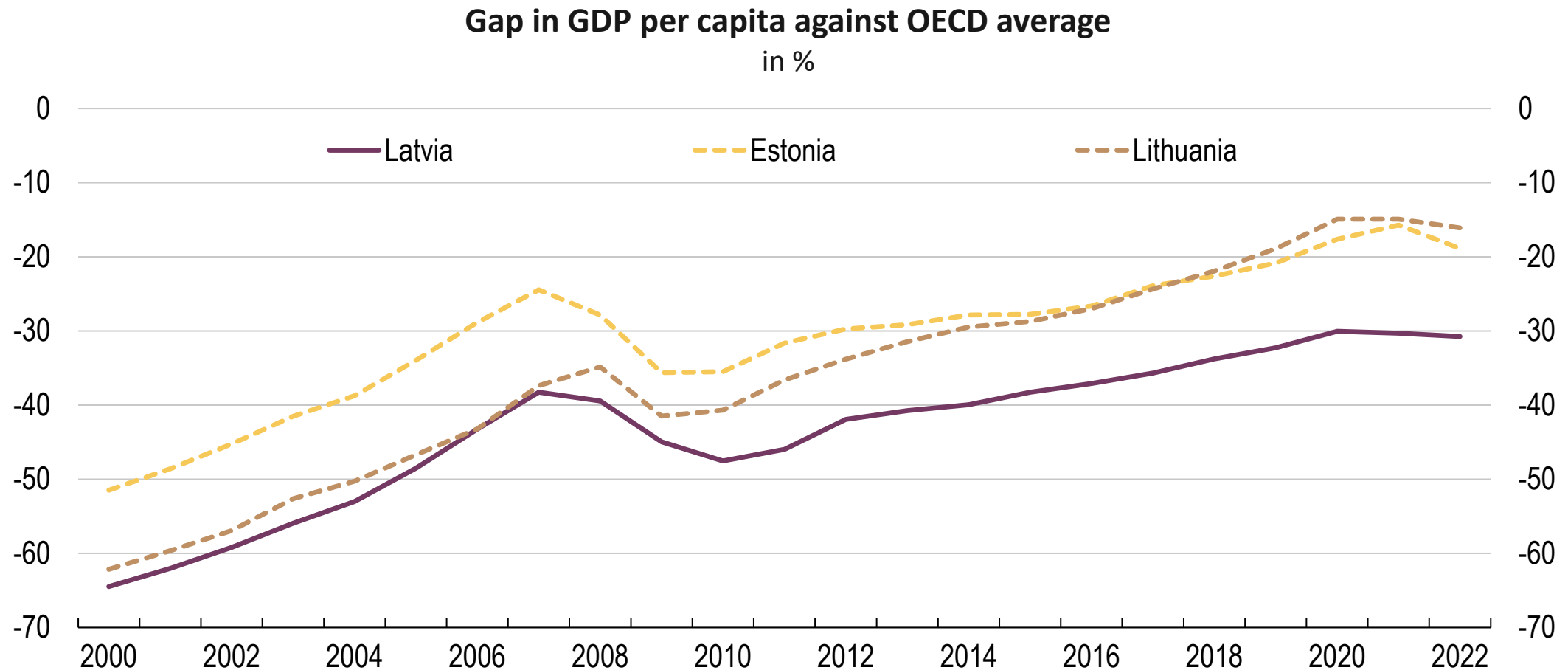
OECD ECONOMIC SURVEY OF LATVIA

Riga

29 April 2024

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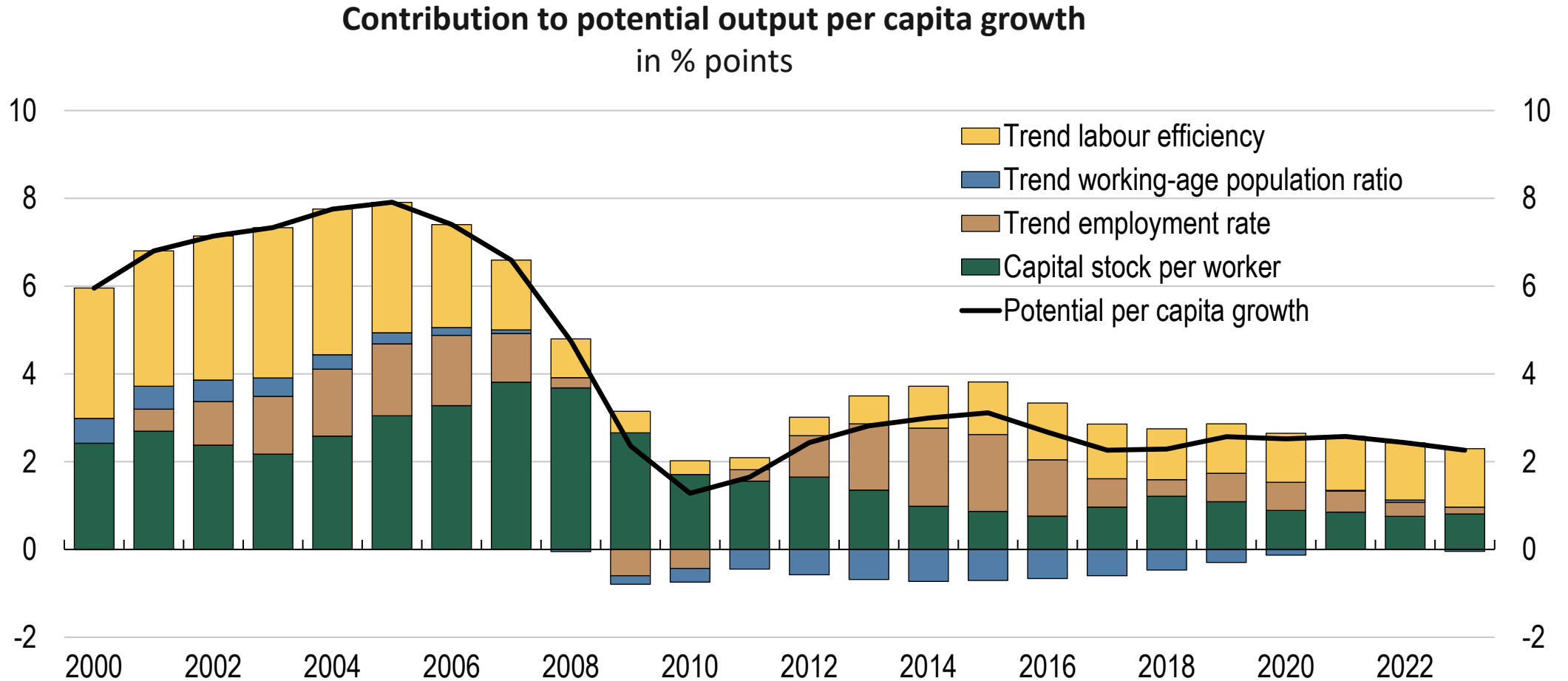
The convergence of living standards has slowed



Note: Percentage gap to the OECD in terms of GDP per capita (in constant 2015 PPPs).

Source: OECD National Accounts database.

Raising investment, labour supply and innovation is key for reviving potential growth

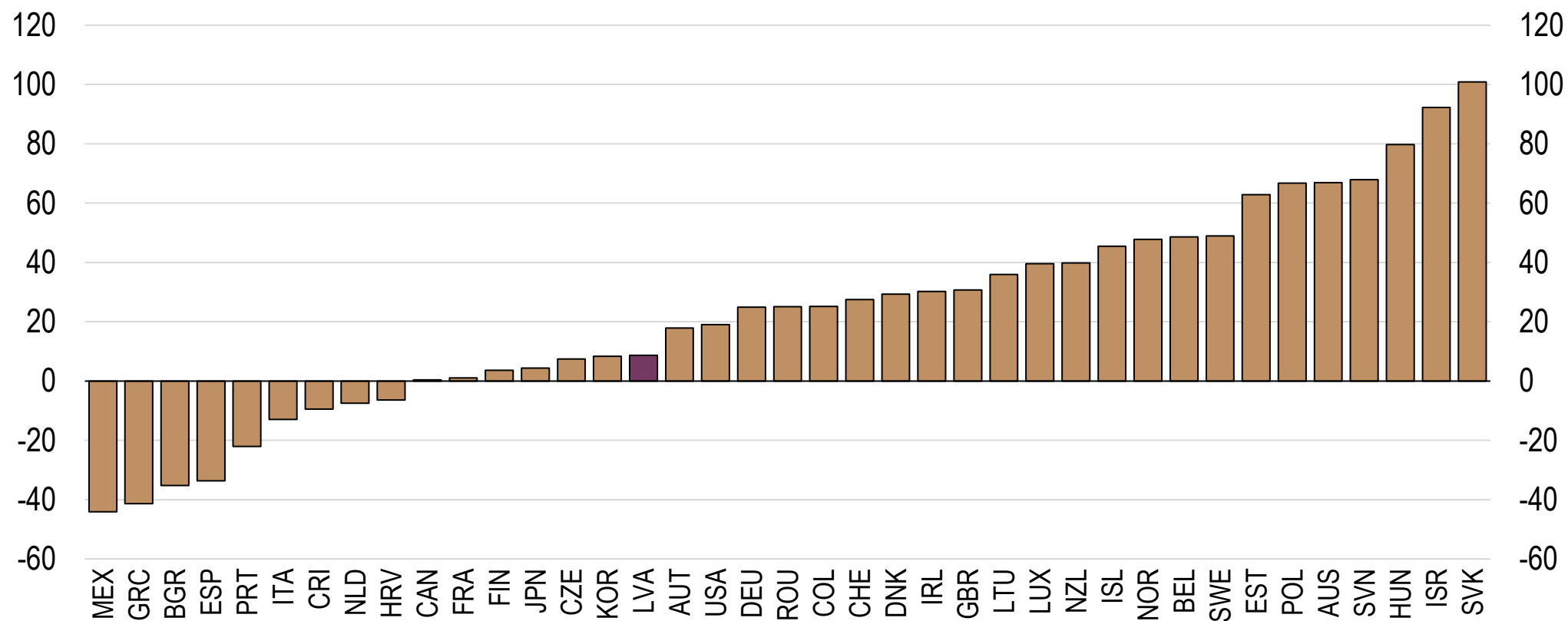


Source: Updates to the OECD Economic Outlook 114 database.

Public investment needs to increase

Growth in real gross fixed public capital formation in 2023 compared with 2009

%



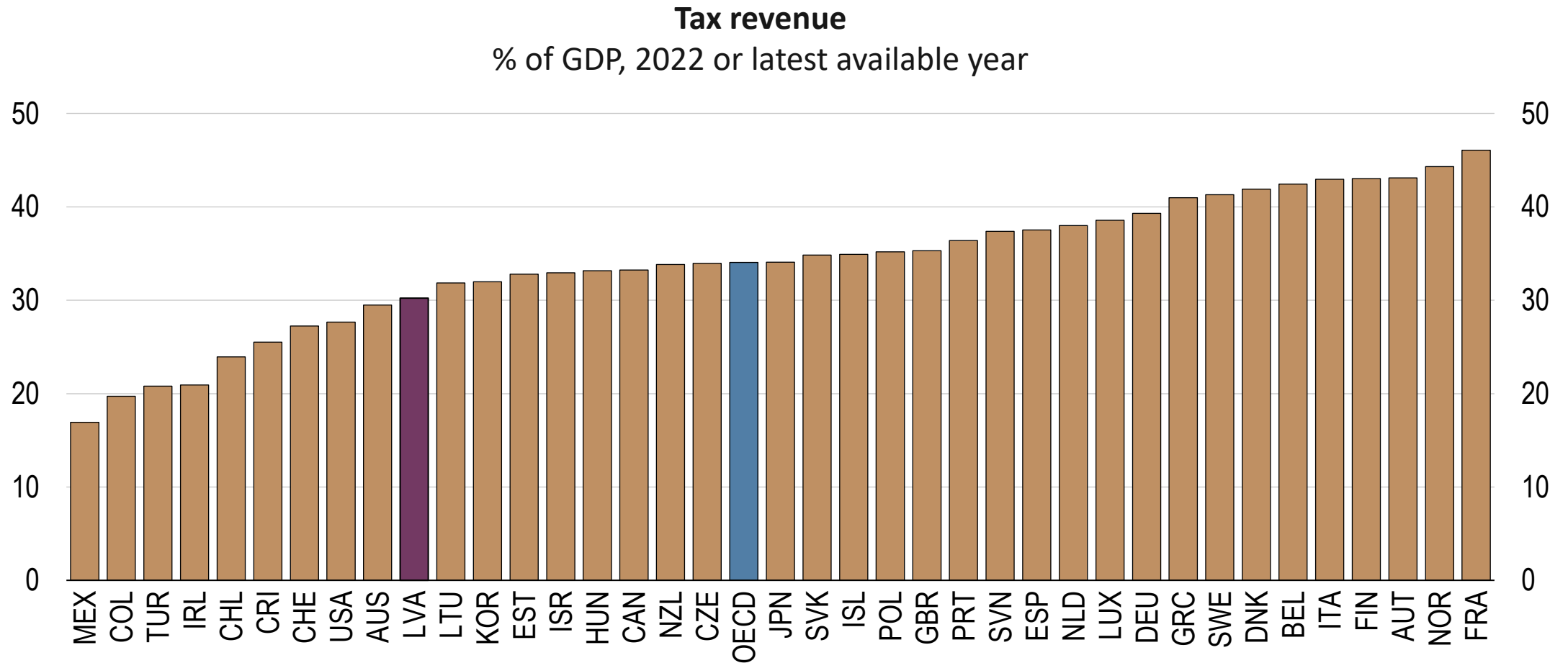
Source: OECD Economic Outlook database and OECD calculations.



Strengthening public finances and public sector capacity

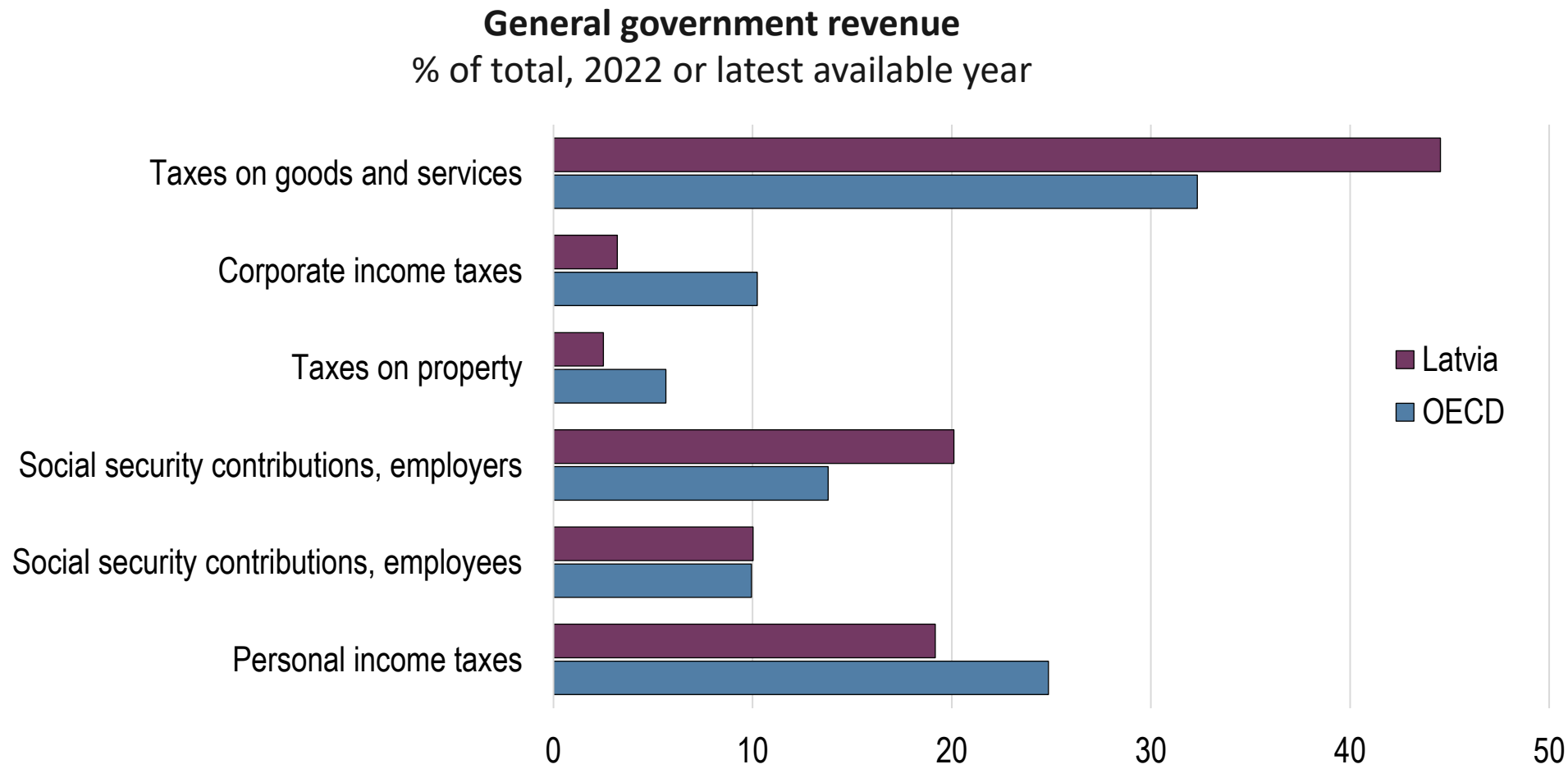


There is room to raise tax revenue



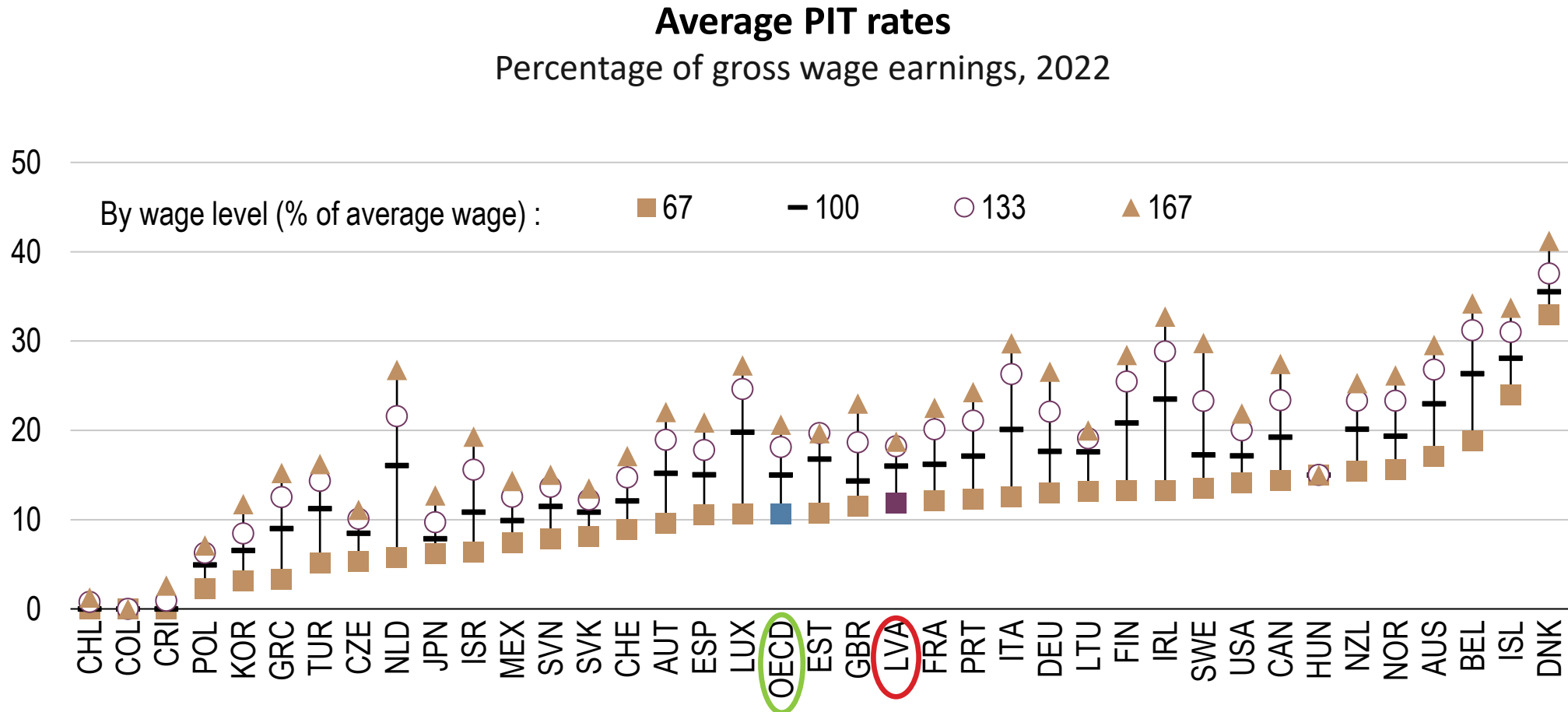
Source: OECD Revenue Statistics.

Tax revenue should be raised from income, property and environmental taxes



Source: OECD Revenue Statistics.

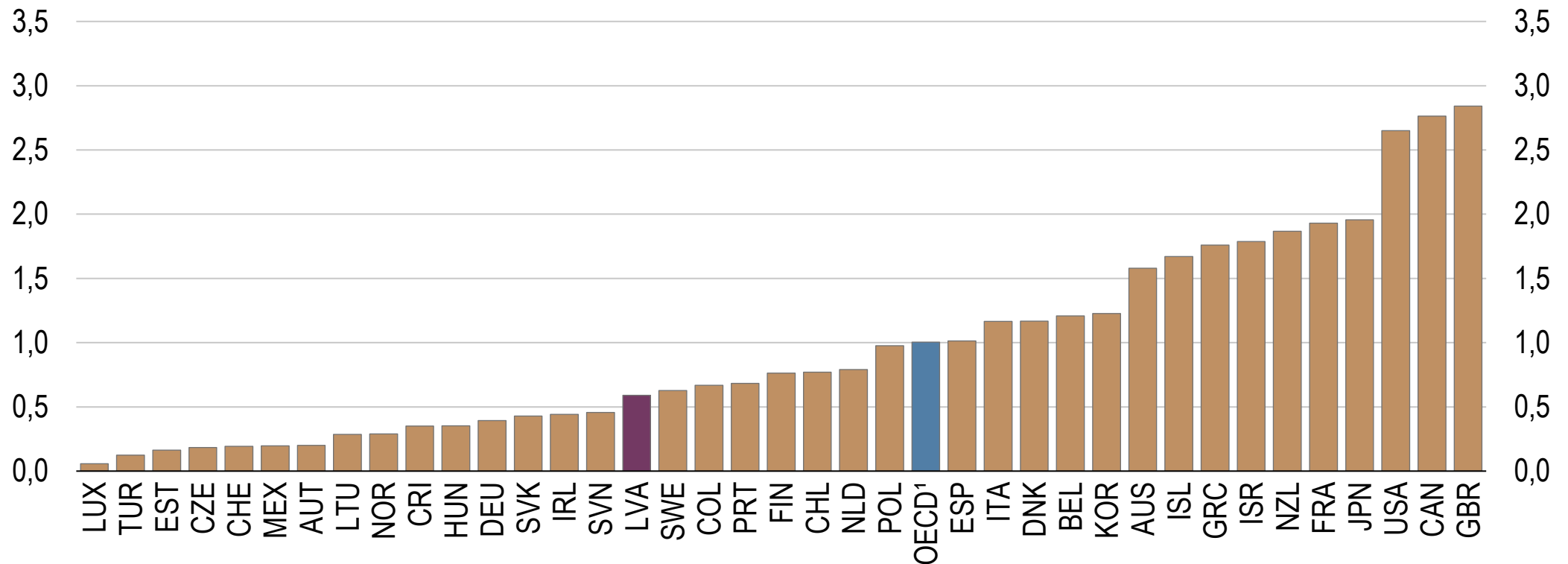
There is room to raise personal income tax (PIT) rates for higher incomes



Note: Data refer to single person without dependant.
Source: OECD Tax database.

Updating cadastre values with market values would allow raising revenue from property taxes

Recurrent taxes on immovable property
% of GDP, 2022 or latest available year

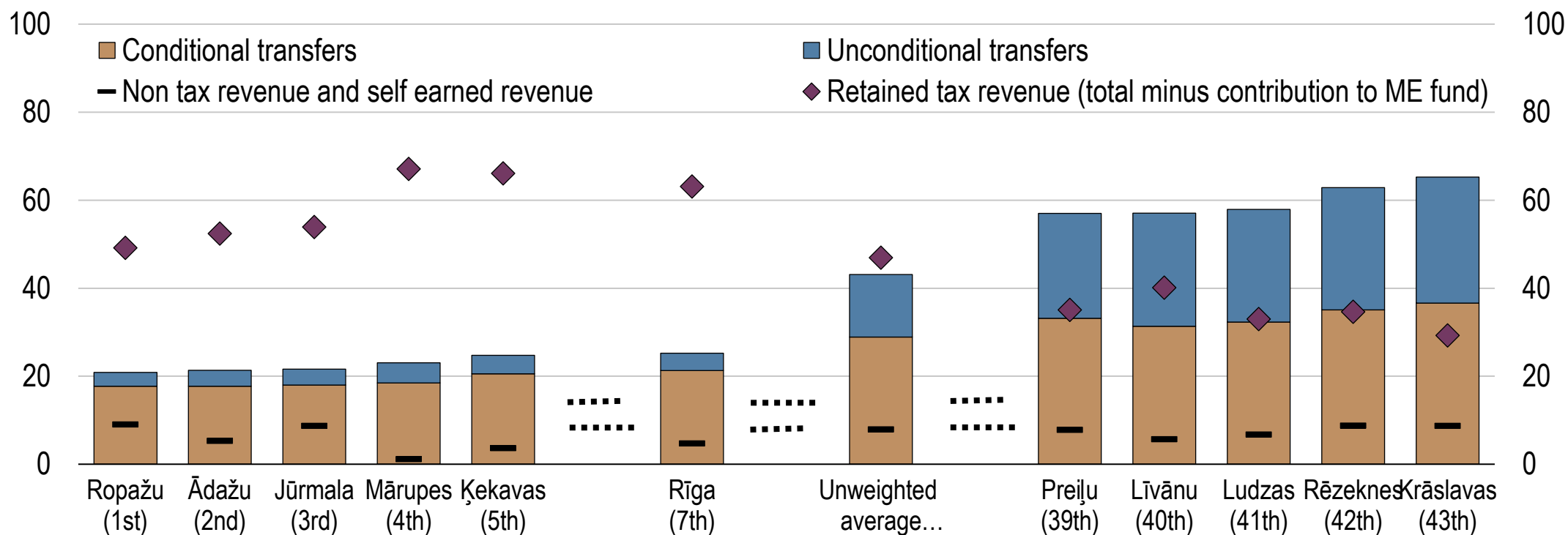


1. Unweighted average.

Source: OECD Revenue Statistics.

This would help improve municipal finances and allow reducing dependency on conditional grants

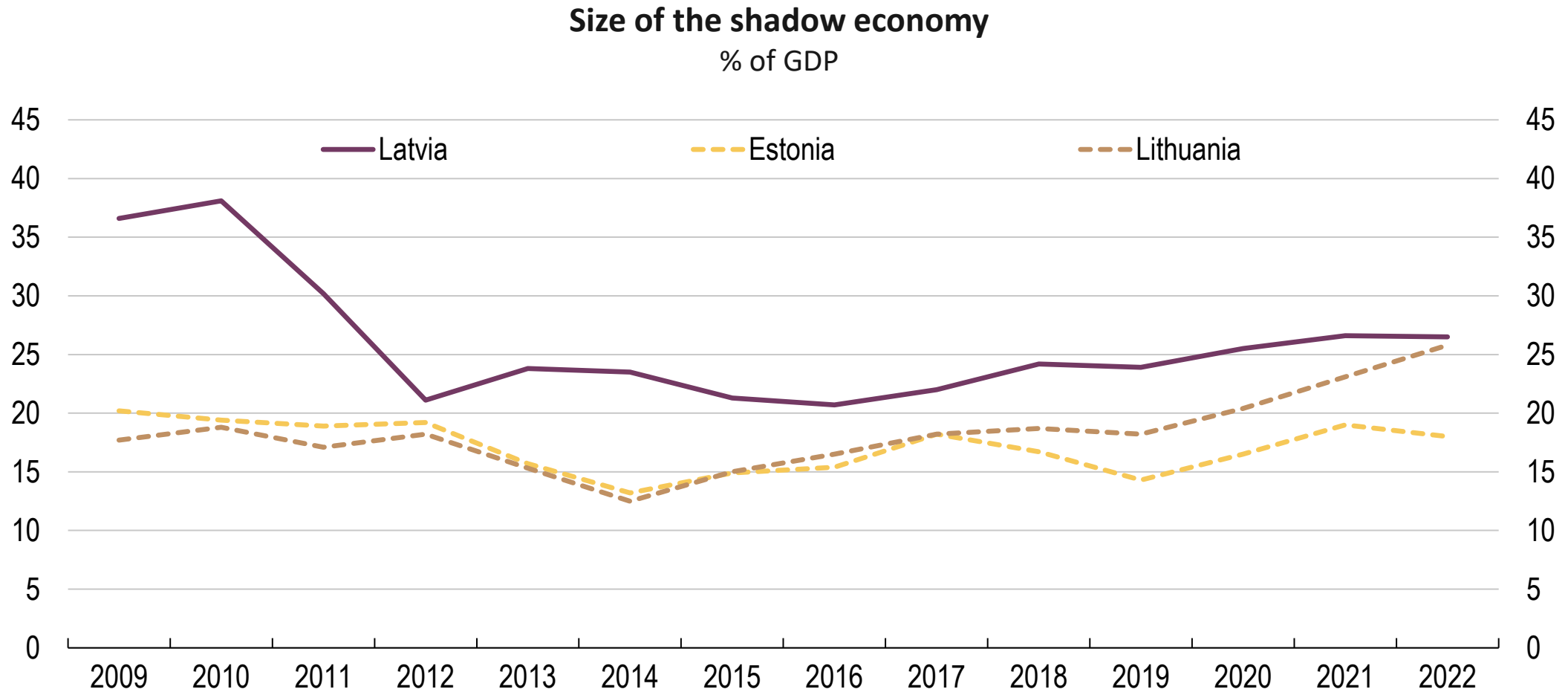
Share of retained tax revenue, non-tax revenue and conditional and unconditional central government transfers in total expenditure (in %), 2022



Note: The unweighted average across municipalities does not account for the size of municipalities.

Source: Ministry of Finance, State Treasury.

Reducing informality is key for expanding the tax base and levelling the playing field between firms

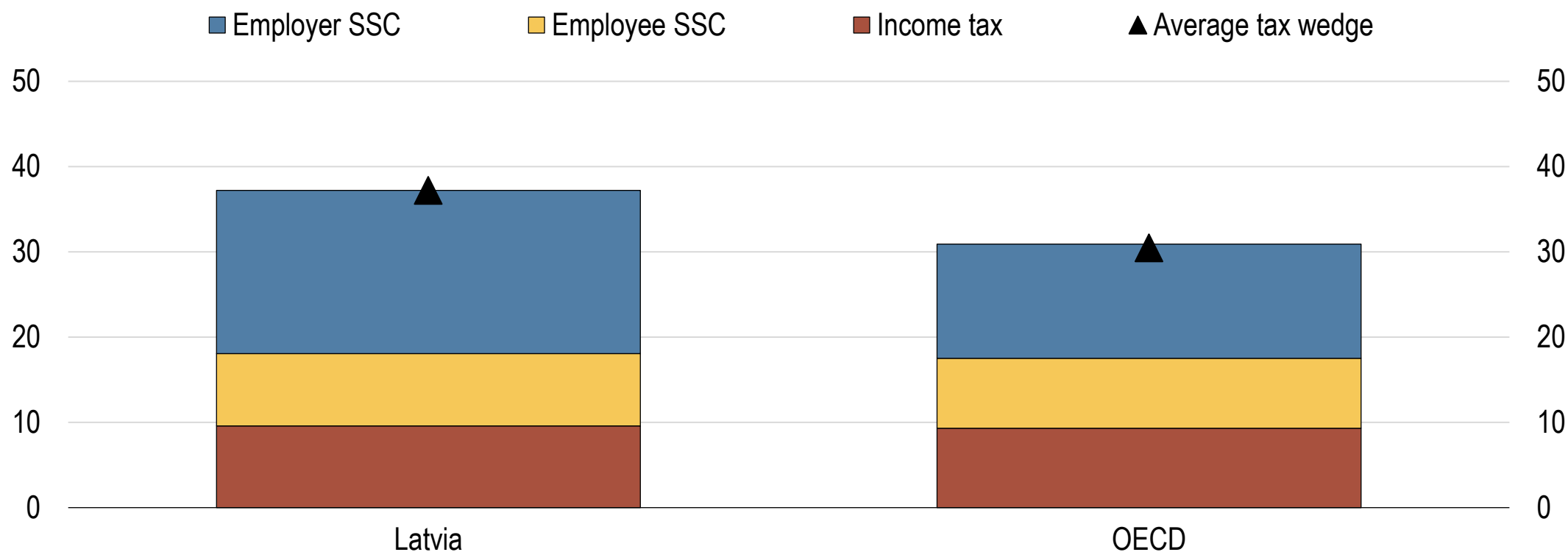


Source: Stockholm School of Economics Riga Shadow Economy Index for the Baltic Countries.

Reducing high social security contributions for low-wage earners would raise incentives to formalise work

Average tax wedge at 67% of the average wage

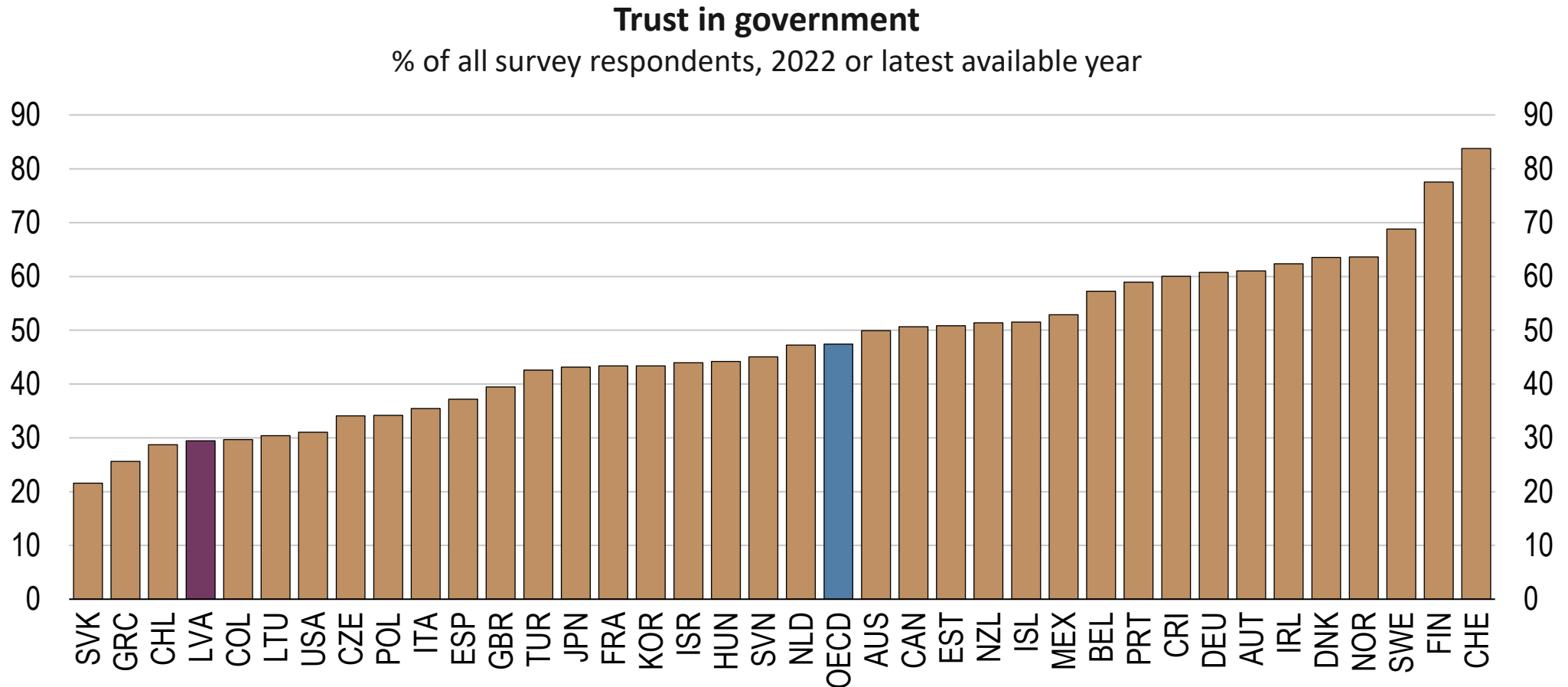
% labour costs, 2022



Note: The tax wedge is the sum of personal income tax, employee plus employer social security contributions, minus social benefits as a percentage of labour costs. The tax wedge is shown for a single individual without children, by income level measured in percent of the income of the average worker (AW).

Source: OECD Taxing Wages database.

Raising trust in institutions would help raise the tax morale and lower informality



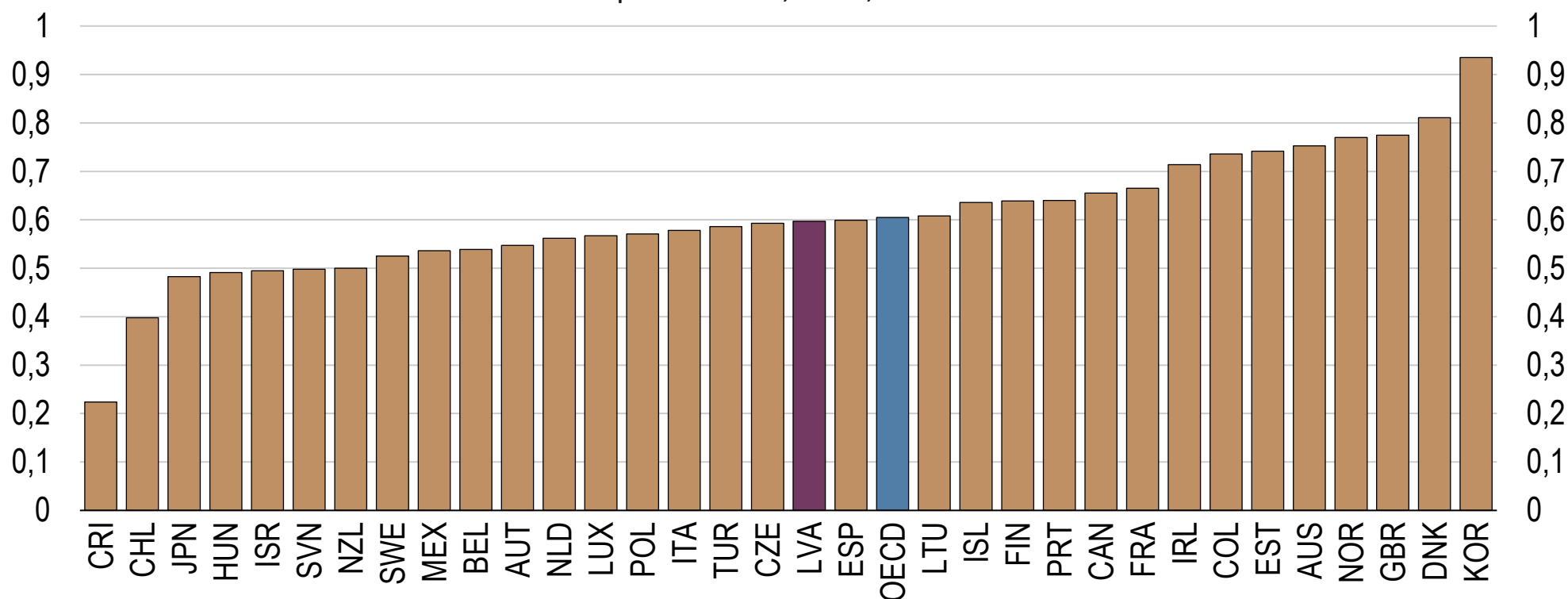
Note: "Trust in government" refers to the share of people who report having confidence in the national government. The data shown reflect the share of respondents answering "yes" (the other response categories being "no", and "don't know") to the survey question: "In this country, do you have confidence in... national government? OECD average is a simple average of available OECD countries.

Source: OECD Government at a Glance database.

Continuing to digitalise the public sector is key for improving the quality of public services

OECD Digital Government Index

Composite index, 2023, score 0 to 1

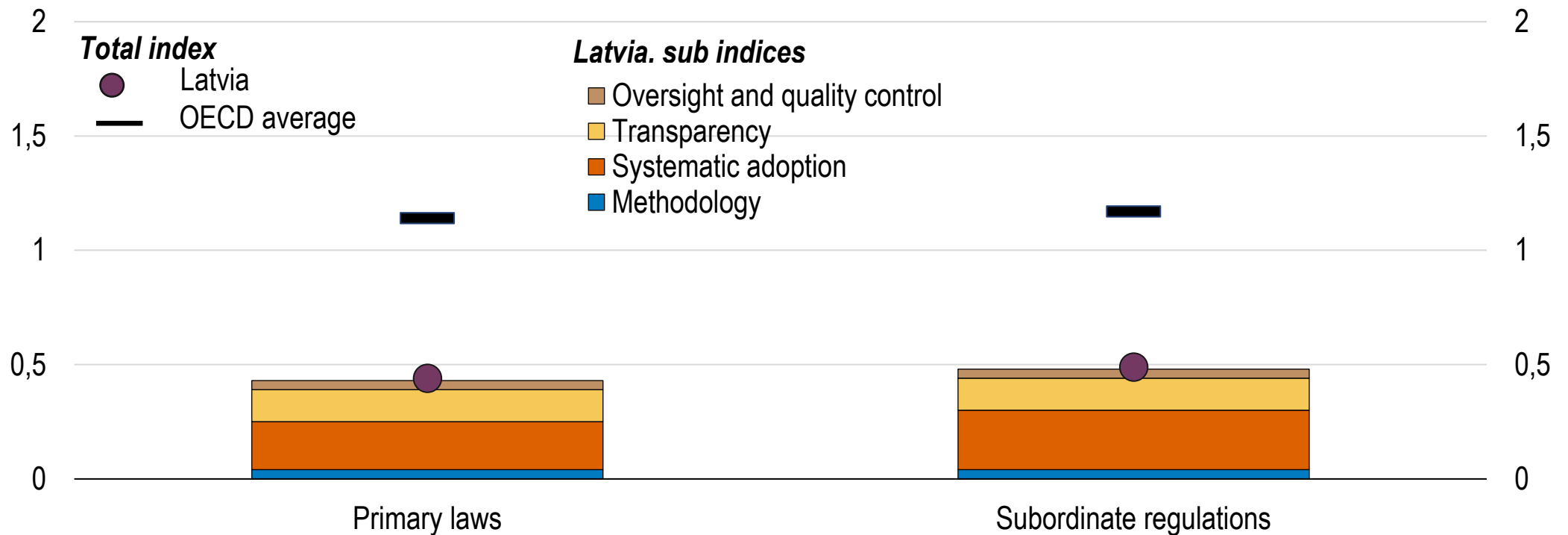


Note: Data are not available for the Slovak Republic, Switzerland, and the United States. The OECD Digital Government Index (DGI) is based on the six dimensions of the OECD Digital Government Policy Framework (DGPF): digital by design, data-driven, government as a platform, open by default, user driven and proactiveness. It measures the capacity of the public sector to deliver a coherent and human-centric digital government transformation, as well as the strategic approaches, policy levers, implementation, and monitoring mechanisms in place to deliver the digital government strategy. Thus, it captures much more than just digitising analogue processes (OECD, 2020).

Source: OECD Survey on Digital Government 2.0.

Better policy impact evaluation is key for raising the quality and efficiency of public policies

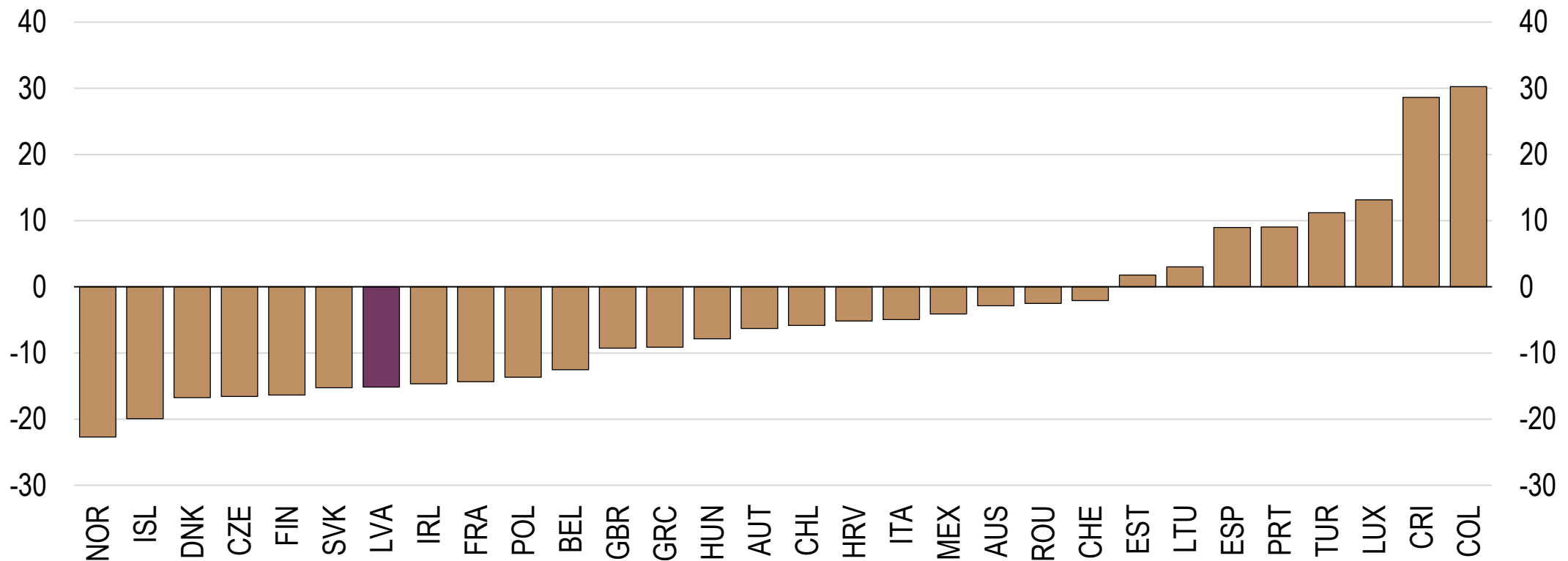
OECD Indicators on Ex-Post Policy Impact Evaluation, 2021
(higher values indicate better performance)



To improve public sector capacity, job attractiveness for higher-skilled jobs should be increased

Public sector wage premium for professionals

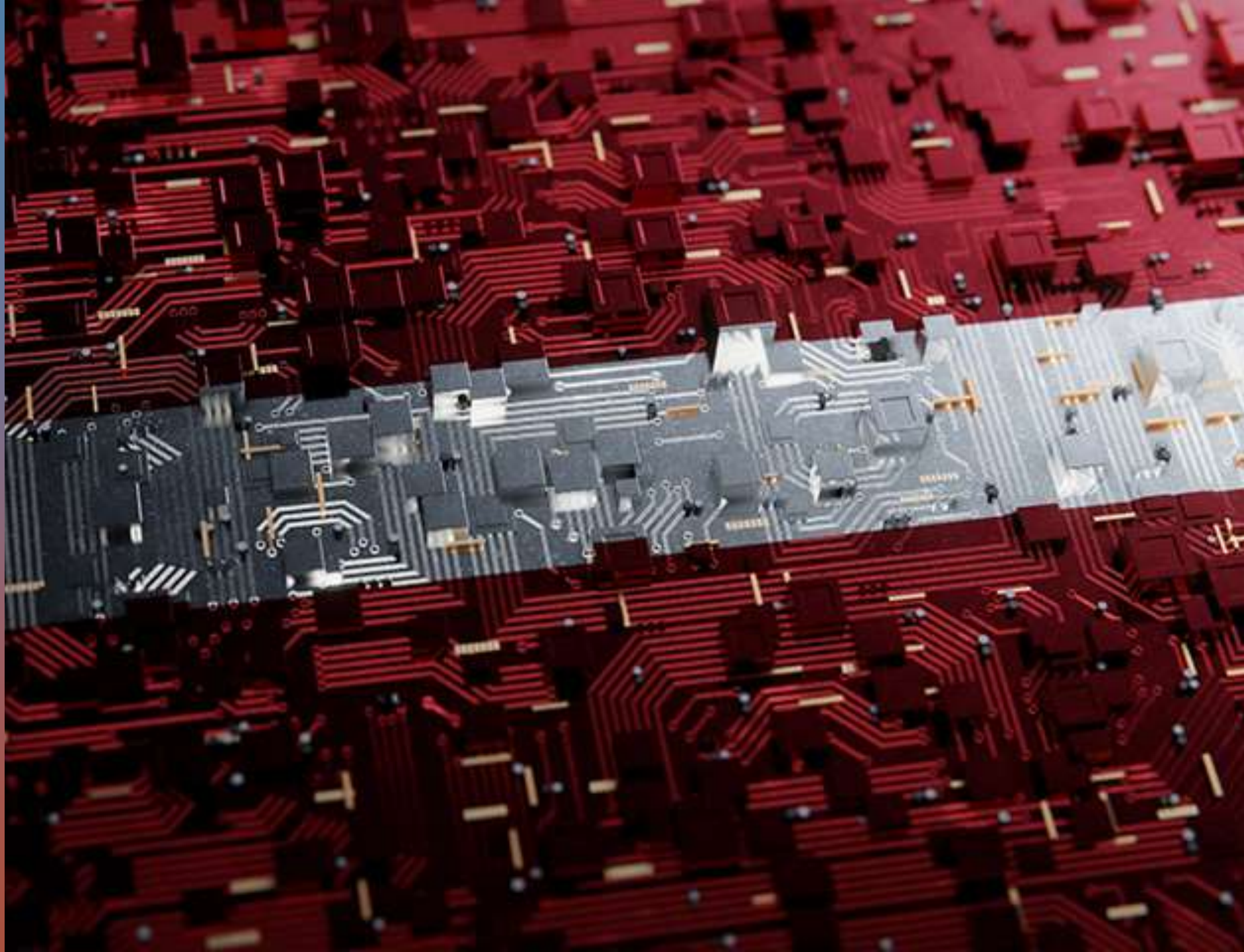
Public sector compared to private sector formal employees, %, 2018 or latest available year



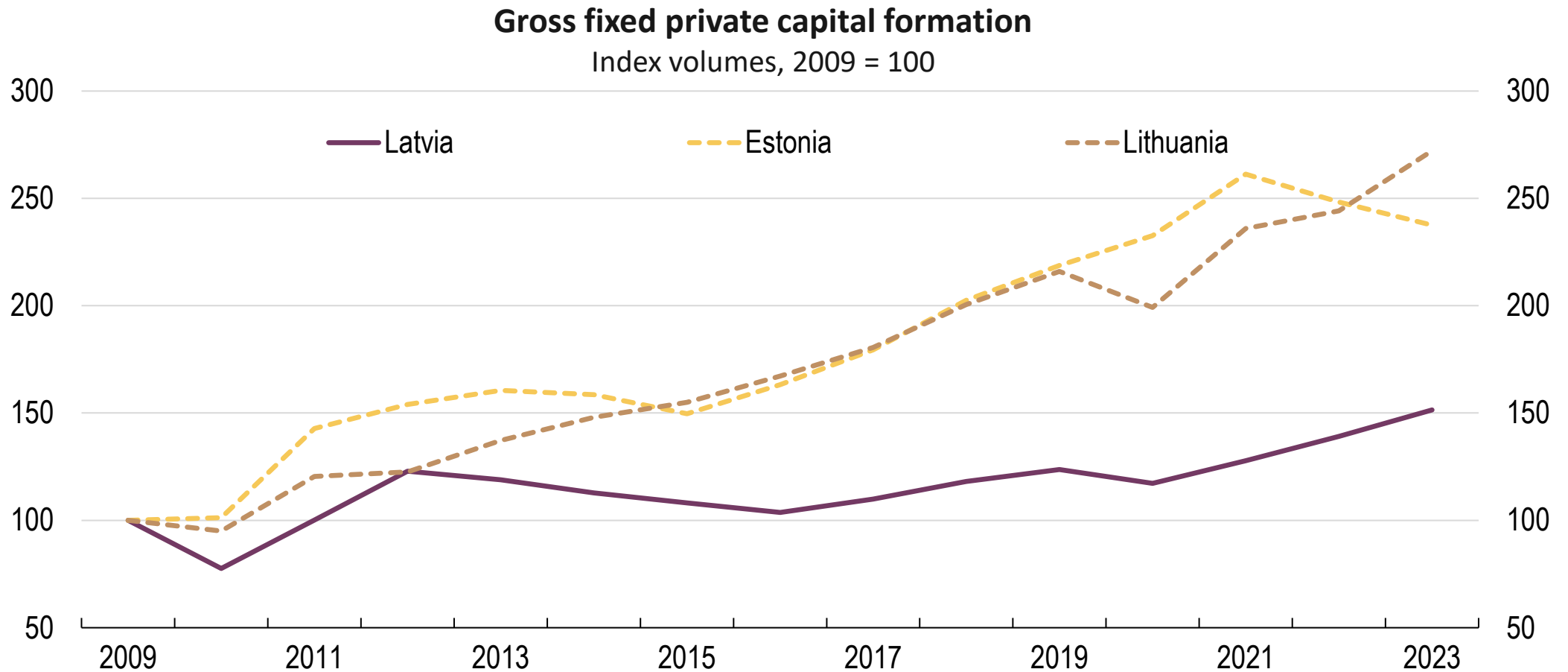
Source: World Bank, Worldwide Bureaucracy Indicators (WWBI).



Fostering
business
dynamism
and
innovation



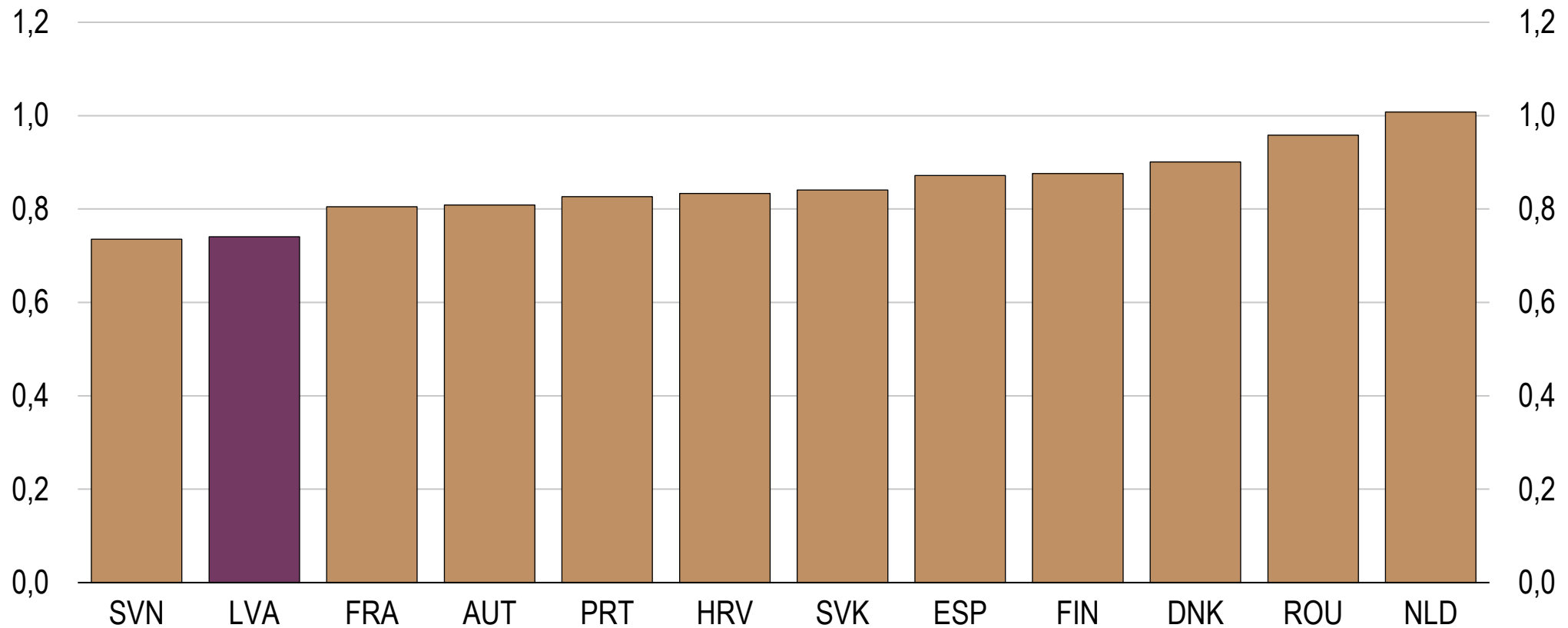
Private investment needs to increase to raise potential growth and living standards



Source: OECD Economic Outlook database and OECD calculations.

Small and medium-sized enterprises need to become more dynamic

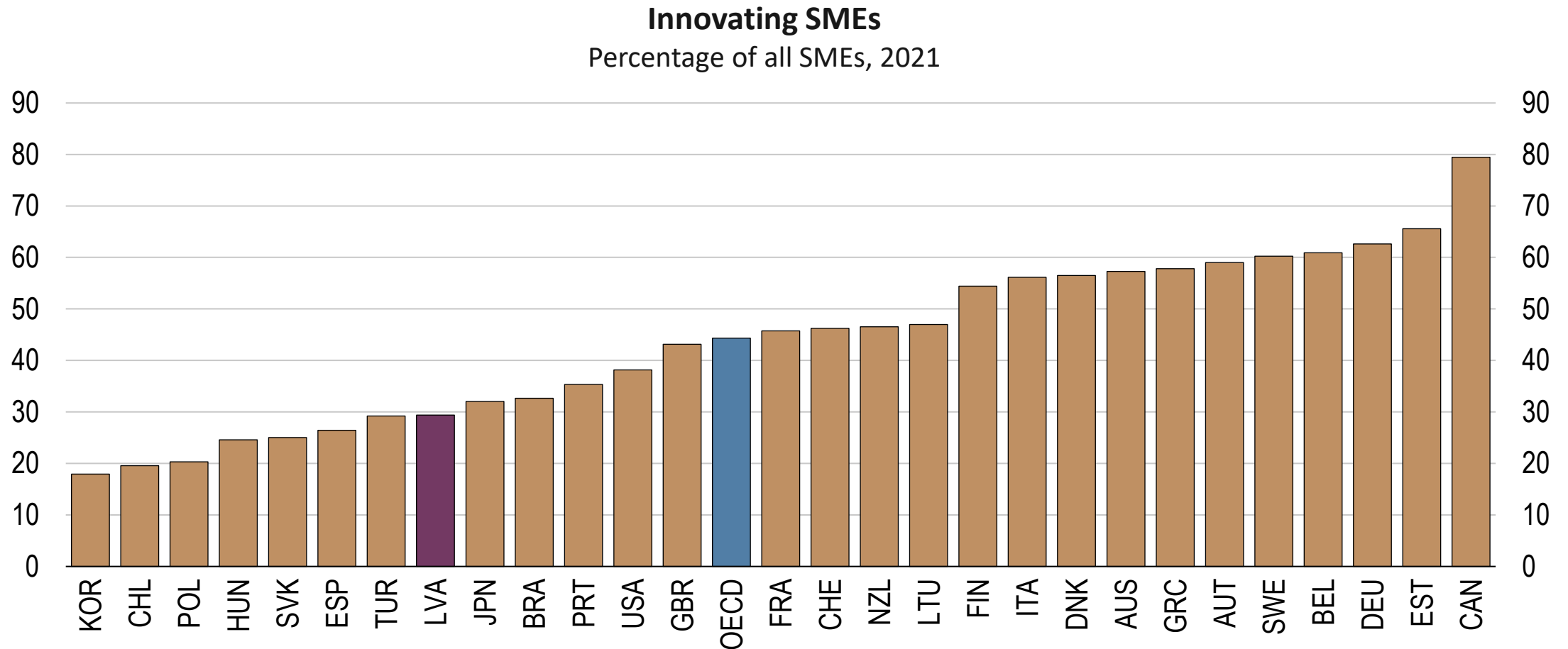
Average turnover growth rate of fast-growing small and medium-sized enterprises
% change, 2017-2020



Note: Fast-growing small and medium-sized enterprises are defined as firms with at least 10 employees that grow in employment or turnover by at least 10% per year, on average, over three consecutive years.

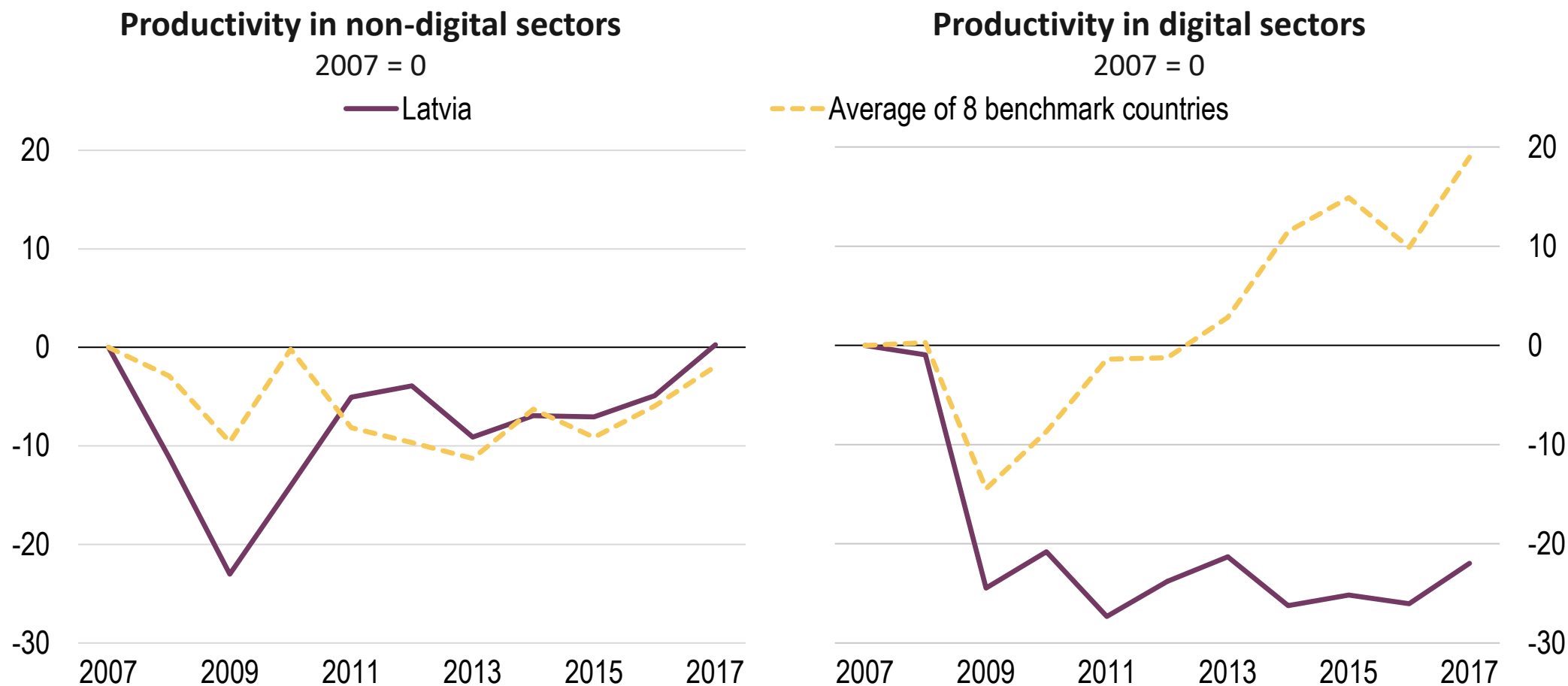
Source: OECD Database on Scalars, Centre for Entrepreneurship, SMEs, Regions and Cities.

SMEs need to be more innovative



Note: Innovating SMEs are those introducing product, process, marketing or organisational innovation.
Source: OECD 2021 Survey of National Innovation Statistics; and Eurostat Community Innovation Survey.

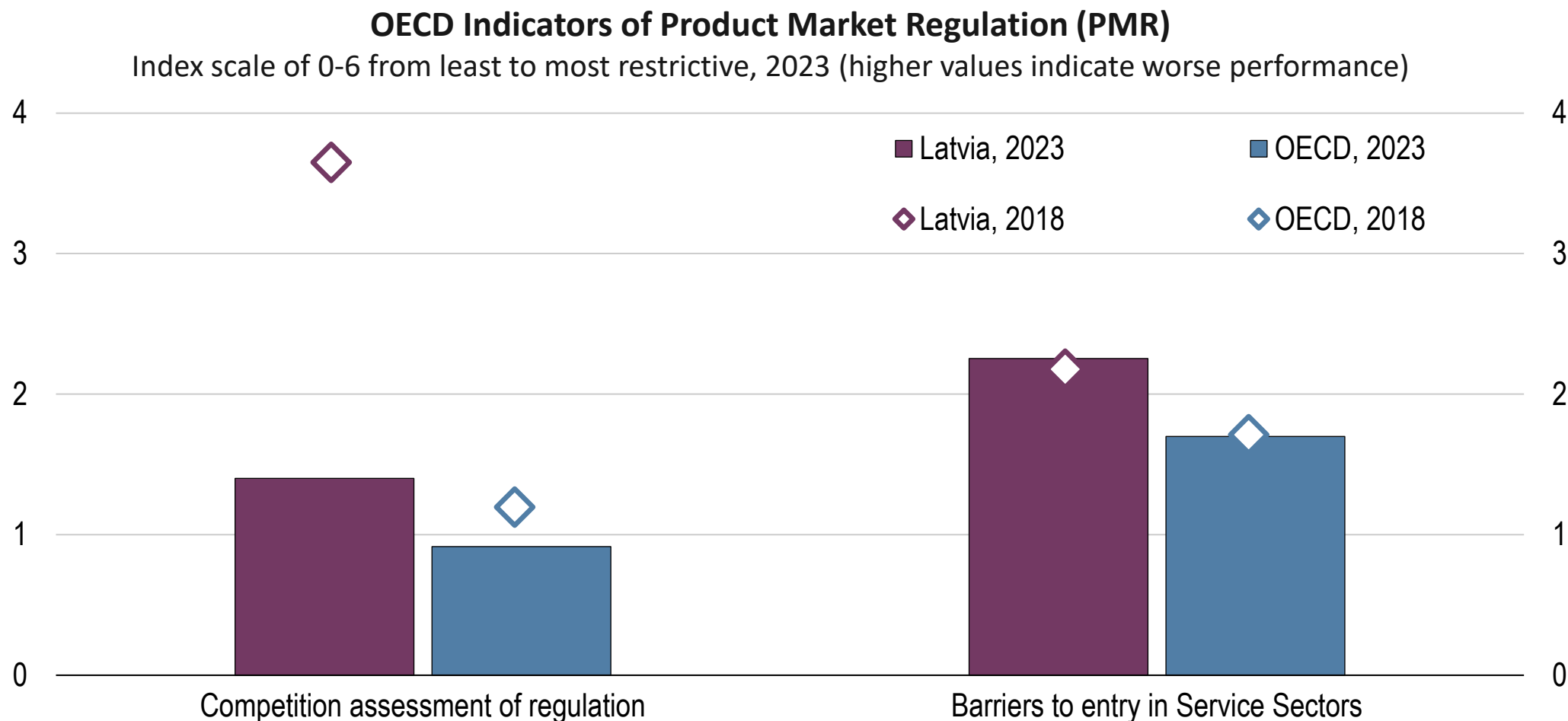
Productivity in digital sectors needs to improve



Note: The graph shows average multi-factor productivity of firms, normalised to zero in 2007. The benchmark country grouping includes Belgium, Croatia, Finland, Hungary, the Netherlands, Portugal, Slovenia and Sweden. Comparable data are not available beyond 2017 for some countries. Digital sectors are defined as sectors that are intensive in digital technologies and have a high share of ICT occupations on average across OECD countries.

Source: OECD MultiProd project.

Recent indicators of product market regulation indicate scope to further strengthen competition

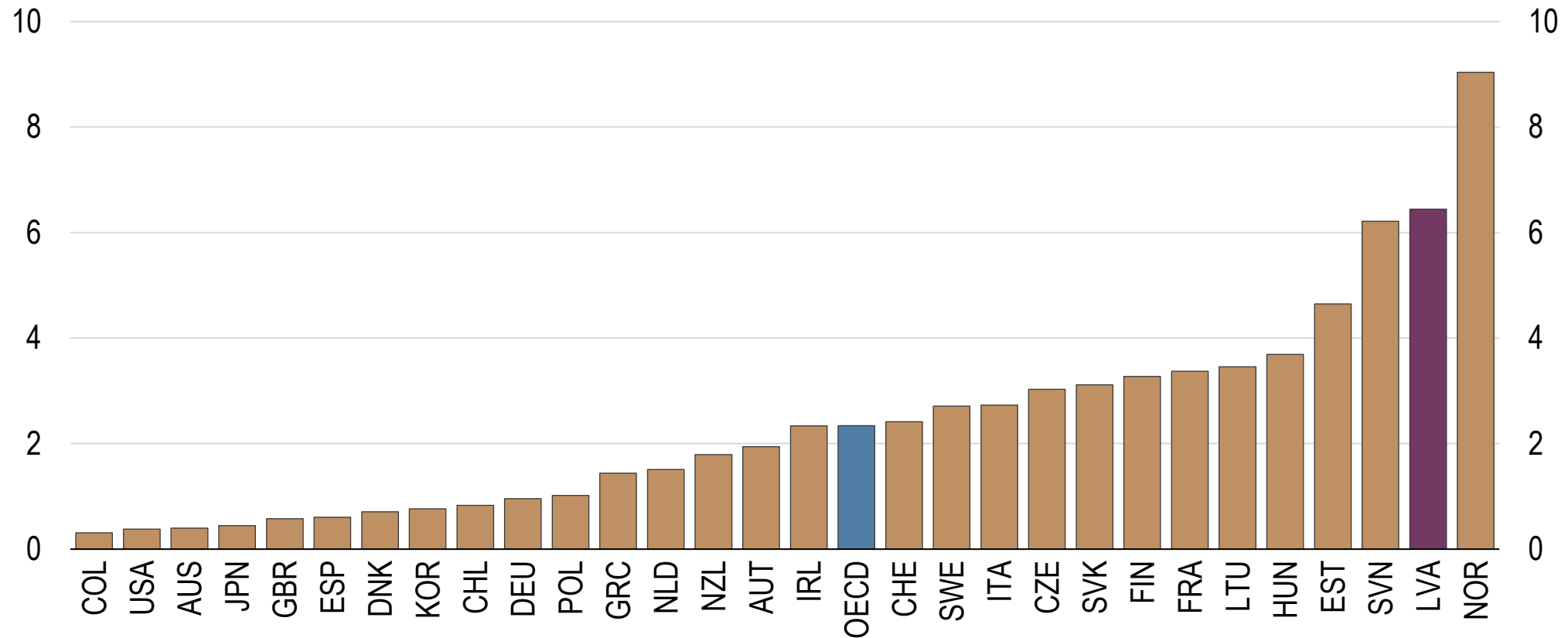


Note: OECD average includes all OECD countries, apart from Belgium, Colombia, Hungary, Mexico, the Netherlands, Slovak Republic, and the United States for which data collection is still ongoing. PMR values for Estonia and Lithuania for 2023 will only be released in Summer 2024.

Source: OECD (2023), Product Market Regulation Database (forthcoming).

Competitive neutrality between state-owned enterprises and private firms should become a stronger priority

Employees in state-owned enterprises (≥50% ownership)
Employees of state-owned enterprises as a % of total employees, 2015



Note: No update to these data from 2015 are available. Since 2015, the number of Latvian state-owned enterprises has not decreased.

Source: OECD calculations based on OECD National Accounts database and OECD (2017), The Size and Sectoral Distribution of State-Owned Enterprises, OECD Publishing, Paris, <https://doi.org/10.1787/9789264280663-en>.

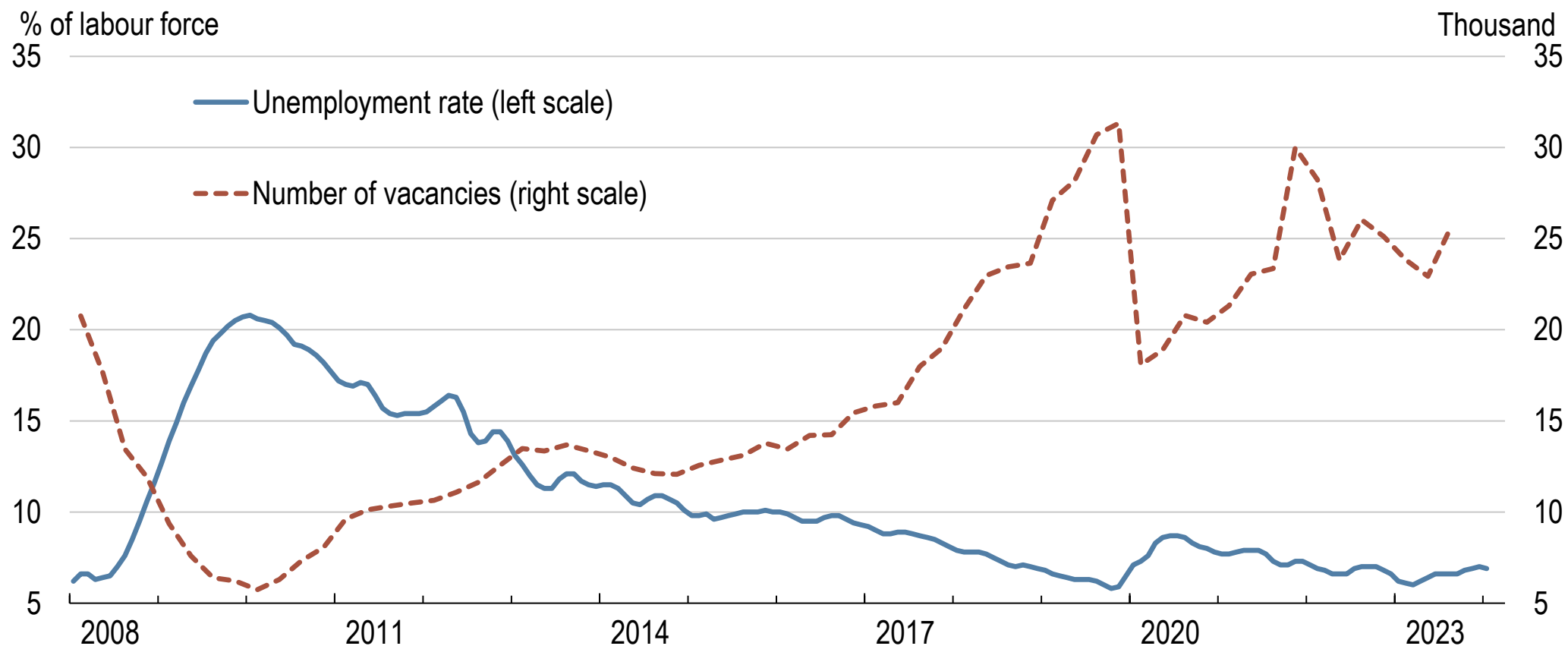


Addressing labour and skills shortages



Labour shortages have intensified

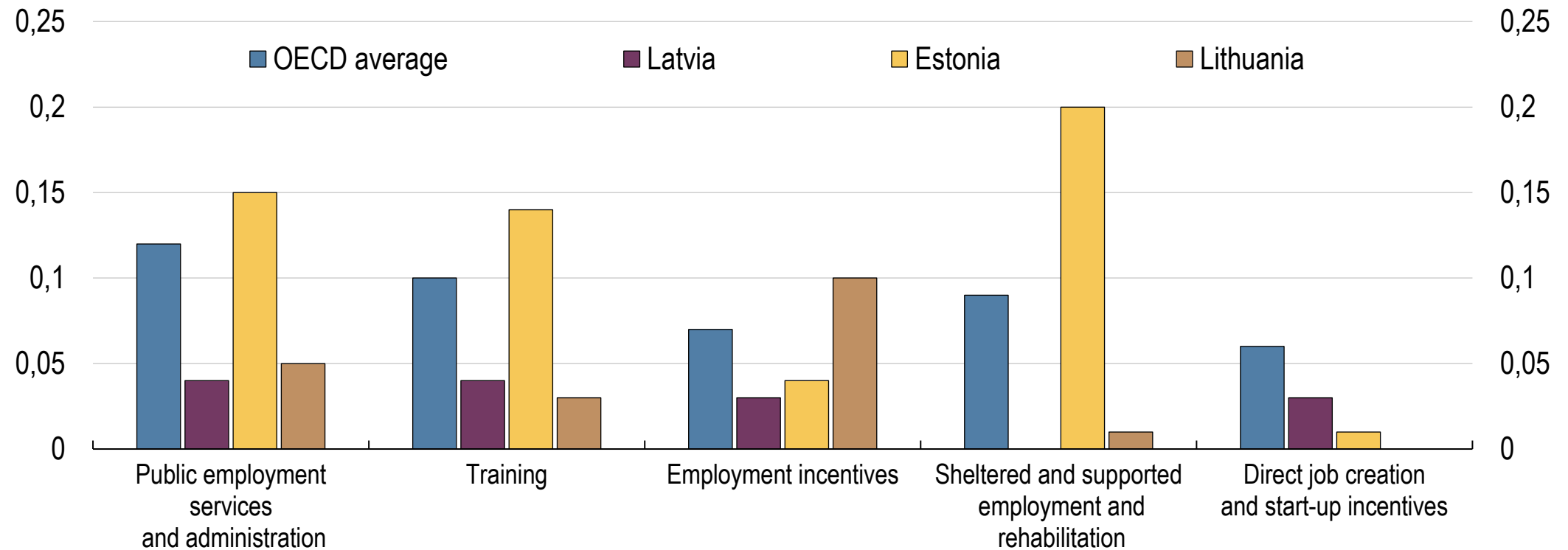
Unemployment rate and vacancies



Source: Central Statistical Bureau of Latvia; and Eurostat.

Improving active labour market policies would help raise domestic labour supply potential

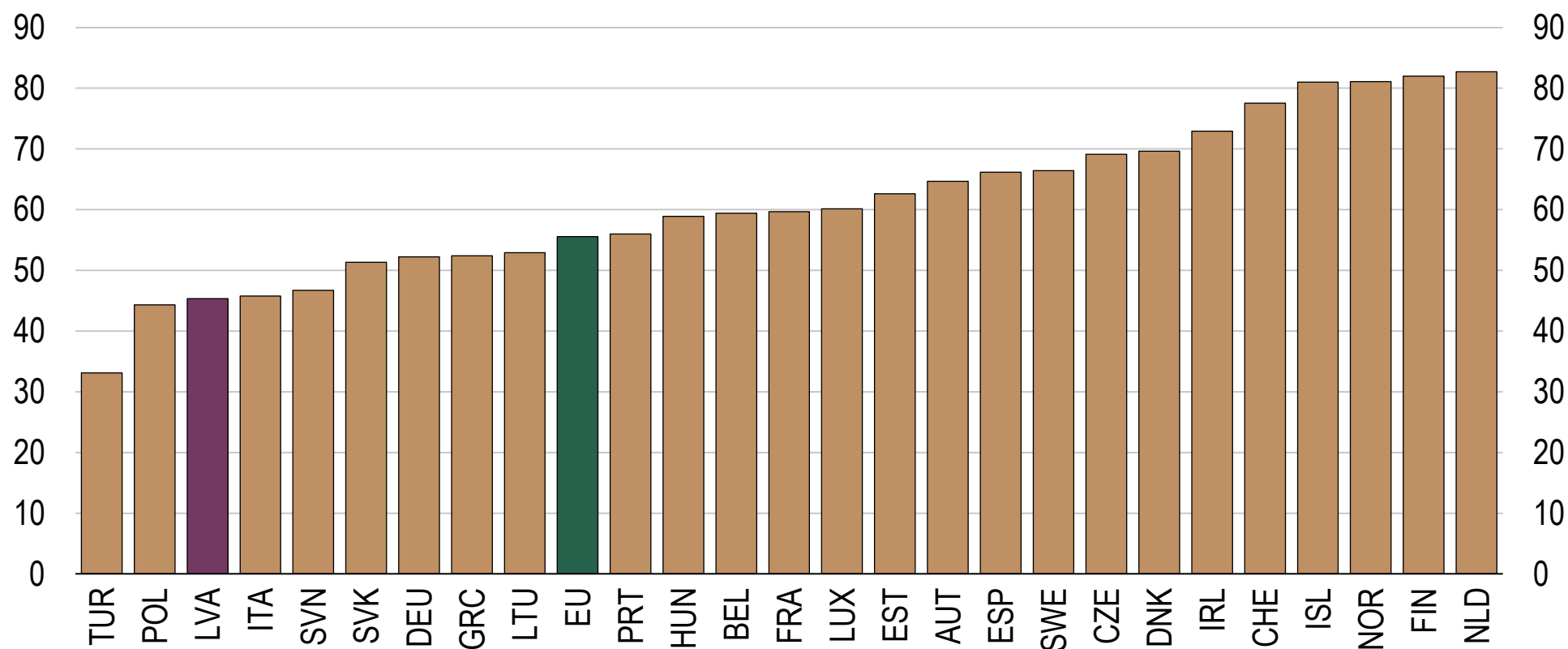
Public expenditure on active labour market policies
% of GDP, 2021



Note: Data exclude temporary employment maintenance.
Source: OECD Labour Force Statistics.

Weak digital skills weigh on the adoption of digital technologies

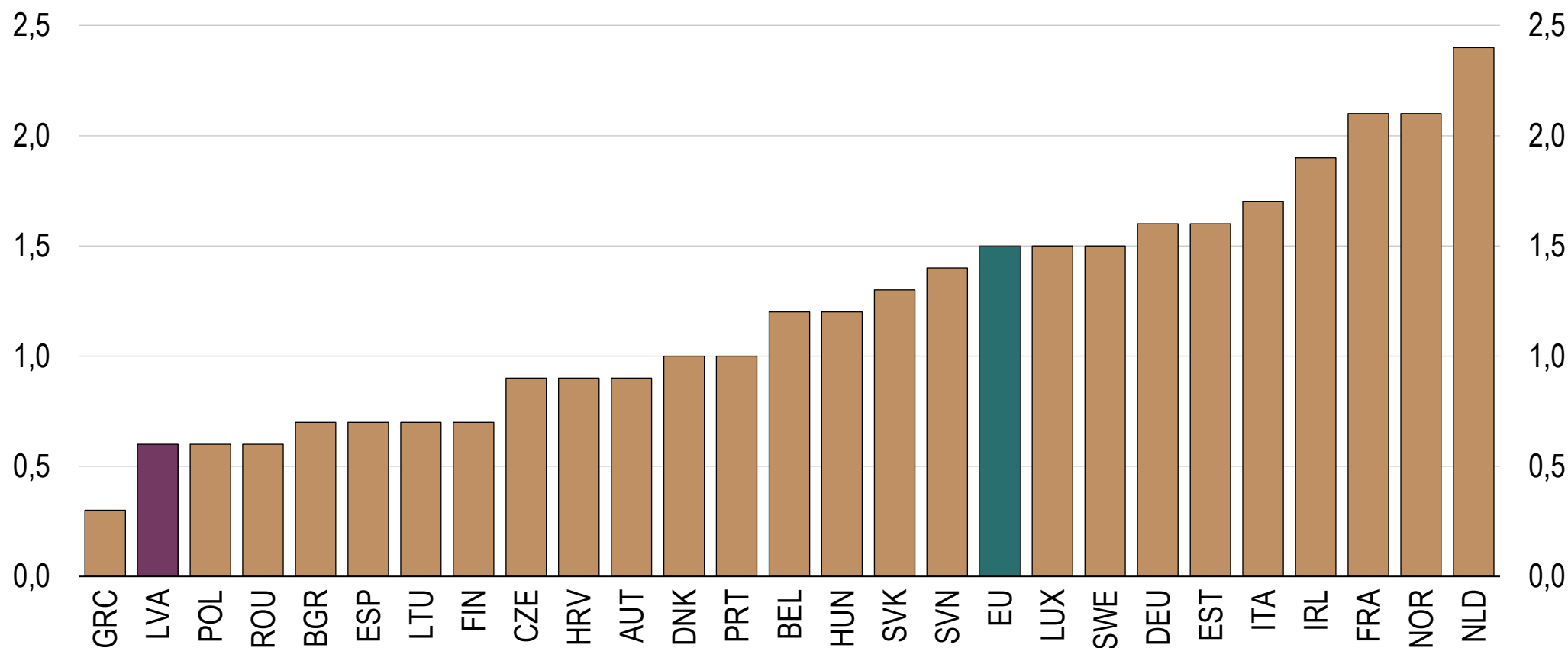
Share of individuals with basic or above basic overall digital skills
%, 2023



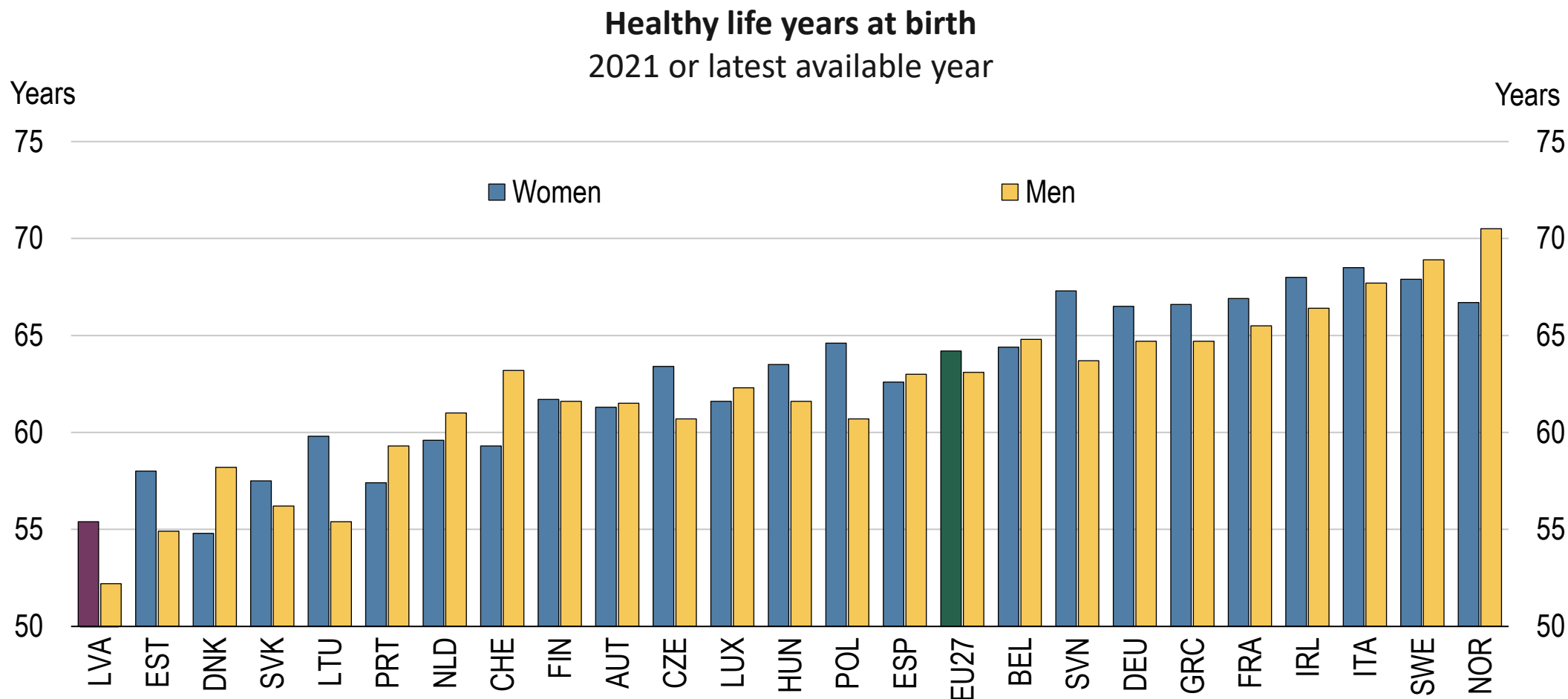
Source: Eurostat.

Firms need to step up training

Spending on continuing vocational training courses
% of total labour cost of all enterprises, 2020

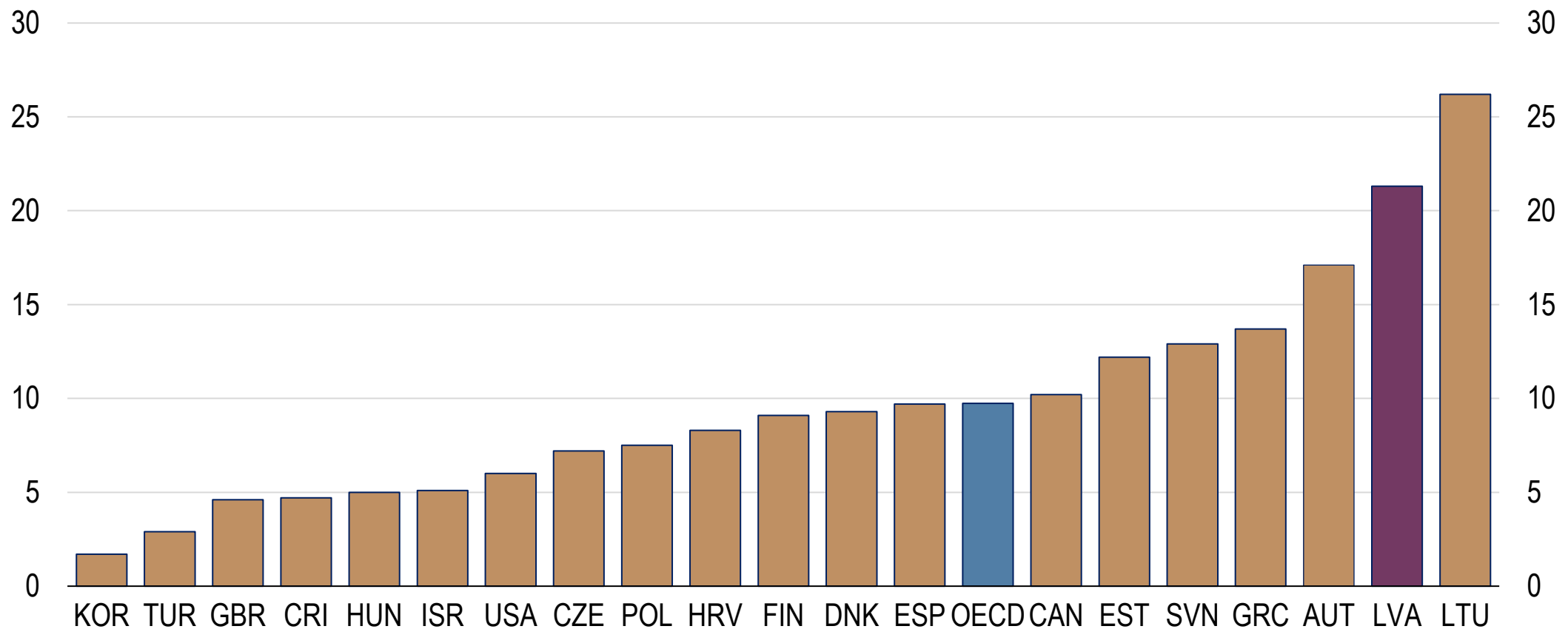


Improving health outcomes is key to enable older people to live and work longer



.. and to reduce the number of sick days taken by workers

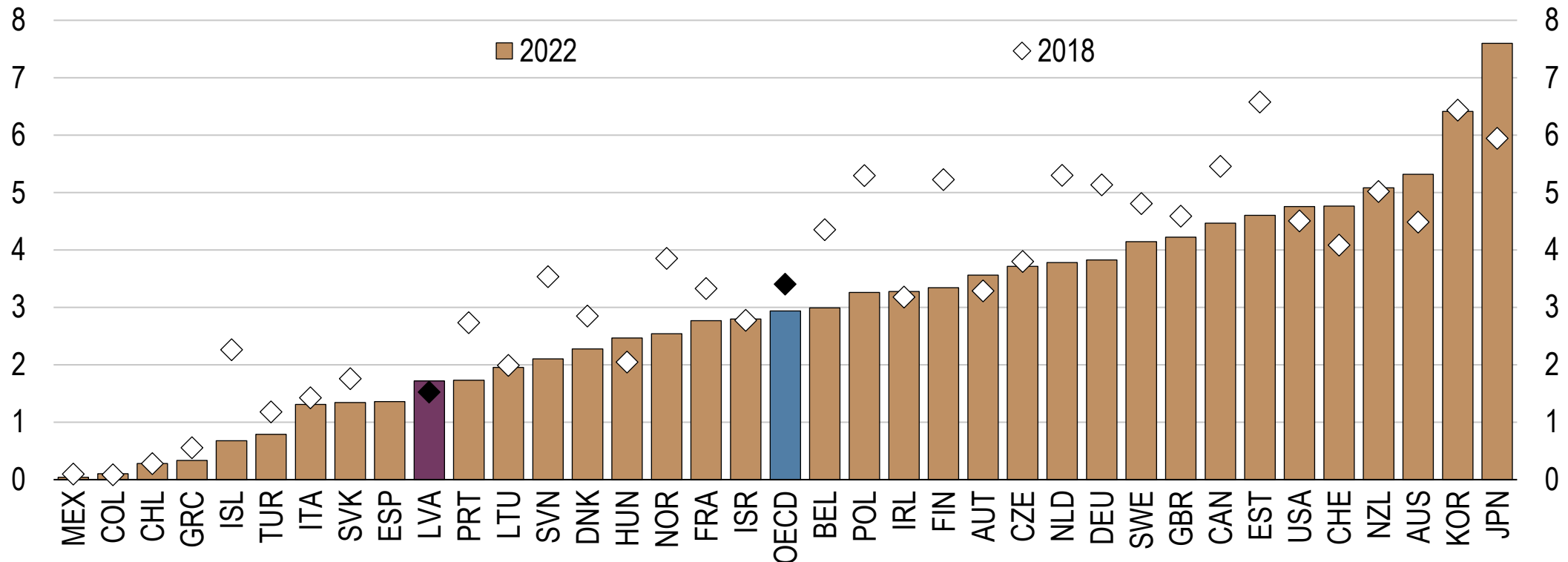
Self-reported absence from work due to illness
Days per year per person, 2022 or latest available year



Source: OECD Health Statistics.

Raising teaching quality is key to improve human capital of the future workforce

Top performers in science, mathematics and reading
% of 15 year-old students

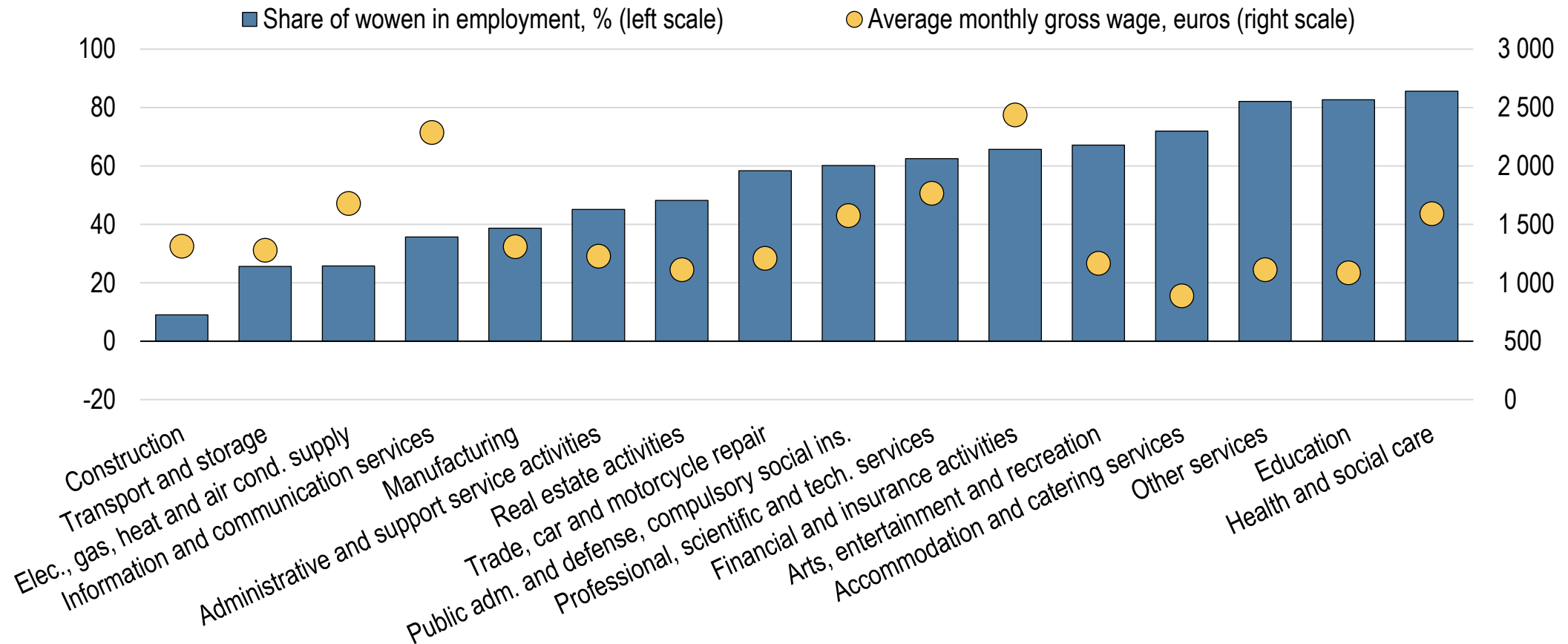


Note: Top performers in science, mathematics and reading are students who achieved the highest level of proficiency (i.e. Levels 5 and 6) on the OECD's PISA assessment.

Source: OECD (2020), PISA 2018 Results (Volume I); OECD (2023), PISA 2022 Results (Volume I).

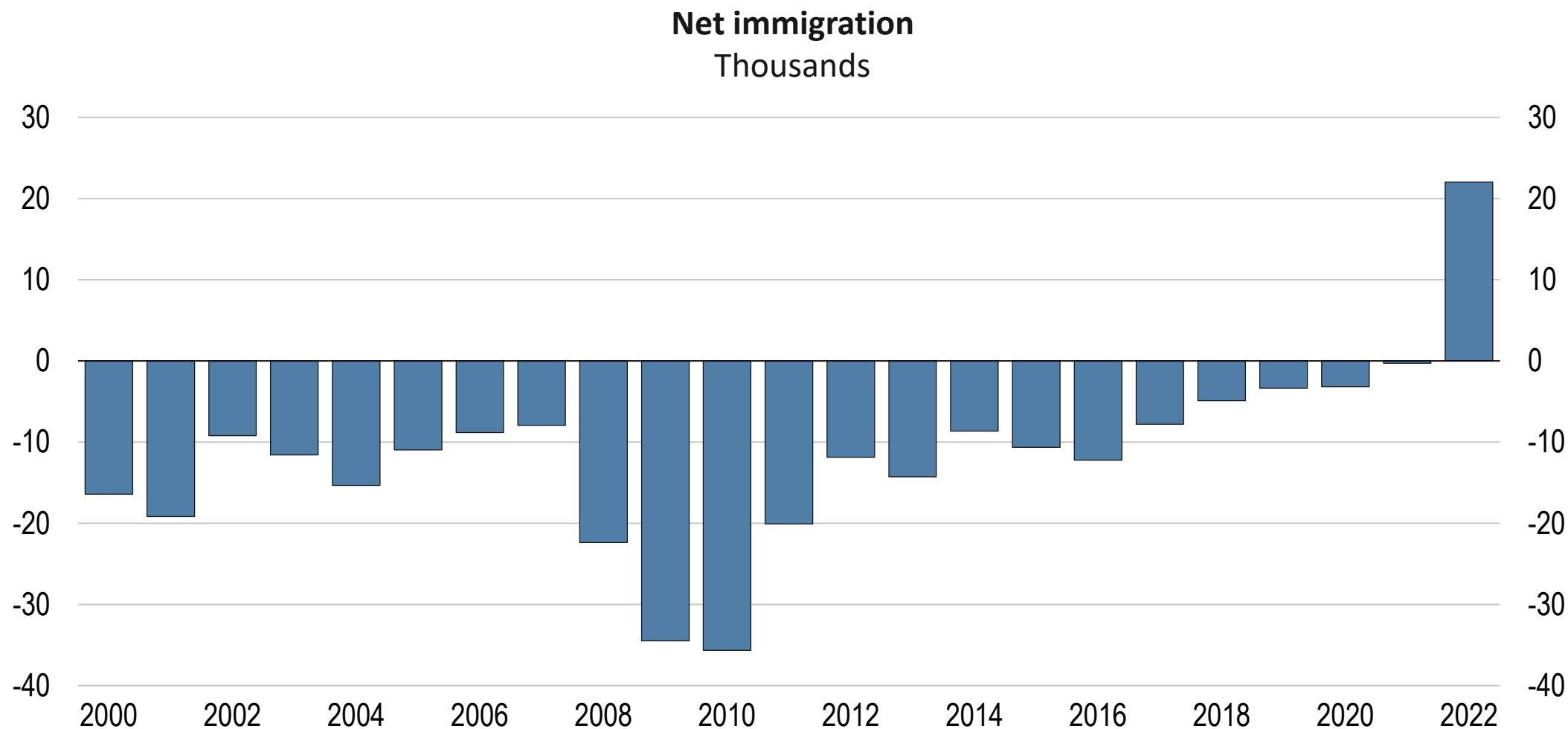
More young women should be motivated to enter high skill professions

Women tend to work in sectors with lower average wages
2022



Source: Central Statistical Office.

Latvia needs to become more attractive for skilled migrants and Latvians abroad



Source: Central Statistical Bureau of Latvia.



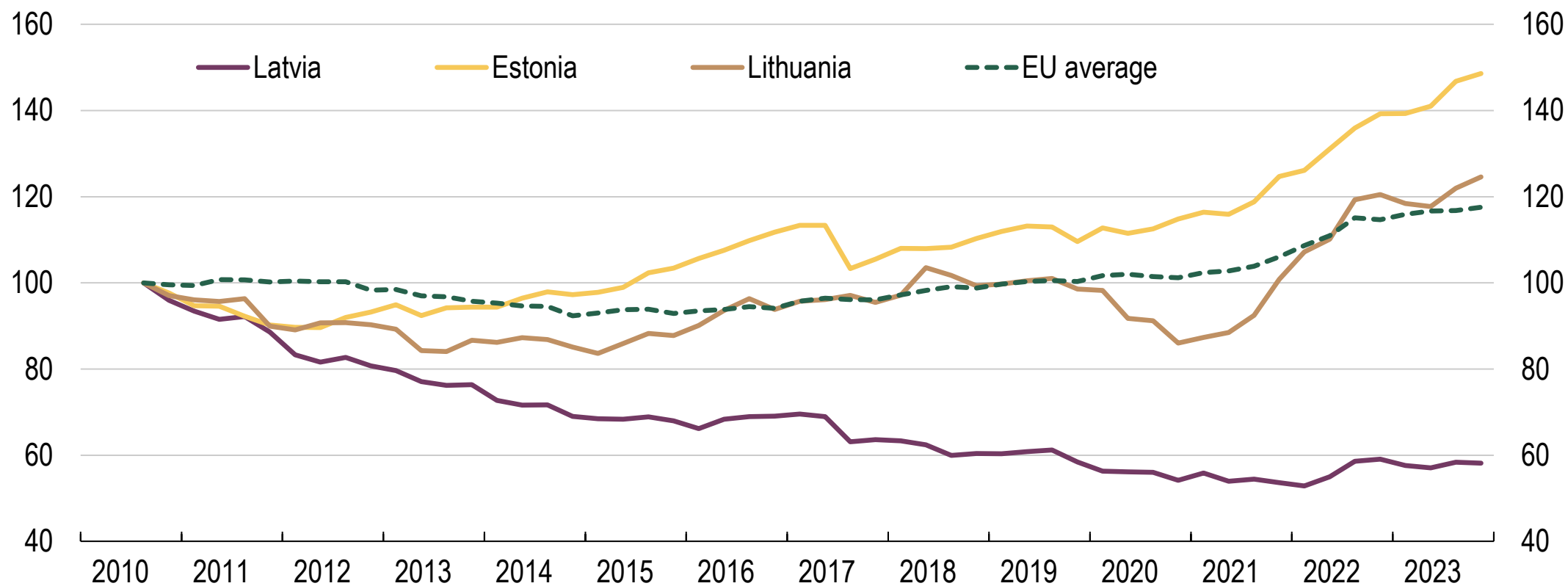
Improving access to finance



Credit to firms needs to increase to support investment

Credit to non-financial corporations

2010 quarter 3 = 100

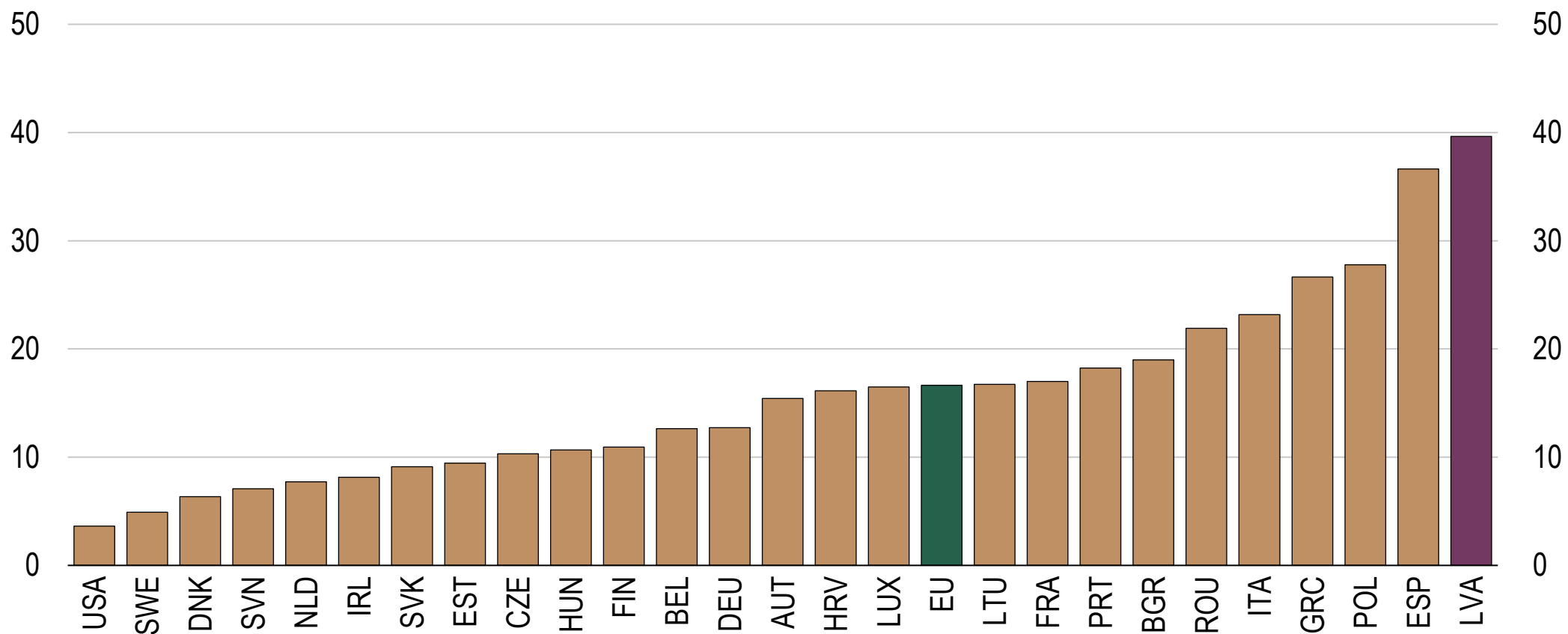


Note: Credit refers to loans and securities other than shares.

Source: ECB Data Portal.

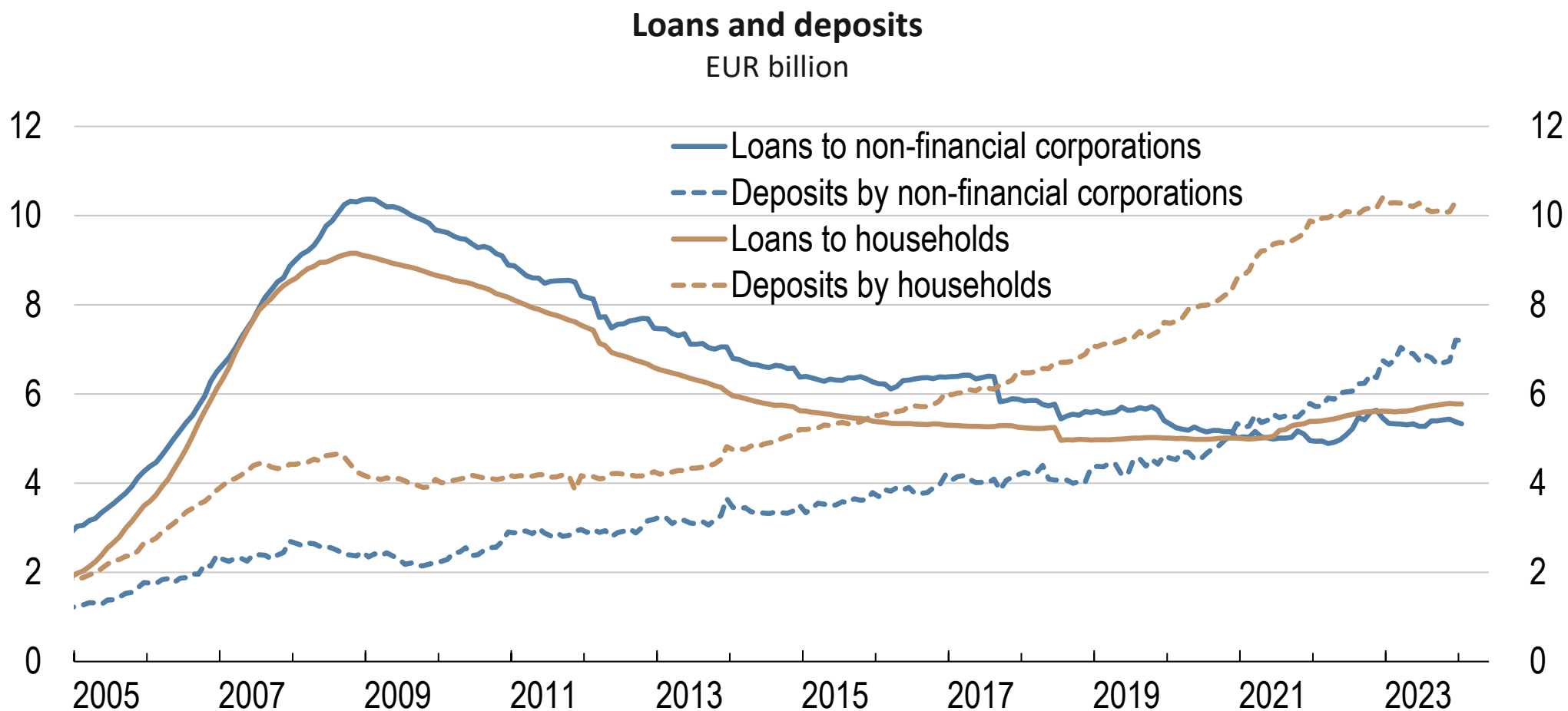
Access to finance is a key obstacle to private investment

Share of firms that cite availability of finance as a major obstacle to investment
2022, %



Source: European Investment Bank, EIB Investment Survey.

Banks have the capacity to lend more

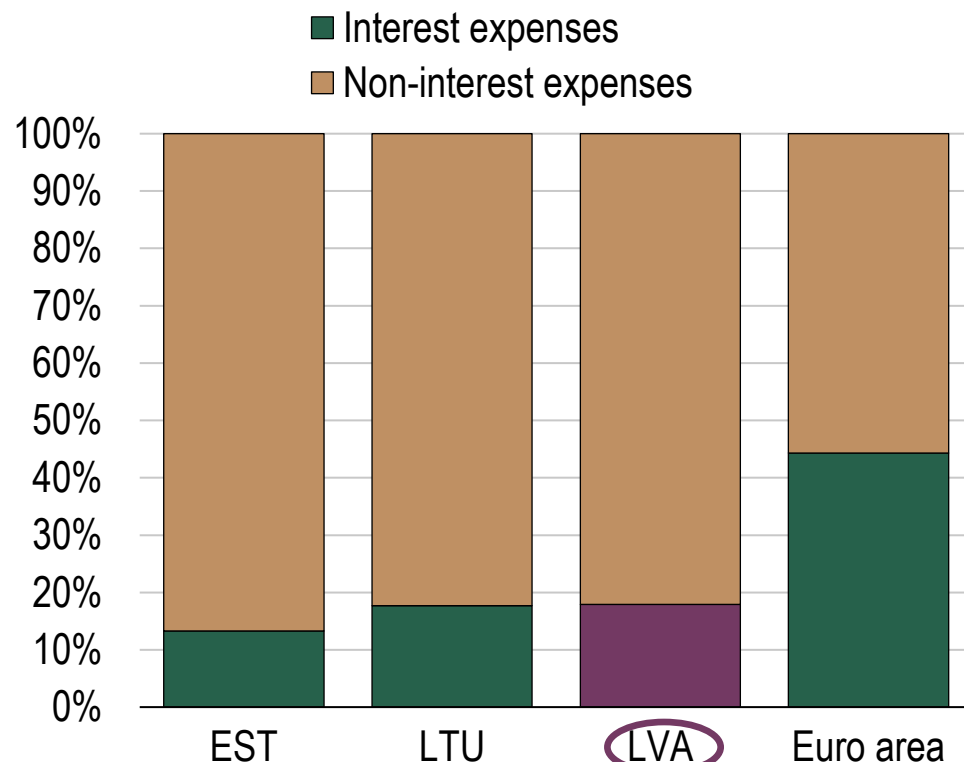


Source: Bank of Latvia.

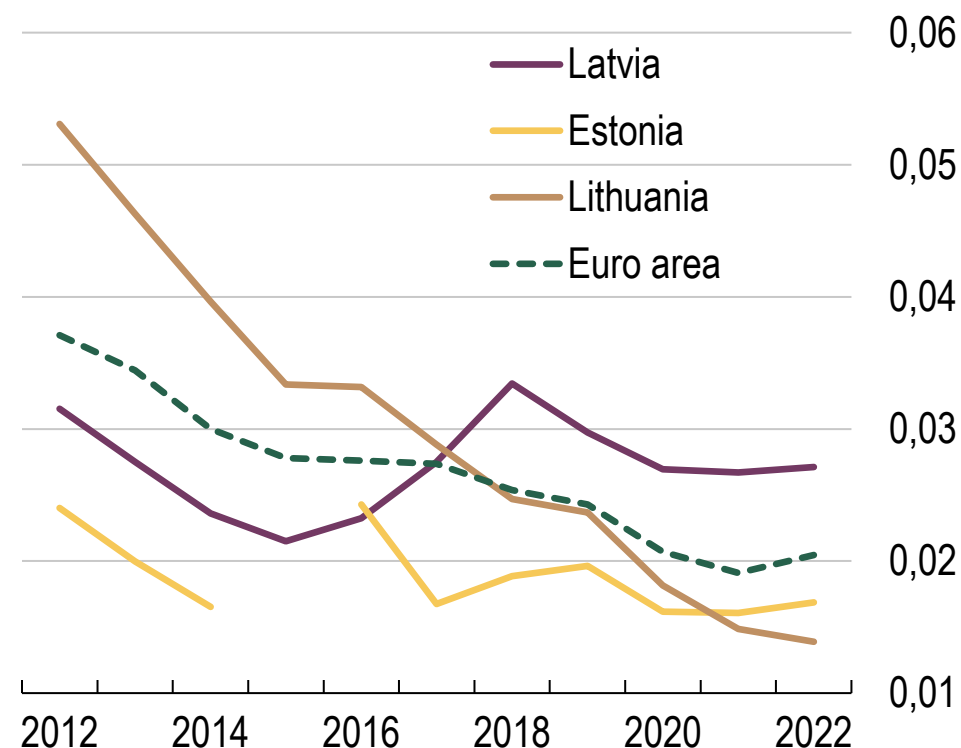
Anti-money laundering risk management should improve to reduce administrative costs and facilitate more lending

Expense structure of the banking sector

2012-22 average



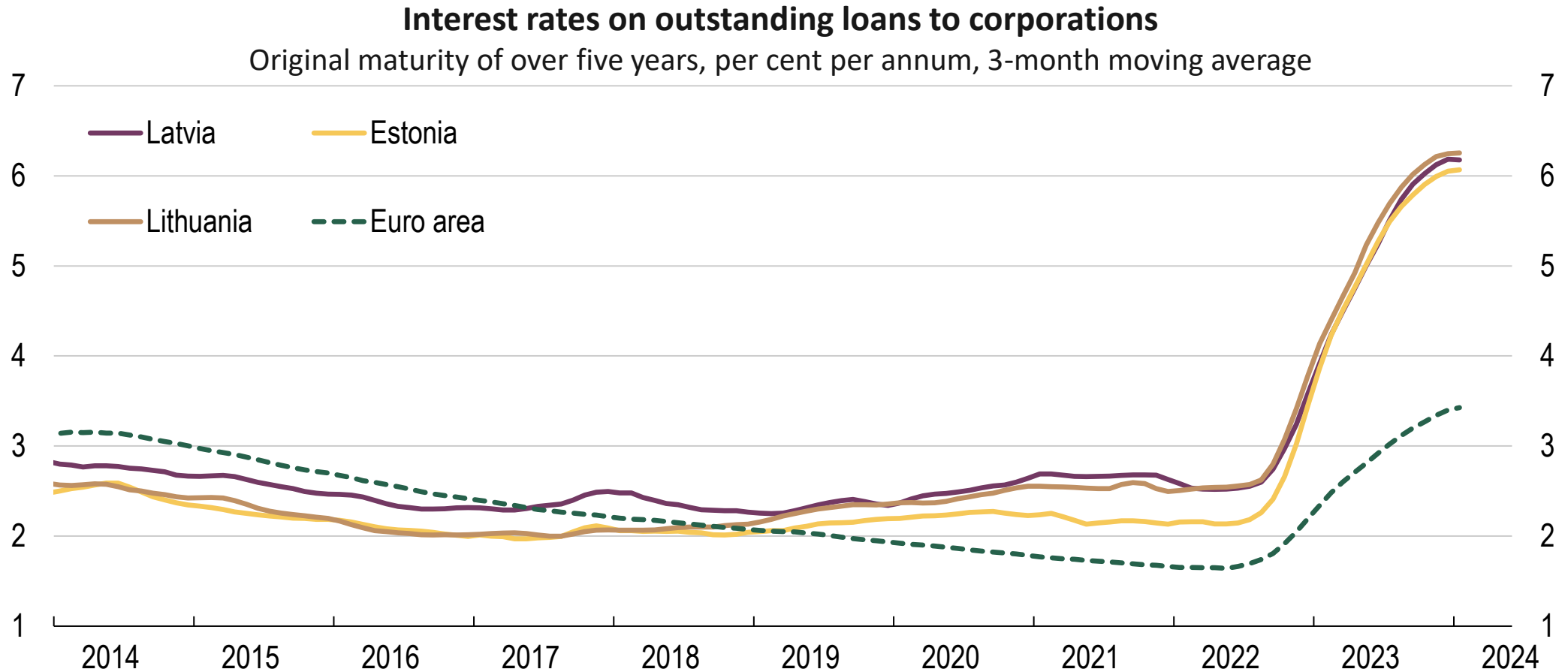
Marginal cost of assets



Note: The euro area aggregate accounts for about 83% of the total assets reported by monetary and financial institutions excluding the Eurosystem of central banks and reflects the unweighted average of around 150 major euro area banks (the exact number varies according to data availability). Marginal costs shown in Panel B relate to interest expenses and non-interest expenses, which include administrative burden. See Box 2.1 on the estimation of the marginal costs. For Estonia, bank-level data in 2015 are discontinued.

Source: Bloomberg; (Benkovskis et al., forthcoming); and OECD calculations.

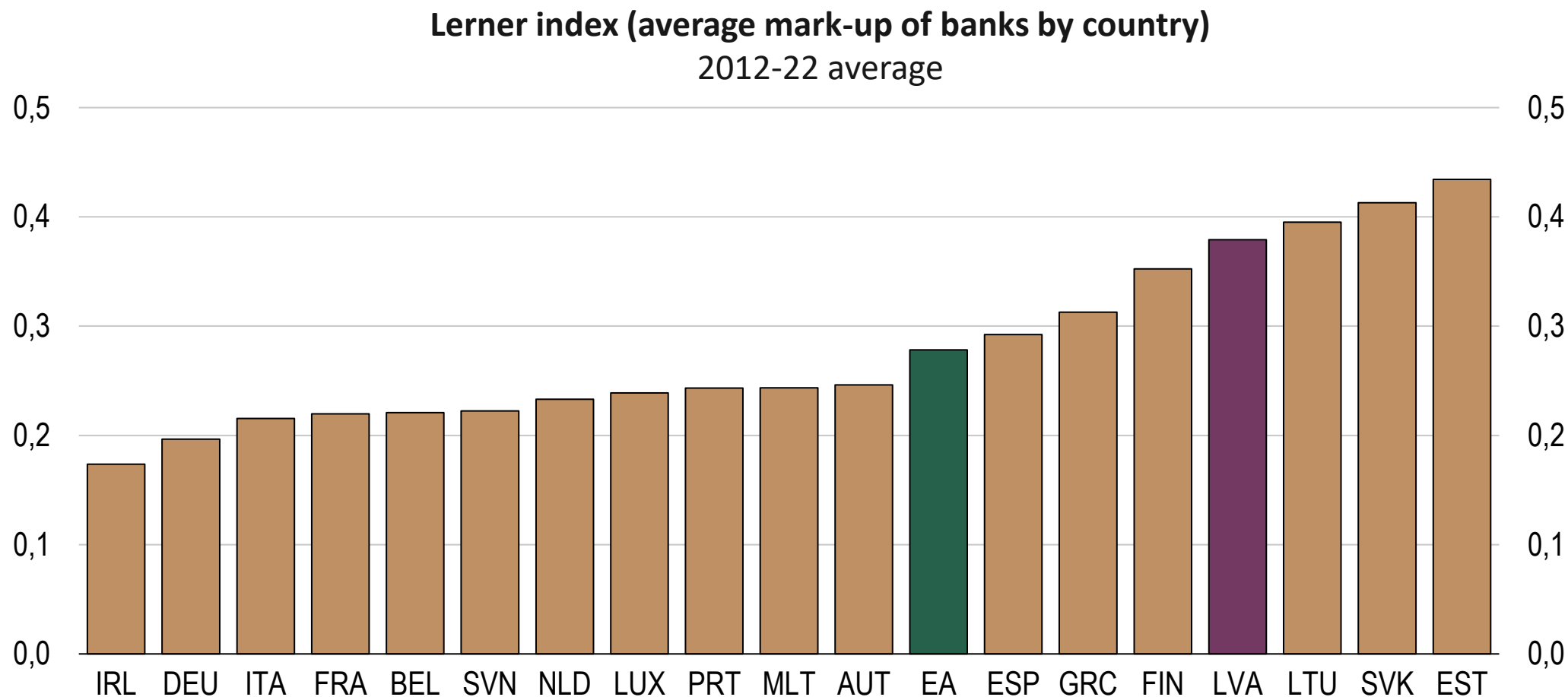
Lending rates have become much higher than in other euro area countries



Note: Chart shows the bank loan rate on outstanding amounts.

Source: Source: MFI Interest Rate Statistics at the ECB Data Portal; and OECD calculations.

There is room to raise competition in the banking sector

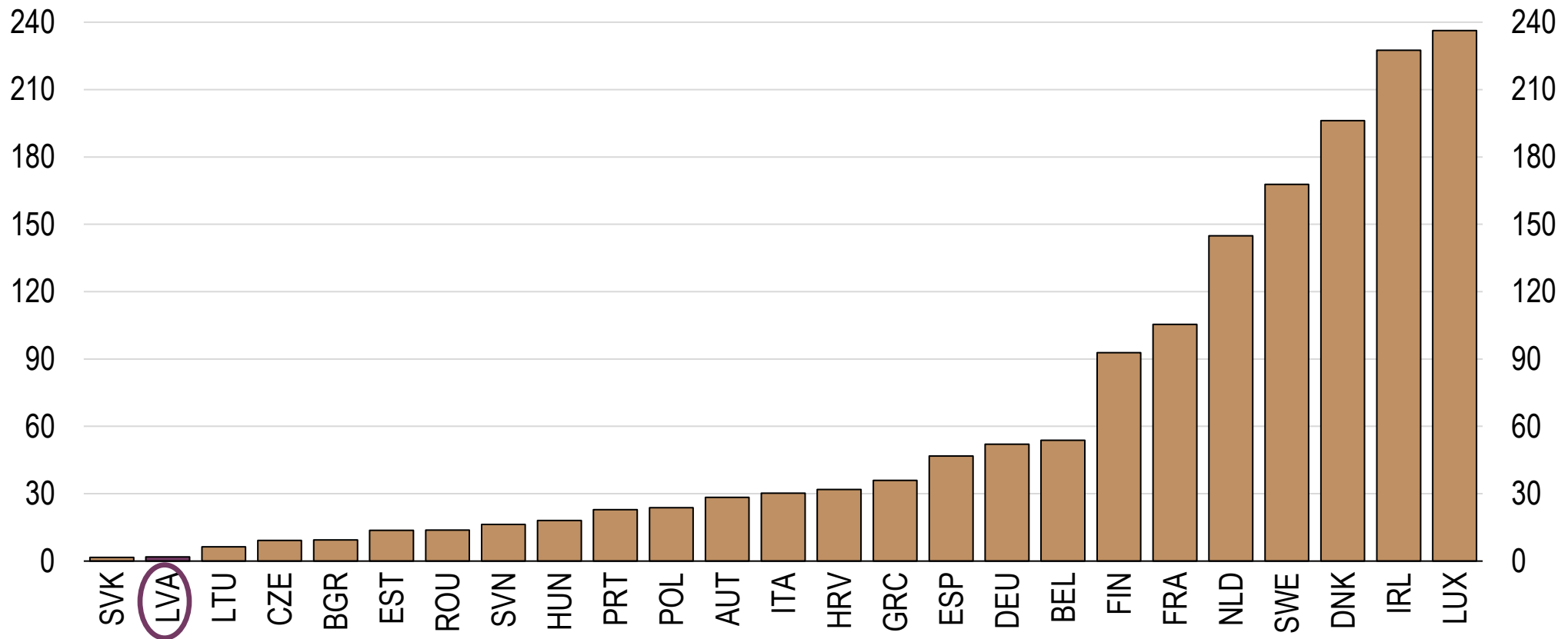


Note: The Herfindahl-Hirschman index (HHI) ranges from 0 to 1. Increasing values of the HHI correspond to higher market concentration in total lending. The bank-level estimates of the Lerner index, which is a direct measure of the price mark-up, follow closely (Demirguc-Kunt and Martínez Pería, 2010[17]) and are aggregated to the country level by taking unweighted averages across banks.

Source: Banking Structural Financial Indicators at the ECB Data Portal; Bloomberg; and OECD calculations.

Equity finance could be promoted further

Outstanding amount of listed shares
February 2024, % of 2023 GDP

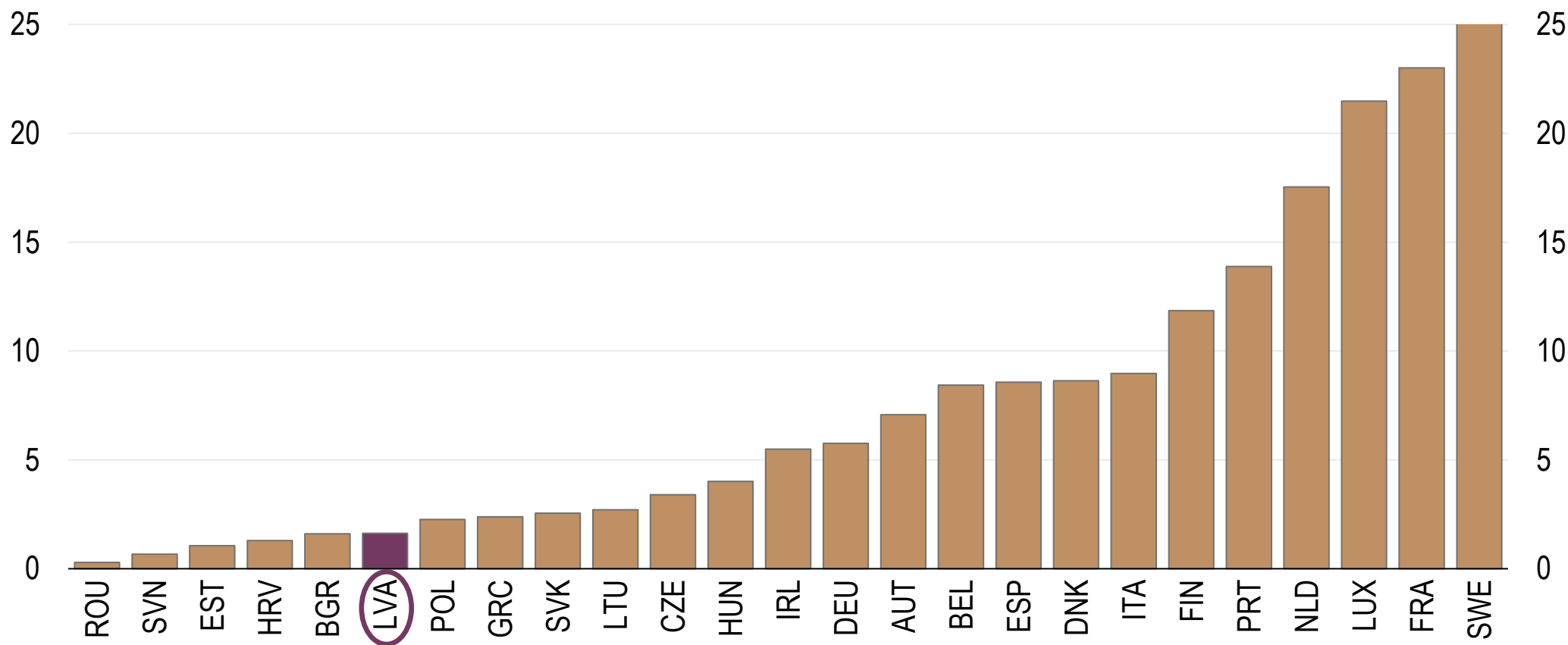


Source: ECB Data Portal; OECD Economic Outlook database; and OECD calculations.

Bond issuance could be facilitated further

Outstanding amounts of debt securities by non-financial corporations

February 2024, % of 2023 GDP

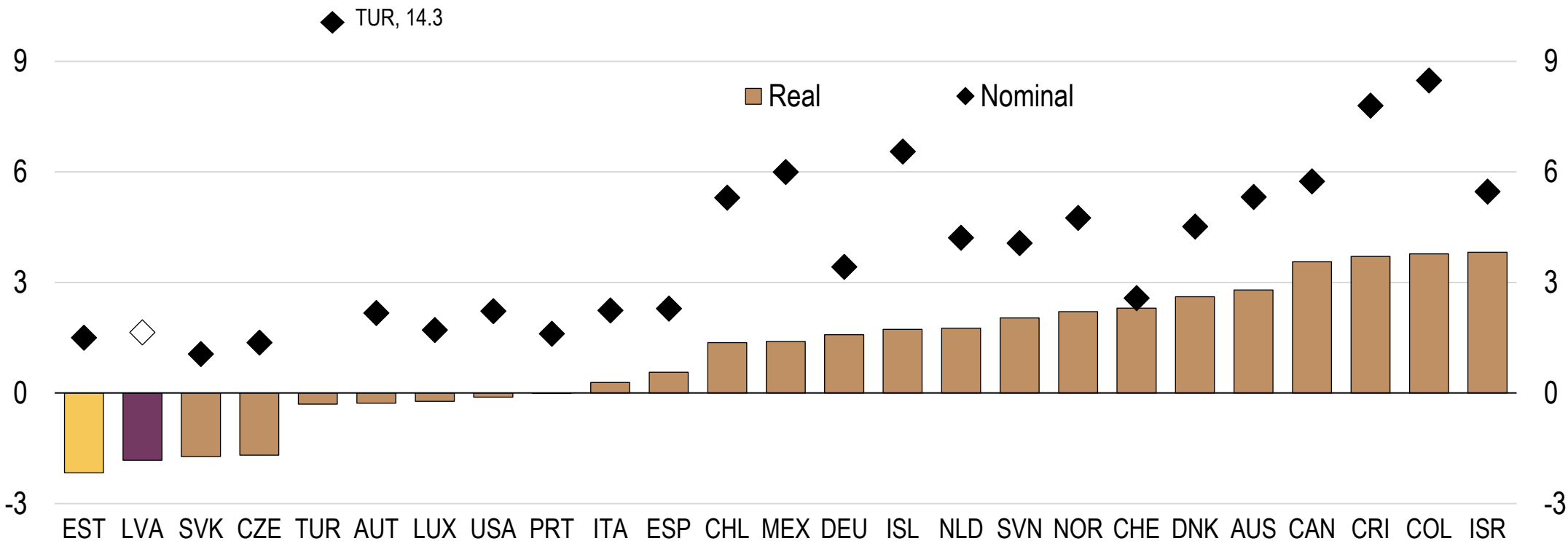


Source: ECB Data Portal; OECD Economic Outlook database; and OECD calculations.



The investment performance of pension plans could improve

Average annual rate of return on pension plan investments over the last 15 years as of 2022



Note: The average is calculated as a geometric mean.
Source: OECD Pension Markets in Focus 2023.



Main messages

Strengthening public finances

Gradually tighten the fiscal stance to reduce the high fiscal deficit. Address rising spending pressures in defence, health and old-age poverty by increasing revenue from income, property and environmental taxes, raising spending efficiency and reallocating spending. Ensure sufficient and stable revenue sources for municipalities.

Improving public sector capacity

Raise public sector capacity by increasing the attractiveness of public jobs and training for employees, improving policy impact analysis, centralising public procurement and the governance of state-owned enterprises, and continuing to fight corruption.



Main messages

Business dynamism and innovation

Foster business dynamism and innovation by reducing high informality, strengthening competition enforcement to ensure competitive neutrality of state-owned enterprises and robust competition assessment of regulation, and continuing to reduce corruption.

Access to finance

Foster credit supply by raising competition in the banking sector and deepening capital markets, including by listing minority shares of large state-owned enterprises and facilitating greater investment of pension funds in domestic securities.

Addressing labour shortages

Improve the quality of health, education and training services, encourage more young women to enter high skill professions, and continue to facilitate skilled migration.



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