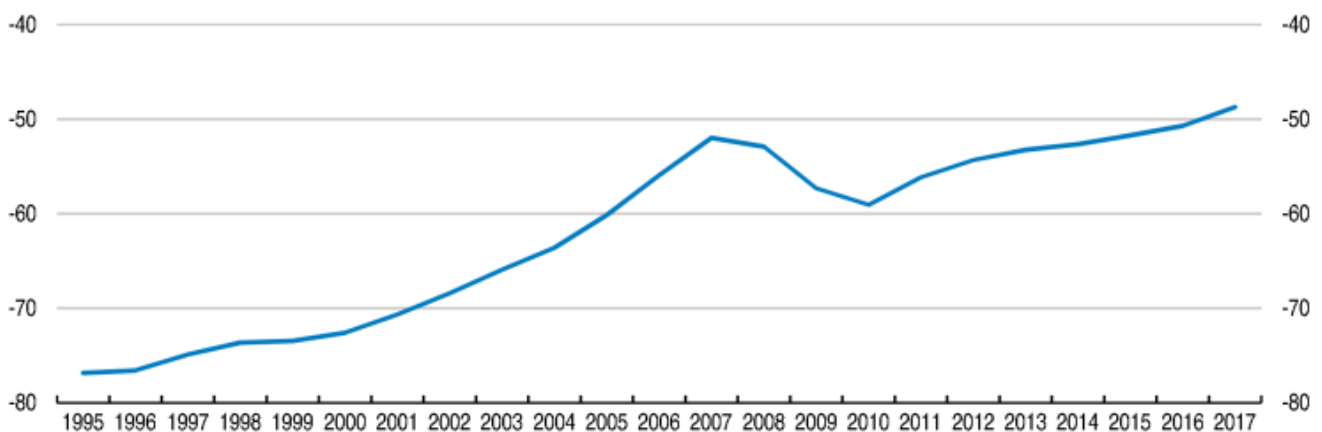


Latvia: Working towards stronger and more inclusive growth

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Latvia is a dynamic economy that joined the OECD in 2016. It has enjoyed strong economic performance in recent years and its macroeconomic policy is sound. Nevertheless, Latvia's per capita GDP is still only about a half of the average level of high income OECD countries (Figure 1). Latvia also faces one of the fastest declines in the working-age population in the OECD due to ageing and outmigration. Hence, strong productivity growth is crucial for Latvia to ensure continued catch up of living standards with higher income OECD countries.

Figure 1. Gap in GDP per capita against the upper half of OECD countries, %



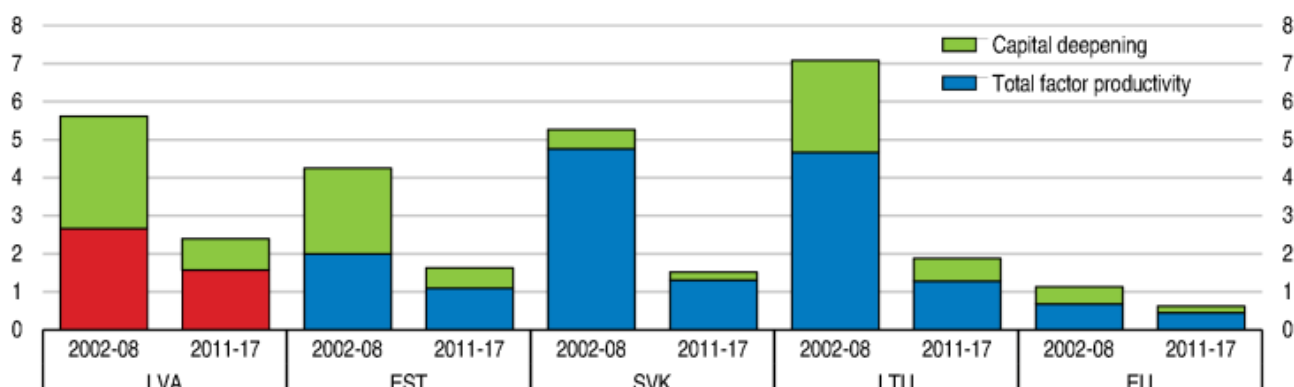
Note: Percentage gap with respect to the weighted average using population weights of the highest 17 OECD countries in terms of GDP per capita (in constant 2010 PPPs).

Source: OECD (2019), Economic Policy Reforms 2019: Going for Growth (forthcoming).

Although Latvia's labour productivity growth is among the highest in the OECD, it decelerated considerably after the crisis mostly due to a smaller contribution of investment (Figure 2). Business-based innovation is weak and the use of digital technologies lags considerably behind other OECD

countries despite fast Internet connection speed. A slow take-up of new technologies is due to shortages of qualified workers and weak knowledge transfer from research institutions to firms. Furthermore, subdued bank lending, owing partly to low debt recovery in insolvency procedures and widespread informality, prevents productive firms from investing and growing larger.

Figure 2. Decomposition of average annual growth in labour productivity, %



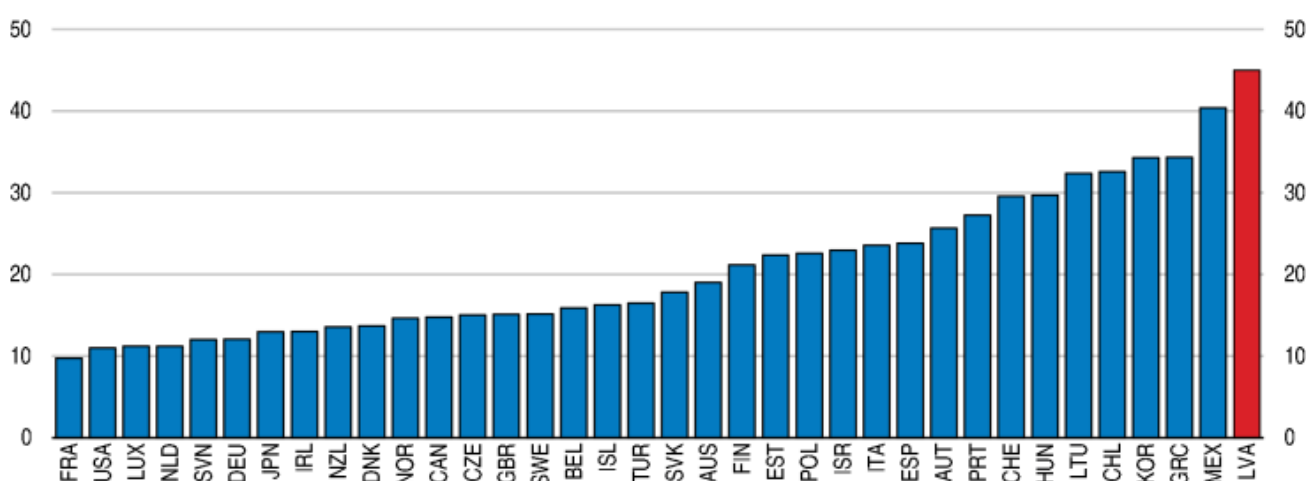
Source: OECD (2019), Economic Policy Reforms 2019: Going for Growth (forthcoming).

The government has implemented reforms to align education and training with labour market needs and promote science-industry linkages with support from EU funds. It is also working hard to strengthen the capacity of the judiciary and law enforcement agencies to fight economic crimes like tax evasion and money laundering. This should help strengthen investor confidence and the ability of firms to better document their income to obtain credit. The 2019 *Economic Survey of Latvia* calls for more investment in skills, innovation and continued efforts to strengthen competition, in particular in sectors with a strong presence of municipal or state-owned enterprises.

More needs to be done to strengthen wellbeing and social inclusion. Building on a recent reform that lowers taxes on

lower-income workers the tax-and-benefit can be used more to reduce high income inequality. Access to healthcare is highly unequal owing partly to exceptionally high out-of-pocket expenditure (Figure 3). The government's efforts to boost healthcare spending need to continue. Its recent decision to suspend a reform that would have threatened universal healthcare is also welcome.

Figure 3. Share of households' out-of-pocket expenditure in health care
 % of total current expenditure on health care, 2017 or latest available year



Source: OECD Health Statistics Database.

The regional gap in public service quality and economic opportunities is also large. The planned territorial reform will be an excellent opportunity to merge municipalities, and improve the efficiency of municipal service provision. A shortage of affordable housing hinders labour mobility and better job matches. More public funding for affordable rental and social housing would help this.

Further reading:

- OECD (2019), OECD Economic Survey: Latvia 2019, OECD Publishing, Paris.