

# MACROECONOMIC AND BUDGETARY REVIEW 2020

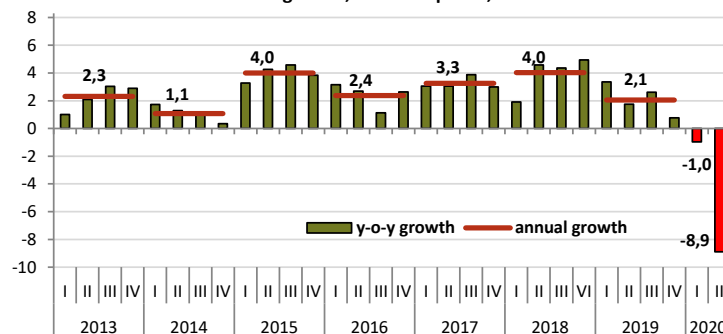
No. 8

| Main macroeconomic indicators  | 2019  | Forecasts** |      |      |      |
|--|-------|-------------|------|------|------|
|  |       | 2020        | 2021 | 2022 | 2023 |
| <b>Gross domestic product (GDP)</b>                                      |       |             |      |      |      |
| current prices (mln euro* and growth, %)                                 | 30463 | -7,4        | 6,5  | 5,3  | 5,2  |
| constant prices (mln euro* and growth, %)                                | 27561 | -7,0        | 5,1  | 3,1  | 3,1  |
| <b>GDP deflator* (y-o-y), %</b>  | 2,4   | -0,5        | 1,3  | 2,0  | 2,0  |
| <b>Consumer price index (y-o-y), %</b>                                   | 2,8   | 0,2         | 1,2  | 2,0  | 2,0  |
| <b>Average monthly gross wage (euro and growth at current prices, %)</b> | 1076  | -1,0        | 3,0  | 5,0  | 5,0  |
| <b>Employment (thsd and growth rate, %)</b>                              | 910   | -4,4        | 0,6  | 1,0  | -0,1 |
| <b>Jobseeker rate (annual average), %</b>                                | 6,3   | 10,5        | 9,8  | 8,1  | 7,3  |
| <b>Exports of goods and services</b>                                     |       |             |      |      |      |
| current prices (mln euro* and growth, %)                                 | 18317 | -14,8       | 7,7  | 4,6  | 5,7  |
| constant prices (mln euro* and growth, %)                                | 17438 | -10,3       | 6,5  | 3,0  | 4,0  |
| <b>Imports of goods and services, mln euro</b>                           |       |             |      |      |      |
| current prices (mln euro* and growth, %)                                 | 18572 | -16,3       | 9,0  | 6,3  | 6,5  |
| constant prices (mln euro* and growth, %)                                | 18763 | -11,5       | 6,8  | 3,2  | 3,4  |

\*According to GDP data revision published on 30/09/2020 by Central Statistical Bureau, not changing projections

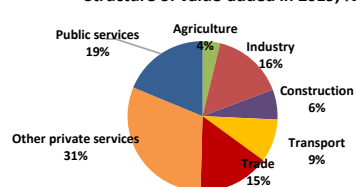
\*\* Projections revised in June 2020 for the preparation of Latvia's medium term budget framework 2021-2023

GDP growth, constant prices, %



GDP

Structure of value-added in 2019, %

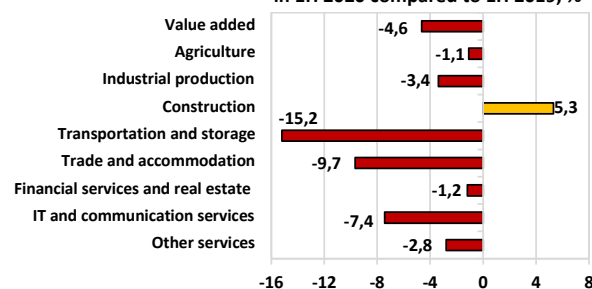


GDP growth of the Baltic states, % y-o-y

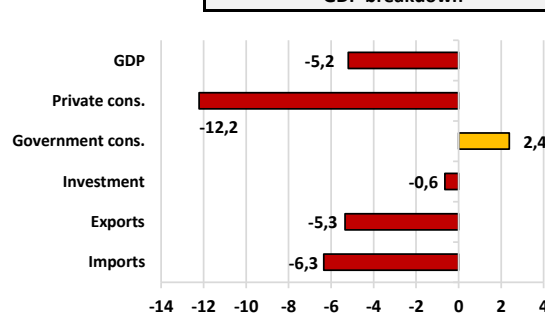
|           | 19'III | IV  | 20'I | II   |
|-----------|--------|-----|------|------|
| Latvia    | 2,6    | 0,8 | -1,0 | -8,9 |
| Lithuania | 3,8    | 3,8 | 2,4  | -4,2 |
| Estonia   | 6,3    | 5,3 | -0,7 | -6,9 |

In the Q1 2020 compared to a corresponding period a year ago, Latvia's GDP declined by 1.0%, while in the second quarter economic contraction became stronger reaching 8.9% as the negative impact stemming from the COVID-19 crisis increased. This was the sharpest GDP fall since 2010, nevertheless economic contraction was not as strong as previously projected because production sectors were more resilient to the crisis and service sectors managed to recover faster than expected. Also, the depth of economic contraction was not as strong as during the previous crisis of 2009-2010 when GDP fall exceeded 10% for five consecutive quarters. Economic downturn in the second quarter was determined by declining private consumption, driven by a sharp decline in accommodation and food service activities, arts, entertainment and recreation, commercial services and transportation sector. The leading indicators suggest that the lowest point of this crisis has been overcome in the second quarter and in the following quarters economic activity is going to resume gradually. Economic sentiment indicator has been improving for the fifth consecutive month in September both in the EU and Latvia, however it has not yet returned to the long-term average level.

GDP growth by sectoral breakdown and from expenditure side in 1H 2020 compared to 1H 2019, %



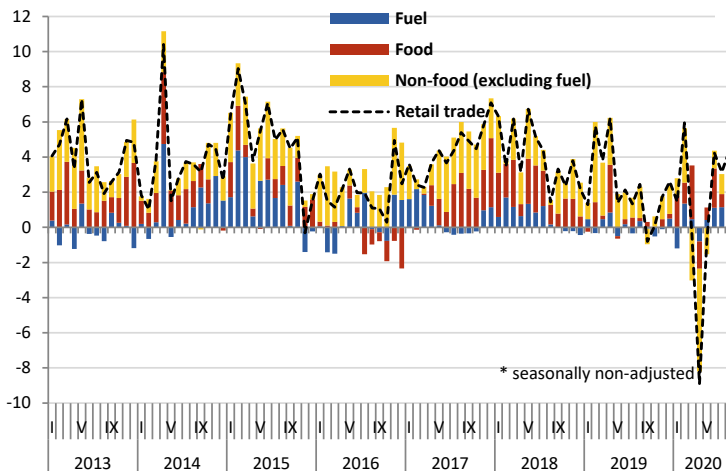
GDP breakdown



Economic contraction in the first half of 2020 was determined by falling private consumption caused by restrictions that have been introduced to limit spread of COVID-19 disease thus significantly reducing consumers activity. At the same time, investments performed rather well, decreasing by only 0.6%, stimulated by a 5.3% increase in the construction sector. Thanks to exports declining slower than imports, net exports provided a positive contribution and the economic downturn was also limited by a 2.4% increase in public consumption expenditures. From the sectoral side, the economic contraction was most significantly affected by a 15.2% decline in the transport sector. Accommodation and food service activities fell by 38.7%, arts, entertainment and recreation - by 27.9% and information and communication services sector - by 7.4% in the first half of 2020. The first half of the year also saw declines in other service sectors, as well as in agriculture and manufacturing. A slight increase in the first half of 2020 was recorded only in the industry, except manufacturing, - by 0.4% and in public administration and defense - by 1.4%, compared to the first half of 2019.

Source: CSP, Eurostat, Ministry of Finance of the Republic of Latvia

### Retail trade growth contributions by product type\*, y-o-y, %



### Retail trade

Structure of retail trade turnover in 2019, %

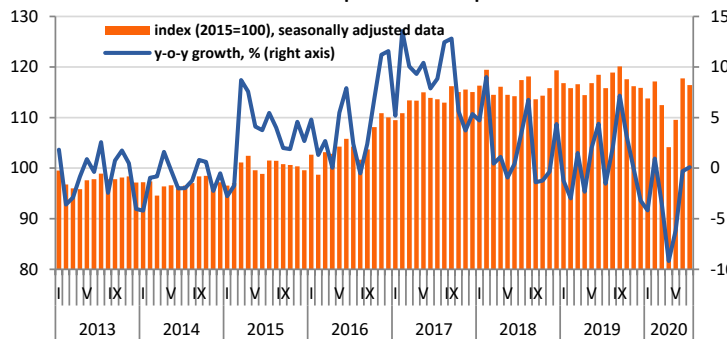
|    |    |    |
|----|----|----|
| 17 | 41 | 42 |
|----|----|----|

Y-o-y growth, c.a., 2020 Jan.-Aug.

|       |       |                       |       |
|-------|-------|-----------------------|-------|
| Total | +1.1% | Non-food (excl. fuel) | -1.2% |
| Food  | +2.9% | Fuel                  | +3.5% |

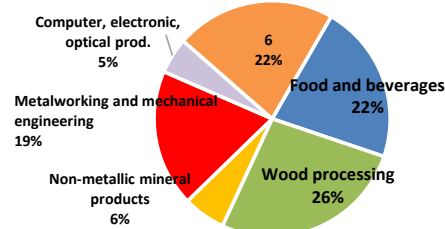
In August, retail trade turnover increased for the third consecutive month and was by 4.4% higher compared to a corresponding month a year ago. Moreover, growth rates registered in the recent months are stronger than last year, however taking into account sharp trade contraction in April sector's growth in the eight months of 2020 is rather weak, constituting 1.1%. In August, retail trade was largely stimulated by rising sales of fuel by 11.3% y-o-y determined by both cheaper fuel and higher mobility by automobiles. Trade volumes of other non-food products increased by 2.0% stimulated by trade growth of electrical household appliances as well as medical and orthopaedic goods. While retail sales in food stores rose by 4.1% y-o-y in August.

### Industrial production output



### Industry

Structure of manufacturing output in 2019, %

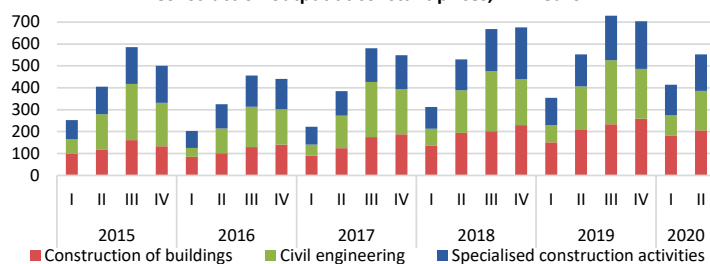


Industry, y-o-y growth, 2020 Jan.-July, c.a.

|                |       |                   |       |
|----------------|-------|-------------------|-------|
| Industry total | -3.2% | Mining, quarrying | +4.9% |
| Manufacturing  | -3.5% | Energy            | -3.5% |

Following the output contraction observed in the last months, in July growth resumed in industrial production sector. Compared to a corresponding month of 2019, total industrial production output in July increased by 0.1%, while manufacturing demonstrated output growth by 1.8%. In July, resumption of growth in manufacturing was determined by strong output increase in the largest manufacturing sub-sector, wood-processing, - by 12.5% y-o-y. Significant growth rates were also demonstrated by manufacture of chemical products - by 13.7% y-o-y, and manufacture of electrical equipment - by 6.6%. While in the second largest sub-sector, manufacture of food products, output volumes have been stable for several months, in July decreasing by 0.2% y-o-y. At the same time, output continued to decline in manufacture of fabricated metal products (-15.5% y-o-y), manufacture of motor vehicles and trailers (-16.8% y-o-y) and manufacture of textiles (-10.8% y-o-y). Contrary to rising manufacturing output, in July total industrial production growth was hampered by contraction of electricity and gas supply by 14.1% due to falling production volumes of electricity that was by 27% lower than a year ago. However, mining and quarrying sector demonstrated output expansion by 11.5% y-o-y in July. Thus, thanks to improvements observed in the last months, in the seven months of 2020 total industrial production contraction was moderate, constituting 3.2%, while manufacturing output declined by 3.5% y-o-y.

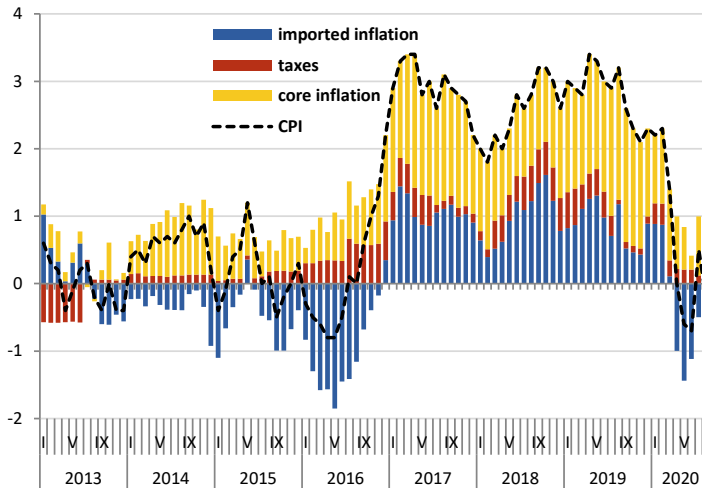
### Construction output at constant prices, mln. euro



### Construction

Following the strong expansion of construction output in the Q1 2020 (+16.9% current prices), sector's growth slowed down in the Q2 2020 when construction output was at the same level as a year ago. In the second quarter, fall was registered in construction of buildings - by 2.5% y-o-y, driven by lower construction volumes of residential buildings, hotels, industrial buildings and warehouses, as well as in construction of civil engineering that contracted by 7.9% y-o-y. While specialised construction activities continued to increase in the second quarter - by 13.9% y-o-y. In the Q2 2020, the expected construction space as indicated in the granted building permits fell by 20.9% y-o-y which was considerably stronger decline than that of the first quarter (-5.7%). This data suggest that construction of buildings could contract in the following quarters while sector's development will be stimulated by implementation of infrastructure projects.

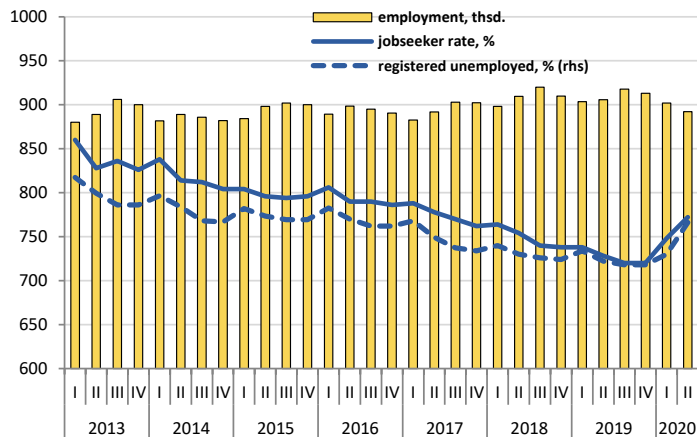
**Inflation breakdown by origin, y-o-y, %**



**Inflation**

Consequences of COVID-19 pandemic continue to determine consumer price dynamics in Latvia. In August 2020, compared to corresponding month a year ago, consumer prices declined by 0.2% due to falling prices of fuel, accommodation and air transport services, goods and services associated with housing as well as rentals of housing. Thus, prices for goods overall were by 1.0% lower than in August 2019, meanwhile prices for services continued to increase and were by 1.6% higher than a year ago. However, growth rate for service prices has halved since the beginning of the year. In the eight months of 2020 inflation in Latvia constituted 0.6%. It is expected that deflation will remain until around October-November. However, taking into account price growth that was registered in the first quarter of the year, in 2020 overall annual average inflation will be positive though significantly weaker than in the previous years.

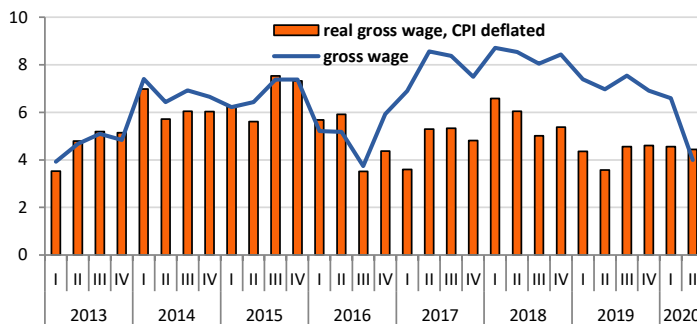
**Unemployment rate, % of economically active population (15-74)**



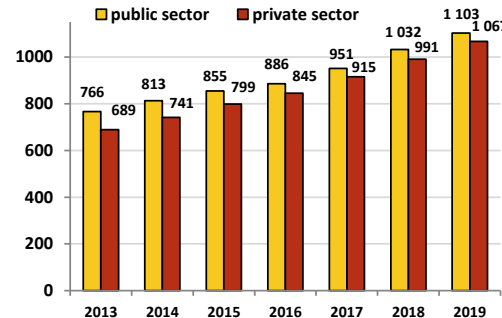
**Employment**

The impact of COVID-19 crisis in the labour market was felt already in the first quarter of 2020, when the number of employed persons decreased by 0.2%, compared to the corresponding quarter of 2019. In the second quarter the number of employed persons decreased by 1.5% y-o-y and unemployment rate grew by 2.2 percentage points to 8.6% of economically active population, labour force survey data showed. However, such an increase in unemployment can be assessed as quite moderate, with the unemployment rate returning only to the level of 2017 and lagging behind the heights reached during the 2009-2010 crisis. According to the State Employment Agency data, between the end of February and the end of June, the number of registered unemployed increased by 20 thousand or 34.4% and registered unemployment rate grew from 6.3% to 8.6%. Since July, the unemployment rate has been declining and the number of registered unemployed decreased by 6.6 thousand or 8.4%. On September 21, the total number of registered unemployed was 71.7 thousand and the unemployment rate - 7.9% of the economically active population.

**Wage dynamics, changes year over year, %**

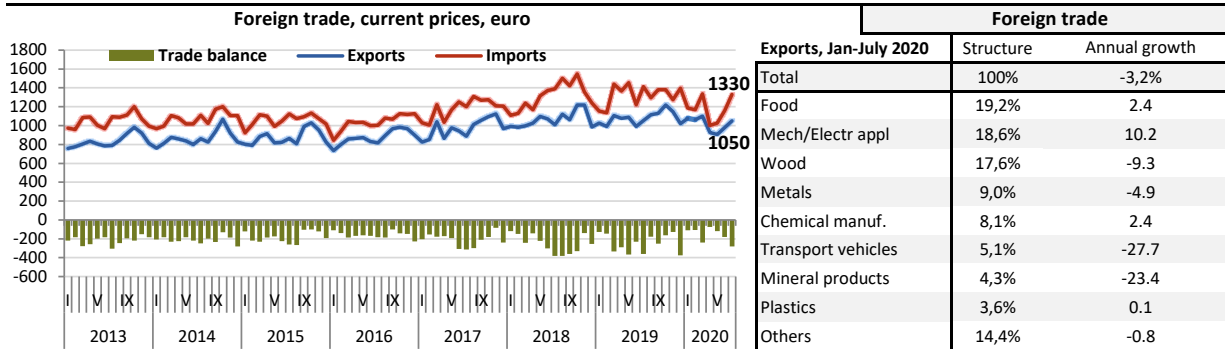


**Wages, euro**

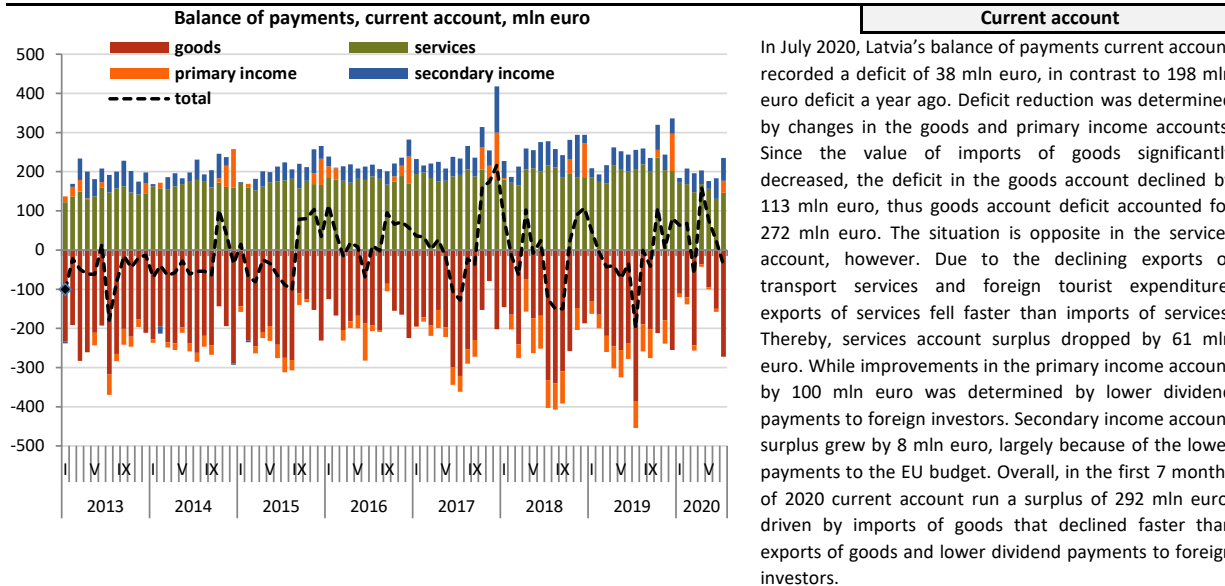


In the first quarter of 2020, average gross wage, compared to the corresponding quarter of 2019, had increased by 6.6%, but in the second quarter wage growth slowed down to 3.9% due to the COVID-19 crisis. In April 2020, compared to April 2019, average gross monthly wage increased by 3.6%, in May the annual growth rate was the lowest - 2.5%, but in June it increased again to 5.6%. In the second quarter of 2020, wage growth rates were the same in the private and in the public sector - 3.8%, compared to the corresponding quarter of 2019. Higher salary remained in the public sector, where the average wage was 1138 euro, while in the private sector it constituted 1108 euro. Average gross wage in the total economy constituted 1118 euro. Compared to the second quarter of 2019, wages increased the most in other service activities (activities of membership organisations, repair of computers, personal goods) - by 14.3% and in professional service activities - by 8.0%, while in accommodation and food service activities average wage declined by 16.5% and in transportation sector - by 5.1% y-o-y.

Source: CSP, Eurostat, Ministry of Finance of the Republic of Latvia



The value of exported goods in current prices in July dropped by 0.3% y-o-y. In the current situation dominated by COVID-19 pandemic when external trade around the world has decreased significantly such export performance is satisfactory. In addition, on monthly basis, exports of goods for the second consecutive month show a significant increase - in June, compared to the previous month, exports increased by 8.0%, and in July - by 7.3%. Data suggest that the deepest point of the COVID-19 crisis is behind and significant reduction of goods exports in the coming months is not expected. Exports of goods in July were negatively affected by three commodity groups, namely, the decline in exports of mineral products, metals and transport equipment. While in the 7 months of 2020 compared to the same period a year ago, exports of goods declined by 3.2%. The largest contribution to export contraction was provided by export fall of transport equipment by 27.7%, largely due to declining exports of cars and car parts. Exports of mineral products also decreased significantly - by 23.4%, that was determined by export fall of refined products due to declining oil prices as well as export decrease of energy due to weaker consumption of electricity. In July, imports of goods declined faster than exports, by 5.9% y-o-y. However, such import decrease was significantly lower than in April and May. Overall, in the first 7 months of 2020, the value of imported goods decreased by 10.7%.

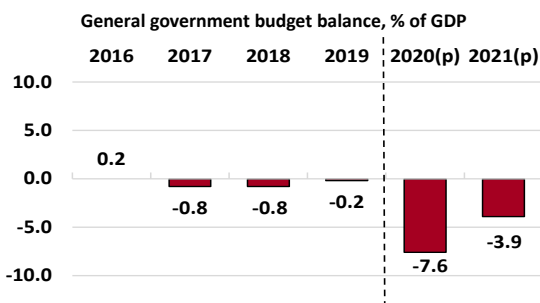


|                              | Main macroeconomic indicators, annual growth rates (unless stated otherwise) |        |         |        |        |        |        |        |        |        |
|------------------------------|--|--------|---------|--------|--------|--------|--------|--------|--------|--------|
|                              | 18'I   | II     | III     | IV     | 19'I   | II     | III    | IV     | 20'I   | II     |
| GDP, constant prices, %      | 1,9  | 4,6    | 4,4     | 4,9    | 3,4    | 1,7    | 2,6    | 0,8    | -1,0   | -8,9   |
| GDP, current prices, %       | 5,7  | 8,5    | 8,6     | 9,2    | 7,0    | 4,6    | 4,8    | 2,2    | 0,0    | -9,9   |
| Inflation, %                 | 2,0  | 2,4    | 2,9     | 2,9    | 2,9    | 3,3    | 2,9    | 2,2    | 1,9    | -0,4   |
| Nominal wages, %             | 8,7  | 8,5    | 8,0     | 8,4    | 7,4    | 7,0    | 7,5    | 6,9    | 6,6    | 4,0    |
| Real wages, CPI deflated, %  | 6,7  | 6,1    | 5,1     | 5,5    | 4,5    | 3,7    | 4,6    | 4,7    | 4,7    | 4,4    |
| Employed persons, %          | 1,8  | 2,0    | 1,9     | 0,8    | 0,6    | -0,4   | -0,2   | 0,4    | -0,2   | -1,5   |
| Unemployed, % of active pop. | 8,2  | 7,7    | 7,0     | 6,9    | 6,9    | 6,4    | 6,0    | 6,0    | 7,4    | 8,6    |
| Productivity, %              | 0,2  | 2,5    | 2,4     | 4,1    | 2,7    | 2,2    | 2,9    | 0,4    | -0,8   | -7,5   |
| Retail trade, %              | 5,4  | 5,0    | 3,0     | 2,7    | 3,5    | 3,2    | 1,0    | 1,5    | 2,2    | -1,7   |
| Industrial production, %     | 4,5  | 0,2    | 2,9     | 0,9    | -0,8   | 1,4    | 2,5    | 0,0    | -2,3   | -5,1   |
| Goods exports, %             | 9,2  | 14,7   | 7,9     | 7,3    | 5,2    | -1,1   | 3,4    | -1,0   | 3,7    | -10,9  |
| Goods imports, %             | 6,8  | 11,7   | 14,2    | 12,3   | 7,3    | 4,9    | -5,2   | -2,2   | -1,0   | -21,5  |
| Trade balance, mln euro      | -507,5   | -664,1 | -1124,2 | -723,7 | -606,6 | -886,6 | -789,0 | -665,8 | -435,7 | -373,4 |
| Current account, % of GDP    | 0,0  | 1,6    | -5,6    | 2,8    | 0,0    | -1,9   | -3,0   | 2,4    | 1,0    | 3,8    |

Source: CSP, Eurostat, Ministry of Finance of the Republic of Latvia, Bank of Latvia

According to the Eurostat, in 2019 general government budget deficit was 0.2% of GDP, which is lower than 0.6 percentage points compared to 2018, with a significant improvement in the local government budget balance. Last year, there was a surplus in local government, with faster growth in personal income tax revenues and slower growth in expenditures. It should be noted that the amount of the 2019 deficit can be revised by submitting a notification to Eurostat by the Central Statistical Bureau (CSB) in October this year. In August Ministry of Finance has updated the general government budget balance forecast for the medium term, taking into account the Treasury data on the execution of the consolidated general budget in the first half of this year, updated tax and non-tax revenue forecasts, mediumterm basic expenditure of the central government basic budget according to the data as of 31 July 2020, additional budget expenditure, having regard to the fiscal impact of the support measures for mitigating the effects of Covid-19 approved by the Cabinet of Ministers and the Saeima by 26 July this year, as well as the most current state special budget expenditure forecasts. The general government budget deficit for 2020 is projected at 7.6% of GDP, which is significantly higher than planned in the Law "On the Medium-Term Budget Framework for 2020, 2021 and 2022" (deficit 0.3% of GDP), but lower than in the spring (deficit 9.4% of GDP), when the Stability Program 2020-2023. year, the decline in GDP under the influence of Covid-19 has already been taken into account. Until 20 September of this year expenditure on support measures has been 0.7 billion euro. The government has approved the planned amount of support measures in the amount of 3.2 billion euro or 11.2% of GDP, of which a direct negative impact on the general government budget balance is 1.3 billion euro or 4.4% of GDP.

#### General government budget balance



According to the ESA 2010

Informative Report "On the forecasts of macroeconomic indicators, revenues and general government budget balances in 2021-2023", approved by the Cabinet of Ministers on 18.08.2020

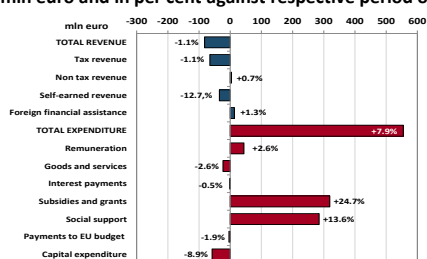
| Budget Revenue and Expenditure                |                                   |                                      | Consolidated General Budget                 |                                   |
|---|-----------------------------------|--------------------------------------|---|-----------------------------------|
|   | 2019 I-VIII<br>execution mln euro | 2020 I-VIII<br>execution<br>mln euro | Execution changes<br>2020/2019,<br>mln euro | Execution changes<br>2020/2019, % |
| <b>CONSOLIDATED GENERAL BUDGET**</b>          |                                   |                                      |   |                                   |
| Revenue                                       | 7651,9                            | 7569,6                               | -82,2                                       | -1,1%                             |
| Expenditure                                   | 7055,0                            | 7609,8                               | 554,8                                       | 7,9%                              |
| <b>Financial Balance</b>                      | <b>596,8</b>                      | <b>-40,2</b>                         | <b>-637,0</b>                               |                                   |
| <b>CONSOLIDATED STATE BUDGET*</b>             |                                   |                                      |   |                                   |
| Revenue                                       | 6382,0                            | 6364,0                               | -18,0                                       | -0,3%                             |
| Expenditure                                   | 5884,2                            | 6513,8                               | 629,6                                       | 10,7%                             |
| <b>Financial Balance</b>                      | <b>497,8</b>                      | <b>-149,8</b>                        | <b>-647,6</b>                               |                                   |
| <b>State basic budget</b>                     |                                   |                                      |   |                                   |
| Revenue                                       | 4418,9                            | 4418,0                               | -0,9  | 0,0%                              |
| Expenditure                                   | 4191,0                            | 4634,3                               | 443,3                                       | 10,6%                             |
| <b>Financial Balance</b>                      | <b>227,9</b>                      | <b>-216,3</b>                        | <b>-444,2</b>                               |                                   |
| <b>State special budget</b>                   |                                   |                                      |   |                                   |
| Revenue                                       | 1997,5                            | 1979,0                               | -18,5                                       | -0,9%                             |
| Expenditure                                   | 1763,0                            | 1951,1                               | 188,1                                       | 10,7%                             |
| <b>Financial Balance</b>                      | <b>234,5</b>                      | <b>27,9</b>                          | <b>-206,5</b>                               |                                   |
| <b>CONSOLIDATED LOCAL GOVERNMENT BUDGET**</b> |                                   |                                      |   |                                   |
| Revenue                                       | 1897,6                            | 1856,1                               | -41,5                                       | -2,2%                             |
| Expenditure                                   | 1798,5                            | 1746,4                               | -52,1                                       | -2,9%                             |
| <b>Financial Balance</b>                      | <b>99,1</b>                       | <b>109,7</b>                         | <b>10,6</b>                                 |                                   |

According to cash flow methodology

\*Including grants, donations and derived public persons

\*\*Including grants and donations

#### Revenue and Expenditure in I-VIII 2020 (cash based changes in mln euro and in per cent against respective period of 2019)



According to the State Treasury published information, the revenue of the consolidated general budget in the eight months of 2020 was 7569.6 mln euro, but expenses were made in the amount of 7609.8 mln euro, thus in the consolidated general budget formed 40.2 mln. euro deficit. The Covid-19 pandemic affected lower-than-expected tax revenues during the reporting period, while, the support measures approved by the government to mitigate the effects of Covid-19 and the increase in social benefits expenditure contributed to a faster increase in consolidated general budget expenditures, as a result, the balance in the consolidated general budget deteriorated by 637 mln. compared to eight months last year.

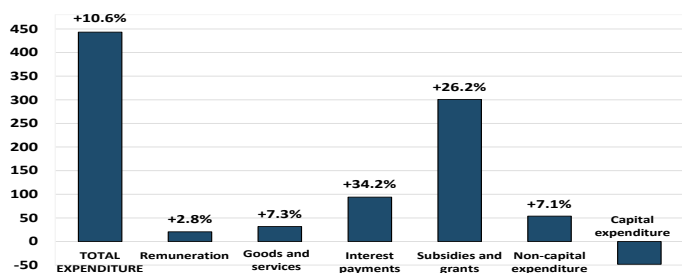
Revenues of the consolidated general budget in the eight months of this year were received by 82.2 mln euro or 1.1% less than in the corresponding period last year, which was mainly

Source: The State Treasury, Ministry of Finance of the Republic of Latvia, Eurostat

affected by a decrease in tax revenue (5771.8 mln euro) by 65.3 mln euro or 1.1%. The decline in which were affected by the decline in economic activity and employment this year. Revenues from foreign financial assistance and non-tax revenues in the consolidated general budget were close to the level of the previous eight months, increasing by 1.3% and 0.7%, forming 1044.8 mln euro and 512.3 mln euro. The non-tax revenue plan in the state basic budget in the reporting period was exceeded by 23.6 mln. euro or 5.7%, because higher revenues were received from dividends of state capital companies, as well as unplanned revenues from confiscation of criminally obtained funds.

Expenditures of the consolidated general budget in the reporting period were made by 554.8 mln euro or 7.9% more than last year. The increase in expenditure was influenced by 319.1 mln euro or 24.7% higher expenses for subsidies and grants (1610.5 mln euro), as well as social support (2381.1 mln euro) increasing by 285.1 mln euro or 13.6%. Higher subsidies and grants amounted to 100 mln allocation of euro to the financial institution ALTUM, to provide loans and provide financing with guarantees to economic operators affected by the Covid-19 crisis. The amount of subsidies and grants for medical institutions has increased, including the restriction of Covid-19. The temperate increase, that was also planned, in the consolidated general budget observed for remuneration expenses, which was by 43.7 mln euro or 2.6% higher than in January-August last year, forming 1719.5 mln euro.

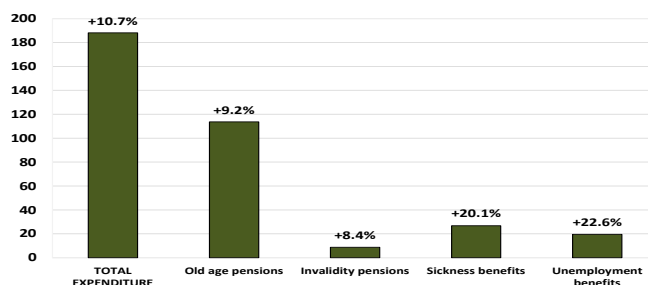
At the same time, in the consolidated general budget in January-August, compared to the corresponding period last year, there is a decrease in expenditures for certain items. Expenditure on goods and services decreased by 23.2 mln euro or 2.6%, but capital expenditures decreased by 58 mln euro or 8.9%. The decrease in these expenditures is mainly observed in the local government budget.

**State Basic Budget Expenditure in I-VIII 2020**  
(cash based changes in mln euro and in per cent against


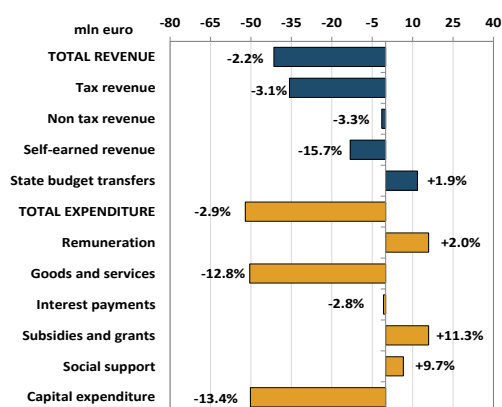
According to the State Treasury published information, the state basic budget in the eight months of this year had a 216.3 mln euro deficit, while in the corresponding period of the last year there was a surplus of 227.9 mln euro.

The state basic budget revenue in the eight months of this year reached 4418.0 mln. euro and compared to January-August 2019, revenues decreased by 0.9 mln. euro. Meanwhile, in the eight months of this year, a significant increase is observed in state basic budget expenditures, increasing by 443.6 mln euro or 10.6%. The increase in the state basic budget expenditure was determined by the funding directed to mitigate the effects of Covid-19, as well as higher spending on the health sector. The increase in social support expenditure can be explained by the 17 mln euro paid in July for unemployment benefits from the state basic budget, although, as a general rule, these expenditures are always made from the state special budget, therefore, the impact will be felt by the end of the year. The largest increases in expenditure were observed for subsidies and grants, which in comparison with the corresponding period of the previous year increased by 300.7 mln euro or 26.2%, forming 1448.4 mln euro, associated with higher subsidies and grants to healthcare institutions, allocation of financing to the financial institution ALTUM (100 million euros), to issue loans and provide financing with guarantees to economic operators affected by the Covid-19 crisis.

Other groups of basic budget expenditure show a much more moderate increase or decrease in expenditure, compared to the corresponding period in 2019. It should be noted an increase in expenses by 31.8 mln euro or 7.3% for goods and services, mainly due to rising defense spending. Meanwhile, lower than last year in the eight months in the state basic budget by 48.0 mln. euro or 11.0% were capital expenditures.

**State Special Budget Expenditure in I-VIII 2020**  
(cash based changes in mln euro and in per cent against


According to the State Treasury published information, the state special budget in the eight months of this year had a 27.9 mln euro surplus, which was by 206.5 mln euro less than in the corresponding period of 2019. The state special budget revenue in the eight months of this year was received by 18.5 mln euro or 0.9% lower than in the corresponding period last year. While, the state special budget shows a significant increase in expenditures. Expenditure increased by 188.1 mln euros or 10.7%. It should be noted that pension expenditure in the eight months of this year, taking into account the indexation made last October, increased by 123.5 mln euro or 9% and is broadly in line with the planned level. In turn, expenditure on other social support increased by 63.2 mln. euro or 16.8%, forming 438.8 mln euro. Significantly has increased Expenditure on unemployment and sickness benefits. Expenditures on unemployment benefits have been made this year by 19.6 mln euro or 22.6% more than in January-August last year, which is mainly due to the rapid increase in the number of registered unemployed. Considering, that in July 17 mln euro for unemployment benefits were paid from the state basic budget, not from a state special budget, the increase in expenditure on unemployment benefits is even higher. According to the data of the State Employment Agency (SEA) the registered unemployment rate in Latvia at the end of August was 8.2%, but last year in the corresponding period 5.9%. Unemployment has risen in the sectors with the greatest impact of Covid-19- transport and storage, accommodation and food services, wholesale and retail. Data from the State Social Insurance Agency (SSIA) in January-August show an increase of 32% in the number of recipients of unemployment benefits. The state special budget expenditure increase also determined by 26.8 mln euro or 20.1% higher expenditure on sickness benefits. According to SSIA data, the average insurance contribution salary for benefit recipients this year was on average more than 10% higher than last year, as well as the average number of days increased significantly in June-August, for which payment is made, thereby also affecting the total number of days paid. According to SSIA information the largest proportion of beneficiaries are for the simple professions, which could also indicate lower access to healthcare for the destitute.

**Revenue and Expenditure in I-VIII 2020 (changes in mln euro and in per cent against respective period of 2019)**


According to the data of the Treasury in the eight months of 2020, the consolidated local government budget had a surplus of 109.7 mln euro, which is by 10.6 mln euro more than in the corresponding period a year earlier. It should be noted, that the improvement in the balance of local government budgets was facilitated by the reduction of goods and services, capital expenditure, as well as the implementation of the good personal income tax (PIT) plan at the beginning of the year.

**Consolidated Local Government Budget**

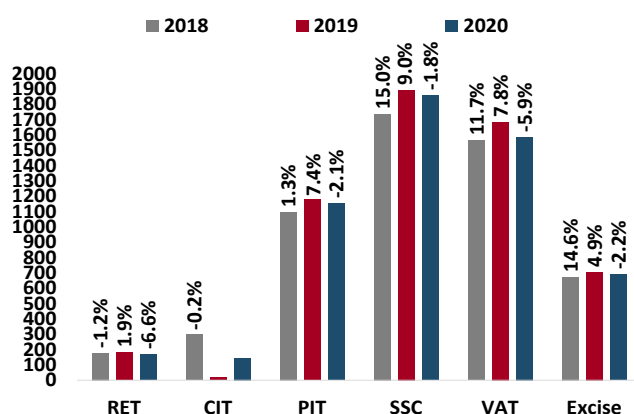
Local government consolidated budget revenue in the eight months of this year amounted to 1856.1 mln euro, which is by 41.5 mln euro or 2.2% less than in the corresponding period of the previous year. Tax revenues in the municipal budget, although received by 35.7 mln euro or 3.1% lower than in January-August 2019, broadly in line with expectations. PIT revenue by 40 mln euro or 3.6% exceeded the planned amount, due to the high overcrowding of the plan in January-February, consisting of rising labor income levels in early 2020, when the Covid-19 situation had not yet developed, as well as settlements at the beginning of the year for dividend payments made in December 2019.

The local government budget expenditures level in the eight months of this year has decreased by 52.1 mln euro or 2.9% compared to the corresponding period last year, amounting to 1746.4 mln euro. The decrease can be explained by a decrease in expenditure on goods and services by 50.4 mln euro or 12.8%. The decrease in expenditures on goods and services in the municipal budget can be explained by the fact that expenditures of public utilities and heating decreased by municipal institutions performing telework in the conditions of a pandemic. Meanwhile, capital expenditures in the local government budget have decreased by 50.2 mln euro or 13.4% compared to the corresponding period last year, forming 323 mln euro. Capital expenditures in the local government budget have decreased directly for the performance of basic functions, this is largely due to borrowing constraints, because funds can be borrowed from the State Treasury only for the implementation of EU funds projects and the infrastructure of pre-school educational institutions. Whereas, expenses for compensation have increased by 15.9 mln. euro or 2%. Subsidies and grants also increased by 15.9 mln euros or 11.3%. The increase was provided by subsidies and grants to businesses for the provision of public transport services. In the local government budget by 6.6 mln or 9.7% increased social benefits. Of these, the largest increases are in expenditure on voluntary initiatives, as well as payment for services provided by social care and rehabilitation institutions.



|   | Consolidated General budget Tax Revenue |                                    |  | Tax Revenue                       |  |
|---|---|------------------------------------|--|-----------------------------------|--|
|   | 2019 I-VIII<br>execution, mln euro      | 2020 I-VIII<br>execution, mln euro | Execution changes<br>2020/2019, mln euro | Execution changes<br>2020/2019, % | January execution of<br>the same period plan |
| <b>Consolidated general budget tax revenue</b>                          | <b>5837,1</b>                           | <b>5771,8</b>                      | <b>-65,3</b>                             | <b>-1,1%</b>                      | <b>91,5%</b>                                 |
| Social security contributions   | 1892,4                                  | 1858,8                             | -33,5                                    | -1,8%                             | 93,2%  |
| <i>in State special budget</i>  | 1826,3                                  | 1796,2                             | -30,1                                    | -1,6%                             | 93,2%  |
| <i>1% for the health financing</i>                                      | 65,5                                    | 62,7                               | -2,8                                     | -4,3%                             | 94,5%  |
| Value added tax   | 1684,7                                  | 1586,0                             | -98,7                                    | -5,9%                             | 86,1%  |
| Personal income tax   | 1178,8                                  | 1154,0                             | -24,8                                    | -2,1%                             | 103,6%                                       |
| <i>in State budget</i>  | 236,9                                   | 228,0                              | -8,9                                     | -3,8%                             | 102,3%                                       |
| <i>in Local government budget</i>                                       | 941,9                                   | 926,1                              | -15,8                                    | -1,7%                             | 103,9%                                       |
| Excise tax  | 705,9                                   | 690,2                              | -15,6                                    | -2,2%                             | 87,3%  |
| Corporate income tax  | 18,1                                    | 145,7                              | -  | -                                 | 76,3%  |
| Real estate tax   | 180,5                                   | 168,5                              | -12,0                                    | 1,5%                              | 89,9%  |
| <b>Informative:</b>   |   |                                    |  |                                   |  |
| <i>Social security contributions to the state funded pension scheme</i> | 339,0                                   | 339,1                              | -5,6                                     | -1,4%                             | -  |

**Total Tax Revenue I-VIII 2020 (mln euro and % change in comparison with the previous year)**



Consolidated general budget tax revenue in the eight months of this year received 5771.8 mln euro, which is by 65.3 mln euro or 1.1% less than in the corresponding period of 2019. The decline in tax revenues was not only due to a contraction in economic activity, but also tax extensions, approved by the government as one of the support measures. Mainly, tax revenues have fallen this year in the sectors hardest hit by the crisis- accommodation and food services, transport and storage, arts, entertainment and recreation.

In the reporting period, virtually all major tax revenues decreased. Value-added tax (VAT) revenue in the eight months of this year was by 98.7 mln euro or 5.9% lower compared to the corresponding period last year. Significant reduction in tax revenue, compared to 2019, observed in the construction industry. The decrease in the total tax revenue of the construction sector related to the abolition of the reverse charge procedure for construction materials as of 1 January 2020, which affected the increase in VAT refunds.

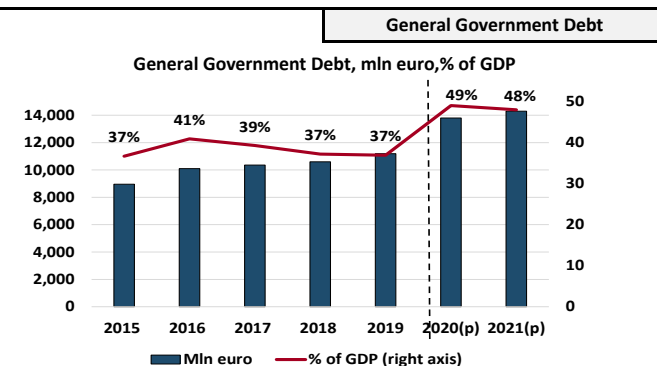
In the eight months of this year, the mandatory social security insurance contributions are 1858.8 mln euro, which is by 33.5 mln. euros or 1.8% less than in the corresponding period of 2019. In the eight months of 2020, personal income tax (PIT) revenues decreased by 24.8 mln euro or 2.1%, than in January-August 2019, amounting to 1154.0 mln euro. It was affected by a decrease in the number of employees, replacement of employees' remuneration with downtime benefits, as well as raising the PIT differentiated non-taxable minimum and relief for dependents.

Excise tax revenue in the eight months of this year is 690.2 mln euro, which is by 15.6 mln euro or 2.2% less, due to declining consumption of alcoholic beverages, tobacco products and petroleum products. The largest reduction, compared to the eight months of 2019 are revenues from excise tax on alcoholic beverages.

Whereas, corporate income tax (CIT) increased by 127.6 mln euros, reaching 145.7 mln euro, taking into account that the level of CIT revenue last year, after the implementation of the reform, was very low (18.1 mln euros in January-August 2019). If the fluctuations in CIT revenue because of the reform not taken into account, revenues from all other taxes in the eight months of this year actually amounted to 192.9 mln euro or 3.3% lower than in the corresponding period of 2019.

In August of this year State Treasury has prepared a general government debt forecast, taking into account the updated forecasts of the state budget financial balance at the same government policy, as well as the updated GDP forecasts at current prices. Given the significant increase in borrowing to finance Covid-19 mitigation measures and economic support in the general government baseline scenario, the debt forecast for 2020 year is 49% of GDP and for 2021 year 48% of GDP.

On August 2020, the credit rating agency S&P Global Ratings affirmed Latvia's rating at the high "A+" level with the stable outlook. The Agency remarks the effective policy response by the Latvian authorities' to limit the spread of Covid-19 in Latvia and implementation of significant measures to support the economy. Thanks to the strong track of the fiscal discipline prior to the COVID-19 outbreak and the level of public debt, which is one of the lowest in the euro area, the government has a sufficient fiscal flexibility to manage country's economy in the current situation.



According to the ESA 2010

Source: The State Treasury, Ministry of Finance of the Republic of Latvia, Eurostat