



MACROECONOMIC AND BUDGETARY REVIEW

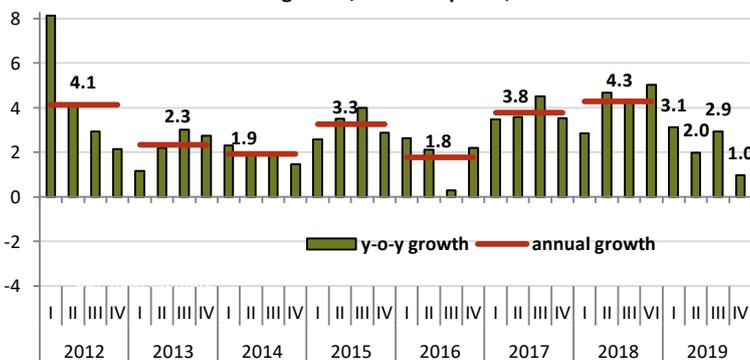
January 2020

Main macroeconomic indicators	2019*	Forecasts**			
		2020	2021	2022	2023
Gross domestic product (GDP)					
current prices (mln euro and growth, %)	30476	5.0	5.3	5.1	4.6
constant prices (mln euro and growth, %)	27497	2.2	2.8	2.8	2.4
GDP deflator (y-o-y), %	2.6	2.7	2.4	2.3	2.2
Consumer price index (y-o-y), %	2.8	2.3	2.1	2.0	2.0
Average monthly gross wage (euro and growth at current prices, %)	1076	6.0	5.5	5.0	5.0
Employment (thsd and growth rate, %)	910	-0.1	-0.1	-0.1	-0.1
Jobseeker rate (annual average), %	6.3	6.4	6.2	5.8	5.7
Exports of goods and services					
current prices (mln euro and growth, %)	18257	3.5	4.8	4.7	3.9
constant prices (mln euro and growth, %)	17387	2.5	3.5	3.4	2.6
Imports of goods and services, mln euro					
current prices (mln euro and growth, %)	18232	3.5	5.3	4.7	3.9
constant prices (mln euro and growth, %)	18426	3.0	4.4	3.7	3.0

* GDP for 2019 according to CSB data published on 28/02/2020

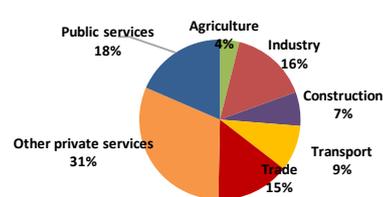
** Projections developed in February 2020 for the preparation of Latvia's Stability Programme 2020-2023

GDP growth, constant prices, %



GDP

Structure of value-added in 2018, %

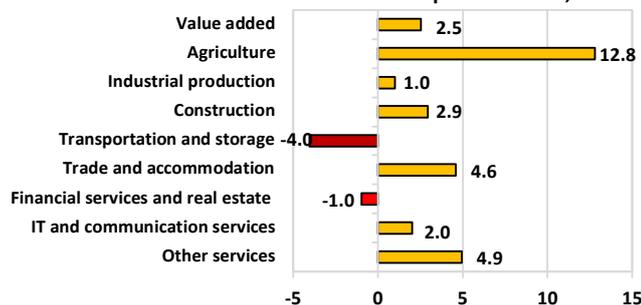


GDP growth of the Baltic states, % y-o-y

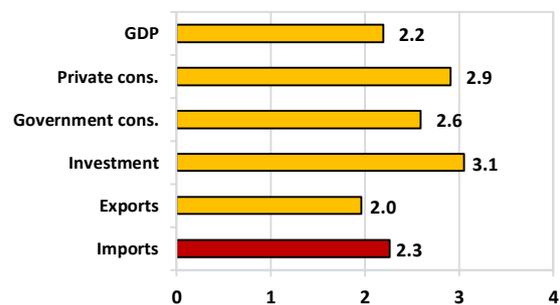
	19'I	II	III	VI
Latvia	3.1	2.0	2.9	1.0
Lithuania	4.2	3.8	3.8	3.8
Estonia	4.8	3.9	4.8	3.9

In the fourth quarter of 2019, Latvia's economic growth slowed down to 1% which was the lowest quarterly economic growth rate during the last year and the weakest growth since Q3 2016. Thus, in 2019 overall Latvia's gross domestic product increased by 2.2%. Growth weakening at the end of 2019 was determined by negative developments in several sectors, including, transport, financial services and manufacturing. Last year, weak external environment and global economic slowdown determined worsening of foreign demand which affected Latvia's economic performance. Moreover, higher economic growth was hampered by several domestic factors, for example, unfavourable weather conditions for electricity production at the beginning of the year and decline of non-resident serving bank business.

GDP growth by sectoral breakdown and from expenditure side in 2019 compared to 2018, %



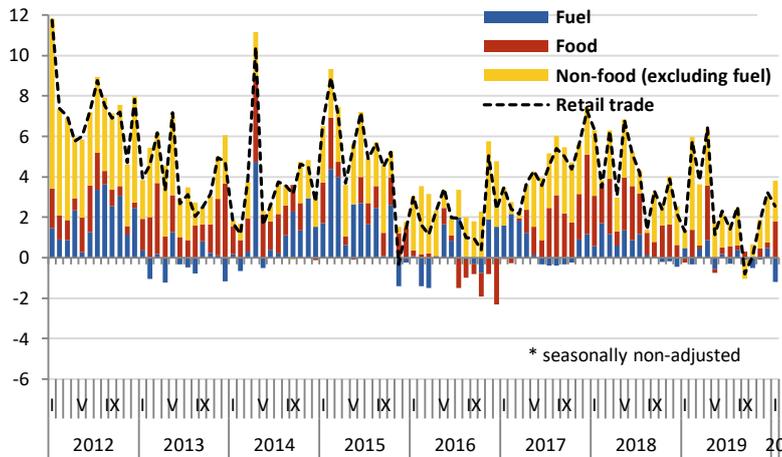
GDP breakdown



In 2019, the fastest growing sectors in the economy of Latvia were agriculture as well as several service sectors. Value added of trade increased by 4.1% determined by rising income and falling unemployment. Thus, private consumption expanded by 2.9% indicating that in 2019 Latvia's economic growth was stimulated by domestic demand. At the same time exports of goods and services increased slower - by 2.0%, determined by global growth slowdown and weakening of external demand. Thus, growth rates of export-oriented sectors last year were lower - manufacturing growth constituted 2.1%, while contraction of transport sector was determined by significantly lower freight volumes in Latvia's ports. Transit flows were negatively affected by Russia's policy to re-direct freight flows to its Baltic Sea ports and falling global demand for coal from Russia. In 2019, shrinking of non-resident serving bank business and financial services exports determined fall of financial and insurance services' value added (-8.8%). In 2019, imports of goods and services increased stronger than exports - by 2.3%.

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

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



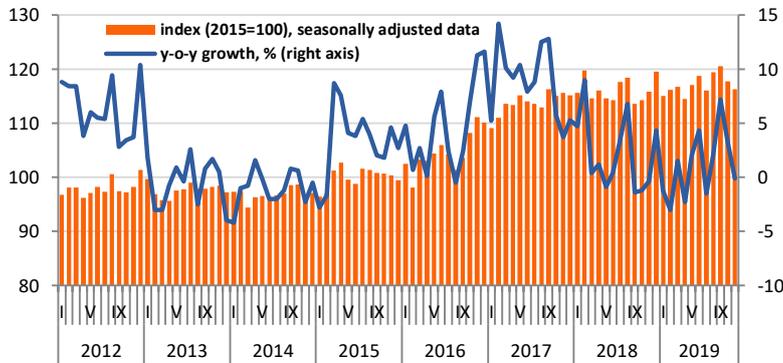
Retail trade

Structure of retail trade turnover in 2019, %		
Fuel	17	41
Food	41	42
Non-food (excl. fuel)	42	

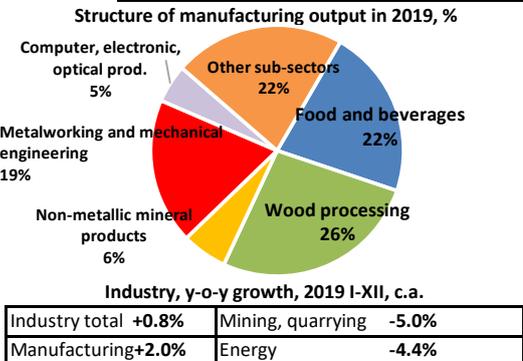
Y-o-y growth, c.a., 2020 Jan.		
Total	+2.6%	Non-food (excl. fuel) +4.7%
Food	+4.4%	Fuel -7.2%

In January 2020 compared to a corresponding month in 2019, retail trade turnover in Latvia increased moderately - by 2.6%. Significantly stronger growth was registered for trade of food which sales volumes expanded by 4.4% y-o-y, and trade of non-food products, excluding fuel, increased by 4.7% y-o-y. However, trade volumes of fuel decreased by 7.2% y-o-y that was affected by excise tax hike as of January 2020 and global oil price growth. In the forthcoming months, retail trade growth in Latvia will be stimulated by rising income and weaker inflation level. Moreover, in February improvements in consumer confidence were observed.

Industrial production output

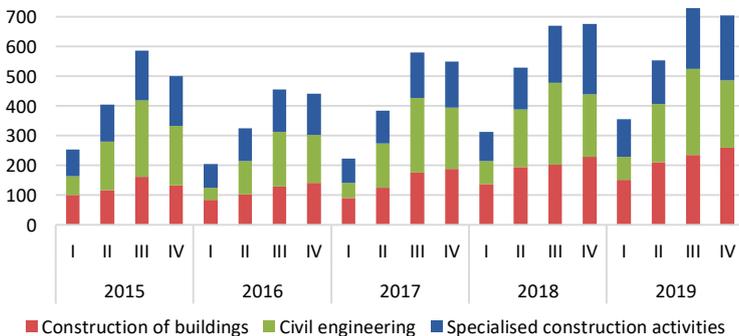


Industry



In 2019 compared to 2018, industrial production output in Latvia increased only slightly - by 0.8%. It was the weakest sector's growth rate in the past five years. Nevertheless, several manufacturing sub-sectors last year performed very well, for instance, the fastest growth was registered in manufacture of electrical equipment - its output volume increased by 16%. Manufacture of fabricated metal products rose by 13.5% last year. Thus, metalworking ensured the strongest contribution to total manufacturing growth in 2019. At the same time, growth rates in the two above-mentioned sub-sectors became weaker at the end of the last year due to weakening of external demand. Growth dynamics of repair and installation of machinery and equipment as well as manufacture of computer and electronic products last year was fluctuating, however overall in 2019 their production volumes increased strongly - by 9.3% and 8.8% respectively. While slight output contraction by 0.2% was registered in the largest manufacturing sub-sector, wood processing. Production output fell also in the second largest manufacturing sub-sector, food production industry, - by 1%.

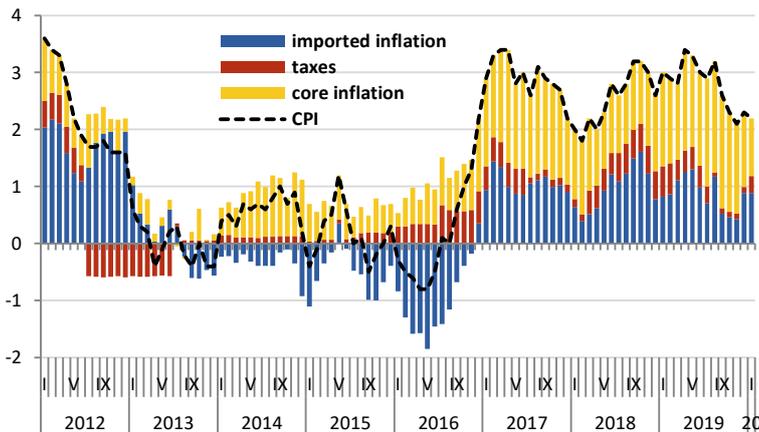
Construction output at constant prices, mln. euro



Construction

In 2019, construction output measured in current prices increased by 7.1% compared to the output level a year ago. Sector's growth was stimulated by construction of buildings that rose by 12.2%, at the same time civil engineering and output of specialised construction activities increased slower - by 4.7% and 4.0% respectively. Construction growth last year was weaker than in 2018 when sector's output had expanded by 26%, and it was associated with stabilisation of EU funds investment. In 2019, the expected construction space as indicated in the granted building permits continued to increase - compared to 2018 it rose by 37.1% y-o-y, especially strong growth was observed for industrial buildings and warehouses, trade as well as public entertainment, education and medical care building permits suggesting that construction volumes could potentially increase in the next periods.

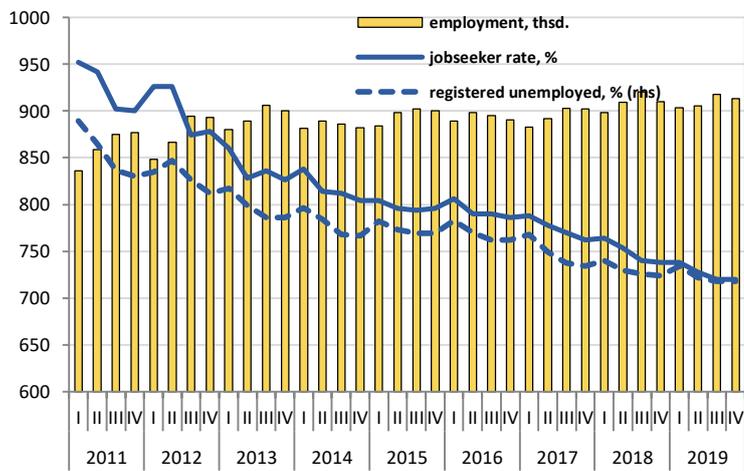
Inflation breakdown by origin, y-o-y, %



Inflation

In January 2020 compared to January of 2019, consumer prices in Latvia increased by 2.2%, thus inflation remained close to the level observed at the end of the last year - slightly above 2%. The largest contribution to consumer price growth in January was provided by price growth for food by 3.4% y-o-y, especially strong price increase was registered for pork, fresh fruits and sugar. Compared to January of 2019, price for fuel was by 8.8% higher this year which was affected by excise tax increase for fuel as of January 2020 as well as higher oil prices in the global markets. Prices for alcoholic beverages increased by 2.4% y-o-y in January that was determined by excise tax hike in March 2019. Price growth for tobacco products by 2.7% y-o-y was also affected by excise tax hike that took place in July 2019.

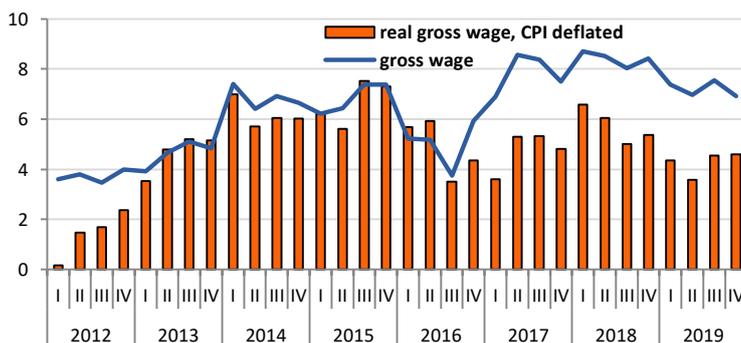
Unemployment rate, % of economically active population (15-74)



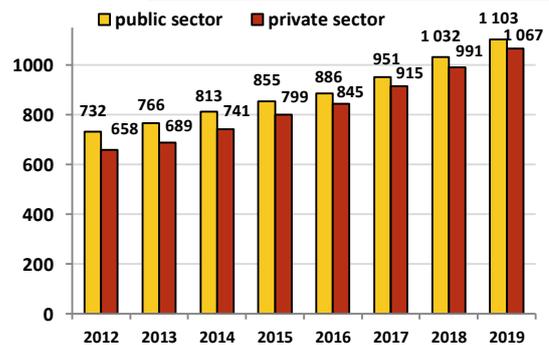
Employment

The number of employed persons, according to the labour force survey data, remained almost unchanged at 910 thsd in 2019, increasing only by 0.1%, compared to the previous year. In comparison, in 2018 the number of employed persons had increased by 1.6%. Statistics on occupied posts at the end of 3Q showed that the number of occupied posts increased the most in administrative services sector - by 4.4%, human health and social work activities - by 3.7% and agriculture and forestry - by 3.3% y-o-y. The largest decrease in employment was observed in public administration - by 3.6%, as well as in electricity and gas supply sector - by 1.1% y-o-y. Unemployment rate decreased by 1.1 percentage point to 6.3% of economically active population in 2019. Registered unemployment rate was 6.4% at the end of January 2020 - by 0.3pp lower than a year ago, and the number of registered unemployed in the last 12 months fell by 5.0% to 58.8 thsd at the end of January.

Wage dynamics, changes year over year, %



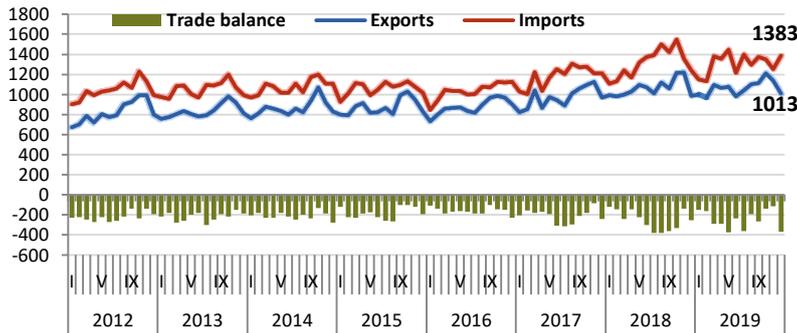
Wages, euro



In 2019, average gross wage increased by 7.2% to 1076 euro, showing a slightly lower growth than in the previous two years, when average gross wage increased by 7.9% in 2017 and by 8.4% in 2018 respectively. In 2019, wage growth rates declined gradually - to 6.9% in the fourth quarter of the year. Last year, wages grew faster in the private sector - by 7.6%, while in the public sector wage growth constituted 6.8%. Higher salary still remained in the public sector, where the average wage was 1103 euro, while in the private sector it constituted 1067 euro. Real net wage increased by 3.9% in 2019, showing weaker growth than in the previous year (+7.2%), when real net wage growth was stimulated by income tax cuts that took place in January 1, 2018.

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

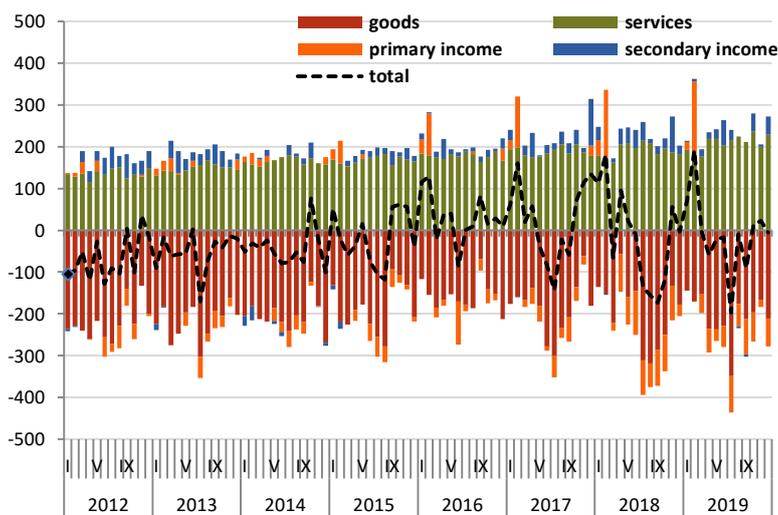
Foreign trade, current prices, euro



Foreign trade		
Exports, 2019 I-XII	Structure	Annual growth
Total	100%	0.4%
Food	21.2%	14.7%
Wood	17.2%	-3.2%
Mech/Electr appl	16.4%	-10.5%
Metals	8.6%	-4.8%
Chemical manuf.	7.9%	9.0%
Transport vehicles	6.0%	-4.8%
Mineral products	5.1%	-12.8%
Plastics	3.3%	6.2%
Others	14.3%	6.0%

Last year for Latvian exporters was challenging - fall of foreign demand, uncertainty related to Brexit, decline of wood prices as well as fall of re-exports of certain goods negatively affected export prospects in Latvia. Thus, export growth was close to negative throughout the year, and in 2019 overall exports of goods grew by only 0.4% constituting 12.8 billion euro. Stronger export growth was registered in December 2019 when export value of goods increased by 3.9% y-o-y. In 2019, positive contribution to total export growth of goods was mainly provided by increase of exports of agricultural and food products by 14.7%. Such growth was determined by high volumes of cereal exports thanks to exceptionally good cereal harvest last year. Rather strong export growth was recorded for chemical products - exports of these products grew by 9.0% in 2019, driven by pharmaceutical products exports to Russia and the Baltic States. At the same time, export growth was negatively affected by decline in exports of machinery and mechanical appliances due to fall in re-exports of turbojet engines by 331 mln euro which was associated with maintenance and repair of new aircrafts in 2018. Thereby, export decline of turbojet engines does not reflect changes in external demand and the competitiveness of Latvian exporters. If this category was excluded from total goods exports, the value of exports would have increased by 3.1% in 2019. Imports of goods increased by 11.6% y-o-y in December of the last year, while in 2019 overall the value of imported goods declined by 0.4%.

Balance of payments, current account, mln euro



Current account

In December 2019, Latvia's balance of payments current account recorded a deficit of 5 mln euro which was an increase by 2 mln euro compared to December 2018. Even though current account balance remained relatively stable, there were significant changes among the accounts. Since the value of imported goods increased faster than exports of goods, goods account deficit grew by 33 mln euro. Despite the sharp drop in the exports of transport services, total services account balance improved – its surplus increased by 46 mln euro in December 2019. Thus, services account surplus reached 229 mln euro fully covering goods account deficit of 211 mln euro. Due to the foreign residents' income growth from financial assets in Latvia and decline of income of Latvian companies from financial assets abroad, primary income account deficit rose by 39 mln euro. While secondary income account surplus increased by 24 mln euro driven by higher transfers by households and financial corporations. In 2019 overall, current account balance ran a deficit of 105 mln euro.

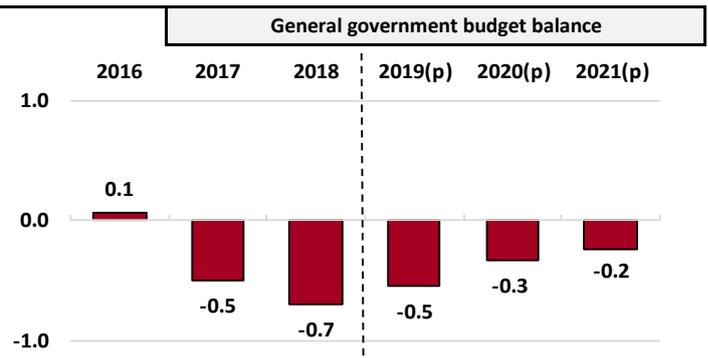
Main macroeconomic indicators, annual growth rates (unless stated otherwise)

	17'III	IV	18'I	II	III	IV	19'I	II	III	IV
GDP, constant prices, %	4.5	3.5	2.8	4.7	4.4	5.0	3.1	2.0	2.9	1.0
GDP, current prices, %	8.2	6.5	6.8	8.6	8.7	9.3	7.2	5.2	5.3	2.4
Inflation, %	2.9	2.6	2.0	2.4	2.9	2.9	2.9	3.3	2.9	2.2
Nominal wages, %	8.3	7.5	8.7	8.4	8.1	8.3	7.4	7.1	7.6	6.9
Real wages, CPI deflated, %	5.4	4.9	6.7	6.0	5.2	5.4	4.5	3.8	4.7	4.7
Employed persons, %	0.9	1.3	1.8	2.0	1.9	0.8	0.6	-0.4	-0.2	0.4
Unemployed, % of active pop.	8.5	8.1	8.2	7.7	7.0	6.9	6.9	6.4	6.0	6.0
Productivity, %	3.6	2.2	1.1	2.6	2.4	4.2	2.5	2.4	3.2	0.6
Retail trade, %	5.0	5.8	5.4	5.0	2.9	2.8	3.5	3.2	1.1	1.8
Industrial production, %	11.4	4.9	4.4	0.2	2.9	0.8	-0.8	1.4	2.6	0.0
Goods exports, %	10.4	11.8	9.2	14.7	7.9	7.3	3.2	-2.3	2.0	-1.8
Goods imports, %	19.9	9.5	6.8	11.7	14.2	12.3	5.3	4.1	-5.7	-3.9
Trade balance, mln euro	-820.5	-503.0	-507.5	-664.1	-1124.2	-723.7	-596.7	-894.4	-812.3	-625.1
Current account, % of GDP	-3.2	4.5	3.6	1.4	-6.1	-0.8	3.8	-1.3	-3.7	n.d.a.

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

General government budget balance, % of GDP

The Ministry of Finance has updated the assessment of the general government budget balance in 2019 according to the State Treasury data on the implementation of the consolidated general budget with reference to the ESA methodology. The general government budget in 2019 was a deficit of 0.5% of GDP. Official data on general government deficit level in 2019 will be available in April in this year, when calculations of all general government sector transactions will be completed, including General Government the results of operations of capital companies, and the CSB will submit a general government deficit and debt notification to Eurostat. The Ministry of Finance informs that according to the Draft budgetary plan, the general government budget deficit in 2020 is projected at 0.3% of GDP.



Budget Revenue and Expenditure

Consolidated General Budget

	January 2019 execution mln euro	January 2020 execution mln euro	Execution 2020/2019, mln euro	Execution changes 2020/2019, %
CONSOLIDATED GENERAL BUDGET**				
Revenue	975.7	990.3	14.6	1.5%
Expenditure	802.0	878.4	76.3	9.5%
<i>Financial Balance</i>	173.6	111.9	-61.8	
CONSOLIDATED STATE BUDGET*				
Revenue	832.4	800.1	-32.3	-3.9%
Expenditure	728.7	797.0	68.3	9.4%
<i>Financial Balance</i>	103.7	3.1	-100.7	
State basic budget				
Revenue	592.8	537.7	-55.1	-9.3%
Expenditure	539.2	564.7	25.5	4.7%
<i>Financial Balance</i>	53.6	-27.0	-80.6	
State special budget				
Revenue	235.6	258.3	22.7	9.6%
Expenditure	205.5	235.8	30.3	14.7%
<i>Financial Balance</i>	30.1	22.5	-7.6	
CONSOLIDATED LOCAL GOVERNMENT BUDGET**				
Revenue	234.6	290.1	55.5	23.7%
Expenditure	164.7	181.2	16.6	10.1%
<i>Financial Balance</i>	69.9	108.8	38.9	

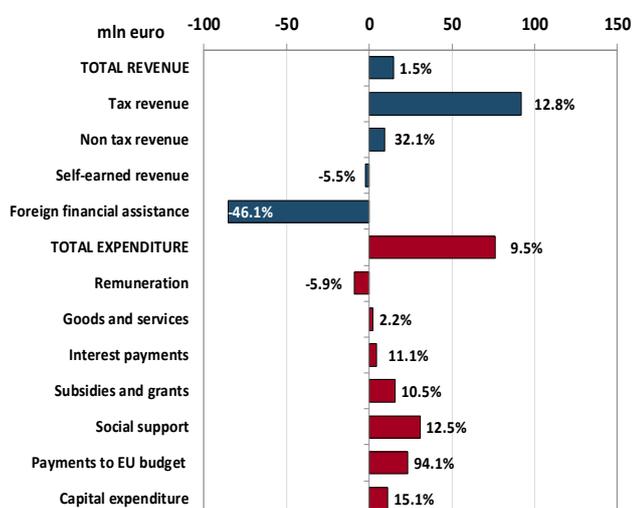
According to cash flow methodology

*Including grants, donations and derived public persons

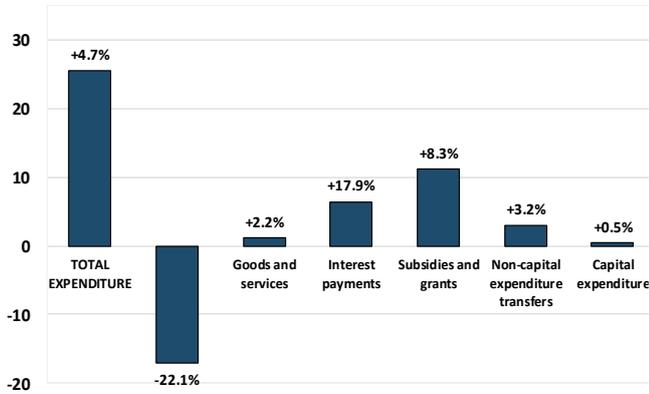
**Including grants and donations

According to the State Treasury in January 2020, the consolidated general budget revenue was 990.3 mln. euro, but expenditure was lower – 878.4 mln euro. As a result, the consolidated general budget had 111.9 mln euro surplus. It should be noted that the January surplus is 61.8 mln euro lower than in January 2019 due to lower foreign financial assistance revenues. In January, the consolidated budget revenue was 990.3 mln euro, what was for 14.6 mln euro or 1.5% more than in January 2019. The largest part of the increase was provided by tax revenue of 809.7 mln euro, what was for 92.0 mln euro or 12.8% higher than last year, mainly due to a significant increase in personal income tax (PIT) revenue. Non-tax revenue in the general budget increased by 9.3 mln euro or 32.1%, amounting to 38.3 mln euro. The increase in non tax revenue is explained by higher income from fines and sanctions. Foreign Financial Assistance (FDI) revenue (99.5 mln euro) was down 46.1% this year, owing to the fact high level of revenue in December last year due to more timely repayments from the European Commission (EC). Consolidated general government budget expenditure in January was 878.4 mln euro, what was for 76.3 mln euro or 9.5% more than in January last year. Expenditures were driven by higher contributions to the EU budget and higher capital expenditures compared to last year. Expenditure on contributions to the EU budget in January this year amounted to 48.4 mln euro what was for 23.5 mln euro or 94.1% more than in January 2019. Contributions to the EU budget have increased as a result of the EC's request for all Member States to contribute approximately one-sixth of their annual contribution to the EU budget in January, compared with about one-twelfth in January last year. Capital expenditure in January in this year increased by 11.4 mln euro or 15.1% in comparison with January 2019, amounting to 86.6 mln euro. The increase in capital expenditures is mainly due to higher expenditures for acquisition of equipment or other fixed assets of the National Armed Forces, as well as fixed assets of the Ministry of Transport.

Revenue and Expenditure in January 2020 (cash based changes in mln euro and in per cent against respective period of 2019)

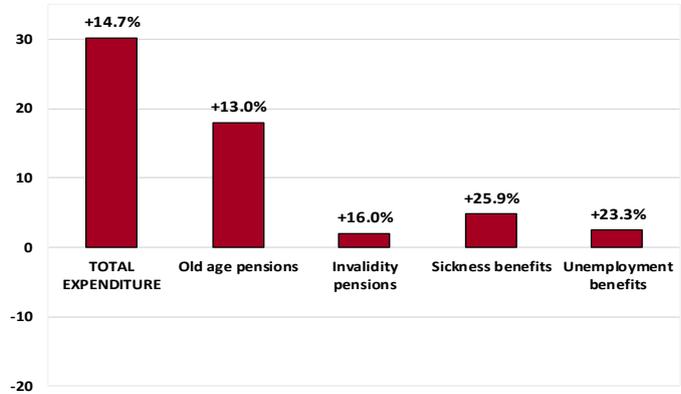


State Basic Budget Expenditure in January 2020
(cash based changes in mln euro and in per cent against respective)



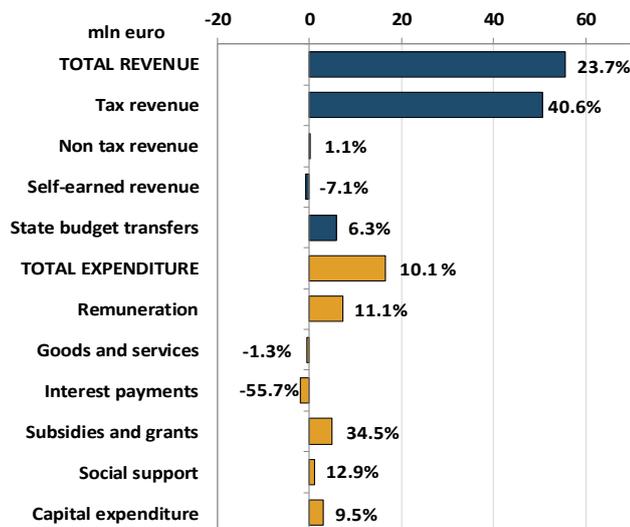
In January 2020, execution data showed that **state basic budget** expenditure exceeds revenue what which generated deficit 27.0 mln euro. In January this year central government basic budget revenue reached 537.7 mln euro and compared to January 2019 revenues decreased by 55.1 mln euro or 9.3%. In turn, expenditure in January, increased by 25.5 mln or 4.7% euro compared to January 2019. Expenditure growth was observed for subsidies and grants, which increased by 11.2 mln euro or 8.3% year-on-year, amountant 146.1 mln. euro. Subsidies and grants have been made extended for rail infrastructure maintenance and press delivery. Expenditure on goods and services increased by 1.2 mln euro or 2.2% compared to January 2019. In January this year, the cost of remuneration (60.1 mln euro) was significantly lower in the basic budget 17.1 mln euro or 22.1% less than in January last year. It should be noted that at the beginning of 2019, allowances were paid to officials of the Internal Affairs and Justice Department with special grades, which significantly increased the reimbursement expenses in the first two months of 2019.

State Special Budget Expenditure in January 2020
(cash based changes in mln euro and in per cent against)



In January 2020, the **state special budget** surplus was 22.5 mln euro, what was for 7.6 mln euro less than in January 2019. Revenue has grown faster than expenditure this year. In January 2020, the expenditure of the special budget (235.8 mln euro) what was for 30.3 mln euro or 14.7% higher than in January 2019. Pension expenditure (175.3 mln euro) in January this year increased by 20.3 mln or 13.1%, compared to January of last year, affected by the highest index in recent years, and partly due to a shift in pension payout dates for holidays and public holidays. In January, expenditure on other benefits was 9.8 mln euro or 19.9% higher than in January last year, driven mainly by higher spending on sickness and unemployment benefits. Sickness benefits in January 2020 was for 4.8 mln euro or 25.9% higher than in January 2019, what related to the increase in the average insurance contribution wage and with increasing incidence. According to the State Social Insurance Agency, in January this year the number of morbidity case increased by 19% compared to the same period last year. Expenditure on unemployment benefits in January this year was 2.5 mln euro or 23.3% higher than in January last year due to the rising number of persons granted unemployment status in the last quarter of last year.

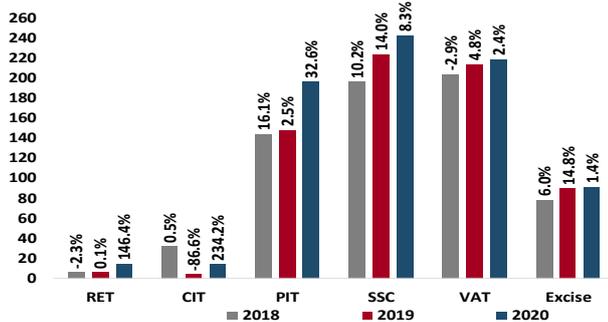
Revenue and Expenditure in January 2020 (changes in mln euro and in per cent against respective period of 2019)



According to the State Treasury, January 2020 ended with 108.8 mln euro surplus, what was for 38.9 mln euro in local government budget euro more than in January last year. Local Government Budget revenue showed excellent growth and reached 290.1 mln euro, what was for 55.5 mln euro or 23.7% more than a year earlier. The most significant increase was provided by tax revenue, what attributable to personal income tax (PIT) income, what increased by 41.9 mln euro. Income from PIT reached 159.6 mln euro. It should be noted that the fulfillment of PIT revenue was driven by a more rapid increase in employee's income and by the amount of dividends paid, which was due to the possibility to distribute the profits earned by 31 December 2017 at 10% PIT. Local government budget expenditure in January this year grew up on 16.6 mln euro or 10.1% and reached 181.2 mln euro. The largest increase was due to subsidies and grants, which increased by 4.8 mln euro or 34.5% and reached 18.5 mln euro. The growth supported by subsidies and grants to businesses to provide public transport services. Capital expenditures (33.9 mln euro) increased by 2.9 mln euro or 9.5% compared to January of the previous year thanks to EU funds' investments, which in the first half of this year increased by 10.4 mln euro.

Tax Revenue
Consolidated General budget Tax Revenue

	January 2019 execution, mln	January 2020 execution, mln euro	Execution changes 2020/2019, mln euro	Execution changes 2020/2019, %	January execution of the same period plan
Consolidated general budget tax revenue	717.7	809.7	92.0	12.8%	107.9%
Social security contributions	223.8	242.4	18.6	8.3%	103.0%
<i>in State special budget</i>	215.9	234.2	1.6	3.4%	102.8%
<i>Solidarity tax</i>	0.0	0.0	0.0	x	x
<i>1% for the health financing</i>	7.9	8.2	0.3	3.9%	107.3%
Value added tax	214.1	219.2	5.1	2.4%	99.3%
Personal income tax	147.9	196.2	48.3	32.6%	132.6%
<i>in State budget</i>	30.2	36.7	6.4	21.3%	123.9%
<i>in Local government budget</i>	117.7	159.6	41.9	35.6%	134.8%
Excise tax	90.0	91.2	1.3	1.4%	96.5%
Corporate income tax	4.2	14.2	9.9	234.2%	88.6%
Real estate tax	5.9	14.6	8.7	146.4%	238.7%
Informative:					
<i>Social security contributions to the state funded pension scheme</i>	47.5	49.1	1.6	3.4%	100.2%
<i>Solidarity tax in private pension scheme</i>	0.9	0.0	-0.9	x	x

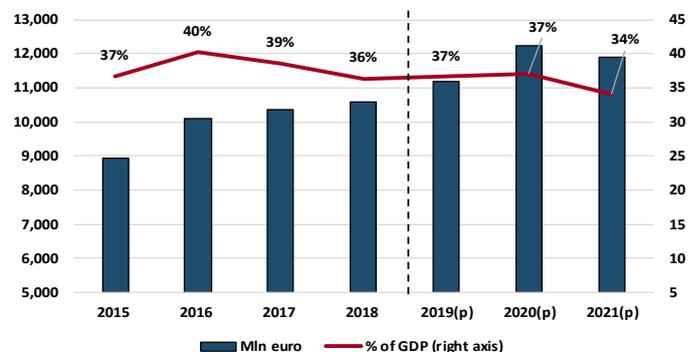
Total Tax Revenue January 2020 (mln euro and % change in comparison with the previous year)


In comparison with period of 2019, the tax revenue of the general budget increased by 92.0 mln euro or 12.8%, amounting to 809.7 mln euro, which was mainly driven by increases in personal income tax (PIT) and social security contributions (SOC). Total SOC revenue in the budget (242.4 mln euro) increased by 18.6 mln euro or 8.3%, compared to January 2019, this increase is driven by the rise in the number of employees and their earnings. Real estate tax (RET) revenue

in January was 14.6 mln euro, compared with January 2019, increased by 8.7 mln euro or 146.4%. Excise tax revenue in January 2020 was 91.2 mln euro compared to January 2019, what increased by 1.3 mln euro or 1.4%. The largest increase (1.7 mln euro or 4.0%) was observed in excise tax revenues on oil products. This is due to the increase in the volume of petroleum products released for consumption. On the other hand, excise tax revenue on alcoholic beverages dropped by 0.6 mln euro in January due to the decline in spirits released for consumption. In January this year, the value added tax (VAT) revenue increased by 5.1 mln euro or 2.4. The increase in VAT revenue is related to the increase in output and services rendered. The tax revenue plan for the general budget in January 2020 was implemented at 107.9%, providing the budget with an overhead revenue of 59.3 mln euro, mainly due to higher PIT revenue. The overflow of the PIT revenue plan was largely influenced by dividend income received at the end of 2019, as well as a more rapid increase in employee income. Significant overhead revenue in the general budget in January came from real estate tax and social security contributions, respectively 8.5 mln euro and 6.9 mln euro. In its turn, the value added tax revenue did not reach the planned 1.5 mln euro or 0.7% and corporate income tax revenue was 1.8 mln euro or 11.4% less than planned.

General Government Debt
General Government Debt, mln euro, % of GDP

According to the State Treasury, the general government debt stood at 36.6% of GDP in 2019 and is projected to increase to about 37% of GDP in 2020. On February 2020 an international credit rating agency S&P Global Ratings (S&P) upgraded Latvia from 'A' to 'A+' level with a stable outlook. S&P in its evaluation has highlighted two main driving factors for the upgrade: (a) Latvia's prudent fiscal policy, which, despite softer medium term growth outlook, will allow to reduce already modest debt also further and (b) vulnerabilities of Latvia's financial system are contained.



According to cash flow methodology

Source: The Treasury, Ministry of Finance of the Republic of Latvia, Eurostat, Medium Term Budget Framework Law 2020.-2022.