Scenario of Macroeconomic Development

Already for three years, the growth rate of Latvian economy is stable, export continues to grow and internal consumption becomes stable. State economy has acquired a stable basis for further growth – entrepreneurs work, increase their turnover and profitability, create new workplaces.

Macroeconomic forecasts for 2014–2016 are based on careful vision about development of the situation in economy in subsequent years. At the same time, according to the scenario of macroeconomic development, it is planned that Latvian economy will further preserve its position as one of the most rapidly growing economies in the European Union.

In the medium term, the growth of Latvia’s gross domestic product is forecasted to be in the amount of 4%. However, similarly as in the previous years, the growth of gross domestic product will be mostly provided due to increase in productivity, but not due to increase in the number of employed people. In the world, there are no considerable changes in prices of energy resources and food forecasted which would affect macroeconomic indicators of Latvia. Changes in consumer prices will be mainly determined by increase in core inflation that corresponds to Latvia’s level of development as well as by the planned changes in administered price and tax policy.

Objective of Medium-Term Fiscal Policy

The objective of Latvian fiscal policy is to provide a balanced budget during an economic cycle, thus promoting sustainable development and macroeconomic stability of the state as well as to reduce negative influence of external factors on national economy. In March 2013, the Fiscal Discipline Law has come into force, and the Law on Medium-Term Budget Framework for 2014-2016 is the first law that has been developed in compliance with the requirements laid down in the Fiscal Discipline Law.

By preparing the draft law on the annual state budget and the draft law on medium-term budget framework, taking decisions and actions related to the state budget, the fiscal policy principles laid down in the Fiscal Discipline Law are being implemented as well as the following medium-term budget policy’s priority directions of development: (1) promotion of sustainable and balanced development of the state economy, providing funding to sectors within the capacity of the state budget; (2) revision of tax burden on labour with a purpose to reduce income inequality of inhabitants and to improve quality of life, in particular among families with children.

According to the Law on Medium-Term Budget Framework for 2014, 2015 and 2016, the government’s tasks within the framework of the fiscal policy is to ensure the level of financial balance of the general government budget (in compliance with the European System of national and regional accounts in the European Union) for the year 2014 amounting to -0.9% from gross domestic product, for year 2015 amounting to -0.9% from gross domestic product, but for year 2016 amounting to -0.8% from gross domestic product. The fiscal policy that is being implemented by the government is oriented towards the stabilisation of macroeconomic situation and the promotion of economic growth.

Central Government Consolidated Budget Revenue

Forecasts about tax and non-tax revenue for the medium-term have been prepared, taking into account the current indicators of economic development and forecasts about their implementation in year 2013. It is planned that tax revenue, compared to year 2013, will increase by 4.3% in year 2014, by 8.8% in 2015 and by 12.4% in year 2016. One of the tasks of the Law on Medium-Term Budget Framework for 2014-2016 is to reduce income inequality of population. The most considerable changes are related to salaries: higher non-taxable minimum, higher allowance for dependent persons and lower tax rate of social contributions. A non-taxable minimum not liable to personal income tax is increased from 64.03 euros to 75.00 euros, an allowance for dependent persons is increased from 113.83 euros to 165.00 euros, thus improving the system of state social aid. At the same time, for employers the rate of social security contributions is reduced by 0.5% and for employees the rate of social security contributions is reduced by 0.5%. Tax rate reduction model prescribed by the law has been changed, at the same time stating that in year 2014 personal income tax rate will remain 24 per cent, however, in year 2015 – it will amount to 23 per cent and from year 2016 – 22 per cent.

To make economic environment more attractive, as of 1 January 2014 the term for application of enterprise income tax allowance relief for new manufacturing technological equipment has been prolonged until the year 2020 as well as the term for application of enterprise income tax allowance relief for the investment projects to be supported has been prolonged until year 2020, providing an allowance for large investment projects exceeding 10 million euros. In addition, as of 1 July 2014 there will be enhanced income tax allowance for the expenditure on research and science.

Amendments to the Value Added Tax Law have been made to bring in order a normative regulation for the application of value added tax in transactions with immovable property and to eliminate ambiguities and interpretations by the application of value added tax. Amendments have also been made to prevent the cases when expensive luxury class cars are being purchased and a pre-tax is being deducted for them, although they are not being fully used for performing the transactions liable to value added tax.

According to the amendments in the Natural Resources Tax Law, as of 1 January 2014 natural resources tax rates have been increased for subsoil resources and for the disposal of household waste in landfills. Rates have been increased for environmentally harmful goods, package and vehicles, for air pollution and for emission of polluting substances into water. New objects of natural resources tax have also been introduced: fireworks and use of water resources for production of electricity in hydroelectric power stations where the total installed capacity of hydroelectric station is lower than two megawatts.

Amendments to the Law on Excise Duties have been made to reduce a difference in a burden of excise duty between the types of fuel, by increasing as of 1 January 2014 excise duty for liquefied petroleum gas (auto gas) from 128.06 euros per 1 000 kilogrammes up to 161.00 euros per 1 000 kilogrammes. As of 1 January 2014, excise duty has been increased for all tobacco products, but as of 1 July 2014, the structure of excise duty for cigarettes will be changed, reducing Ad valorem rate to 25 per cent and increasing specific excise duty rate from 39.84 euros to 51.80 euros per 1 000 cigarettes, as well as increasing a minimum level of excise duty up to 85.60 euros per 1 000 cigarettes.

For the period from 1 January 2014 until 31 December 2017 there has been a new tax introduced – subsidised electricity tax which will be applied to manufacturers of electricity that have obtained the rights to sell electricity within the framework of compulsory purchase. The Subsidised Electricity Tax Law provides for introduction of term subsidised electricity tax what is necessary in order to finance the establishment of electricity consumers’ support fund and to compensate increasing electricity costs also to less wealthy inhabitants.
The Law on the State Budget for 2014 is the first law that is prepared in the euro currency, and there is funding provided for the implementation of priorities of the National Development Plan for 2020 and of the State Defence Concept as well as for the implementation of other activities of national importance.

**Approved New Policy Initiatives, million euros**

<table>
<thead>
<tr>
<th>Characteristics</th>
<th>2014</th>
<th>2015</th>
<th>2016</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total, incl.</td>
<td>266.8</td>
<td>393.0</td>
<td>443.4</td>
</tr>
<tr>
<td>For new policy initiatives that provide for the implementation of the National Development Plan of Latvia, including:</td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>For the priority ‘Growth of national economy’</td>
<td>137.3</td>
<td>218.7</td>
<td>248.3</td>
</tr>
<tr>
<td>For the priority ‘Human Security’</td>
<td>43.8</td>
<td>76.0</td>
<td>74.4</td>
</tr>
<tr>
<td>For the priority ‘Growth of Regions’</td>
<td>35.7</td>
<td>73.3</td>
<td>78.0</td>
</tr>
<tr>
<td>For new policy initiatives for the implementation of the State Defence Concept</td>
<td>57.6</td>
<td>67.4</td>
<td>95.9</td>
</tr>
<tr>
<td>For other new policy initiatives</td>
<td>115.2</td>
<td>139.9</td>
<td>156.7</td>
</tr>
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</table>

Funds have been allocated for the activities, the objective of which is to implement one of three priorities of the National Development Plan for 2020:

- **‘Growth of National Economy’** – funding for the support of electricity consumers in order to provide a common price of competitive electricity (for the Ministry of Economics: in year 2014 – 29.3 million euros, in year 2015 – 47.8 million euros, in year 2016 – 56.2 million euros), for transitional solutions on improving the energy efficiency of buildings, providing the implementation of initiated activities in the field of energy efficiency of buildings between the planning periods (for the Ministry of Economics: in year 2014 – 4.8 million euros, in years 2015 and 2016 – 0.1 million euros);
- **‘Human Security’** – for increase of the state aid for persons with a disability, as of 1 July 2014 increasing the amount of state social security benefit for persons with a disability group I from 64.03 euros to 70.52 euros a month, persons with a disability group II – from 64.03 euros to 76.84 euros a month, persons with a childhood disability group I – from 106.72 euros to 138.74 euros a month, persons with a disability group II – from 106.72 euros to 128.06 euros a month, as well as increasing the amount of benefit for a person with a disability who needs special care – from 142.29 euros to 213.43 euros a month (for the Ministry of Welfare: in year 2014 – 6.7 million euros, in year 2015 – 14.0 million euros, in year 2016 – 14.7 million euros), for the provision of health care services and health promotion activities as well as for the reduction of the waiting queues for out-patient and in-patient care services, for increase in the amount of state paid rehabilitation services, for the Ministry of Defence: in year 2014 – 4.4 million euros, in year 2015 – 5.2 million euros, in year 2016 – 5.0 million euros, for the provision of assistance services to persons with a disability (for the Ministry of Welfare: annually 1.7 million euros), for the improvement of demographic situation, including such essential activities – for increase in the amount of child care benefit (form 142.29 euros to 171.00 euros a month), for provision of payment of child care benefit also to the recipients of parental benefit (as of 1 October 2014), for the prolongation of the period of parental benefit’s receipt until child’s age of 1.5 (as of 1 October 2014), for payment of parental benefit amounting to 30% from the allocated parental benefit to the employed persons until child’s age of 1.5 (as of 1 October 2014), for more rapid increase in the amount of state support, prescribing a benefit of 71.14 euros for a child aged 0 to 7 and 78.26 euros for a child aged 7 to 18 years;

- **‘Growth for Regions’** – for the implementation of the Road Construction Programme for 2014–2020 and for the maintenance of roads (for the Ministry of Transport: in year 2014 – 38.0 million euros, in year 2015 – 47.0 million euros, in year 2016 – 65.5 million euros), for reduction of administrative burden for the clients of the State Revenue Service (SRS), improving the availability and quality of e-services provided by the SRS (for the Ministry of Finance: in year 2014 – 2.6 million euros, in year 2015 – 6.1 million euros, in year 2016 – 5.0 million euros), for implementation of the principle ‘Money returns to nature’ (for the Ministry of Environmental Protection and Regional Development: in years 2014 and 2015 – 2.1 million euros, in year 2016 – 2.9 million euros).

For implementation of the objectives included in the State Defence Concept there are funds allocated to the Ministry of Defence, including for the following important activities: establishment of NATO Centre of Excellence for Strategic Communications (in year 2014 – 3.3 million euros, in year 2015 and year 2016 – 3.1 million euros annually), mechanisation of Infantry Brigade of the National Armed Forces (in year 2014 – 2.2 million euros, in year 2015 – 14.6 million euros and in year 2016 – 18.6 million euros), strengthening of the National Guard’s capacities and improvement of efficient reserve system (in 2014 – 1.4 million euros, in 2015 – 7.7 million euros and in 2016 – 6.6 million euros), etc.

Funds have been allocated also for other activities, e.g. for increasing the funding science and research (for the Ministry of Education and Science: in 2014 – 4.4 million euros, in 2015 – 12.2 million euros and in 2016 – 16.4 million euros), for culture (for the Ministry of Culture: in year 2014 – 11.9 million euros, in year 2015 – 14.5 million euros and in year 2016 – 16.4 million euros), ensuring the functioning of electronic mass media (for radio and television: in year 2014 – 2.5 million euros, in year 2015 and year 2016 – 2.3 million euros). Additional funds have been allocated for remuneration as of 1 January 2014 – for increasing a minimum monthly salary – 18.1 million euros annually, and for equalisation of monthly salaries in years 2014 and 2015 – 7.9 million euros, in year 2016 – 15.7 million euros (including for employees in state administration), for providing remuneration on the basis of equal principles to the employees of the Ministry of the Interior and the Ministry of Justice’s Prison Administration – 6.5 million euros annually. Furthermore, the total allocated funds for teachers’ salaries in year 2014 – 9.5 million euros, in year 2015 – 23.4 million euros and in year 2016 – 26.1 million euros. Additional funds have been allocated also for the activities related to the planned accession to the Organisation for Economic Co-operation and Development: in years 2014 and 2015 – 1.9 million euros and in year 2016 – 2.1 million euros.

**Central Government Consolidated Budget, mln. euros (net)**

**Central Government Consolidated Budget, mln. euros (gross)**

**Social Security Special Budget, mln. euros**