Latvia

In BEEPS V, the top three business environment obstacles identified by Latvian firms were workforce skills; access to finance; and political instability (Chart 1). SMEs and young firms were mostly concerned about access to finance, while large and manufacturing firms were constrained by electricity issues. Young firms were also affected by competitors' practices in the informal sector. In BEEPS IV tax administration, rather than access to finance, was among the top three business environment obstacles.

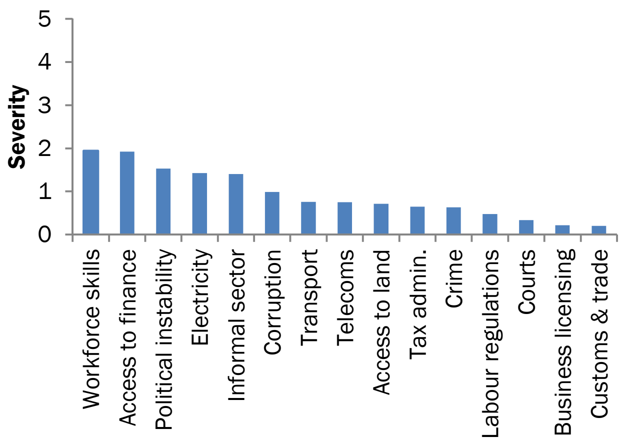
Workforce skills remain a challenge and access to finance is a constraint

Latvian firms identified **workforce skills** as the top obstacle. In 2004, when the country first joined the EU, most of the emigrant workers were moderately educated individuals from rural areas, where unemployment rates are the highest. However, the number of emigrants, and the human capital they take with them, has increased over the years. Young and highly educated workers now tend to migrate to western Europe in search of better career opportunities. This is a concern for Latvia, as it is a country with an ageing and shrinking population. As of 2012, around 80% of the emigrants are under 35.

When it comes to **access to finance**, the share of bank loans used to finance fixed assets has decreased in all countries in central Europe and the Baltic states (CEB). The reduction was particularly striking in Latvia, where the share in BEEPS V was less than a quarter of the share in BEEPS IV and less than half of the average share in CEB (Chart 2). Only around 6% of fixed assets purchases were financed through bank loans, compared with a CEB average of almost 16%. The share of firms with a loan or a credit line more than halved too, from 48.5% in BEEPS IV to 20.1% in BEEPS V, which is below the CEB average of 40.5% (Chart 3). However, only 24.0% of firms reported needing a bank loan and more than 60% of those turned out to be credit-constrained – they either did not apply for a loan (despite needing it) or were rejected by the bank when they did. Among young firms, only 12.5% reported needing a bank loan, but all of them were credit-constrained. The share of credit-constrained large firms almost doubled from 24.8% in BEEPS IV to over 45% in BEEPS V.

Political instability was perceived to be the third most severe obstacle to Latvian firms. In 2011 parliament was dissolved following a corruption scandal. The relationship between businesses and politics, combined with low levels of trust in parliamentary and political institutions, has posed problems in Latvia since the country regained its independence in 1991.

Chart 1. Business environment obstacles



Estimated for a hypothetical "average" firm. Higher values correspond to a weaker business environment.

Chart 2. Sources of financing of fixed asset purchases

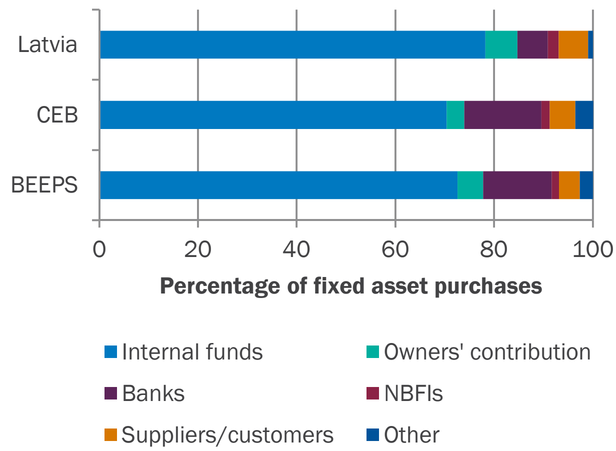
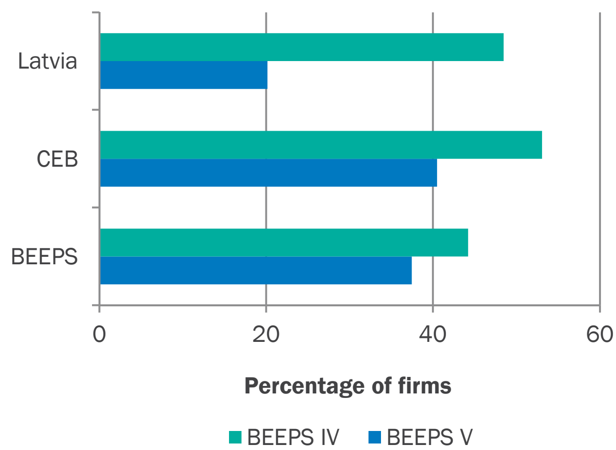


Chart 3. Firms with a loan or a credit line



Survey fieldwork period: January 2013 – January 2014. CEB: Croatia, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic and Slovenia. Small and medium-sized enterprises (SMEs) have 5-99 employees. Young firms are less than 5 years old.