



# Latvia Country Strategy 2021-2026

Approved by the Board of Directors on 15 September 2021



**European Bank**  
for Reconstruction and Development

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Annex 1 - Political Assessment	18	ESIA	Environmental and Social Impact Assessment	PEF	Private Equity Fund
		ETI	Expected Transition Impact	PPP	Private-Public Partnership
		ETS	Emission Trading System	PPS	Purchasing Power Standards
		EU	European Union	PR	Performance Requirement
		FDI	Foreign Direct Investment	PTI	Portfolio Transition Impact
		FI	Financial Institution	R&D	Research and Development
		FI	Financial Institutions	RE	Renewable Energy
		GDP	Gross Domestic Product	RRF	Recovery and Resilience Facility
		GEFF	Green Economy Financing Facility	RSF	Risk Sharing Facility
		GET	Green Economy Transition	SME	Small and Medium sized enterprises
		GHG	Greenhouse Gas	SOE	State-owned Enterprise
		GVC	Global Value Chains	SPO	Secondary Public Offering
		HPP	Hydro Power Plan	TC	Technical Cooperation
		HR	Human Resources	TPES	Total Primary Energy Supply
		ICA	Industry, Commerce & Agribusiness	VC	Venture Capital
		ICT	Information and communications Technology	WDI	World Development Indicators
				WEF	World Economic Forum



The Republic of Latvia's commitment to and application of principles set out in Article 1 of the Agreement Establishing the Bank has continued over the period since the adoption of the previous Country Strategy. The constitutional and legislative framework for a pluralistic parliamentary democracy is in place. The separation of powers and checks and balances in the political system, and guarantees for human rights and fundamental freedoms are largely in line with international and European standards. The media are pluralistic and competitive and civil society operates independently. Elections are conducted in a manner deemed by the OSCE to be free and in line with international standards. Latvia has been a member of the European Union since 2004.

Nestled between its Baltic neighbours, benefitting from EU membership and strong economic ties with its Nordic neighbours, Latvia has enjoyed rising prosperity for its citizens and convergence towards the EU average over the past decade. However, more needs to be done to complete its transition towards a knowledge-economy and fully integrate the country with its Baltic country peers to overcome the limitations of a small (albeit open) domestic market. Transition gaps are particularly acute in competitiveness (with a low capacity of companies to innovate and adopt technologies to enhance the country's participation in GVCs), resilience (the capital market remains shallow) and green (with a high energy intensity and need to transition towards renewable energy other than hydro).

The economy was significantly affected by the pandemic, thereby temporarily increasing EBRD's additionality to provide support for recovery during the first part of the strategy period. In light of a strong policy response and considerable EU funding expected under the RRF and MFF, the strategy will be reviewed as part of an extended Country Strategy Delivery Review in 2023, which will be informed by an analysis of market level additionality and will consider whether the objective of pursuing Covid-19 recovery has been completed. As a consequence of such review, and the country being on a sustained recovery path, the Bank's objectives in the remainder of the strategy period will be adjusted as needed to focus on core strategic sectors and products where the Bank's additionality and the transition gaps are evident and material. In line with EBRD's graduation policy, Latvia will indicate the country's intended path and plausible pace of graduation at the appropriate time.

Latvia has been a consistent beneficiary of EU structural funds and the economy will further benefit from the expected EU stimulus; the EBRD is well positioned to continue to focus on areas where it remains additional and can deliver high transition impact, including the continued support for green transition in achievement of the country's Nationally Determined Contributions. Furthermore, the Bank will continue to stimulate the development and integration of the pan-Baltic capital market, grow the country's investor base through the promotion of new and green instruments, and foster innovation and digitalisation to enhance the country's competitiveness; where applicable leveraging Invest EU guarantees. Throughout, the Bank will promote regional investment and transfer of regional knowledge in the Baltic countries.

The Bank will pursue the following strategic priorities in Latvia 2021-2026:

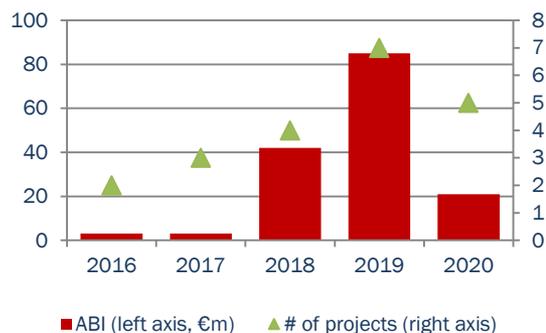
- i. Support Latvia's Green Economy Transition; and*
- ii. Foster Latvia's Knowledge Economy through More Diversified Sources of Private Finance.*



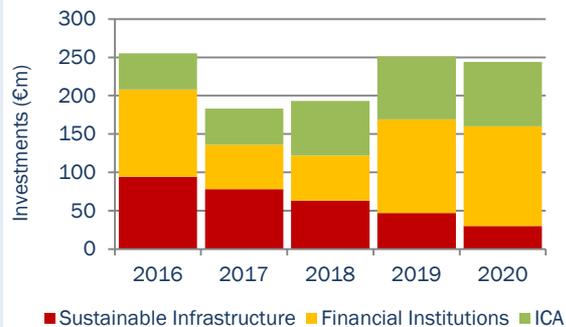
## EBRD Investment Activities in Latvia (as of year-end 2020)

Portfolio	€243m	Active projects	35
Equity share	46%	Operating assets	€205m
Private Sector Share <sup>1</sup>	92%	Net cum. investment	€777m

## ABI and Operations



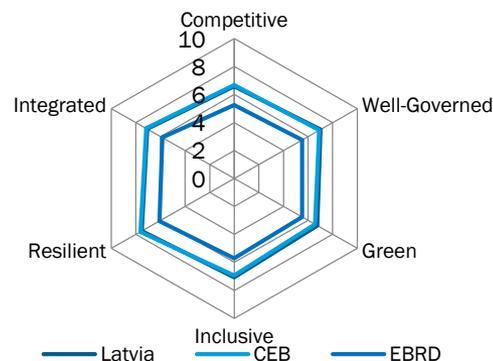
## Portfolio Composition



## Portfolio Dynamics



## Transition Gaps <sup>2</sup>



## Country Context Figures

	Country	Comparators
Population (million) <sup>3</sup> (2019)	1.913	Lithuania (2.8), Estonia (1.3)
GDP per capita (PPP, USD) <sup>3</sup> (2019)	32,191	Lithuania (38,502), Estonia (38,915)
Global Competitiveness Index (WEF) (2019) (out of 140 economies)	41	Lithuania (39), Estonia (31)
Unemployment (%; ILO est.) <sup>4</sup> (2019)	6.5	Lithuania (6.5), Estonia (4.6)
Youth unemployment (%; ILO est.) <sup>4</sup> (2019) share of youth not in employment, education or training (NEET)	7.9	Lithuania (8.7), Estonia (6.9)
Female labour force participation (%; ILO est.) <sup>4</sup> (2019)	55.8	Lithuania (57.3), Estonia (57.6)
Energy intensity (TPES/GDP) <sup>5</sup> (2016)	0.16	Lithuania (0.17), Estonia (0.24)
Emission intensity/GDP (kgCO <sub>2</sub> /10'\$) <sup>5</sup> (2018)	0.2	Lithuania (0.2), Estonia (0.6)

1 Cumulative Bank Investment: 5 year rolling basis on portfolio.

2 Cf. EBRD Transition Report 2020. 3 World Bank WDI. 4 International Labour Organisation (estimates). 5 IEA's Energy Atlas.

# 1. Implementation of Previous Strategy (2016-2020)

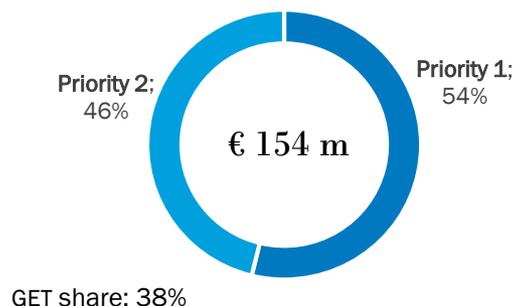


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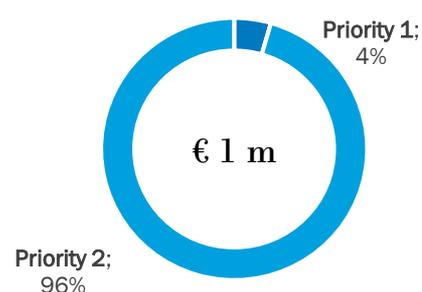
## 1.1. Key Transition Results Achieved during previous Country Strategy

### Strategic Alignment 2016-2020

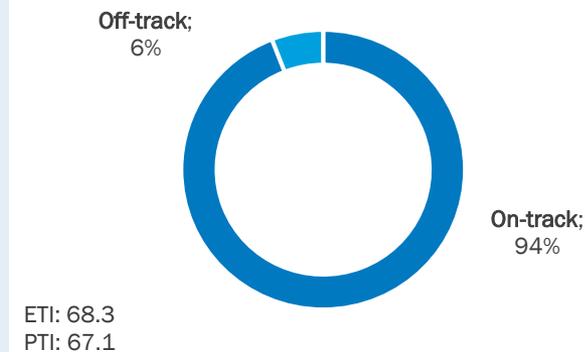
#### Annual Business Investment (ABI)



#### Technical Assistance and Investment Grants

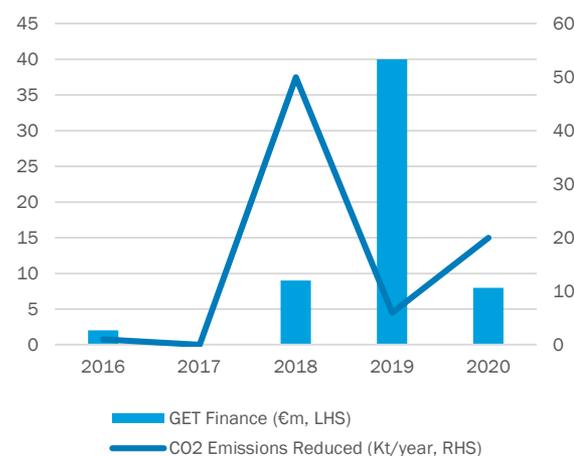


### Transition Impact Performance\*



## Priority 1: Strengthening energy security and improving energy efficiency

### Green Economy Transition



### Key Transition Results

- Supported private participation in new biomass CHP plants to generate 55,000 MWh of zero carbon electricity and save 113,850 tons CO2 per annum.
- Contributed to improved environmental standards of client private sector power generation company (Graanul Invest Group), in line with international best practice ISO 50001 certificates.
- The Bank's client fund, BaltCap Infra fund has invested in three biogas CHPs.
- Signed Risk Sharing Facility targeting RE and EE projects with Citadele Banka.
- Provided €2m loan for Latvian Baltic Energy Efficiency Facility (LABEEF) to finance ESCOs based on Energy Performance Contracts, as result of extended policy dialogue and successful strengthening of regulatory framework for EPCs. Energy Performance Contract developed through TC engagement and tender processes for two EPC projects successfully finalised.
- Invested in an innovative Baltic agribusiness company, with proceeds to be used in energy efficiency investments – specifically targeting reduction of fertilizers/chemicals and contributing to sustainable land use.
- Invested in the EFTEN Baltics Sustainable Property Fund with €10.1m out of a total of €30.5m for the Baltics. This is the first local property fund in the Baltic countries with a climate agenda and green objectives as an integral part of the business concept.
- Increased cooperation with Altum Latvian development FI and other market participants.

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\* Transition impact performance reflects how likely projects are to achieve the transition impact expected of them at signing. Calculated based on active mature (> 2 years) portfolio.

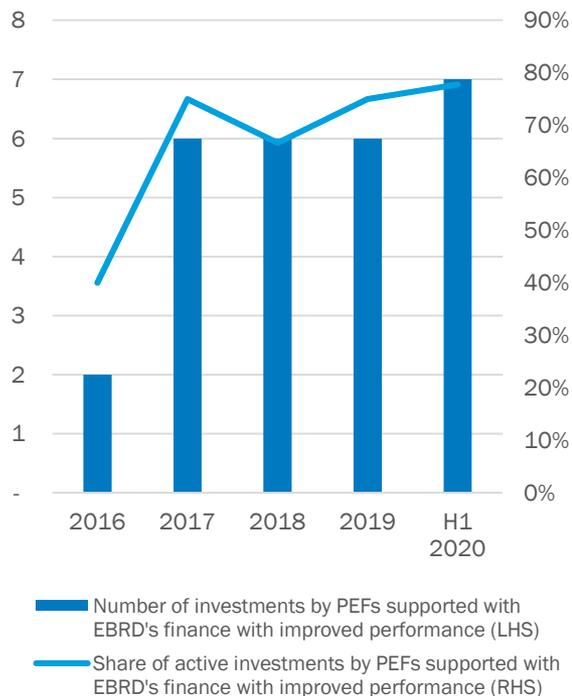
# 1. Implementation of Previous Strategy (2016-2020)



## 1.1. Key Transition Results Achieved during previous Country Strategy

### Priority 2: Boosting private sector competitiveness

#### EBRD supported PEF performance



#### Key Transition Results

- Provided €50m loan to UniCredit Leasing Latvia, to foster competitiveness by increasing availability of financing to private MSMEs.
- Signed a Risk Sharing Facility with Citadele Banka.
- Invested in an innovative Baltic agribusiness company present in all three countries promoting innovation by expanding R&D activities and offering of innovative farming inputs to local farmers.
- Equity investment in local waste management group, envisaged to finance construction of the first mechanical biological treatment (MBT) plant in the region, linked to a new long-term waste management contracted tendered in Riga.
- EBRD client funds (BaltCap PEF II and BPM Mezzanine Fund) invested in innovative companies with operations in Central Europe and the Baltic countries (SMN, Uprent, Optometrijas Centrs respectively).
- Invested €40m in a regional private equity investor, Resource Eastern European Equity Partners.
- Committed to the first pan-Baltic Infrastructure fund.
- Investments in five regional equity funds which include investments in innovative and export oriented companies in their portfolios, including €25m investment in the BaltCap Private Equity Fund III. This supports the emergence of a stronger, more sustainable private equity sector through the provision of equity and quasi-equity financing at all stages of company development.
- Assisted Altum in selecting PE/VC fund managers for allocating EU structural funds.
- Secured SRSS funding for the development of capital markets, through extensive engagement with authorities and stakeholders. MoU signed in 2017 by Baltic Finance Ministers supporting Pan-Baltic capital market development in areas such as covered bonds and SME financing. The EBRD continuously worked on the development of the Pan-Baltic capital market, including a number of debt transactions (Maxima, Lietuvos Energija and Luminor) as well as equity.
- Continued work under Baltics Integrated Approach, leading to establishment of the Baltic Venture Capital Association.

# 1. Implementation of Previous Strategy (2016-2020)



## 1.2. Challenges to Implementation and Key Lessons

### Context for Implementation

Over the last country strategy period, Latvia's economy has continued on its course of EU convergence albeit at modest GDP and low productivity growth, well below its CEB peers. A banking scandal in early 2018 triggered urgent reforms and increased support for newly-established parties running on an anti-corruption platform. In the wake of Covid-19, however, the country witnessed a severe decline in economic activity that outpaced that of its Baltic neighbours. Since starting operations in 1992, the EBRD has invested over €780m through 90 projects in Latvia. Between 2016 and 2020, the Bank has increasingly focussed on areas where it remains additional, such as energy security and efficiency, deepening the financial sector and improving the competitiveness of the export sector.

### Implementation Challenges

- Existing hydropower infrastructure from Soviet era reduced the urgency to develop further renewable energy in power generation.
- Limited progress on IPOs of the state-owned enterprises.
- Challenges of improving energy efficiency of existing housing stock.
- Slow progress in engaging with the previous Riga city authorities and city owned POEs.
- Only one city in Latvia previously eligible for Green Cities Programme (Riga).
- Uncertainty in banking sector created by the MONEYVAL / FATF process has deterred investor confidence and activities beyond just the banking sector.

### Key Lessons & Way Forward

- Heightened awareness of hydrological risk (i.e. increasing variability of rainfall as a result of climate change) has created awareness of the need to develop alternative renewable energy sources for power generation.
- Technical Support Instrument-funded and EBRD-implemented TC on reform of SOEs could unlock opportunities for IPOs and/or increased private sector participation.
- Importance of a strong counterpart to administer a streamlined funding and implementation scheme. An expansion of financing of energy efficiency improvements in the existing housing stock.
- EBRD will seek re-engagement with the newly-elected Riga city council following the 2020 elections.
- Reduction of minimum population size of the Green Cities Programme opens opportunities for more cities.
- Latvian authorities acted decisively to clean up banking sector, which has improved investor perception. Continue to support development of pan-Baltic capital market to increase attractiveness of Latvia and the Baltic countries as an investment destination.

## 2. Economic Context

### 2.1. Macroeconomic Context and Outlook for Strategy Period



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#### Latvia - Main macroeconomic indicators

	2016	2017	2018	2019
GDP growth (% y-o-y)	2.4	3.3	4.0	2.1
CPI inflation (% avg.)	0.1	2.9	2.6	2.7
Government balance (% of GDP)	0.2	-0.8	-0.8	-0.2
Current account balance (% of GDP)	1.3	0.7	-0.3	-0.6
Net FDI (% of GDP)	0.9	3.8	1.3	3.1
External debt (% of GDP)	149.1	142.3	123.7	117.1
Gross reserves (% of GDP)	-	-	-	-
General government gross debt (% of GDP)	40.9	39.3	37.2	36.9
Unemployment (15-64, % pop)	9.9	8.9	7.6	6.5
Nominal GDP (€bn)	25.4	26.9	29.1	30.5

Latvia's GDP per capita has further converged towards the EU average, but at a slower pace compared to its Baltic peers. In 2019, GDP per capita in PPS reached 69% of the EU average, behind all CEB peers, marking a modest increase of 3% compared to 2016. Productivity growth has also been slower than in Baltic peers.

**GDP growth has been driven by consumption and investment.** GDP growth averaged 2.9% in the previous strategy period. Strong wage growth on the back of a tightening of the labour market spurred private consumption, which had an average contribution to GDP of 1.6% since 2016. Despite strong investment growth in 2018 and 2017, net exports had a negative contribution to GDP growth in this period. This reflects the limited ability of the economy to gain export market shares and its reliance on less advanced manufacturing sectors.

**Latvia was also the most affected by the Covid-19 crisis among Baltic states.** In the first half of 2020, GDP fell by 4.9% year-on-year. Sufficient fiscal space has enabled a decent policy response to the crisis, but private consumption remained subdued in the first three quarters of 2020, declining by 10.4% y-o-y.

**Outlook remains uncertain in the short-term, while further convergence in the medium term will require addressing transition gaps.** The high uncertainty will continue dragging down economic recovery at least in the first half of 2021. The budget deficit in 2021 is expected to remain high as the government will continue stimulating the economy. The increase in unemployment may also affect the recovery of private consumption. In this sense, the national recovery and resilience plan will be key in unlocking additional EU resources to support government spending. In the medium to long term, addressing existing transition gaps, especially towards improving the competitiveness of the private sector, will allow Latvia to move closer to average EU income levels and bridge the gaps with the Baltic peers.

## 2. Economic Context

### 2.2. Key Transition Challenges



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#### Competitive (6.58/10)

- **Competitiveness of the private sector is lagging behind the Baltic country peers.** Capital investment has been sluggish amid lower integration into GVCs and FDI inflows, while manufacturing is dominated by traditional sectors. SMEs are innovating less than Baltic peers and digitalisation is slower. Innovation expenditure is among the lowest in the EU.
- The score on the **economic complexity** dimension reveals that the performance of the three Baltic countries is slightly **weaker than regional CEB peers**. Low complexity products (agricultural products and minerals) mainly dominate Latvia's exports.
- **The Baltic countries display a relatively limited state presence** in the private sector and pursue liberal economic policies, although Latvia has a larger state footprint in the economy amid slower privatisation efforts.

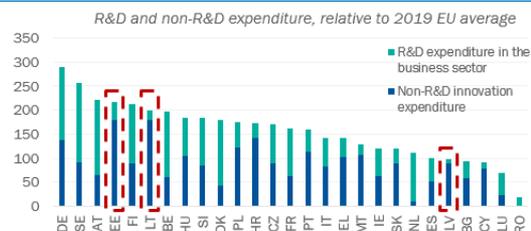
#### Well-governed (Latvia: 7/10)

- **On the corporate level**, Latvia scores particularly highly in structuring and functioning of the board, and rights of shareholders. **On the national level**, Latvia scores above the regional average in many areas including rule of law, government effectiveness, and freedom of media.
- **Latvia has made substantial progress in strengthening regulation over the financial sector.** In the past two years Latvia's progress in anti-laundering measures include banning the servicing of non-resident shell companies, amending legislation to improve the governance and clarify responsibilities of main stakeholders, and strengthening the capacity of key institutions.
- **Latvia lags behind the EBRD average in e-governance participation and enforcement of contracts;** and is behind the regional average on issues such as budget transparency and informality.

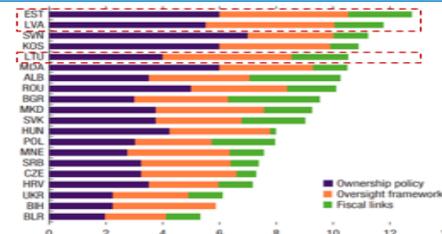
#### Green (6.74/10)

- **Green transition towards 2020 targets has been notable, but gaps remain** in the carbon-intensive transport sector, high energy-intensive building stock and industry. Latvia has relied on its existing hydro infrastructure, while efforts to deploy alternative sources have been modest.
- **While improvements have been made, PPP-adjusted energy intensity remains high in Baltic states**, at around 25% more than the EU average in 2018, with the highest gap in Latvia (43.3%).
- **Landfilling of waste is significantly higher than in regional peers.** Landfilling accounted for 83% in Estonia, 64% in Latvia, and 19% in Lithuania in 2016.
- **Energy efficiency improvements have been driven by the residential sector** and should continue via building renovations, as energy intensity remains high.

#### R&D remains low despite high levels of innovation expenditure



#### Governance of SOEs in the Baltic states is among the best in CEB region



#### Final energy intensity remains high



# 2. Economic Context

## 2.2. Key Transition Challenges



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### Inclusive (7.07/10)

- The three Baltic countries rank in the top of the inclusive ranking for all EBRD countries of operations. Estonia has the highest rankings of the three, followed by Latvia and then Lithuania.
- Regional inequality is widest in Latvia, as Riga dominates the domestic economy. Population decline will pose significant challenges going forward.
- At-risk-of-poverty rate is significantly higher than the EU average, indicating the need for more effective social transfers.

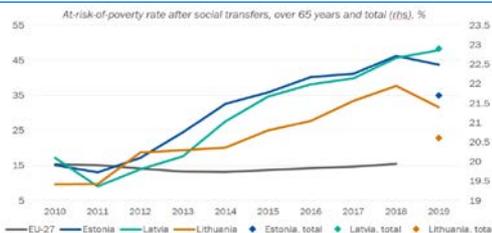
### Resilient (6.85/10)

- Baltic's banking sector is highly concentrated and majority owned by Nordic banking groups, with a number of only four key banks in each of the three countries. Credit penetration in Latvia is the lowest among Baltic peers, at 35 per cent of GDP in 2019, as the credit stock to firms has been declining since 2017.
- Asset quality is high and continues to improve. In the Baltic countries, Non-Performing Loans (NPLs) have declined steadily since 2010, but it remains relatively high at 5 per cent in Latvia.
- The capital markets remain shallow compared to EU. Against this background, the creation of a pan-Baltic integrated market is at the core of the capital markets development strategy in the region.
- The three Baltic countries' electricity grids still operate synchronously with the Russian and Belarusian systems. By 2025, the synchronisation with the continental European network is expected to be completed.

### Integrated (7.08/10)

- Thanks to European Union membership, the country is part of 44 regional trade agreements (EBRD countries average: 19), but also have a high number of non-tariff measures originating from EU or domestic regulations (Latvia: 2031, Lithuania: 1989, Estonia: 197, EBRD countries average: 900).
- In relation to the assessment of the international logistic performance, Latvia and Lithuania are below Estonia and the average of the OECD comparator countries. The domestic logistic performance is the lowest in Latvia, as intercity travel times are 47% longer than in frontier countries (compared to 31% in Estonia and 20% in Lithuania), indicating a lower quality of its transport infrastructure.
- The Energy and ICT infrastructure is above the CEB country average in the three Baltic countries, and only Slovenia is performing better.

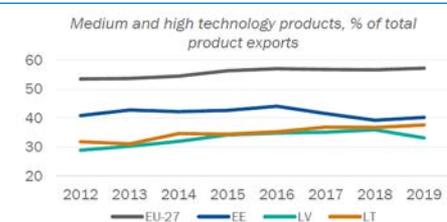
### Relative poverty remains elevated in Latvia



### The Baltics' stock market size combined is small compared to regional peers



### Exports are dominated by low-technology goods



Source: Eurostat.

Source: Federation of European Securities Exchanges, Nasdaq Baltics, Eurostat.

Source: European Innovation Scoreboard 2020

# 3. Government Priorities and Stakeholder Engagement



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## 3.1. Government Reform Priorities

Current focus on short-term crisis response measures to provide liquidity to the economy, particularly to SMEs and exporting companies, and protect the labour market through revenue support to vulnerable workers and individuals.

**Energy** – in line with the Paris Agreement, achievement of a 55% reduction of GHG emissions, a 45% share of energy produced from RES in gross final energy consumption and a 20% lower final energy consumption than the optional national target for 2020. Strengthened energy security through the synchronisation of transmission system with Central Europe and the reduction of national energy imports.

**Education and innovation** – long-term investment in human capital to increase productivity; modernisation and reform of both school and higher education systems; improvement of the labour force participation; reduction of social inequalities through access to education; increased support of innovation and entrepreneurship.

**Administrative territorial reform** – after the 2021 municipal elections, reduction of current 119 municipalities to 43, to consolidate administrative territories and improve efficiency and quality of public services.

**Healthcare** – facilitation of access to state-funded health care services and medication, reduction of waiting-lines, increasing the availability of human resources for state-funded healthcare system, and increasing the quality and effectiveness of health care.

**Rule of law** – strengthened access to justice through fostering mediation and legal aid services, strengthening of judicial policies and improved quality of court management, as well as a launch of a pilot “One Stop legal aid Advice Service”. Development of the quality and professionalism of the judiciary, which is essential for the economic development and security of the state (development of the capacity and competence of the Economic Court, reform of the further education system of justice), as it is an important aspect of increasing the presence of investors and guaranteeing their rights in Latvia.

**Anti-Money Laundering** - continued implementation of a set of financial legislative reforms and MONEYVAL recommendations to further strengthen the integrity and stability of the financial system.

## 3.2. EBRD Reform Areas Broadly Agreed with Authorities

- Given the impact of the pandemic on the Latvian economy, the Bank will support private sector recovery through private investments and policy advisory.
- Transition gaps are acute in green, competitiveness and resilience, accordingly the Bank will support Latvia's green and digital transition through direct and indirect investment as well as technical cooperation.
- The Bank will support Latvia's achievement of its NDC targets through green investments in the private sector, including financing renewable energy generation, and energy and resource efficiency improvements.
- The Bank will continue to support the growth of corporates through debt, equity and risk-sharing products, as well as continued participation in investment funds.
- Continued capital market development is a shared priority. EBRD will continue to cooperate with the Bank of Latvia and support and invest in innovative and green financial instruments.

## 3.3. Key Messages from Civil Society to EBRD

- Civil society organisations welcomed the Latvian strategy priority and increased EBRD support for the Green Economy Transition (GET), in particular for energy efficiency improvements. However, they pointed to a lack of proper understanding of the green economy, especially among public authorities in Latvia. It is crucial to educate policymakers in this regard, including with help from CSOs.
- A clear pathway and milestones are needed to reach GET targets. They need to be properly set and made clear for investors, in order to provide more predictability, clarity and improve the business climate. In particular, developments are necessary in the area of renewable energy, in order to go beyond Latvia's hydropower plant legacy and promote wind and other renewable energy sources.
- CSOs endorsed the Bank's focus on knowledge economy and digitalisation, but highlighted that proper incentives are needed for SMEs in this area. They also drew attention to the issue of economic inclusion and inequality, specifically between the capital Riga and the rest of the country. Furthermore, according to civil society improvements are necessary in the area of governance, public procurement and open data monitoring, especially for local municipalities.

# 4. Defining Latvia Country Strategy Priorities



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What needs to change? (Country Diagnostic)	Can it be changed? (Political Economy)	What can the Bank do? (Bank's additionality)	Strategic Priorities (2021-2026)	What We Want to see (Key Objectives)
<ul style="list-style-type: none"> <li>• Renewable energy accounts for 50% of gross final energy consumption (albeit mostly generated by old HPPs).</li> <li>• Higher energy intensity compared to EU average, particularly owing to the transport and residential sectors.</li> <li>• Landfilling accounts for 64% of waste, significantly higher than regional peers.</li> <li>• Circular material use rate (6.6% in 2017) below EU avg. (11.2%).</li> </ul>	<ul style="list-style-type: none"> <li>• Ambitious National Energy and Climate Plan and plans to adopt a long-term renovation strategy.</li> <li>• Heightened awareness to develop alternative sources for renewable energy other than hydro.</li> <li>• Government commitment to improve energy efficiency in legacy housing.</li> <li>• Baltic energy market interconnection initiative for an integration of the Baltic power grid with the European power grid by 2025.</li> </ul>	<ul style="list-style-type: none"> <li>• Strong track record of institutional support and financing of RE and EE in buildings.</li> <li>• Substantial experience supporting the transition to a green, low-carbon economy through policy engagement and investments. This includes greening the financial sector, industrial decarbonisation, green buildings, circular economy, promoting sustainable cities and mobility.</li> </ul>	<p><b>Support Latvia's Green Economy Transition</b></p>	<ul style="list-style-type: none"> <li>• Improved energy and resource efficiency</li> <li>• Reduced GHG emission, increased renewable energy</li> </ul>
<ul style="list-style-type: none"> <li>• Low SME productivity (30% lower than EU average) and low economic complexity compared to CEB peers.</li> <li>• Low capacity of firms to innovate and low levels of investment (private R&amp;D at 0.3% of GDP, Latvia ranks 23rd / 27 on EC Innovation Scoreboard).</li> <li>• Integration into GVCs lags behind Central European peers.</li> <li>• Limited access to diversified sources of finance ( domestic private sector credit / GDP at 36.6% compared to avg 86% in Euro area).</li> <li>• Small public bond (1.2% of GDP) and equity market capitalisation (2.7% of GDP).</li> </ul>	<ul style="list-style-type: none"> <li>• Innovative entrepreneurship a long-term priority in Latvia's Sustainable Development Strategy (e.g. supported through promotion of a risk capital sector).</li> <li>• In recent years, more appetite by firms for alternative sources of finance.</li> <li>• Strong government support for private equity and development of the pan-Baltic capital market.</li> <li>• EU Technical Support Instrument programme important anchor of capital market reform efforts.</li> </ul>	<ul style="list-style-type: none"> <li>• Capacity to support private sector competitiveness.</li> <li>• Expertise to identify and invest in innovative, high-growth companies directly through structured debt and equity products and indirectly through participating in investment funds, and through partner FIs.</li> <li>• Track record in capital markets development including through policy dialogue and technical cooperation, as well as active participation as an anchor investor</li> <li>• Expertise and dedicated financial instruments for growing the country's issuer and investor base and promoting greater capital market integration.</li> </ul>	<p><b>Foster Latvia's Knowledge Economy through More Diversified Sources of Private Finance</b></p>	<ul style="list-style-type: none"> <li>• Improved access to finance for innovation and digitalisation</li> <li>• Deepened and diversified debt and equity capital markets</li> </ul>

# 5. Activities and Results Framework

## Priority 1: Support Latvia’s Green Economy Transition

Key Objectives	Activities	Tracking Indicators (Outcomes)
Improved energy and resource efficiency	<ul style="list-style-type: none"> <li>• Finance energy efficiency improvements of the built environment.</li> <li>• Support development of circular economy through financing of recycling, waste management and technologies that reduce material demand.</li> <li>• Support Latvia’s achievement of its NDCs through Green Economy Transition investments in the private sector.</li> <li>• Support and finance sustainable urban development and regeneration projects.</li> <li>• Explore opportunities to finance private sector led water infrastructure solutions.</li> </ul>	<ul style="list-style-type: none"> <li>• Total primary energy saved (GJ/yr)</li> <li>• Materials, solid waste reduced or recycled (tonnes/yr)</li> </ul>
Reduced GHG emission, increased renewable energy	<ul style="list-style-type: none"> <li>• Support development of renewable energy with a focus on.</li> <li>• Support and finance development of sustainable, inclusive and green transport &amp; infrastructure solutions including through InvestEU (e.g. Baltic energy interconnections).</li> <li>• Finance environmental improvements and support green skills in industry and agriculture.</li> <li>• Explore options to support EBRD Green Cities in Latvia.</li> </ul>	<ul style="list-style-type: none"> <li>• Total CO2e emissions reduced (tonnes/yr)</li> </ul>

# 5. Activities and Results Framework

## Priority 2: Foster Latvia's Knowledge Economy through More Diversified Sources of Private Finance

Key Objectives	Activities	Tracking Indicators (Outcomes)
COVID-19 recovery (2021-2023)	<ul style="list-style-type: none"> <li>Deploy equity, debt and risk sharing products focused on Covid-19 recovery, to Build Back Better focusing on areas of additionality.</li> </ul>	<ul style="list-style-type: none"> <li>New instruments introduced or existing ones tailored to support resilience and Covid-19 recovery</li> </ul>
Improved access to finance for innovation and digitalisation	<ul style="list-style-type: none"> <li>Continue participation as active investor in VC/equity/property funds.</li> <li>Explore opportunities to finance innovative scale-ups (including fintechs and the IT sector) and support continued policy engagement.</li> <li>Support growth of corporates incl. their expansion abroad and corporate governance improvements, inclusion and gender equal opportunities.</li> <li>Promote acceleration of digitalisation in the corporate sector, and invest in infrastructure that supports innovation, inclusion and green digitalisation.</li> </ul>	<ul style="list-style-type: none"> <li>Total number of innovative companies supported</li> </ul>
Deepened and diversified debt and equity capital markets	<ul style="list-style-type: none"> <li>Continue policy engagement to develop the pan-Baltic capital market through leveraging Technical Support Instrument funds (e.g. dev't of a sustainable finance strategy, single index classification, CMDF, CFDARP).</li> <li>Grow investor and issuer base through financing and introduction of new and green instruments (e.g. SME listing platform, sustainability-linked bonds).</li> <li>Explore further opportunities to support, and invest in IPOs, incl. policy advisory for commercialisation and corporate governance improvements to prepare SOEs.</li> </ul>	<ul style="list-style-type: none"> <li>Pan-Baltic covered bond framework adopted and implemented, number of Pan-Baltic capital market instruments launched</li> <li>Volume of capital market transactions facilitated</li> </ul>

# 6. Mapping of International Partners Complementarity in EBRD Business Areas

EBRD BUSINESS AREAS																
		Sectors										Cross-cutting Themes				
		Industry, Commerce & Agribusiness					Sustainable Infrastructure		Financial Institutions			Strategic Initiatives				
Previous strategy period indicative annual investment/ Grants, €m (2016-2019 average unless otherwise specified)	2020	Agribusiness	ICT	Manufacturing & Services	Natural resources	Property & Tourism	Energy	Infrastructure	Banking	Non-bank Financial Institutions	Green Economy	Inclusion and Gender	Local Currency and Capital Markets	Small Business		
EU (ESIF)*	1,407	NA	€	€			€	€P			€P	€P	€P	€P		
EIB	91	119	€		€		€	€	€		€	€				
NIB	46	500					€	€			€					
EIF **	18	2		€	€									€		
CEB ***	7	150										€				
<i>EBRD</i>	34	21	€	€	€				€	€	€P		€P			

€ Area of significant investments      ● Focus mostly on private sector  
P Area of significant policy engagement      ○ Focus mostly on public sector

## Potential Areas of cooperation for the next Country Strategy Period

**Green:**  
Co-operate with authorities on the development of renewable energy; partner with the EIB on energy efficiency improvements to the built environment

**Coordinated Green Economy**  
investments with the EIB – given its strengthened focus on climate and environmental sustainability, and with the EIF – as it is expanding to themed fund products.

**Competitive:**  
Leverage RRF funding for regional development that fosters the growth of green and innovative corporates  
Finance corporates in coordination with other IFIs (NIB, EIB)

**Resilient:**  
Build on the Technical Support Instrument funded policy work, and the close collaboration with the Central Bank, Ministry of Finance, and the NIB in capital market development, including the introduction of new instruments (eg Commercial Paper).

Align Covid response measures with other locally active IFIs.

Note: IFI activity mapping based on publicly available information. Significant IFI investment defined as projects exceeding 5% of annual investment and signed from 2016.

\*Based on the EU contributions to the Latvia Country Budget for 2014 – 2020. \*\* European Investment Fund, including EIF Baltic Innovation Fund 2 and EFSI SME Guarantee Window.

\*\*\*Council of Europe Development Bank

# 7. Implementation Risks



Risks to the Strategy Implementation	Probability	Effect	Environmental and Social Implications
<ul style="list-style-type: none"> <li>Adverse impact of COVID-19 on domestic capacity to introduce innovative products and progress with greening transition.</li> </ul>			<p><b>Assessment and Management of E&amp;S Impacts:</b> Ensure that direct, indirect, cumulative and transboundary E&amp;S impacts of projects and associated facilities are appropriately assessed and mitigated in accordance with EBRD PRs. Consider environmental and social capacity building to ensure adoption of good international practice. Support clients to strengthen E&amp;S management capacity and disclose information.</p>
<ul style="list-style-type: none"> <li>Preponderance of grant and soft loans could limit the ability to leverage debt finance.</li> </ul>			<p><b>Labour and Working Conditions:</b> Ensure that clients' HR policies and labour practices comply with EBRD requirements, particularly in respect to labour terms and conditions; contractor management; potential discrimination in the workplace, promotion of equal opportunities and managing impacts of large scale retrenchment and preventing potential discrimination towards minority and other vulnerable groups.</p>
<ul style="list-style-type: none"> <li>State financed (COVID-19 crisis response) equity and debt funds could crowd out private sector equity funds and debt financing in the corporate sector</li> </ul>			<p><b>Resource Efficiency and Pollution Prevention and Control:</b> Support capacity building initiatives in relevant sectors; ensuring that alternatives are considered to identify investments that support compliance with EU standards and EU Best Available Techniques (BAT), transition to a low carbon and resource efficient economy, strengthen resilience to climate change and promote circular economy. Support clients to comply with relevant EU Directives and improve the efficiency of industry-specific processes in line with EU Best Available Techniques.</p> <p><b>Health and Safety:</b> Improve occupational and community health and safety with specific focus on activities which are associated with common accidents reported on Bank's projects. Additional emphasis and TC support will be placed on road safety by requiring road safety audits, capacity building and raising awareness within communities at risk.</p> <p><b>Land Acquisition, Involuntary Resettlement and Economic Displacement:</b> Ensure that any projects requiring acquisition of land comply with compensation and livelihood restoration requirements of the Bank, with particular attention on informal land users and vulnerable groups.</p> <p><b>Biodiversity Conservation and Sustainable Management of Living Natural Resources:</b> Support capacity building initiatives for robust biodiversity assessments and mitigation approaches that will ensure that species and habitats of conservation importance are protected where projects could encroach upon nature protected areas, sensitive flora, fauna, ecosystem services and/or legally protected and internationally recognised areas of biodiversity value.</p> <p><b>Cultural Heritage:</b> Work with clients to ensure appropriate assessment processes to identify and consult with key stakeholders to protect cultural heritage.</p> <p><b>Financial Intermediaries:</b> Ensure that FI partners have adequate E&amp;S capacity and risk management procedures in place.</p> <p><b>Stakeholder engagement:</b> Support clients in developing and implementing stakeholder engagement plans and ensure transparent participatory consultation is carried out as part of local permitting and ESIA's.</p>

High Medium Low

# 8. Donor Co-Financing Assessment



## 8.1. Needs Assessment for the New Country Strategy Period

Some funding will be needed to achieve the strategic objectives of the Country Strategy, including for:

- Policy dialogue activities, including potential engagements in further capital market development and integration, as well as in renewable energy (e.g. regulatory support for auctions)
- Project preparation and implementation support for investments in energy efficiency and other green initiatives
- Guarantees offered under the InvestEU programme to facilitate new investment opportunities

## 8.2. Potential Sources of Donor Funds

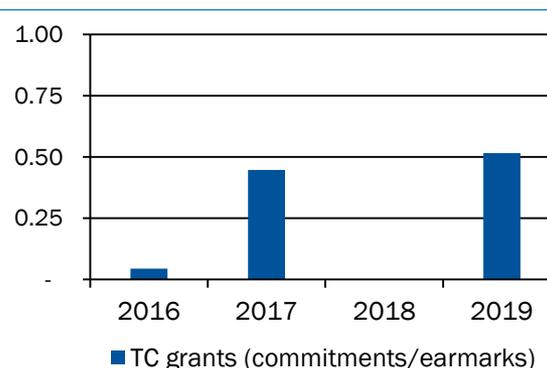
- As an advanced transition country, **Latvia** is expected to provide its own financing to help support investments and policy engagement, both in Latvia as well as in other countries of operation
- The **EU** is an important source of funding in Latvia, most notably via monies allocated through **European Structural and Investment Funds**, the **Recovery and Resilience Facility**, and the **Just Transition Mechanism**. These could include opportunities for:
  - Blended finance, including through the use of guarantees, under the proposed **InvestEU** programme;
  - Co-financing in the context of the **Recovery and Resilience Facility**;
  - Funding for engagements promoting structural reforms, including capital markets development, under the proposed **Technical Support Instrument**;
  - Funding for initiatives promoting research and innovation under the proposal for **Horizon Europe**;
  - Access to TC funds from the EU's sectoral programmes, including in support of investments backed up by **InvestEU** guarantees.
- Limited resources may also be available from the **Shareholder Special Fund (SSF)**.

### Selected Affordability Indicators

		EBRD regional percentile rank <sup>1</sup>
GDP per capita (PPP, current. \$) <sup>2</sup>	32,204	76 <sup>th</sup>
ODA Country <sup>3</sup>	No	N/A

1. Simple percentile rank reported as the share of EBRD economies that are represented below Latvia.  
 2. Source: WDI (2019 or most recent year)  
 3. Source: OECD (2018)  
 4. 2016-2019 TC data is based on earmarks at the project level.  
 5. Based on the primary Transition Quality of TC grants earmarked in 2018 and 2019.

### Donor finance during last strategy (€m)<sup>4</sup>



### Use of grants in 2018-2019<sup>5</sup>



# Annexes

PUBLIC



**European Bank**  
for Reconstruction and Development



*The Republic of Latvia's commitment to and application of principles set out in Article 1 of the Agreement Establishing the Bank has continued over the period since the adoption of the previous Country Strategy. The constitutional and legislative framework for a pluralistic parliamentary democracy is in place. The separation of powers and checks and balances in the political system, and guarantees for human rights and fundamental freedoms are largely in line with international and European standards. The media are pluralistic and competitive and civil society operates independently. Elections are conducted in a manner deemed by the OSCE to be free and in line with international standards. Latvia has been a member of the European Union since 2004.*

In the period since the adoption of the previous Strategy, Latvia has made further progress in all areas of democratic reform building on the sustained efforts towards consolidating a multiparty democracy. At the same time, some challenges remain in the area of rule of law and minorities.

## **Free Elections and Representative Government**

Latvia is a parliamentary republic, with the legislative power lying with the 100-seat parliament, which approves the government and elects the president. Effective checks and balances amongst the branches of power are in place. The legislature is independent and has powers to hold the government to account. Key political decisions are made by elected officials, who are free of undemocratic constraints on their powers to govern effectively.

The electoral legal framework, which was amended since the 2014 parliamentary elections, generally provides a sound basis for the conduct of democratic elections, as assessed by the OSCE's Office for Democratic Institutions and Human Rights (OSCE/ODIHR). The last general elections took place in October 2018. The elections were competitive and voters were given a diverse choice of political alternatives. The campaign was conducted in an environment characterised by a general respect for the freedom of expression, association and assembly, despite remaining

divisions along ethnic and linguistic lines. The voting process was well managed and the election administration performed its duties in a professional and timely manner. Voters were able to use a range of tools to exercise their right to vote and special efforts were made to support voters with disabilities. At the same time, the OSCE/ODIHR offered several recommendations related to the inclusivity of the electoral process, including the inclusion of female candidates and voters from ethnic minorities. The OSCE/ODIHR report also highlighted that language and identity issues continue to create a divisive political landscape.<sup>1</sup>

## **Civil Society, Media and Participation**

The Constitution enshrines the right to form associations, political parties and trade unions. Civil society is diverse and independent, and there are multiple channels of civic and political participation. The freedom to form political parties is implemented in practice and is highlighted by the existence of a significant opposition, able to campaign freely and oppose government initiatives. Political parties, however, are divided along ethnic lines, and parties representing Russian speakers are usually excluded from governing coalitions at national level.

The media environment is pluralistic. It includes public and private broadcasters and offers citizens a wide range of political views. At the same time, media ownership continues to be concentrated and transparency is limited. While censorship is outlawed, defamation remains a criminal offence.<sup>2</sup>

## **Rule of Law and Access to Justice**

Legislative and institutional safeguards for the supremacy of law and independence of the judiciary are in place. The Constitution guarantees everyone the right to a fair trial and citizens are free from arbitrary arrest or detention. The government and citizens are equally subject to the law. While improvements were achieved in the reform of the judiciary in the period since the adoption of the last Strategy, it still faces low levels of trust by the public (45%).<sup>3</sup> Concerns have been raised, in particular, regarding the efficiency of court management and quality of judicial services.

<sup>1</sup> ODIHR (2019): *Parliamentary Elections 6 October 2018 Election Assessment Mission Final Report pp.1-3 and pp. 21-24.*

<sup>2</sup> ODIHR (2019): *Parliamentary Elections 6 October 2018 Election Assessment Mission Final Report pp. 16-18.*

<sup>3</sup> Freedom House (2020): *Nations in Transit 2020*



Transparency International's 2020 Corruption Perceptions Index ranks Latvia 42<sup>nd</sup> out of 180 countries assessed.<sup>4</sup> Latvia's legal and institutional framework to prevent and address corruption has been further strengthened in the period since the adoption of the last Strategy and further work is ongoing. The latest Council of Europe Group of States against Corruption (GRECO) report highlighted areas for improvement to increasing the integrity of central government officials in top executive functions and increasing the transparency of law enforcement agencies.<sup>5</sup>

## Civil and Political Rights

The fundamental freedoms of speech, information, religion, conscience, movement, association, assembly and private property are fully guaranteed in the Constitution and upheld in practice.

The last United Nations Universal Periodic Review (UPR) assessed Latvia in 2016. Regarding remaining weaknesses, the priority recommendations concerned gender equality, the inclusion of vulnerable groups into society, including women, children and LGBTI people.<sup>6</sup> The protection of gender equality in Latvian legislation has improved significantly in the period since the last Strategy, however, with the World Bank listing Latvia among the top five economies in the 2019 Women, Business and the Law index.<sup>7</sup>

Latvia has a sizeable Russian-speaking minority and around 11 per cent of the population is classified as "non-citizens". According to the United Nations Human Rights Council, Latvia has made good progress in reducing the number of "non-citizens" since the 1990s. However, concerns have been raised since the adoption of amendments to the education law in 2018 that may significantly limit education in minority languages in high schools.<sup>8</sup>

Constitutional guarantees against harassment, intimidation and torture are in place and upheld in practice.

<sup>4</sup> Transparency International (2020): *Corruption Perceptions Index 2020*

<sup>5</sup> GRECO (2018): *Fifth Evaluation Round Evaluation Report Latvia June 2018 p.4 and p.50.*

<sup>6</sup> CoE (2016): *Report of the Commissioner for Human Rights of the Council of Europe, following his visit to Latvia 5-9 September 2016.*

<sup>7</sup> World Bank Group (2019): *Women, Business and the Law 2019*

<sup>8</sup> Latvian Human Rights Committee: *Minority education attached in Latvia: 2018 amendments to education laws 14 September 2018.*