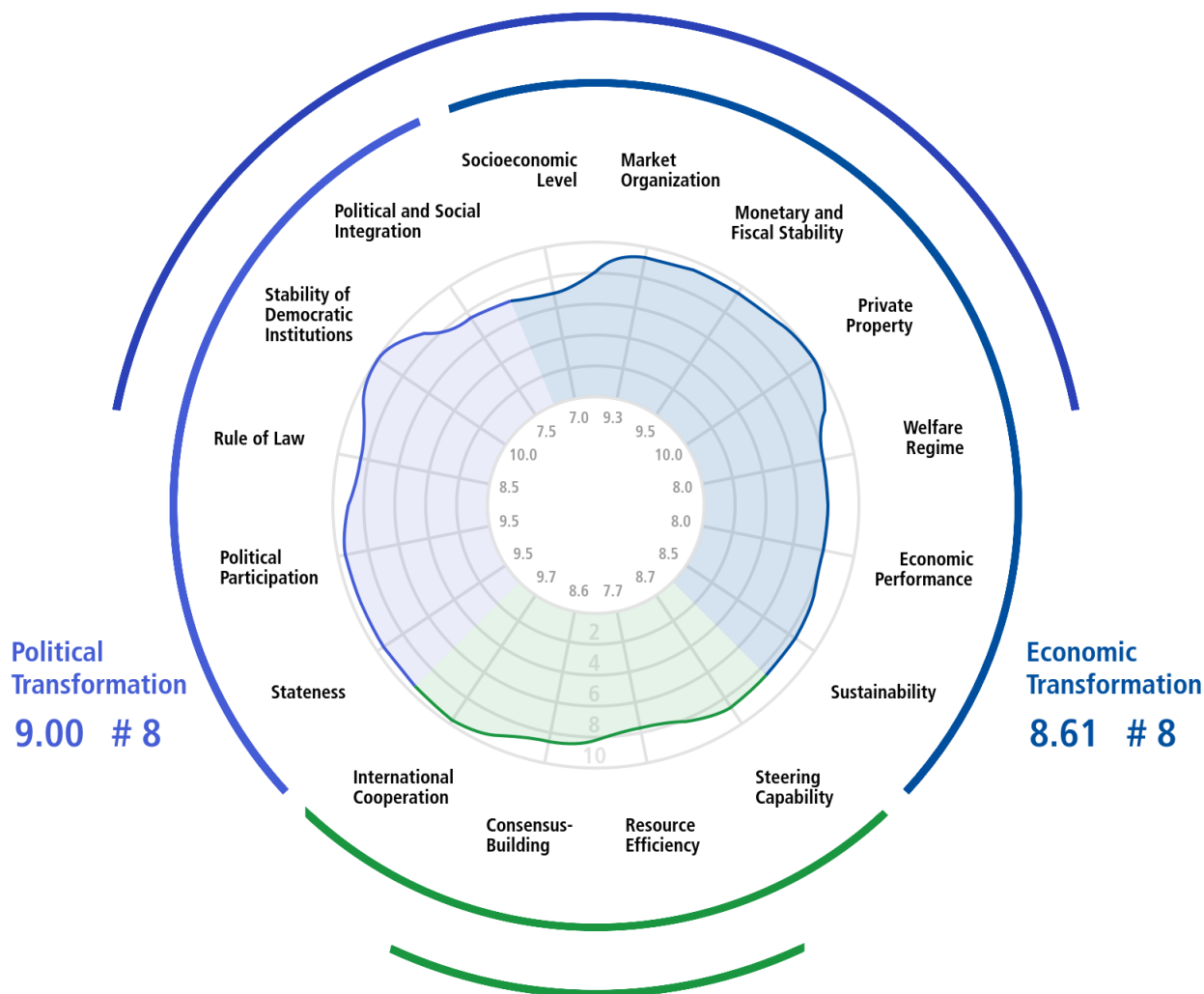


Latvia

Status Index

8.80 # 7

on 1-10 scale out of 137



Political Transformation
9.00 # 8

Economic Transformation
8.61 # 8

Governance Index

7.11 # 6

on 1-10 scale out of 137

This report is part of the **Bertelsmann Stiftung's Transformation Index (BTI) 2022**. It covers the period from February 1, 2019 to January 31, 2021. The BTI assesses the transformation toward democracy and a market economy as well as the quality of governance in 137 countries. More on the BTI at <https://www.bti-project.org>.

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Key Indicators

Population	M	1.9	HDI	0.866	GDP p.c., PPP \$	32019
Pop. growth ¹	% p.a.	-0.6	HDI rank of 189	37	Gini Index	35.1
Life expectancy	years	75.2	UN Education Index	0.883	Poverty ³	% 0.9
Urban population	%	68.3	Gender inequality ²	0.176	Aid per capita \$	-

Sources (as of December 2021): The World Bank, World Development Indicators 2021 | UNDP, Human Development Report 2020. Footnotes: (1) Average annual growth rate. (2) Gender Inequality Index (GII). (3) Percentage of population living on less than \$3.20 a day at 2011 international prices.

Executive Summary

A new Latvian government took office in January 2019, after a record-breaking three months of political negotiations following the October 2018 election. It remains in office in early 2021, but is increasingly marked by bickering between the unwieldy five coalition partners that include radical right nationalists, conservatives, populists and liberals.

Prime Minister Krisjanis Karins looked jaded after just one year in the post and rumors swirled that he was ready to resign after he had demanded the resignation of the populist KPV LV's ("Who Owns the State?") economics minister, Ralfs Nemiro. Indeed, KPV LV openly debated leaving the government coalition, which would have caused the latter's collapse. However, as the COVID-19 pandemic swept Europe, reaching Latvia, the KPV LV stated that they would remain in government for the sake of the nation.

Latvian state, local government institutions, and businesses quickly adapted to the COVID-19 "new normal." Quick, extensive and affordable fixed-line and 4G networks across the country enabled people to work from home and schools to teach students online. The ministry of education purchased tablets and laptops for poorer families and created new educational television programming to back up the school curriculum. A state of emergency in the spring was replaced by a summer of near normality. However, the tourism and hospitality industry suffered in the summer as tourists from the "Baltic bubble" created by the three Baltic states, and eventually extended to Finland and beyond, did not compensate for the usual tourist flows packing the Old Town of Riga and the Jurmala beach resort.

Politics continued as usual and the parliament, using a new e-Saeima application, continued debating and voting on laws, in particular the Administrative Territorial Reform, that cut the number of local authorities and municipalities from 119 to 42. An early election in the Riga municipality was delayed twice but eventually took place in August 2019. After more than a decade of holding the mayor's office, the center-left pro-Russian speaker Harmony party, which

had been marred by corruption and graft in recent years, was replaced by a center-right modernizing coalition under the liberal mayor, Martins Stakis, of the progressive For Development/For! party alliance.

An equally important development saw Latvia fundamentally reform governance of the financial sector during 2019 and thus avoided being “gray listed” by the Council of Europe’s MONEYVAL Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism in their report on Latvia in 2020.

Some things, however, have remained unchanged. The Rail Baltica project, a €5 billion multiyear regional infrastructure project, primarily financed by the European Union, to construct an 870 km electric passenger and freight railway that will connect the Baltic states to Western Europe, made slow progress while the three Baltic states continued to bicker about the project’s management, construction and routes. Nevertheless, preliminary engineering work continued, albeit at a slow pace.

History and Characteristics of Transformation

Over the last 800 years, Latvian territories have been a part of the Swedish, Polish and Russian empires. However, throughout these different eras of empire the effective governors of Latvia remained the Baltic Germans, who had first conquered Latvian territory in crusades against the pagans of Northern Europe in the early thirteenth century.

The modern Latvian nation emerged in the mid-nineteenth century as a result of Tsarist peasant emancipation, urban industrialization and the subsequent emergence, a generation later, of an educated Latvian middle class. An independent Latvia was established in the years following the end of the First World War, as the Tsarist empire collapsed, and a wave of new nation-states were formed all across East and Central Europe. The new Latvian state adopted a parliamentary constitution in 1922, although this failed to provide solidity – 13 government coalitions were formed by 1934. This political instability, accompanied by an economic downturn in the early 1930s, led to a peaceful coup in 1934, and the benign dictatorship of Karlis Ulmanis. He had been the dominant figure of inter-war Latvia, having served as Latvia’s first prime minister and as the head of the committee that declared Latvia’s independence in 1918. These years of dictatorship are remembered with great popular affection, largely because of the brutality and violence of the following Soviet and German occupations during the Second World War, and Latvia’s subsequent forced annexation into the Soviet Union.

Soviet occupation after 1945 saw the collectivization of agriculture, an increased pace of industrialization and sharp demographic change. The large German and Jewish minorities that had long lived in the Latvian lands were largely eradicated by the Holocaust and the dislocations of the Second World War, while many Latvians (largely the middle-class elite) fled west or were deported to Siberia. The post-1945 era saw a large influx of Russian speakers. The Soviet regime

floundered in the 1980s as falling energy prices threatened economic stability, and the democratic reforms of Mikhail Gorbachev allowed the forces of Latvian nationalism to organize and compete in free elections. Three major factions emerged in the late 1980s: the radical nationalists of the Latvian National Independence Movement, the more moderate and inclusive Latvian Popular Front (LPF) and the anti-reform Interfront movement, an amalgamation of pro-Soviet forces primarily composed of ethnic Russian Latvian Communist Party members and Soviet officers who had settled in Latvia after their retirement. The contemporary Latvian party system still largely reflects this order, with radical Latvian nationalist, moderate centrist nationalist and left-leaning pro-Russian-speaker parties in the Latvian parliament. The LPF won a majority in the 1989 elections to the USSR Congress of People's Deputies, and again in the 1990 elections to the Latvian Supreme Soviet, which then voted to restore independence in May 1990, leading to the establishment of parallel Latvian and Soviet government structures. De facto independence was achieved following the failed August 1991 anti-Gorbachev coup in Moscow.

At this point, Latvia faced a radical political and economic transition. The political transition to a multiparty democracy began with the re-adoption of the 1922 constitution and the first post-Soviet parliamentary elections in 1993. Since then, Latvia has had seven parliamentary elections, all of which have been judged as free and fair by international observers. However, Latvia's extreme multipartyism has meant that government stability has been hard to come by, with governments lasting, on average, little over a year. The other major political challenges have been an agreement on the withdrawal of Russian forces from Latvian territory (reached in 1994), internationally acceptable rules on the naturalization of Russian-speaking Soviet-era immigrants and accession to the major Euro-Atlantic organizations (Latvia joined the European Union and NATO in 2004).

Reforms to the economy have been equally challenging. Many of Latvia's largest industrial enterprises, such as the electronics manufacturer VEF and the minibus producer RAF, went bankrupt, while others were privatized or returned to previous owners. Unemployment was high in the early 1990s, and the quality of public services fell as government receipts collapsed. Two currency reforms (first instituting the Latvian ruble, then the Latvian lats) and rampant inflation in the early 1990s, as well as the collapse of several commercial banks in the mid-1990s, wiped out people's savings. The early-2000s saw Latvia experience rapid economic growth, albeit primarily as a result of a construction and consumer-spending boom funded by cheap credit, especially after accession to the European Union and NATO in 2004. However, the Latvian economy fell back to earth in late 2008 as Latvia's largest domestically owned bank, Parex, collapsed and the government turned to an IMF-led international consortium for a financial bailout. A dramatic recession – the deepest in the world – followed, with Latvia experiencing a cumulative GDP decline of 23.9%. Modest growth followed stabilization of the economy in 2010 and, in October of that year, the Latvian electorate surprisingly returned the Valdis Dombrovskis government – which had introduced sharp spending cuts in 2009 and 2010 – to power. Dombrovskis was again elected after the snap election of September 2011, called after the then president, Valdis Zatlers, complained that parliament was controlled by a number of oligarchs that threatened the very basis of democracy in Latvia. The subsequent election saw the vote for two of the three oligarchs collapse, while the party of the third oligarch (the

Green/Farmers' Union) was pushed into parliamentary opposition with a reduced number of parliamentary deputies.

However, the 2014 parliamentary election saw the Green/Farmers' Union increase their share of the vote and a Green/Farmers Union parliamentary deputy, Raimonds Vejonis, was elected state president the following summer. In February 2016, after the government of the Unity party's Laimdota Straujuma fell, the Green/Farmers' Union seized the opportunity to take the prime minister's office for its own candidate, Maris Kucinskis.

The BTI combines text analysis and numerical assessments. The score for each question is provided below its respective title. The scale ranges from 1 (worst) to 10 (best).

Transformation Status

I. Political Transformation

1 | Stateness

The Latvian state's monopoly on the use of force is uncontested.

Question
Score

Monopoly on the
use of force

10



The Latvian state has been home to substantial ethnic minority groups throughout its 100-year history. The large Baltic-German community, which represented the largest ethnic minority in the inter-war period, left Latvia shortly before and during the Second World War. Latvian refugees fleeing to the West and Soviet deportations further depleted the population. An intensive Russification process saw 700,000 Russian speakers (approximately one-third of the Latvian population) settle in Latvia in the postwar decades, and Russian speakers remain the largest minority in the country. By 1989 the Soviet census revealed that Latvians represented just 52% of the population of the Latvian Soviet Socialist Republic.

State identity

8



This precarious ethnic Latvian demographic situation motivated Latvia's politicians to adopt a 1994 citizenship law that denied automatic citizenship to those Russian speakers and their descendants who had moved to Latvia during the Soviet era. The law also introduced restrictive language laws protecting the status of Latvian in public life.

While the citizenship law has been liberalized and, by the late 1990s, anyone meeting the country's residency and language proficiency criteria could become a naturalized citizen, the state still protects the status of the Latvian language. In recent years the government has passed laws that will see Russian-language secondary schools transition to teaching in Latvian, effectively ending the Russian-

language school system in the 2021/2022 academic year. In 2019 the Latvian parliament passed legislation ensuring that, as of 2020, children born to non-citizens in Latvia will not inherit their parents' "non-citizen" status. Non-citizens cannot vote in national, local or European elections, and are barred from holding certain public posts, but otherwise enjoy full economic and social rights and protections. In 2020, Latvia had 213,000 resident non-citizens and a total population of approximately 1.9 million people.

Latvia's Russian-speaking population has protested against the restrictions on the use of Russian in the public sphere and a polarizing February 2012 referendum, supported by the biggest pro-Russian speaker party in Latvia, Harmony, on whether Russian should be recognized as Latvia's second official language saw particularly heated debates. There have also been public protests attempting to "Save Russian Schools" in Latvia. However, these are challenges to certain public policies rather than challenges to the legitimacy of the Latvian state.

Latvia has three major Christian denominations, Lutheran, Catholic and Orthodox. Latvia's 1922 constitution, the Satversme, separates the church and state. Nevertheless, church leaders are active participants in public debate, typically criticizing the encroachment of "Western liberal" ideas – primarily the growing social and legislative acceptance of same-sex relationships, as well as rights for women – and speaking out against economic inequality. In January 2021 church leaders supported an initiative from the governing coalition National Alliance party that aims to amend the constitution to define a family as being composed of a man and woman. This is in response to a November 2020 Constitutional Court ruling that households composed of same-sex partners should be recognized as families and that the state has an obligation to protect and financially support these families.

The state delivers all basic and essential services.

However, since 2016 there has been increased public debate over the quality of service provision. As a result, successive governments have committed to increasing the percentage of public spending on education, family benefits and, especially health care. A major reform of local government, passed into law in 2020, targeted improved provision of services in small towns, villages and rural areas through consolidation of schools and health care providers. This merging of local governments was triggered by an ongoing demographic decline in Latvia's rural regions.

European Union structural and cohesion funds have upgraded Latvia's core road infrastructure and the overwhelming majority of inhabited territories in the country are connected to broadband and wireless internet. Greater future investment is planned in rail transport and green technologies.

Due to the COVID-19 pandemic and the strain this had on the health care system, some health care services were suspended in spring 2020 during the first wave of the pandemic and also from December 2020, when a state of emergency was

No interference of religious dogmas

10



1

Basic administration

10



1

declared in the sector. This meant prioritizing COVID-19 patients and emergency patients and the provision of acute care in hospitals. Outpatient health care services were provided, as well as oncological and life-saving surgeries, as well as surgeries without which the patient was at risk of developing a disability. However, planned surgeries were not available.

In previous years many public services, such as submitting annual tax declarations were digitalized and the pandemic led individuals to increasingly utilize these digital options. For example, the number of documents signed by electronic signature doubled in 2020, compared with the previous year.

2 | Political Participation

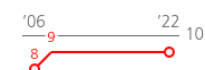
Latvia's three regular elections – European, national parliamentary and local government – are free and fair. The 2018 parliamentary election (the ninth since the renewal of independence) saw 16 parties compete for the 100 seats in the parliament. Seven passed the 5% threshold needed to win seats in parliament. In contrast to the 2014 election (when courts found several candidates guilty of buying votes in exchange for small cash payments), there were no irregularities in the process. The 2019 European Parliament election similarly passed without incident, although the August 2020 municipal snap election in the capital city of Riga was marred by three isolated incidents of more than 600 unsealed, and therefore invalidated, ballots found in ballot boxes at three polling stations. A court ordered invalidated ballots to be counted, but this did not impact the election result. There were also concerns regarding the impartiality of the Riga municipal election commission, following leaked reports that the head of the commission had benefited from generous consultancy payments from the municipal public transport service.

The Central Election Commission, which organizes and oversees elections in Latvia, is an independent organization with an experienced management team and sufficient resources to fulfill its core functions. In 2019 the chairman of the commission, who had held the post for more than 20 years, was not re-elected to the post by the Latvian parliament. A number of parliamentary deputies claimed that it was important to refresh the committee's leadership.

The extraordinary Riga city council election in 2020 was postponed twice due to the COVID-19 pandemic. On both occasions, this was done via a legislative amendment adopted in the Saeima (Latvian parliament). Safety of voters and election committee staff were cited as justification for the postponement. When the election was held on August 29, 2020, people were requested but not compelled to use face masks, maintain social distancing and use their own pen to avoid risk of infection.

Free and fair elections

9



1

There are no individuals or groups holding veto powers over democratically elected representatives.

For two decades, from the late 1990s onwards, there were long-standing concerns that three powerful Latvian “oligarchs” held undue influence over the Latvian political system. Indeed, a 2011 referendum on the recall of parliament called by the then president of Latvia, Valdis Zatlers, was based on concerns that these three oligarchs had accrued a disproportionate influence over parliament and the government. The resulting September 2011 election saw support for two of the oligarchs’ political parties collapse (and two parties subsequently folded). The third “oligarch” party (the Green/Farmers’ Union, a political vehicle for Aivars Lembergs, the mayor of Ventspils) was re-elected, and in 2021 was still represented in parliament, albeit not as part of the governing coalition.

Substantial reforms to party financing laws, reducing the size of private donations to parties and substantially increasing public financing, as well as limiting the scope of election advertising have further weakened the political influence of wealthy benefactors.

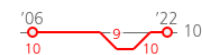
There are no formal restrictions on association or assembly. On the few occasions that local governments have banned marches – such as the Riga municipality’s refusal to allow gay pride and far-right nationalist parades – the courts have consistently overturned these bans and the marches have gone ahead.

In December 2020 the Latvian government declared a state of emergency (which was later extended into the first months of 2021), imposing a curfew on Friday and Saturday nights, between 22:00 and 05:00 the next day. Organized meetings, pickets and marches were still permitted outdoors, but with a maximum attendance of 25 people, who were expected to observe any pandemic safety measures in place. The restrictions were legal, necessary and proportionate in light of a rapidly increasing COVID-19 infection rate and fears that the Latvian health system might be overwhelmed.

An anti-government/COVID-19-denier protest march was organized in the heart of Riga in December 2020. The rowdy protest exceeded the 25-person limit by several hundred and the largely male, aggressive marchers, many of whom ignored instructions to wear face masks and socially distance, attempted to provoke both media and police. In the following weeks, the same organizers traveled across Latvia, putting on smaller, but equally belligerent, protests in towns and cities.

Effective power to govern

10



1

Association / assembly rights

10



1

The Latvian constitution guarantees freedom of expression, and the Latvian court system, particularly the Constitutional Court, has actively defended this right. There is no censorship.

Recent years have seen a polarization between the mainstream media and some politicians and their supporters, who accuse the media of “fake news” and acting in cahoots with government officials. The independent Re:Baltica investigative journalism organization, whose leading reporters represent liberal values, have found themselves harassed on social media and even in their own offices.

Oversight of the media is deeply politicized. The National Electronic Mass Media Council (NEPLP), which supervises radio, TV, the printed press and online media, is elected by parliament and composed of political party representatives. The council works in a highly politicized climate, and parliamentarians and the media, including the Latvian Journalists Association, regularly criticize individual members of the board.

The public media remains underfinanced and its management is regularly accused of bias by both the government and the political opposition. In fact, journalists in the public media, especially public radio, are among the most objective in Latvia, producing independent coverage of the political system, investigating corruption and incompetence, and acting as a check on political power.

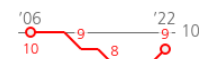
The privately owned print and electronic media was facing financial challenges before the COVID-19 pandemic. Latvia’s two largest independent television channels, and their news organizations, merged in late 2019, and one of the last remaining printed newspapers switched to an online-only presence in 2020. In 2020 and 2021 the government provided extra public financing for print and digital commercial media organizations to compensate for falling advertising revenues during the pandemic.

A significant change in the media environment was caused by the December 2020 government decision to increase funding to public media so that it could abandon its financial reliance on advertising. This decision means additional hours for quality content on public media, while also providing new opportunities for commercial media.

In December 2020 two individuals were detained after repeated publications of fake news about COVID-19 on social media. The criminal case is defined as hooliganism with risk to public safety, and guilty verdicts could result in two years imprisonment.

Freedom of expression

9



1

3 | Rule of Law

The key democratic institutions in Latvia are the 100-member parliament (Saeima), the head of state (the president), the executive (the prime minister and cabinet of ministers) and the court system, particularly the Constitutional Court. Political power is separated and balanced between these institutions.

The parliament is elected by proportional representation every four years and is Latvia's central legislative actor. However, it suffers from a deficit of policy planning and evaluation capacity, with a parliamentary research service only being set up in 2017 with a small number of junior researchers. Parliamentarians are also hampered in carrying out their work by having only a small budget for assistants.

Parliament elects the state president in an open ballot (since 2019), who, in the case of a political party affiliation, resigns their party membership. Presidents regularly return laws to parliament and also initiate legislation. The president is charged with formally nominating a candidate to form a government that is then voted on by the parliament.

The political executive (the cabinet of ministers) has strengthened as political parties have created more effective party organizations and tightened internal discipline, leading to more harmonious cooperation between ministers from the same parties. As a result, recent prime ministers have typically spent two years in office, an increase on the one-year average in the 1990s and early 2000s. However, the prime minister is a much weaker figure than in other European democracies, effectively controlling only his own party's ministerial portfolios, while other coalition parties maintain effective control of their own ministerial fiefdoms. The Cooperation Council's (formerly the coalition council) Monday meetings, where the major political figures of the coalition parties gather every week, enable political coordination.

The Constitutional Court remains an important check on both the executive and the legislature, regularly returning laws when it adjudges them to be unconstitutional. For example, in November 2020 the court ruled that the state has an obligation to protect the family of same-sex partners in issues pertaining to labor law. The National Alliance, a radical right party that forms part of the governing coalition, reacted by proposing a revision to the constitution explicitly stating that a family in Latvia is composed of a man and a woman.

A state of emergency was twice declared in Latvia during 2020 in response to the COVID-19 pandemic. The state of emergency was enacted in accordance with the constitution and other legislative acts. Both parliament, the executive and courts rapidly switched to online formats for meetings, debates and voting, and there was minimal disruption to the political process.

Separation of powers

9



1

In April 2020, the parliament amended the law on the state of emergency to provide for an unlimited number of extensions of the emergency situation by the government for up to three months. Initial legislation provided for the emergency situation to be extended only once, but the government successfully argued that the change was needed in the uncertainty of the COVID-19 pandemic.

Latvia has an independent judiciary and judges are a distinct and differentiated profession. The Supreme Court has the highest public trust ratings (51% in 2020) of Latvia's main state institutions. Channels of appeal work efficiently. Senior judges are appointed by parliament, but there is little to no politicization of appointments.

The biggest threat to the independence of the judiciary remains judicial corruption. Major cases prosecuted against high-profile political and business figures are often drawn out over many years (12 years in the case against Aivars Lembergs, regarded as an “oligarch” since the mid-1990s) and frequently end with acquittal or minor sentences.

In June 2020, parliament passed legislation creating a specialized economic affairs court that would focus on commercial cases as well as financial crimes.

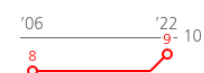
Evidence for the autonomy of the judiciary can be seen in the November 2020 ruling of the Constitutional Court that the state must protect all families, including same-sex couples. In 2020 the Constitutional Court also ruled that several social allowance benefits violated the constitution.

There has long been a strong public perception that public officeholders in Latvia are rarely prosecuted for abusing their positions. Two political parties – Who Owns the State? and the New Conservative Party – made this corruption discourse central to their 2018 parliamentary election campaigns and won more than a third of parliamentary seats. However, both parties have seen prominent party members prosecuted by the legal authorities for alleged abuse of power and, combined with no substantial change in the speed or scope of officeholder prosecutions, both parties have lost their anti-corruption luster.

The best example of the ongoing struggle that Latvian legal and security authorities have in winning major corruption cases is Aivars Lembergs, the long-standing mayor of the wealthy port and transport hub city of Ventspils and one of Latvia's three formerly influential “oligarchs.” Lembergs was indicted with large-scale bribery, money laundering and corruption charges in 2006 and later that year was briefly detained and then placed under house arrest amid allegations from the prosecution that he was interfering with the case and hindering further investigation. Since then, there have been a number of breaks in the court process due to illness (of the accused, his lawyers, the judges, etc.) and other technical issues. This has demonstrated the ease with which the Latvian judicial system can be delayed and manipulated. As a result, some legal disputes involving international actors have been resolved in British and other jurisdictional courts, due to international actors' skepticism toward having their cases heard fairly in Latvia.

Independent judiciary

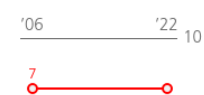
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Prosecution of office abuse

7



1

Latvia protects all core human rights, including the right to life and security, while also prohibiting torture and cruel or inhumane treatment or punishment. There is no evidence of any form of discrimination in the legal system. Latvia has an independent, active and vocal Ombudsman's Office and Latvians also have recourse to the office of the European ombudsman.

The Latvian Ombudsman's Office regularly defends individual and group rights against the state. In recent years the ombudsman has argued for a fairer and more generous social insurance system and a higher minimum wage. It has also called for more racism awareness training in Latvian schools and has stood up for sexual and other minorities.

Families where partners cohabit but are unmarried, including same-sex couples (who cannot marry or register partnerships in Latvia), are disadvantaged in terms of access to health care, inheritance rights and other similar issues. There has been little political will to revise legislation. However, the Latvian Constitutional Court, which ensures that laws and administrative practices do not conflict with the constitution, has recently overturned several major parliamentary acts. The court's November 2020 ruling that same-sex couples have the right to paid paternal leave (ordering parliament to amend the law by June 1, 2022) was heavily criticized by the more conservative segment of Latvia's political spectrum, which proposed to amend the constitution so that the state does not need to recognize same-sex partnerships. The court ruling has also opened a discussion on the legal challenges faced by cohabiting couples.

4 | Stability of Democratic Institutions

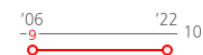
The best indicator of the strength and rigor of Latvia's institutions is the country's membership of every major western international institution, including the OECD and the European Union, as well as Latvia's adoption of the Euro currency in 2014.

The constitution and other laws grant a mandate to parliament, the executive, national and municipal bureaucracies, and judicial institutions to take decisions and implement them. Checks and balances are in place, and the state president and the Constitutional Court regularly return laws to parliament and the executive.

Autonomous policy formulation and analysis capabilities have been identified as a weak point in the political system. Both parliament and individual ministries have moved to develop analytical units and a productivity think-tank has been established, as well as a fiscal discipline council, which has an international composition and reviews budget procedures and provides advice to the government. These institutions have improved the policy process.

Civil rights

9



1

Performance of democratic institutions

10



1

All major political organizations and actors accept the legitimacy of Latvia's democratic institutions.

Commitment to democratic institutions

10



5 | Political and Social Integration

Latvia's dominant political cleavage remains ethnicity. The Russian-speaking population, which represents between one-quarter and one-third of the voting population, overwhelmingly supports political parties prioritizing the interests of Russian speakers. Since 2015 this has been the Harmony party. However, despite winning the largest share of the vote in the last three parliamentary elections, Harmony has never been a part of a governing coalition in Latvia. There is a high level of polarization between the Russian-speaking and ethnic Latvian parties (and voters).

Party system

6



Government coalitions comprise parties from the majority “Latvian” part of the political spectrum. There have been three core ideological groupings of “Latvian” parties in the 21st century: (i) radical right nationalists; (ii) technocratic nationalists (both rural and urban based); and (iii) centrist liberals (both economically liberal and value-based liberal). In recent years a fourth group of pure anti-government populist parties has emerged, although they are organizationally more fragile than the other groups of parties.

Parties in Latvia have been organizationally weak, with the smallest party memberships in Europe (measured as a percentage of the electorate that have party membership) and their finances are reliant on generous corporate and individually wealthy donors. The latter issue was addressed in 2019 when the parliament passed a law, strongly supported by the president, to increase party financing sixfold and lower the maximum value of corporate donations. In the long term this is intended to strengthen the independence of party central offices and address the high level of volatility in the Latvian party system. However, there is no political will to address the membership issue.

Sixteen political parties fielded candidates in the October 2018 parliamentary election. Electoral volatility remains high, with three of the seven parties winning seats entering parliament for the first time. Almost half of the deputies (49 of 100) were also newcomers to parliamentary politics. Among them was the populist Who owns the State? (KPV LV) that gained the second largest share of the vote and 16 seats in the 100-seat parliament. By early 2021 however, the party lost all its leaders either by expulsion or voluntary exit.

One of the impacts of accession to the European Union in 2004 has been an increased role for interest groups in policymaking procedures in Latvia. Interest groups systematically participate in ministerial working groups, parliamentary committees and court processes. At the highest executive level, the government's tripartite council systematically engages with business and trade union interests. It also holds an annual bilateral cabinet of ministers and foreign investors council meeting.

Although the range of organized interests is broad, business groups in particular, and trade unions to a lesser extent, have far deeper resources to further their interests. The Latvian Employers' Association, the Latvian Chamber of Commerce and Finance Latvia (which represents the financial sector) are particularly well-financed. Other interest groups, such as those representing environmental or social groups, have substantial public support and legitimacy but are reliant on the enthusiasm of a small group of members rather than extensive and stable financial resources. Similarly to political parties, interest groups tend to have few paid-up members. For example, the Latvian branch of Transparency International, Delna, which is the most visible and active anti-corruption group in Latvia, has consistently had just a few dozen fee-paying members. The lack of grassroots membership and stable financing, rather than legal or political barriers, are the major obstacles to even greater interest representation and influence on policymaking.

A positive development in the last few years has been the growth and grass-roots activities of citizens groups in the city of Riga. Following the election of a new municipal government in August 2020, they have found greater opportunities for cooperation and influence, such as competitive online votes for different grassroots municipal projects that would be funded by the municipality.

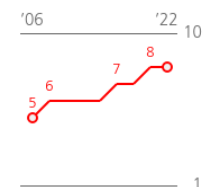
The 2019 Eurobarometer revealed that 52% of Latvians are satisfied with democracy in Latvia, although a higher number – 62% – are satisfied with democracy in the European Union.

This largely reflects ongoing dissatisfaction with domestic political institutions in Latvia. The summer 2020 Eurobarometer revealed that just 22% of Latvians trust parliament (EU average: 36%), 41% trust the legal system (EU average: 52%), 35% trust the public administration (EU average: 52%) and 32% trust the national government (EU average: 40%). Trust in political parties was particularly low – just 6%, a quarter of the EU average of 23%. The highest levels of trust, approximately at the EU average, were in key national nonpartisan institutions such as the military (71%) and the police (68%).

The Latvian government's response to the COVID-19 pandemic was judged predominantly in positive terms by Latvian society in spring 2020, when Latvia had very few infections and the majority (63%) of the public trusted information

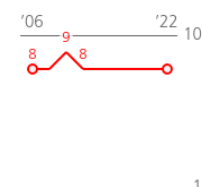
Interest groups

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Approval of democracy

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provided by the government. By fall 2020, the percentage of the public trusting information from the government declined to 53%. Over the same period, the number of people distrusting information from the government increased from 28% in the spring to 37% in the fall.

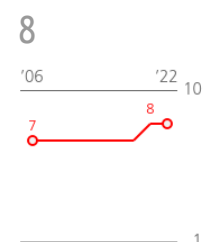
Social capital remains low in Latvia. A 2020 survey by the Providus think-tank found that just one-third (32%) of inhabitants trust other people, only a marginal improvement on the 24% of people that similarly trusted other people in an identically worded question in the 1998 World Values Survey.

Latvia has a strong tradition of public participation in various choirs, folk-dance groups, sports clubs and other cultural associations. However, this is not replicated in terms of participation in politically oriented interest groups, largely because the Soviet era eradicated traditions of donating finances or time to social causes, while the strains of the political and economic transformation of the 1990s left individuals with little mutual trust or time to support political and social initiatives.

Membership and participation in NGOs remain low although there are several promising signs of improvement in recent years. For example, the “Lampa” democracy festival, which among other aims explicitly aims to develop Latvia’s social capital, has seen ever larger crowds in the five years that it has been operating in the small city of Cesis. It went ahead as a virtual democracy festival during the COVID-19 pandemic. The innovative online platform that gives people the opportunity to formulate and then circulate online citizens’ initiatives (“Mana Balss” or “My Voice”) continues to see initiatives regularly submitted to parliament.

The first wave of the pandemic in spring 2020 increased the sense of solidarity and trust in self-organizational capacities of Latvian civil society. This was demonstrated by the rapid establishment and subsequent popularity of the volunteering movement that – via an application – enabled volunteers to help people in self-isolation or quarantine with basic needs such as groceries and walking dogs. The situation changed in the second wave of the pandemic in the fall of 2020, when infection rates were significantly higher and the durability of the introduced restrictions affected society’s abilities to mobilize. However, crowdfunded initiatives to provide restaurant meals or country holidays to health care professionals continued into 2021.

Social capital



II. Economic Transformation

6 | Level of Socioeconomic Development

Latvia ranked 37 in the 2020 United Nations Human Development Index Ranking, behind neighbors Estonia (29) and Estonia (34). Inequality has long been high in Latvia. Almost a quarter (27.3% in 2019) of the Latvian population was at risk of poverty in 2018, according to Eurostat’s “at risk of poverty” indicator, the fourth highest among the European Union’s 27 member states. Those at greatest risk are the elderly, particularly pensioners, and those living in rural regions, particularly the eastern region of Latgale which borders Russia. Although the number of people at risk of poverty is decreasing, the shrinking population means that the proportion of Latvian society at risk of poverty is actually increasing – it was 19% in 2010. This is hardly surprising, as the Latvian government had adopted a harsh austerity policy to deal with the dramatic economic downturn that hit Latvia in 2008. Latvia also has one of the highest Gini rates of inequality (35.6 in 2017) in Europe.

The COVID-19 pandemic may well entrench inequality. Although the government made funds available for furlough payments to employees unable to work due to the state of emergency and other lockdown restrictions, many low-paid employees in, for example, the hospitality industry or other sectors with a large shadow economy, received only minimal benefits. Indeed, the Latvian Fiscal Discipline Council, which has spent years criticizing governments for failing to produce surplus budgets, criticized the government for failing to spend enough on these benefits.

Economic indicators		2017	2018	2019	2020
GDP	\$ M	30383.5	34399.2	34055.5	33505.2
GDP growth	%	3.3	4.0	2.0	-3.6
Inflation (CPI)	%	2.9	2.5	2.8	0.2
Unemployment	%	8.7	7.4	6.3	8.2

Question
Score

Socioeconomic
barriers

7

'06 '22 10



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Economic indicators		2017	2018	2019	2020
Foreign direct investment	% of GDP	3.8	1.2	3.2	-
Export growth	%	6.4	4.3	2.1	-2.7
Import growth	%	8.6	6.4	3.0	-3.3
Current account balance	\$ M	398.9	-98.9	-221.8	1004.1
Public debt	% of GDP	39.0	37.1	37.0	43.5
External debt	\$ M	-	-	-	-
Total debt service	\$ M	-	-	-	-
Net lending/borrowing	% of GDP	-0.7	-0.2	-1.7	-
Tax revenue	% of GDP	23.5	22.8	21.4	-
Government consumption	% of GDP	18.1	18.0	19.0	20.0
Public education spending	% of GDP	4.4	4.2	-	-
Public health spending	% of GDP	3.4	3.7	-	-
R&D expenditure	% of GDP	0.5	0.6	-	-
Military expenditure	% of GDP	1.6	2.1	2.0	2.3

Sources (as of December 2021): The World Bank, World Development Indicators | International Monetary Fund (IMF), World Economic Outlook | Stockholm International Peace Research Institute (SIPRI), Military Expenditure Database.

7 | Organization of the Market and Competition

Latvia is a member of the European Union (and has adopted the euro currency), the World Trade Organization and the OECD and complies with the international laws and norms that regulate and enforce market competition. Persistently high levels of corruption and allegations of judicial bribery do, however, distort competition in areas such as state procurement, enforcement of contracts and bankruptcy administration. The shadow economy (which is estimated to be approximately 24% of GDP, on a downward trend) and widespread use of “cash-in-hand” salaries (i.e., non-taxed wages in cash) also create an unequal playing field between enterprises. Successive governments have acknowledged these challenges but failed to substantially address them.

Latvia ranks 19 (of 190 states) in the World Bank’s 2020 Doing Business survey. The country ranks 26 in the “Starting a Business” category, with four separate procedures taking on average 5.5 days with a paid-in minimum capital requirement of just one euro.

Market organization

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Latvia complies with European anti-monopoly legislation and also has national-level laws and authorities.

The Latvian Competition Council is perceived as one of the stronger and more independent public bodies in Latvia, not least because of its close working relationship with the competition authorities in Brussels.

In 2019 the Latvian Competition Council imposed fines totaling over €3 million, investigated four cases of prohibited agreements, one abuse of a dominant position, 18 mergers and two procedural infringements. High-profile cases have included price rigging on procurement at the Riga municipal transport company and a cartel of construction companies. The council has calculated that its activities bring an annual €25 million benefit to the Latvian economy.

As a member of the European Union, Latvia's foreign trade relationships are regulated and overseen by the European Commission. As a small, open, liberal state, Latvia's governments have traditionally been strongly pro-trade, most recently supporting a wide-ranging trade relationship with the United Kingdom following Brexit as well as the stalled Transatlantic Trade and Investment Partnership (TTIP) with the United States.

Latvia developed the largest banking sector in the Baltic states after the collapse of the Soviet Union and there was a long-standing debate on developing Riga as a regional financial center. However, these debates seemed to have come to an end following a 2018 notice by the U.S. Treasury's Financial Crimes Enforcement Network (FinCEN) that accused ABLV, Latvia's largest domestically owned bank, of money-laundering. ABLV was subsequently forced into liquidation and the government swiftly passed legislation banning banks from servicing shell companies.

MONEYVAL – a permanent monitoring body of the Council of Europe entrusted with the task of assessing compliance with international standards of countering money-laundering and the financing of terrorism – issued a negative report in 2019 on the Latvian financial sector and gave Latvia a year to implement reform of the sector. A flurry of legislation, and the effective dismissal of the head of the financial regulator followed, and the Latvian financial sector was given a positive evaluation in the follow-up report in 2020.

Latvia's financial regulator, the Financial and Capital Market Commission, conducted 12 inspections of banks linked to money-laundering issues in 2020 and found only three violations, much fewer than in previous years.

Competition policy 10



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Liberalization of foreign trade 10



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Banking system 9



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At 5%, the ratio of non-performing loans was high in 2019, however it will fall sharply in future years as in March 2020 the new governor of the Bank of Latvia, Martins Kazaks, called on Latvia's banks to write off some 10,000 non-performing loans that had been taken on during Latvia's 2004 – 2008 credit bubble. Swedbank became the first bank to respond and began to write off bad debts in the autumn of 2020. The government has also called on banks to ease credit requirements, arguing that businesses would benefit from increased access to capital. However, banks have remained conservative in their policies in this area.

The COVID-19 pandemic has had a modest impact on the Latvian banking sector. Banks were quick to offer clients credit holidays. The banking sector remained profitable, with a combined profit of €40 million in the first half of 2020 (albeit representing a 70% decline in profits compared with the first half of 2019), with return on equity (ROE) declining from 9.5% in 2019 to 3.2% in 2020. According to the IMF, the bank capital to assets ratio in 2019 was 9.7, down from 12.8 in 2018.

8 | Monetary and fiscal stability

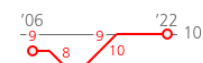
Latvia joined the eurozone in 2014 and monetary stability is now governed through the European Central Bank (ECB). Inflation has remained around the 2% mark in Latvia over the last decade, reaching a high of 2.7% in 2019 before falling close to zero in 2020. ECB policies have had no noticeable impact on the Latvian economy since the country joined the eurozone in 2014, as domestic policies had been closely aligned with the ECB in the years running up to accession.

Membership of the eurozone means that Latvia's budgetary policies are tightly constrained by the structure of the European Semester. Latvia typically runs small budget deficits of under 1% of GDP, although ambitions to create a fiscal surplus have not been met. A non-partisan Fiscal Discipline Council composed of local and international experts was created in January 2014 and helps to oversee government budget discipline by actively commenting (and frequently criticizing) government policies.

The COVID-19 pandemic has had a significant impact on public finances, with Latvia's budget deficit soaring to 7.4% of GDP and gross public debt rising from 36.9% of GDP in 2019 to 47.5% of GDP in 2020. The level of government debt remains comparatively low and sustainable. Indeed, the otherwise hawkishly conservative Fiscal Discipline Council has criticized the government for not spending enough on support for businesses and furloughed workers during the pandemic. The increase in debt is primarily down to increased spending on health care and support for businesses, as well as increased spending on unemployment benefits.

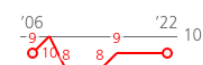
Monetary stability

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Fiscal stability

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9 | Private Property

Private property rights are well-regulated and protected. Following criticism of insolvency procedures by the Foreign Investors Council in Latvia (FICIL), the government undertook a major legislative reform of the sector while a number of court cases were initiated against insolvency administrators.

From early 2021 Latvia will have a specialized economic affairs court focusing on financial crimes involving private companies.

Three decades after the collapse of the Soviet Union the Latvian economy is dominated by private enterprise, although the state maintains a stake in the major mobile and fixed-line telecommunications operators and the electricity monopoly Latvenergo. All are seen as a part of Latvia's critical infrastructure and there are no plans to privatize the remaining public stakes in these enterprises. The private sector has two powerful associations – the Latvian Employers' Association and the Latvian Chamber of Commerce – defending their interests.

The COVID-19 pandemic saw the state step in to invest €250 million in the Latvian national airline airBaltic, after the company's commercial activities came to a virtual standstill after travel restrictions were imposed in Latvia and all across Europe. The state intends to recover the investment by 2025 - 2027.

10 | Welfare Regime

Latvia has a comprehensive range of cash and non-cash welfare benefits although the size of paid benefits has been criticized by international institutions.

Pensions for men and women can be claimed at 63 years and nine months if social insurance payments have been made for a period of at least 15 years. It will be raised by three months every year until reaching 65 years in 2025. Latvia has a three-tier pension system where the first and second tiers are mandatory (with second tier contributions invested by an intermediary bank in the financial market) and a third tier comprising voluntary contributions made by employers and employees into a private pension fund. The OECD has urged Latvia to increase pension benefits, particularly the minimum pension, which was set at just €136 per month in 2021, pointing out that more than 25% of people aged 65 and older have an income below the relative poverty line. Women are especially vulnerable, with more than one third of females over 75 living in poverty.

Unemployment benefits can be claimed by those who have paid social insurance benefits for at least 12 of the last 16 months and are granted for a maximum of nine months. They are calculated based on previous earnings and gradually reduced by increments every three months.

Property rights

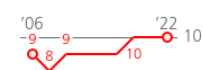
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Private enterprise

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Social safety nets

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A high number of family benefits are available as the government has attempted to reverse Latvia's long-standing demographic decline by encouraging families to have more children. Maternity and paternity benefits, child birth benefits (a one-off payment amounting to €421.17 for each child), childcare allowances and benefits (€11.38 per month for the first child, and an increasing amount for additional children up to the fourth, which would result in €50.07 per month).

Universal health care is available to all citizens and permanent residents. However, at 3.4% of GDP in 2017, Latvia has one of the lowest levels of health care funding in the EU. Latvia also has one of the lowest life-expectancy rates in the EU. Successive governments have planned to increase spending on health care but have done so at a very gradual rate. However, the pandemic has put the spotlight on Latvia's relatively low health care spending and there is a consensus that more public funds should be directed toward the sector in the future.

During the COVID-19 pandemic the government opted for furlough support to employees and support to companies who could not operate due to the restrictions. Cash transfers were not adopted until February 2021. At the same time, food programs continue to be managed by municipalities and NGOs, and the maximum income level that qualifies for this support has been increased, thus allowing a larger number of vulnerable individuals and families to receive help. In addition, there is a specific food program for all school children in the first four grades who are undertaking distance learning, since the state provides free lunch to these children. They receive either product packages or warm meals, depending on the municipality. Children in grades 5 - 9 from poor families or families with more than two children also receive this support during the pandemic.

All citizens and permanent residents, regardless of their gender or ethnic origin, have equal access to the education system, public services and employment. Indeed, a significantly greater share of women enroll in higher education than men. Ratio of female to male enrollment in tertiary education in 2020 was 1.3, gross enrollment in tertiary education was 93.0. The female labor force in 2020 represented 49.9% of the total labor force. Latvia was ranked 11 in the Global Gender Gap Index (a rise of six places compared to 2018). However, Latvia fares more poorly in the EU's 2020 Gender Equality Index, ranking 17 of 27 states (7.1 points lower than the EU average score). This lower ranking can be attributed primarily to the significant gap between women and men in educational attainment.

Russian speakers are at a disadvantage in the education system. Russian-speaking public schools score lower average grades than Latvian schools (largely because of the challenge of finding fluent Latvian-speaking teachers willing to teach in minority schools). Approximately two thirds of students in higher education are privately funded. Many of these are Russian speakers who choose to study in their native language because free public higher education is only available in the Latvian language. In 2018 the Latvian parliament decided to eliminate this option,

Equal opportunity

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'06 '22 10

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by approving amendments to higher education law that would require teaching only in Latvian in both public and private higher education institutions. However, the Constitutional Court in 2020 ruled that this decision the basic law and ruled that private universities should be free to decide their language of instruction.

State-funded places at university are based on merit rather than means. Students have access to cheap student loans to fund their education. The higher education system allows students to hold part-time or, in some cases, even full-time employment, while enrolled in tertiary programs.

Noncitizens are barred from working in the civil service or occupying posts directly related to national security. A long list of professions requires Latvian language skills, including in the private sector, which may influence the employment of Russian-speaking people. At the same time, employers are not permitted to ask employees for information on their knowledge of certain foreign languages, unless the language is needed for the fulfillment of work tasks. These regulations, which were introduced in 2018, followed complaints about the barriers to employment faced by young people lacking knowledge of Russian.

11 | Economic Performance

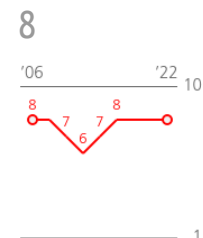
Latvia's economy has been among the best performing in the EU since returning to growth after the economic crisis in 2010. Prior to the pandemic, Latvia's core macroeconomic indicators were good, with balanced budgets, low inflation and falling unemployment. In recent years employers' biggest gripe has been the shortage of information, communication and telecommunications (ICT) professionals. New inflows of FDI (3.1% in 2019) remain disappointingly low. A new head of the Latvian Investment and Development Agency, charged with attracting FDI into Latvia, was appointed in 2020, while the new mayor of Riga (elected in August 2020) plans to create a new investment and development agency for the city.

Despite the demand for skilled labor, the unemployment rate has remained high (6.5% in 2020) largely because of structural unemployment in Latvia's rural regions and small towns. The unemployment rate in the capital city of Riga was 4% at the end of 2019, prior to the pandemic.

Apart from managing the impact of the COVID-19 pandemic, the greatest concern in Latvia remains the significant lag between Latvia and its Baltic neighbors, despite all three being at a similar starting point in 1991. In 2019, according to Eurostat, Latvia's per capita GDP (PPS) was just 69% of the EU average, while both Lithuania and Estonia had reached 84%.

GDP growth in 2019 was 3%, while the economy contracted by 3.6% in 2020, according to the Central Bureau of Statistics. The effects of the COVID-19 crisis

Output strength



are likely to be negative, as Latvia was not significantly affected by the first wave of the pandemic and most sectors remained open during the summer, including mobility within the Baltic countries that helped the local accommodation and tourism industry to operate. Much tougher restrictions were however introduced at the end of 2020.

Public debt in 2019 was 36.8% of GDP, while the current account balance was 0.5% of GDP. Public debt rose to 47% of GDP by the end of 2020, as government spending increased to deal with the costs of the pandemic.

12 | Sustainability

Despite a powerful Green political party (which is one member of the Greens/Farmers' Union alliance) in parliament since the 1990s, environmental issues have never been a major concern for Latvian politicians. For example, 62% of registered vehicles in Latvia are diesel driven, well above the EU average of 41%. Latvia's solid performance on different environmental indicators (such as ranking 37 in Yale University's 2018 Environmental Performance Index, EPI) can be attributed primarily to a low and declining population, dense forest cover and deindustrialization in the 25 years following the collapse of the Soviet Union. Consumption remains lower than the EU average, primarily due to differences in income.

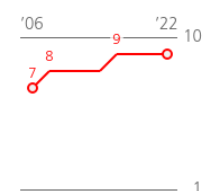
However, a substantial segment of society has a deeply ingrained awareness of nature, with many having a garden or a countryside residence. Moreover, picking wild berries and mushrooms, as well as fishing are highly popular activities across all age groups.

Efforts to improve the quality of the environment continue, albeit often primarily driven by the European Union rather than initiated domestically. Latvia has introduced taxes and regulations to limit the use of plastic bags. Policy on waste management entails taxing of unseparated waste. Between 2019 and 2020 the government set plans for increased energy efficiency and the promotion of a circular economy. There are also plans for large-scale electrification of the Latvian rail network, while new car taxes make higher-polluting cars pay more. A new bottle deposit system will be introduced in 2022 after a consortium of drinks manufacturers won a tender for the contract in late 2020.

A further impulse to steer national goals toward increased sustainability is the European Union's Green Deal and the focus on sustainable investments in the EU's Cohesion Policy 2021 - 2027, in addition to the EU's COVID-19 Recovery Fund.

Environmental
policy

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There is public and political consensus that the Latvian education and research sector is in need of reform and investment. However, there is little agreement on the direction of reform and little prospect of a significant increase in education spending.

Spending on education fell to just 4.4% of GDP in 2017, well below its top of 7% in 2013, while just 0.6% of GDP was spent on research and development in 2018. This has resulted in a sub-par performance in various international education indexes, such as the OECD's PISA report and international rankings of universities, where no Latvian institution makes it into the global top 500 of any major ranking. In contrast, Estonia is one of the top three European performers in the OECD PISA report, and the University of Tartu, which received approximately the same level of public money as the entire Latvian tertiary sector, is well established as a top 300 global university.

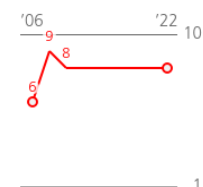
However, the UN Education Index puts Latvia above Estonia (0.883 in 2019), while the literacy rate in Latvia is identical with Estonia (99.9% in 2018).

University reforms since 2019 have focused on reforming governance through the creation of new councils, appointing (rather than university staff electing) rectors, reducing the functions of self-elected university senates, and eliminating higher education institutions' constitutional councils (that elect rectors and set the development direction of universities). Universities oppose these reforms but there appears to be sufficient political will to implement the changes.

Recent primary and secondary school reforms have focused on closing down or merging rural schools with low student numbers due to both a shrinking population in rural regions and the poorer performance of these schools in centralized examinations. At the same time, a school curriculum reform was undertaken in 2019 to focus on competencies instead of acquisition of knowledge. Public schools that continue to teach in the Russian language are transitioning to Latvian language instruction by the 2021/22 academic year.

Education policy /
R&D

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Governance

I. Level of Difficulty

There are few structural constraints to governing Latvia. While the country is among the poorest in the European Union (as of 2020, only Bulgaria and Croatia were poorer as Romania rose to the same level as Latvia), it is also a Baltic Sea state with growing economic, cultural and political links with the wealthy Nordic countries. Latvia's border with Russia and Belarus, established transit infrastructure (including the biggest airport in the Baltic region and the largest national airline) and widespread knowledge of the Russian language and culture, grants it unique trade and economic opportunities, although current sanctions on Russia and a generally negative attitude toward the "east" means there is little scope to develop these opportunities. Latvia has been a strong supporter of increased EU sanctions against Russia, for example, after Russia's military attacks in Ukraine in 2019, and the poisoning of opposition politician Alexei Navalny in 2020. Russia has responded by gradually moving lucrative cargo transit flows away from Latvian ports toward newly built Baltic Sea ports in Russia proper.

Continuing low investment in education and health care means that the Latvian labor force remains less healthy, less educated and less productive than its Western counterparts.

In the first wave of the COVID-19 pandemic, Latvia saw only approximately 20 deaths from the virus between April and June 2020), but the situation has changed dramatically since late October 2020. The highest rate of deaths per day was 44, recorded at the end of December, when the 14-day cumulative number of infection cases reached 680. While the number of excess deaths increased by 3.4% between 2019 and 2020, the number of deaths in December 2020 was 27% higher than in December 2019. Up to February 28, 2021, 1,618 people had died from COVID-19 in Latvia, in a population of 1.9 million.

There are very visible improvements in citizen activity in recent years and a new generation of local and national politicians are seeking to develop these links further. However, Latvian civil society still suffers from financial constraints caused by low fee-paying membership in public associations and relatively rare charitable donations. As a result, civic associations have few members and struggle financially. While there is little that governments can do to address the membership issue, there are now more systematic opportunities for public funding for NGOs through the Society Integration Foundation, which is charged with financially

Structural constraints

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'06 _____ '22 10

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Civil society traditions

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'06 _____ '22 10

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supporting and promoting the integration of society, as well as supporting the implementation of development programs and projects by the public and non-governmental sector. In 2015, a dedicated NGO fund was established, providing recipients with an opportunity to acquire public funding for capacity-building and sustainability. The total funding awarded annually has significantly increased from €400,000 in 2015 to €1.4 million in 2021. There are also opportunities provided by EU funds and other bilateral grants.

This reliance on public and international funds does little to bolster the popular legitimacy of civil society. Indeed, it creates skepticism, and the Soros conspiracy theory (that civil society serves the interests of George Soros and other international financial interests) is often used by populists to discredit media and NGOs critical of populist or radical forces in society.

Social capital in Latvia is low as a result. There are few institutionalized links between civil society and government. Political parties remain rather isolated from these organizations, although several candidates from civil society organizations have been elected to parliament and Riga city council between 2019 and 2020.

Another positive recent development is the increased representation of professionals representing various civil society organizations in parliamentary committees and ministerial working groups. However, groups representing economic interests, which have greater financial resources, still enjoy more influence than civic groups.

There is little risk of civil war or violence in Latvia. Latvia's ethnic cleavage between Latvians and Russian speakers is the source of political rather than social polarization. An emerging divide between conservatives and liberal pro-Europeans has only partially superseded the ethnic cleavage. The latter divide has been exacerbated by the economic and social strains of the COVID-19 pandemic.

At the domestic political level, the last three decades have been dominated by the Latvian Russian speaker divide. The two communities partially united in opposing the Soviet regime in the late 1980s (although a significant number of Russian speakers supported reactionary pro-Soviet movements). This fragile coalition fell apart after Latvia gained independence. Automatic citizenship was denied to former citizens of the Soviet Union and the 1990s and 2000s were marked by political battles over citizenship, education, and language rights. Ethnic tensions were again raised by Russia's occupation of Crimea in 2014 as well as recent school education reforms which will see public schools that still teach in Russian switch over to Latvian language teaching by the 2021/2022 academic year. Pro-Russian-speaking parties have become effectively a permanent political opposition with little prospects of being included in a government coalition.

More recent tensions have centered around a battle to prevent liberal (sometimes also identified as "European") values creeping into Latvia. Society was first divided over the issue of the refugee relocation quotas agreed by the European Council in 2015. More recently, there was a battle over ratification of the Istanbul Convention

Conflict intensity

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(2017) and the UN Migration pact (2018), both of which were ultimately rejected by parliament. In November 2020 conservative movements were electrified by a Constitutional Court ruling that effectively called on the government to recognize same-sex relationships.

Throughout 2020 this battle played out on social media, between those supporting the science of COVID-19 (including government-imposed measures to limit the spread of the virus) and the so-called COVID-deniers. Both groups dismissed the other side's arguments and emotions were further inflamed when the Facebook pages of COVID-deniers were closed or received warnings. The level of vitriol on social media has been very high and demonstrations by COVID-deniers have been bawdy events, although violence has been limited. However, this divide can be expected to widen in the future.

II. Governance Performance

14 | Steering Capability

Latvian governments effectively execute international strategic priorities (conditionality) but struggle with setting domestic strategic priorities. Throughout 2019 the government swiftly and successfully introduced a series of reforms to the financial sector laid out by MONEYVAL – the Council of Europe's Committee of Experts on the Evaluation of Anti-Money Laundering and the Financing of Terrorism – in order to avoid being placed on the organization's "gray list" of non-compliant countries. However, equally important domestically driven reforms of the higher education system have still not progressed as of early 2021.

Throughout the 1990s and early 2000s the short political life of most governments (which had an average term of one year of effective government) meant that establishing domestic priorities was far more difficult than simply executing international instructions in order to join an organization (such as the EU, the eurozone or NATO).

An attempt to enhance the strategic capacity of the government to prioritize and organize policy measures was made with the establishment of the Cross-Sectoral Coordination Center in the state chancellery in 2011. However, this institution has been weakened by its operational capacity (a limited staff of some twenty civil servants) and a lack of influence over ministries that continue to work as single entities, which makes it difficult to cooperate and work cohesively on policy priorities.

Procedures that govern the development of policy documents and legislative proposals formally ensure that the government is able to consult external experts. The National Tripartite Council involves representatives of trade unions and

Question
Score

Prioritization

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employers, as well as the government, and is another channel for gathering expertise. However, evidence-based policymaking, regular impact assessments and strategic planning remain underdeveloped. A further problem is that Latvian political culture still tolerates the introduction of last-minute amendments in the final reading of legislation.

In addition to the Latvia 2030 long-term planning documents, government coalitions formulate their short-term aims in a coalition contract, overseen by the Cooperation Council (formerly the coalition council) that meets on Monday mornings and which sets the agenda for each ministry.

The endemic weaknesses of long-term planning mean that the COVID-19 pandemic has had little impact on domestic priorities. The €1.65 - 2 billion earmarked for Latvia through the EU's Recovery and Resilience Facility provides a motivation to enhance the government's strategic planning ability in order to ensure that the funds are spent effectively.

Latvian governments have demonstrated the capacity (for the state) to implement difficult and controversial reforms. This was the case throughout the difficult post-communist transformation in the 1990s and again at the height of the economic crisis in 2009, when Prime Minister Valdis Dombrovskis oversaw a dramatic fiscal adjustment of 9.5% of GDP.

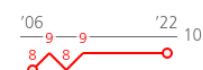
However, the Latvian public administration is relatively small in size and can undertake only a limited number of major reforms at any time.

Major recent reforms include a wide-ranging reform of the tax system in 2018, which included a more progressive income tax system and a tax exemption on reinvested profit. In 2020 parliament passed into law a fundamental reorganization and consolidation of Latvia's local authority and municipal system that will lead to wide-ranging reforms in the delivery of public services in Latvia's regions. This was among the seven priorities that the current government set in January 2019. The other priorities include continuation of reforms in the education and health care sector (e.g., the introduction of competency focused primary and secondary education in 2020 and a reform of university governance in 2021) and planning to group hospitals according to the services provided, thus enabling more effective use of resources and specialized support. The current government also prioritized work on monitoring and supervising financial institutions after a warning that Latvia could be placed on the "gray list" of countries involved in money-laundering as a result of a critical 2018 report by the Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism – MONEYVAL, a permanent monitoring body of the Council of Europe. This priority has been met according to MONEYVAL's positive assessment in 2020. However, it can be said that this was a priority dictated by external factors.

To date there are no signs that the COVID-19 pandemic has had an impact on the implementation of policies.

Implementation

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The development of domestic competences in policy learning and innovation has been neglected by successive Latvian governments, which have instead relied on external advice – from the World Bank and the IMF in the 1990s, and the European Union and OECD in the 2000s - in their undertaking of fundamental reforms. The EU sets the institutional framework for knowledge exchange, as nothing of that kind is established on the national level.

This weakness is being partially addressed by the development of research and analytical capacity in the Latvian parliament and ministries. A productivity and competitiveness council as well as a fiscal discipline Council have been established.

The COVID-19 pandemic has been a case in which the government intensively learned from scientists and followed expert advice on its response to the emergency. In 2020, a dedicated research program was established to enable scientific research on the impact of COVID-19 and to develop solutions to a wide range of issues including the epidemic itself, its psychological impact, IT solutions for risk assessments and public financial support mechanisms. The research was conducted in close cooperation with ministries.

15 | Resource Efficiency

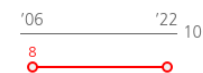
Latvia has a relatively small yet efficient public sector. Between 2017 and 2020 the number of public sector employees was cut by 7% (from 42,000 public employees to 39,000), following a plan to reduce the number of public sector employees by 2% every year over a three-year period. The work of the different parts of the public sector is overseen by the Cross-Sectoral Coordination Center, which was created in 2011 and employs approximately 20 civil servants. Its key tasks are to: (1) develop a long-term strategic approach to public policymaking; (2) monitor decision-making to ensure that public policies are effective; (3) oversee ministries' progress toward meeting goals set in the government declaration; and (4) coordinate the management of state-owned enterprises. There is significant financial transparency in the public sector, with public salaries published on ministerial and agency websites, and all public officials submitting annual financial declarations which are subsequently made available to the public.

The Cross-Sectoral Coordination Center has not yet managed to introduce a centralized recruitment procedure. Therefore, government ministries and agencies still operate noticeably different recruitment procedures that remain subjective and open to political influence. This is particularly the case for the most senior civil service positions. Ministers hire and fire the most senior civil servants in a ministry. The highest position is state secretary and in many cases state secretaries have not hidden their political allegiances. High-profile bureaucrats often leave the civil service in order to enter national politics.

In macroeconomic terms, Latvia has had a balanced budget with small deficits (although the fiscal discipline council has argued that Latvia should have been

Policy learning

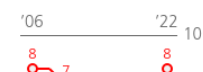
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Efficient use of assets

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operating a surplus budget in the pre-COVID-19 pandemic years of solid growth). Latvia's budget deficit grew sharply in 2020 and 2021 due to the economic dislocations of the pandemic, caused by emergency measures and other restrictions that had an impact on the economy. There can be a lack of cohesion between ministries, as in the coalition government ministries are allocated among the different parties, who tend to be fierce protectors of their own fiefdoms. This was highly visible in 2020 and 2021, as ministries fought for their share of the €1.65 - 2 billion of European Recovery and Resilience funds allocated to Latvia. This prevented the development of a cohesive national vision for investing the available funds.

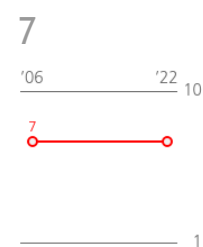
Coordination between ministries and other state institutions remains problematic due to the decentralized, party-based distribution of ministers. Moreover, the political parties that comprise government coalitions often feud and compete, and treat government as a zero-sum game. The prime minister typically has little control over ministries that are governed by other coalition parties.

Ministries ferociously hang on to their powers. For example, in recent years the ministry of education has refused to consider collaborating with the ministry of economics on the export of higher education sector, while the ministry for local government and the environment maintains an exclusive responsibility for the digitalization and information technology sectors.

While the coalition agreement sets government priorities and an agenda, the decentralized nature of government ministries means that there can be problems pursuing and meeting these aims. The Cross-Sectoral Coordination Center was created to address some of these problems, and it has certainly improved the exchange of information from the prime minister's office to ministries and vice versa. At the political level, the weekly Coordination Council of governing party representatives provides a forum to resolve conflicts and build coalitions.

The period in Latvia prior to accession to the European Union and NATO saw the establishment of the Corruption Prevention and Combating Bureau (KNAB). Although KNAB has been hampered by political interference and an instability at the leadership level (not least because the director is elected by parliament, thus making the position part of the political horse-trading process), a powerful and independent new chief, Jēkabs Straume, who has a background in military intelligence, was appointed in 2017. He has enhanced the effectiveness of KNAB, which was always good at fighting low-level corruption (bribes to police officers and low-level bureaucrats), but is now making progress in major corruption cases. In 2018 KNAB detained the president of the Latvian central bank for alleged corruption, and several people were detained for alleged corruption in the public procurement processes of the capital city's public transport company, Rīgas Satiksme.

Policy coordination



Anti-corruption policy



KNAB also has oversight of political party campaigning and publishes all private contributions on a publicly accessible website within days of the donation being made.

Latvia has a powerful state auditor's office, which frequently publishes influential and critical reports of state and local government institutions, and public servants, including politicians, submit annual income and asset declarations.

There have been attempts to make public procurement more transparent by including civil society representatives – including the Latvian branch of Transparency International – on procurement committees.

An important step was taken on May 1, 2019, when a comprehensive new whistleblower law came into force and a whistleblowers' contact point was established in the state chancellery.

16 | Consensus-Building

All major political actors agree on democracy as the core element of the political system. There are no significant political parties advocating authoritarian rule or seeking to undermine the democratic apparatus of the state. However, populist discourse in the 2018 election did chip away at some of the core elements of a liberal democracy, with threats to the freedom of the press and the impartiality of civil servants, as well as a lack of civility to political rivals. KPV LV, the populist party responsible for the most virulent discourse, subsequently joined the government and adopted a mainstream discourse and mode of behavior, albeit at the cost of losing its electoral supporters. One of the leaders of KPV LV, Aldis Gobzems, broke with the party to create a new party – Law and Order – and adopted an even more belligerent anti-elite discourse and political style. While Gobzems and his supporters do not threaten the democratic system, their uncivil discourse undermines the norms of democratic debate in Latvia.

All major political parties agree that Latvia should be an open, liberal, pro-trade market economy. The opposition pro-Russian-speaker Harmony tends to emphasize a marginally more redistributive agenda but does not oppose the core elements of the market economy.

Consensus on goals

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The Latvian military (which is composed of 5,000 professionals and 8,300 members of the national guard) is firmly under civilian control and makes no effort to influence politics beyond lobbying on behalf of its needs. There are no significant organized groups threatening Latvian democracy, although there are a number of extremely small extremist and radical associations (both Latvian nationalist and pro-Russia) that are active on the fringes of politics. However, their activities are largely confined to occasional small protests and the internet.

Latvia's primary ethnic Latvian versus Russian speaker cleavage exists primarily at the political rather than social level, as Latvians and Russian speakers live peacefully side-by-side. An emerging liberals versus national conservative cleavage could prove to be far more polarizing at the social level.

Russia's occupation and annexation of Crimea in 2014 exacerbated the Latvian-Russian speaker cleavage largely because of the differing news sources and reporting consumed by the two groups, which resulted in different attitudes toward the annexation. A few years earlier, a February 2012 referendum campaign on adopting Russian as an official state language was the setting for emotional speeches by politicians from both sides (Russian speakers wanted "respect" and "recognition" while Latvians believed their culture to be under threat). More recently Russian-speaking groups have mobilized against reforms of the education system under the banner of "defending Russian schools!" These protests have not led to societal violence.

There is an emerging cleavage between liberals and national conservatives. Liberals advocate support for refugees and the LGBT community, and they are explicitly pro-European. National conservatives (who come from the nationalist extremes of both the Latvian and Russian-speaking communities) are sharply anti-refugee and advocate "traditional" family policies. This divide is now reflected in the Latvian parliament, with the For Development/For! party alliance and the New Unity party forming a liberal block in parliament (with 21 out of 100 seats), while the radical right National Alliance and the New Conservative Party hold 29 seats. All four parties have been in the government coalition since January 2019 and frequently bicker over values issues with, for example, the former supporting legislation to support same-sex partnerships and the latter opposing them.

Anti-democratic actors

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Cleavage / conflict management

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NGOs representing a wide variety of interests regularly participate in parliamentary committees, ministerial working groups and other forums, including meetings with the state president. Political parties have also started recruiting NGO activists as candidates for local, national and European elections which inevitably enhances links with these organizations. Nevertheless, business interest groups are better resourced and are more influential.

At various points during the pandemic the government has encouraged volunteers with IT skills to participate in the battle against the spread of COVID-19. Initially, in spring 2020, a volunteer group developed a smartphone application to track COVID-19 contacts. In early 2021 the minister for health called for volunteers to develop an IT system to help plan the effective delivery of vaccinations to the public.

There is little political enthusiasm and support for a reconciliation of the ethnic Latvian and Russian-speaking communities. Attempts to reach across the political divide and create a multiethnic party or government coalition have failed. Most dramatically, Valdis Zatlers, the leader of the Zatlers Reform Party, which came third in the 2011 snap election, attempted to form a national government coalition with Harmony Center (now called Harmony) after the vote. However, other Latvian parties refused to countenance a coalition with Harmony Center, and Zatlers also faced opposition from within his own party. The move proved so unpopular with voters that the party effectively disintegrated within a few years. A political reconciliation between the two communities has subsequently been seen as the “third rail” of Latvian politics, and no major Latvian political actors propose politically bridging the gap between the two communities.

Although the passing of time has reduced the salience of the communist versus anti-communist divide, the issue came to the surface again in December 2018 when the Latvian National Archive finally published the KGB archives – the dossiers of 4,300 out of about 25,000 KGB agents active in the period from 1953 to 1991. This led to a public backlash against those named in the files. At the same time, some of the individuals provided detailed explanations of how they had been recruited, providing a greater explanation of the era and the basis for greater social understanding.

Civil society participation

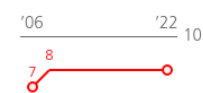
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Reconciliation

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17 | International Cooperation

Latvia has two key planning documents, the medium-term National Development Plan for 2021 - 2027 (NAP 2027) and the Sustainable Development Strategy (Latvia 2030). The latter elaborates seven long-term development priorities: development of cultural space, investment in human capital, change of the paradigm in education, an innovative and environmentally efficient economy, nature as future capital, perspectives of spatial development, innovative government and civil society participation.

The NAP 2027 has four strategic objectives: (i) equal rights – to uphold fundamental rights and equal access to government services; (ii) quality of life – to increase well-being and opportunities for all; (iii) developing a knowledge society in areas of education and science, civic awareness, the media space and the economy; and (iv) a responsible Latvia – that addresses sustainability challenges primarily posed by climate change and demographic trends.

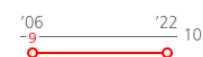
These objectives are coordinated with the strategy for spending EU cohesion and structural funds for the 2021 - 2027 EU multiannual budget.

European Union funds, as well as support for the agricultural sector, are central to Latvia's future development. EU funding is key to maintaining and developing the agricultural sector and is an important source of finance for higher education, innovation and research, developing transport networks, and constructing facilities in small towns and rural areas. Latvia received over €4.5 billion in structural and cohesion funds in the 2007 - 2013 financial period, €4.2 billion in the 2014 - 2020 period, and a further estimated €4.2 billion in the 2021 - 2027 period. Latvia will also receive an estimated €1.65 - 2 billion through the EU Resilience and Recovery Mechanism.

One criticism is that rather than focusing funds on the most competitive areas – such as education and innovation or developing transport infrastructure – the funds are used in a decentralized, scattershot way, with a more or less even distribution across regions. This has resulted in newly refurbished libraries and cultural centers, three large, new regional concert halls, bicycle paths and other upgrades to living infrastructure, but at the cost of investing in infrastructure that could upgrade skills or attract new investment.

Effective use of support

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Latvia takes its international commitments seriously. Militarily, Latvia has provided troops for NATO missions in Afghanistan and the Balkan region, and participated in the “coalition of the willing” in the U.S.-led war in Iraq. As the military threat from Russia has grown in recent years, Latvia has started hosting a greater number of military troops on its territory. Canadian troops head the one thousand-plus international NATO troops in Latvia.

Latvia has also proved itself to be a reliable partner with international financial institutions. In 2012, the country successfully “graduated” from the IMF-led international lender program it began in 2008. A conference in Riga that same year saw IMF President Christine Lagarde laud Latvia for its “collective determination and resilience,” and she cited the country as an inspiration for other European countries.

Indeed, Latvia has proved to be one of the more reliable EU member states and is consistently among the members that has most quickly transposed EU law into national law. Latvia joined the eurozone in 2014 and the OECD in 2016.

Nevertheless, in recent years Latvia has been a rather less compliant partner. The government coalition was split on accepting a refugee quota as part of the EU’s relocation program, although the government did eventually agree to the plan. In 2017, Latvia failed to ratify the Council of Europe’s Istanbul Convention (on preventing and combating violence against women and domestic violence) and in 2018 it similarly rejected the United Nations Migration Pact. This reflects a growing suspicion of “liberal” European policies in what remains a rather conservative society.

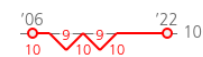
Nevertheless, the government and Latvian society remain committed to membership of the European Union and the other major Western international organizations.

Latvia is an active participant in key regional organizations centered around the Baltic Sea, such as the Council of Baltic Sea States and the informal Nordic-Baltic 6 (NB6) group in the EU, as well as a number of other regional initiatives including the creation of the Baltic Sea macro-region. The Baltic Sea Strategy (BSS) aims to further governmental and regional cooperation among the EU states that border the Baltic Sea.

However, despite a common past and close geographic links, cooperation with Lithuania and Estonia has been far weaker. Institutions of regional cooperation do exist (such as the Baltic Council of Ministers and the Baltic Assembly, which bring together parliamentarians), but they have little substantive output. The closest links between the three Baltic states are in the sphere of defense, where there is a joint Baltic Defense Academy in Tartu, Estonia, a Baltic battalion and multiple other regional initiatives that have assumed a much greater importance following Russia’s annexation of Crimea in 2014 and rising security threats in the region. However,

Credibility

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Regional cooperation

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membership of the European union appears to have drawn the Baltic states closer together and there is an increasing realization that their interests – such as ensuring continued flows of cohesion and other EU funds and being hawkish on Russia – coincide to a greater degree than they do with the Nordic states, who want to cut the EU budget and adopt a more compromising position toward Russia. The Baltic countries also cooperated more closely in their COVID-19 response by creating a so-called Baltic bubble in summer 2020, enabling travel between the three countries until infection rates fell.

Latvia also has an interest in the post-Soviet region and continues to use the EU's Eastern Neighborhood Policy to promote democratization and marketization in other post-Soviet states, particularly Georgia, Moldova and Ukraine – countries which the Latvian government feels could benefit from the experience of Latvia's transition to a market democracy. Cooperation with these states remains a foreign and development policy priority.

However, relations with Latvia's eastern neighbor, Russia, continue to be strained at the political level and the economic sanctions levied on Russia in 2014 have led to a further weakening of bilateral economic relations. Transit flows from Russia have fallen dramatically over the last few years, further weakening economic links with Latvia's biggest neighbor. Relations with Russia are not helped by the fact that Latvia is among the supporters of EU sanctions against Russia, for example, due to military attacks in Ukraine in 2019 and the poisoning of opposition politician Alexei Navalny.

Strategic Outlook

Latvia has two major interlinked existential challenges – demographic decline and faltering economic convergence with Western Europe – as well as the continuing challenge of fighting corruption and reconciling the growing values divide between conservatives and liberals. The economic effects of the COVID-19 pandemic have been more limited in Latvia than in Western Europe, providing an opportunity for greater economic convergence with Western Europe over the next few years. Convergence will, in turn, reduce the negative demographic trend.

Negative birth rates and emigration to Western Europe, initially the UK and Ireland, but latterly Germany and the Nordic states, has seen some 400,000 people emigrate from Latvia in the twenty-first century. Latvia has also experienced profound domestic demographic change as urbanization has seen ambitious young people relocate to the capital city of Riga and the rural regions gradually depopulate. Increased life expectancy combined with low birth rates has seen Latvia's old-age dependency ratio increase. This brings challenges to service provision in both the private and public sectors, as a decreasing number of people pay for the services for an increasing number of pensioners. It also has a negative effect on the labor market. The urbanization trend is likely to continue and investments in fast rail and road links between the capital city Riga and Latvia's regions would allow dynamic service-based businesses to develop outside the Riga metropolitan area and enlarge the viable commuting area around to Riga.

However, persuading people not to migrate from Latvia will be dependent on developing the Latvian economy and ensuring economic convergence with the more established EU member states. Long-term productivity gains will only come with radically increased investment in the higher education, innovation and research sectors, as well as the expansion of digital skills across the entire workforce. Considerable investment in higher education will be required as no Latvian university makes the top 500 in any global index of universities, and the most talented Latvian students continue to enroll in European universities outside of Latvia. Latvian research centers fare comparatively badly in EU-funded research framework competitions, and Latvia spends far less on innovation (perhaps because there are few viable recipients for the funds). There is a clear need for higher education reforms that introduce stricter evaluations, performance-based financing and a restructuring and reorganization of higher education institutions (Latvia has well over 50 HE institutions) and research institutions. Infrastructure investments from EU funds are needed if Latvia is to continue to grow economically and eventually converge with the Baltic Sea states and the European Union. The €1.65 - 2 billion allocated to Latvia through the EU's short-term Resilience and Recovery mechanism provides an opportunity to invest in education and innovation systems and drive Latvian development.

In terms of fighting corruption, the independence of the anti-corruption authority (KNAB) must be maintained and enhanced. The values divide in Latvian society (and politics) will be more difficult to bridge, as it is partially generational (the young tend to be more liberal) and geographic (citizens of Riga tend to be more liberal than those living in rural areas). The most important point is that the debate between the two sides remains civil with both sides accepting, even if not agreeing, with legislative and judicial outcomes.