

2.14. LATVIA

In 2017, GDP growth in Latvia reached 4.5%, driven by solid growth in all components including double-digit investment growth as a result of EU investment funding programmes. GDP growth accelerated during the first quarter of 2018, mostly due to continued strong growth in investment. As this trend is unlikely to be sustained at such levels, GDP growth is forecast to slow down in the coming quarters.

Overall, GDP growth is set to average 3.3% in 2018, led by private consumption and investment, which is expected to continue receiving strong impetus from the use of EU investment funds but should slow down towards the end of the year, as the fund flows near their peak. On the other hand, the downsizing of the non-resident banking sector and continued contraction in transit services are expected to weigh on export growth.

In 2019, economic growth is expected to remain above 3% supported in a balanced way by private consumption, investment and exports. As the use of EU investment funding peaks, the boost to investment should wane, bringing its growth more in line with that of the economy generally. Export growth, however, is expected to recover as the effects of the decline in financial services exports fades.

Wages are expected to rise rapidly over the forecast horizon, with the falling supply of labour and the moderate increase in employment also causing unemployment to decrease further. Wage pressures, however, should temper somewhat as the rate of investment growth normalises.

Inflation is expected to slow down in 2018 and remain flat in 2019. Although energy prices are expected to pick up in 2018, their effects should be outweighed by lower food price increases. In 2019, reversed dynamics are expected as energy prices are set to increase more slowly while service prices are expected to pick up as a result of the high wage increases in recent years.

Risks to the forecast are tilted to the downside as the structural decline in Latvian financial and transport services exports is expected to continue and any worsening in the external environment could weigh on national income and domestic demand.

