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OECD"s periodic surveys of the Latvian economy. Each edition surveys the major challenges faced by the country, evaluates the short-term outlook, and makes specific policy recommendations. Special chapters take a more detailed look at specific challenges. Extensive statistical information is included in charts and graphs.

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Latvia"s economy is set to stagnate in 2024. Private consumption has not yet recovered despite pronounced wage growth, whereas public expenditure is set to remain strong, through additional spending on healthcare and research. The economy is forecast to pick up in 2025 and 2026, with GDP growth reaching 1% and 2.1%, respectively. A decline in energy prices and a broad-based slowdown in other price categories are set to bring inflation down to 1.2% in 2024. As energy prices normalise, inflation is expected to reach 2.2% in 2025 and 2026. Unemployment is projected to increase in 2024 and to decrease slightly in 2025 and 2026. The general government deficit is forecast to increase to 3.2% of GDP in 2025 and 2026 driven by weaker growth of tax revenue.

In the context of the 2024 benchmark revision of the national accounts, real GDP growth was revised up to 1.7% in 2023 compared to an initially estimated contraction by 0.3%, supported by a stronger investment growth and public consumption expenditure.

The unemployment rate is forecast to reach 6.7% in 2024, to then decrease slightly in 2025 and further in 2026 on the back of increasing labour demand. After having reached 15.7% in 2023, compensation per employee growth is set to stay strong in 2024 at 8.8%, supported by increases in the minimum wage and in public wages, well above productivity growth. Nominal wage growth is set to reach 4% in 2025 and 3.5% in 2026, driven by labour market tightness.

In the first nine months of 2024, energy prices declined fast and have fuelled a rapid decrease of HICP inflation as expected. Combined with a broad-based slowdown in prices of other HICP items, inflation is set to fall to 1.2% in 2024. As base effects from energy prices fade away, inflation is set to reach 2.2% in 2025 and 2026. Driven by development in wages, services inflation is projected to reach 4.5% in 2024 and decrease gradually to 2.3% by 2026. Headline inflation excluding energy and food is expected to remain above HICP inflation in 2024 and 2025, driven by pressures in services and processed food prices and to converge to a similar level to headline inflation by 2026.

In 2024, the general government deficit is projected at 2.8% of GDP, up from 2.4% of GDP in 2023. The impact of the complete phase-out of energy-related measures by the end of 2023 was more than offset by additional expenditure on public wages, healthcare and education, supplementary payments to pensioners and public investment. Revenue increase from taxes on products is expected to be rather modest in 2024 compared to 2023 mainly due to a decline in energy prices. At the same time, the introduction of corporate income tax advance payments from the financial sector, an increase in the rates for several excise duties and additional dividend payments from state-owned companies are expected to yield a moderate increase in revenue.

In 2025, the government deficit is forecast to increase to 3.2% of GDP. The deficit increase stems from the revenue side, including tax revenue reduction due to the labour tax reform, in particular on taxes on income and wealth, as well as a projected decline of revenue from property income, which was elevated in 2023 and 2024 due to high profitability of state-owned companies in energy and forestry sectors. The revenue from advance payments in the corporate income tax from the financial sector is projected to decrease in line with expected lower profit margins following a decline in interest rates.

In 2026, the government deficit is forecast to remain at 3.2% of GDP, mainly due to the projected revenue decrease from property income, impact from the labour tax reform carried out in 2024 and moderate growth of government consumption expenditure.