



European Construction Sector Observatory

Country profile **Latvia**

January 2022



In a nutshell

In 2021, Latvian GDP is expected to grow by 4.7% reaching EUR 28.0 billion.

Latvia's GDP totalled EUR 26.7 billion in 2020, recording a 3.6% decline from the previous year. This is lower than the growth experienced in 2019 (2.0%), which is explained by the outbreak of the COVID-19 pandemic and subsequent measures taken to contain the virus. Notwithstanding, since 2010, Latvia's GDP has grown by 28.8%.

The **number of enterprises** in the Latvian broad construction sector increased by 48.6% between 2010 and 2020, totalling 31,903. This growth was mainly driven by the increase in the number of enterprises in the architectural and engineering activities (+98.1%), the narrow construction (+93.2%), the manufacturing (+36.7%), and the real estate activities (+18.6%) sub-sectors over the same reference period.

Number of enterprises in the narrow construction sub-sector between 2010 and 2020  **93.2%**

In parallel, the **volume index of production** in the broad construction sector recorded an increase of 27.4% during 2015-2020, mainly driven by a 48.8% increase in the construction of buildings and a 7.2% growth in the construction of civil engineering, over the same period.

Similarly, the **turnover** of the broad construction sector grew by 79.4% between 2010 and 2018, reaching EUR 8.5 billion. It further increased to EUR 9.0 billion in 2020, marking a 91.2% acceleration since 2010. This overall increase was mainly driven by the turnover growth in the manufacturing (+119.7%), narrow construction

(+92.2%), the architectural and engineering activities (+78.6%), and the real estate activities (+65.3%) sub-sectors over the 2010-2020 period.

In parallel, the **gross operating rate** of the broad construction sector, which is used to assess the profitability of the sector, stood at 16.1% in 2018, 1.1 percentage point (pps) above the rate registered in 2010 (15.0%). The real estate activities sub-sector registered the largest profit margin in sales (36.1%) in 2018, followed by the architectural and engineering activities (16.8%), the manufacturing (15.4%) and the narrow construction (9.7%) sub-sectors.

In terms of employment, there were 144,831 **persons employed** in the Latvian broad construction sector, registering a 38.1% increase in comparison to the 2010 level (104,894 persons). This was mainly driven by the growth registered in the number of persons employed in the architectural and engineering activities sub-sector (+63.5%) followed by the narrow construction (+53.3%), the manufacturing (+40.4%) sub-sectors, over the 2010-2020 period.

Number of persons employed in the narrow construction sub-sector between 2010 and 2020  **53.3%**

Skills shortage and mismatch are the main obstacles to the sustainable growth of the Latvian construction sector. In fact, low-skilled workers are in lower demand and face higher unemployment. The number of vacancies in the construction sector has increased in 2020, indicating a severe shortage of manpower across skillsets. The country has adopted a construction industry development strategy for 2017-2024 to address various industry

issues, such as, ensuring a qualified workforce, increasing productivity, and improving the quality of construction services. Moreover, the government has introduced preferential conditions to attract highly qualified specialists from abroad in the identified professions.

The housing market is relatively dynamic and resilient despite the COVID-19 pandemic. Between 2015 and 2020, the house price index for existing dwellings grew by 45.4%. According to data published by Eurostat, between 2010 and the second quarter of 2021 house prices in Latvia have increased by almost double (+99.0%).

House price index for existing dwellings between 2015 and 2020



The demand for housing has risen following the introduction of the Housing Guarantee Programme, which provides guarantees on mortgages to support the purchase and/or construction and renovation of a first home. The programme also enables families and young professionals to obtain a mortgage against lower down payment than banks would normally require. As of November 2020, the programme has supported more than 14,000 housing guarantees.

In November 2020, the Construction Board of Riga City Council adopted a principle of a Green Corridor for sizeable development projects to assist more speedy advancement of the largest projects. Currently, the Green Corridor is available in the permitting process of buildings of the second and third category if they envisage construction of more than 100 apartments.

The Recovery and Resilience Plan (RRP) of Latvia will be financed by EUR 1.8 billion in grants from the European Commission. 38.0% of the plan will support climate objectives and 21.0% of the plan will foster the digital transition¹.

The plan includes providing support for the green transition through investments of EUR 295.0 million into overhaul of the Riga metropolitan area

transport, EUR 248.0 million in energy and energy-efficient and renovation of public and private buildings and EUR 80.0 million will be invested for the modernisation and greening of electricity networks. The country will invest EUR 12.5 million for increasing connectivity with the deployment of high-speed broadband, EUR 129.0 million in the digital transformation of the public sector and the digitalisation of businesses. Furthermore, as per the plan, the country will invest EUR 43.0 million towards affordable housing. The plan also includes two measures on connectivity infrastructure: last-mile connectivity in rural areas and construction of passive infrastructure on the Via Baltic 5G corridor².

In terms of the civil engineering market, Latvia has launched its first **public-private partnership** project to design and construct the *Kekava* bypass on the European Route E67. In July 2021, The Nordic Investment Bank (NIB) co-financed the project through a 21-year loan agreement of EUR 61.1 million. In May 2021, the construction of the first round of the east highway from *Leriku* street to *Vietalva* street in Riga was launched. In November 2021, tenders for the procurement of the main railway construction work of the **Rail Baltica project** in Latvia was announced. The project is expected to be completed in 2025. Further, the country has begun **investing in new trains** to increase the attractiveness of rail commutes and thereby increase the use of public transport for commuting.

Overall, the Latvian construction sector has a positive outlook in the long-term. The policy and investments initiatives taken by the government for the infrastructure and housing market are expected to drive the growth of the construction sector. In addition, investment in energy efficiency measures towards apartment buildings, digitalisation of the economy and EU-backed projects are expected to dominate the sector's growth.

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Key figures

Construction market

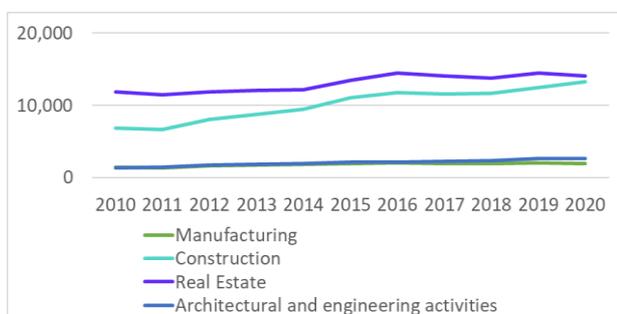
The **number of enterprises** in the broad construction sector in Latvia totalled 31,903 in 2020³ (Figure 1), representing a 48.6% increase compared to the 2010 level (21,464). The increase was mainly driven by the growth registered in the architectural and engineering activities and narrow construction sub-sectors, reporting an increase of 98.1% and 93.2%, respectively, between 2010 and 2020. This was followed by a 36.7% increase in the manufacturing sub-sector and an 18.6% growth in the real estate activities sub-sector during the same period.

While the real estate activities (44.1%) and the narrow construction (41.6%) sub-sectors together accounted for 85.7% of the total number of enterprises in the broad construction sector in 2020, the share of architectural and engineering activities and the manufacturing sub-sectors stood at 8.3% and 5.9%, respectively.

Number of enterprises in the broad construction sector between 2010 and 2020

↑ 48.6%

Figure 1: Number of enterprises in the broad construction sector in Latvia between 2010 and 2020



Source: Eurostat, 2021.

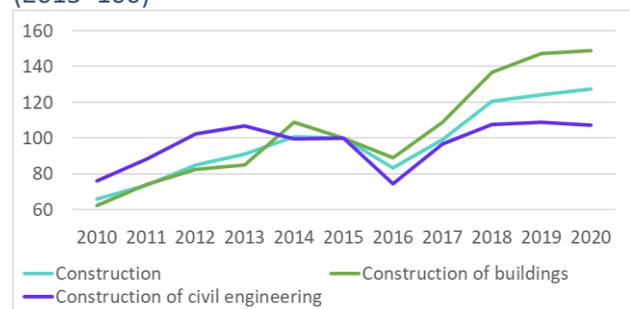
The **volume index of production** of the broad construction sector increased by 27.4% between 2015 and 2020 (Figure 2). Likewise, production in

the construction of buildings and the construction of civil engineering grew by 48.8% and 7.2% respectively over the same period.

Volume index of production in the construction of buildings between 2015 and 2020

↑ 48.8%

Figure 2: Volume index of production in the Latvian broad construction sector between 2010 and 2020 (2015=100)

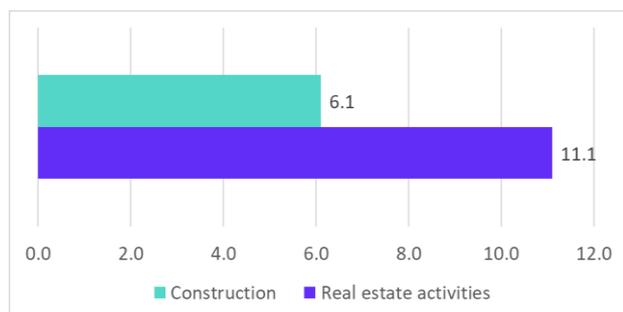


Source: Eurostat, 2021.

The **total value added at factor cost⁴** of the broad construction sector amounted to EUR 2.8 billion in 2020⁵, representing an increase of 118.4% since 2010. The narrow construction sub-sector accounted for 45.8% (EUR 1.3 billion) of the total value added in 2020, followed by the real estate activities (28.8%, i.e. EUR 813.1 million), the manufacturing (20.1%, i.e. EUR 565.7 million) and the architectural and engineering activities (5.3%, i.e. EUR 149.3 million) sub-sectors.

The **share of the gross value added (GVA)** of the broad construction sector in the GDP stood at 19.3% in 2018⁶, above the 2010 level (15.9%). Further, the share of GVA of the real estate activities sub-sector in the GDP stood at 11.1% (above the EU-27 average 10.3%) in 2020, followed by the narrow construction sub-sector, being at 6.1%, and hence above the EU-27 average of 5.1% (Figure 3).

Figure 3: Gross value added as a share of GDP in the Latvian broad construction sector in 2020⁷ (%)



Source: Eurostat 2021.

Productivity

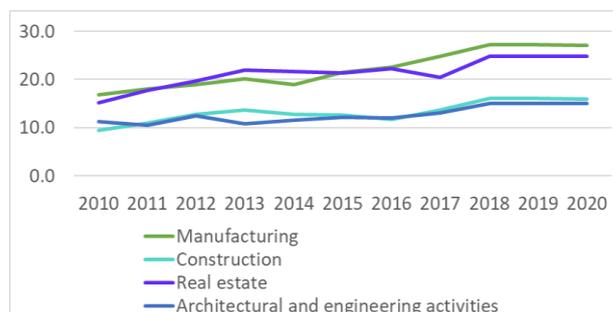
The **apparent labour productivity**⁸ in the broad construction sector has been experiencing an increasing trend, growing from EUR 12,310.5 in 2010 to EUR 19,854.0 in 2018⁹ (+61.3%), below the EU-27 average of EUR 51,960.1 in the same year.

In terms of sub-sectors, the narrow construction sub-sector reported the highest increase of 67.5%, growing from EUR 9,500 in 2010 to EUR 15,916 in 2020¹⁰. This was followed by the real estate sub-sector (+63.1%), increasing from EUR 15,200 to EUR 24,785 in the same period. The manufacturing sub-sector reported a 60.4% growth, rising from EUR 16,874 in 2010 to EUR 27,062 in 2020¹¹. Similarly, the architectural and engineering activities sub-sector reported the lowest growth of 34.2% over time, from EUR 11,200 in 2010 to EUR 15,031 in 2020¹².

Apparent labour productivity in the narrow construction sub sector between 2010 and 2020 **↑ 67.5%**

In October 2019, to represent the National Productivity Board, Latvia appointed the University of Latvia think tank LV PEAK. This is in accordance with the European Commission recommendation to set up a productivity board to boost productivity. The LV PEAK, founded in May 2018 by the University of Latvia and led by academics and experts, conducts independent analysis on productivity issues and formulates policy recommendations¹³.

Figure 4: Labour productivity in the broad construction sector in Latvia between 2010 and 2020 (EUR k)



Source: Eurostat, 2021.

Turnover and profitability

The **total turnover** of the broad construction sector amounted to EUR 8.5 billion in 2018, registering a 79.4% above the 2010 levels (EUR 4.7 billion). It further increased to EUR 9.0 billion in 2020¹⁴, marking an increase of 91.2% since 2010. The growth was driven by increases in all the four sub-sectors, namely – the manufacturing (+119.7%), the narrow construction (+92.2%), the architectural and engineering activities (+78.6%) and the real estate activities (+65.3%) sub-sectors over the same period. In 2020, the largest share of the turnover came from the narrow construction sub-sector, which accounted for 57.7% (i.e. EUR 5.2 billion) of the total. It was followed by the manufacturing (21.1%, i.e. EUR 1.9 billion), the real estate activities (17.7%, i.e. EUR 1.6 billion), and the architectural and engineering activities (3.5%, i.e. EUR 316.2 million) sub-sectors.

Total turnover of the narrow construction sub-sector between 2010 and 2020 **↑ 92.2%**

Similarly, the **gross operating surplus** of the broad construction sector increased from EUR 710.9 million in 2010 to EUR 1.4 billion in 2018¹⁵, 92.0% higher than the level registered in 2010. Notably, the highest growth was registered by the narrow construction sub-sector (+137.7%), followed by the manufacturing (+99.3%), the real estate activities (+67.1%) and the architectural and engineering activities (+47.3%) sub-sectors, over the same reference period.

At the same time, the **gross operating rate** of the broad construction sector¹⁶, which gives an indication of the sector’s profitability, stood at 16.1% in 2018¹⁷ (EU-27 average-16.7%), which is above the 2010 level (15.0%). This indicates tighter profit margins, which are partly explained by increasing construction costs. The real estate activities sub-sector reported the highest gross operating rate of 36.1%, followed by the architectural and engineering activities (16.8%) and manufacturing (15.4%) sub-sectors. Notably, the narrow construction sub-sector was the least profitable sub-sector, with a gross operating rate of 9.7% in 2018¹⁸.

Similarly, the **construction cost index** increased by 27.3% between 2015 and 2020. This was mainly due to a 53.9% increase in the labour cost during the same period (following the increase in wages). The input prices for materials, too, increased, albeit at a slower rate of 7.9% between 2015 and 2020 (Figure 5). Moreover, lengthy and cumbersome processes to obtain building permits have also contributed to high construction costs.

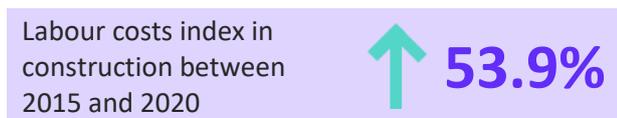


Figure 5: Construction cost index between 2010 and 2020 (2015=100)



Source: Eurostat, 2021.

According to Central Statistical Bureau of Latvia, the construction costs in Latvia increased by 4.2% in the third Quarter of 2021, over the previous quarter¹⁹.

Labour remuneration of workers and maintenance and operational costs of machinery and equipment grew by 1.7% and 2.1% respectively in the same period. However, prices of building materials increased by 6.2%²⁰.

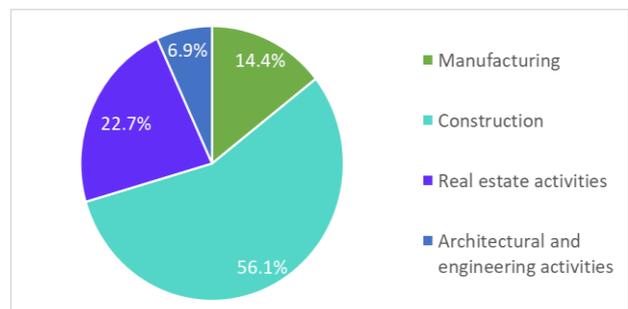
Employment

In 2020²¹, there were 144,831 **persons employed** in the Latvian broad construction sector, 38.1% more than the 2010 levels (104,894). Specifically, the architectural and engineering activities sub-sector employed the 6.9% of the total construction workforce in 2020 (9,930 persons) – a 63.5% growth compared to 2010 (6,074). This was followed by the narrow construction (+53.3%) and the manufacturing (+40.4%) sub-sectors, reaching 81,190 and 20,903 persons respectively in 2020. The least increase (+5.9%) between 2010 and 2020 in the number of persons employed was in the real estate activities sub-sector, standing at 32,807 persons in 2020 (Figure 6).

Furthermore, in 2018²², SMEs employed 90.1% of the total workforce in the broad construction sector, while the EU-27 average stood at 87.1%. This in turn, highlights the importance of SMEs in construction employment in Latvia.



Figure 6: Percentage of persons employed by broad construction sub-sectors in Latvia in 2020



Source: Eurostat, 2021.

As for **employment by specific occupation**, the number of elementary occupations in the narrow construction sub-sector increased by 77.5% between 2010 and 2020. This was followed by a 44.7% incline in the demand for technicians and associate professionals and 32.9% for craft and related trades workers. Meanwhile, demand for plant and machine operators and assemblers in the narrow sub-sector witnessed a decline of 3.8% over the same period. In the manufacturing sub-sector, the largest growth was recorded in the number of technicians and associate professionals (+73.4%) over the same period, which was trailed

by a 42.5% rise in the number of professionals. However, there was a decline in the demand for plant and machine operators and assemblers (-24.1%), managers (-17.1%), and elementary occupations (-7.4%) in the same sub-sector between 2010 and 2020. On the contrary, the number of managers in the real estate activities sub-sector witnessed a 91.3% incline over the same reference period.

Demand for elementary occupations in the narrow construction sub-sector during 2010-2020  **77.5%**

Additionally, the number of **self-employed workers** in the narrow construction sub-sector represented 9.6% of the total self-employed persons in the general economy in 2020. This is below the EU-27 average of 11.7% but higher than

the 2010 level of 8.0%. In the real estate activities sub-sector, the share of self-employed workers increased to 3.4% in 2020 from 2.8% in 2013²³, thus standing above the EU-27 average of 1.6%.

In parallel, **full-time employment** in the narrow construction and the real estate activities sub-sectors increased by 36.0% and 1.3%, respectively, between 2010 and 2020, while in the manufacturing sub-sector, it grew by 4.8% over the same reference period. Meanwhile, **part-time employment** witnessed a decline of 43.2% and 15.4%, respectively, in the manufacturing and narrow construction sub-sectors.

Full-time employment in the narrow construction sub-sector between 2010 and 2020  **36.0%**

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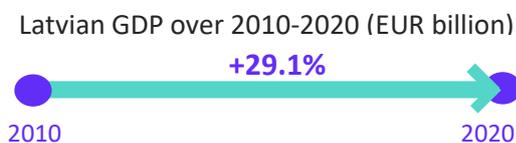
Macroeconomic indicators

Economic development

Over the 2010-2020 period, the Latvian GDP experienced an increase of 29.1%, reaching EUR 26.7 billion. In 2020, the country's GDP declined by 3.6%, while in 2019 it registered a 2.0% growth.

In 2020, the drop in the growth rate was mainly due to the global COVID-19 pandemic and subsequent containment measures. As a result, private consumption and exports suffered the most with the reduced consumer demand and restricted supply of services²⁴.

In addition, the **potential GDP** amounted to EUR 27.5 billion in 2020, translating into a negative **output gap** of 3.6%. The negative output gap indicates that the Latvian economy tends to underutilise its resources, with actual outputs falling short of full capacity output. In 2021, Latvian GDP is expected to grow by 4.7% reaching EUR 28.0 billion. The **inflation rate** stood at 0.1% in 2020, after experiencing a long period of fluctuation since 2010. This is well below the 2019 level (2.7%), mainly attributable to a significant decline in energy prices and an inflation of unprocessed food prices growth²⁵.



Demography and employment

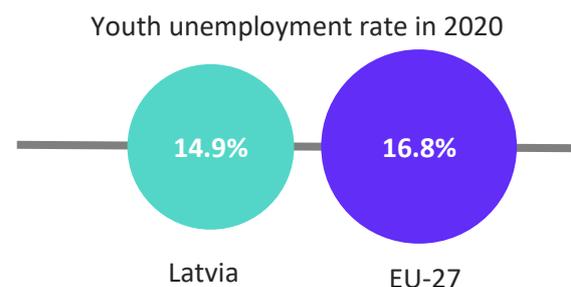
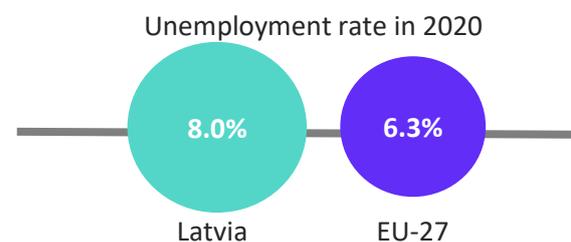


In 2020, the average unemployment rate in Latvia decreased to 8.0% in 2020 from 17.7% in 2010, thus standing above the EU-27 average of 6.3%.

In addition, **youth unemployment** (below the age of 25) reached 14.9% in 2020, below the EU-27

average of 16.8% and much below the Latvian level of 2010, when it stood at 36.2%. The **total population** in Latvia stood at 1.9 million people in 2020, representing a decline of 9.4% since 2010. It is projected to further decline by 10.2% by 2030, and by 18.5% by 2050, reaching 1.4 million. Since 2010, the **net migration rate** has remained negative, emphasising the increasing emigration of Latvian citizens. However, in 2020, the net migration rate declined by 91.2% dropping to -3,150 people from -35,640 in 2010.

At the same time, the **working age population** in Latvia made up 63.5% of the total population in 2020, below the EU-27 average of 64.3%. By 2050, the share of the working age population is expected to decrease to 55.0%. On the other hand, the **aged population** (65 years or older) made up 20.5% of the total population in 2020, being on the same level as the EU-27 average. By 2050, the share of the aged population in Latvia is expected to increase to 31.2%. This shift in terms of population may imply an increasing need for adequate care buildings and infrastructure. This in turn may generate more opportunities for the Latvian construction sector.



Public finance

In 2020, the **general government expenditure** in Latvia accounted for 43.6% of GDP, below the EU-27 average (53.4%) and the 2010 level (46.0%). Conversely, the **general government deficit** decreased to -4.5% of GDP in 2020, from the 2010 levels of -8.6%. This is also below the EU-27 average for 2020 (-6.9%). Lastly, the **general government gross debt** accounted for 43.5% of the country's GDP, below the 2010 level of 47.9% and the EU-27 average (90.7%).

The government debt-to-GDP ratio is expected to increase from 43.5% in 2020 to 50.3% in 2022, mostly due to the large government support targeted towards national economy and population for mitigating the consequences of the COVID-19 pandemic²⁶.

Entrepreneurship and access to finance



According to the World Bank Doing Business 2020 report, Latvia ranked 26th out of 190 countries in ease of starting a business in 2019. This is a decline in comparison with previous year's ranking (24th)^{27,28}.

As per the report, starting a business in Latvia requires four procedures, taking 5.5 days and costing 1.5% of income per capita²⁹. In terms of entrepreneurship, 37.1% of the Latvian adult population perceive that there are good opportunities in starting a firm in the country, and 17.2% of the adult population, currently not involved in entrepreneurial activities, intended to start a business in the coming three years³⁰.

According to the **Small Businesses Act (SBA) Fact Sheet 2019**, Latvia is considered among the leaders in early-stage entrepreneurial activity. However, the status given to successful entrepreneurship and opportunity driven entrepreneurial activities are low. There is also a lack of a global governmental strategic approach, fostering entrepreneurial spirit in society by starting entrepreneurship education in the school curriculum and by providing guidance to specific groups of people on starting a business³¹.

In terms of start-up environment, Latvia has put considerable effort in boosting and strengthening its start-up environment by providing various types of support mechanisms. Due to this favourable environment, the number of start-ups in Latvia increased four times since 2012, reaching 450 active start-ups in 2020 and engaging EUR 303.0 million in investments³².

In 2020, the COVID-19 pandemic had a major impact on the Latvian SMEs leading to a drop in the SME value added by 4.0% and employment by 2.5%. However, with the government taking numerous policy measures to support the economy, these indicators are forecasted to grow by 7.3% and 2.2% respectively in 2021³³.

However, in the construction sector also SME employment fell by 3.3% whereas there was an increase of 5.8% in SME value added against the overall declining trend in SME value added. In 2020, ALTUM - state-owned development finance institution launched a EUR 200.0 million COVID-19 working capital loan programme to support Latvian businesses impacted by the COVID-19 crisis. The loan will be available in situations where credit institutions have stopped financing or do not grant new working capital loans or credit facility lines and will be provided for up to 3 years³⁴.

The **loans to non-financial corporations in the general economy** in Latvia declined by 43.6%, reaching EUR 5,011.0 million in 2020 from EUR 8,888.0 million in 2010. This reflects worsening conditions of access to finance in the country.

As per the World Bank Doing Business 2020 report, in terms of access to finance Latvia ranked 15th out of 190 countries for the ease of getting credit³⁵.

The Latvian government has taken several measures to improve the conditions of access to finances for SMEs in the country, such as³⁶

- a credit guarantee scheme to support businesses that have experienced difficulties in making loan repayment to banks due to the COVID-19 crisis. The scheme allows credit institutions to postpone payments of the principal amount of the loan.

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- state aid granted to a company affected by the COVID-19 crisis, in order to compensate for the fall in the flow of current assets and to overcome the second wave of the crisis. This support programme was extended until mid-2021.

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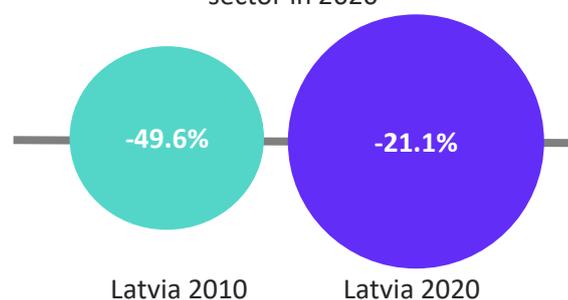
Key economic drivers of the construction sector

Business confidence

In 2020, all the confidence indicators continue to lie in the negative territory, with the construction confidence indicator having the highest deterioration from the previous year. Notwithstanding, all the confidence indicators have shown significant signs of improvement since 2010.

The **consumer confidence** indicator stood at -14.9 in 2020, considerably better than 2010 (-25.1) and slightly below the EU-27 average of -14.6. Similarly, the **industry confidence** indicator slightly improved from -7.6 in 2010 to -6.8 in 2020. This also stands above the EU-27 average of -14.4 in 2020. Further, the **construction confidence** indicator registered a substantial improvement over the 2010 and 2020 period, rising from -49.6 to -21.1. This, however, is lower than the EU-27 average of -9.3 in 2020.

Confidence index in the construction sector in 2020



Following this trend, the **investment ratio** also increased from 19.6% in 2010 to 23.7% in 2020. Likewise, **investment per worker** has been increasing from EUR 10,710 in 2010 to EUR 15,482 in 2019³⁷. In terms of sub-sectors, investment per worker in the real estate activities and the narrow construction sub-sectors increased (102.7% and

3.8% respectively) from EUR 18,700 and EUR 2,600 in 2010 to EUR 37,900 and EUR 2,700 in 2019³⁸, respectively. Conversely, investment per worker in the architectural and engineering activities sub-sector decreased by 52.9%, from EUR 3,400 in 2010 to EUR 1,600 in 2019³⁹.

In April 2021, although the construction confidence indicator remained in negative territory, it showed significant signs of improvement. It increased by 7.4 pps from March 2021 reaching -13.7 in April 2021⁴⁰.

Domestic sales

The ranking of the five **most domestically sold construction products** in Latvia has seen some fluctuations in recent years. Three out of the top five ranked product groups showed significant growth in their sales value between 2010 and 2020. 'Doors, windows and their frames' being the second most domestically sold construction product, experienced the largest increase in sales value, with a 609.2% incline. This incline was followed by 'Prefabricated buildings of metal' (+359.5%) and 'Ready-mixed concrete' (+106.3%) over the 2010-2020 period. Notably, the products group 'Pallets, box pallets and other load boards of wood' (+226.3%) and 'Other worked ornamental or building stone' (+156.4%) also recorded a growth over the same reference period. These products, however, are not the top five most domestically sold construction products in the country in 2020. The top five most domestically sold construction products, accounting for 63.7% of the total of construction products sold domestically in 2020, are presented in the table below (Table 1), including a comparison with the most sold products in the EU-27 region.

Table 1: Five most domestically sold construction products in Latvia and in the EU in 2020

Latvia				EU-27
	Product	Value (EUR m)	Share in construction product domestic sales (%)	Product
1	Other plywood, veneered panels, etc. (group 162118)	72.7	16.4	Other structures and parts of structures, plates, etc. (group 251123)
2	Doors, windows and their frames, etc. (group 251210)	68.2	15.4	Ready mixed concrete (group 236310)
3	Prefabricated buildings of metal (group 251110)	52.0	11.7	Doors, windows and their frames (group 251210)
4	Ready-mixed concrete (group 236310)	45.2	10.2	Prefabricated buildings of metal (group 251110)
5	Other structures and parts of structures, plates, etc. (group 251123)	44.4	10.0	Prefabricated structural components (group 236112)

Source: PRODCOM, 2021.

Export of construction-related products and services

The ranking of the **most exported construction products** experienced some fluctuations in recent years. Most of the products strongly increased in terms of sales value of exports between 2010 and 2020. Indeed, robust exports has been a driving factor in the country's economic upswing. Notably, the largest increase in value of exports was seen in product group 'Boards, blocks and similar articles' (+2148.8%), followed by a 1196.7% increase in 'prefabricated structural components for building or civil engineering, of cement, concrete or artificial stone', over the period 2010 and 2020. However, these two products were not in the top five list and together accounted for just 6.2% of the total construction product exports in 2020. The top five most exported construction products from Latvia and the EU-27 are summarised in Table 2. Together, these five products made up 58.3% of all construction products exports in 2020.

Table 2: Five most exported construction products in Latvia and in the EU in 2020

Latvia				EU-27
	Product	Value (EUR m)	Share in construction product export sales (%)	Product
1	Pellets and briquettes, of pressed and agglomerated wood (group 162915)	328.4	21.8	Ceramic tiles and flags (group 233110)
2	Other plywood, veneered panels and similar laminated wood (group 162118)	241.0	16.0	Other structures and parts of structures, plates, etc. (group 251123)
3	Oriented strand board (OSB) (group 162113)	126.7	8.4	Fibreboard of wood (group 162115)
4	Other structures and parts of structures, plates, etc. (group 251123)	97.1	6.4	Doors, windows and their frames (group 251210)
5	Pallets, box pallets and other load boards of wood (group 162411)	86.9	5.8	Builders joinery and carpentry, of wood, n.e.c. (group 162319)

Source: PRODCOM, 2021.

In terms of **cross-border provision of construction services**⁴¹, Latvia **exported** EUR 368.0 million worldwide in 2020, registering an increase of 523.7% compared to the 2010 level of EUR 59.0 million. Of this total, 92.3% (i.e. EUR 338.0 million) went to the EU-27 in 2020. Similarly, the country imported EUR 76.0 million worth of construction services worldwide in 2020, an increase of 52.0% from the 2010 level (EUR 50.0 million), with 89.5% (i.e. EUR 68.0 million) coming from the EU-27 countries. Thus, this generated a **trade surplus** of EUR 292.0 million for the year.

Latvia's export of construction services worldwide between 2010 and 2020

 **523.7%**

Access to finance in the construction sector

Access to finance for Latvian construction companies has become an increasingly pressing issue since the economic crisis. In particular, lending to the construction sector has seen a declining trend since 2010. **Outstanding loans** to the narrow construction sub-sector have fallen from EUR 991.5 million in 2010 to EUR 110.1 million in 2020, witnessing a fall of 88.9%.

According to the Survey on the Access to Finance of Enterprises (SAFE) 2021 report, **access to finance** remains the most important concern for 7.2% of SMEs in Latvia, at par with the EU-27 average of 7.1%. As per the report, bank loans are still the main source of financing for 28.3% of SMEs in Latvia, below the EU-27 average of 45.7%. In the period of April to September 2021, 14.2% of Latvian SMEs applied for a bank loan, while 9.4% did not, because of fear of rejection. Out of those who applied for a bank loan, 52.3% received the full asking amount, which is below the EU-27 average of 71.3%⁴².



The EIB Investment Survey (EIBIS) for 2020 shows that 14.0% of firms in the Latvian construction sector are dissatisfied with the collateral, 7.0% with the cost, 4.0% with the amount and 4.0% with the maturity of financing⁴³.

Loan rejections account for more than half of the overall share of financially constrained firms with around 14.0% of Latvian firms being financially constrained. This is higher than the EU-28⁴⁴ average of 6.0%⁴⁵. Additionally, availability of finance is considered as a long-term barrier to investment by 73.0% of the firms in the construction sector.

The European Investment Fund (EIF) supports SMEs, and the construction sector, through its

activities. Specifically, **BaltCap Private Equity Fund III**, a venture capital investment fund in the Baltics, aims to generate long-term capital gains from equity and quasi-equity investments in SMEs, mainly in Latvia, Estonia and Lithuania⁴⁶.

In March 2020, the European Commission approved the Latvian subsidised loan scheme and loan guarantee scheme for companies affected by the COVID-19 pandemic. The schemes aim at enhancing the access to external financing for those companies that are most severely affected and ensure that these companies can continue their activities faced with the difficult situation caused by the COVID-19 pandemic. The overall budget for the subsidised loan scheme is EUR 200.0 million while the loan guarantee scheme is budgeted at EUR 50.0 million⁴⁷.

Additionally, in April 2020, NIB and the Republic of Latvia signed a 10-year loan agreement of EUR 500.0 million to finance the economic stimulus measures such as loans, capital injections, extra measures for the most affected business sectors, potentially additional support for small and medium-sized enterprises in the form of working capital or guarantee mechanisms⁴⁸.

Access to housing

The **number of households** in Latvia increased, reaching 861,200 in 2020 from 809,100 in 2010 (+6.4%). At the same time, the share of total **population living in cities and greater cities** rose to 43.3% in 2020 from 42.9% in 2011⁴⁹. While in 2010, 46.7% of the total population lived in densely populated areas, in 2019, it reduced to 43.8%. Notably, the share of the population living in intermediate urbanised areas increased to 189.1% in 2019 from 2.3% in 2010.

Furthermore, the **mean equalised net income** has grown by 78.4% over the period 2010-2019, reaching EUR 9,749.0 from EUR 5,466.0 in 2010. However, it lies below the 2019 EU-27 average of 19,567.0⁵⁰.



Mean equalised net income in EUR

Moreover, the **interest rates on mortgages** (for loans over five years of original maturity), have been declining from 3.7% in 2010 to 2.3% in 2020, remaining almost stable since 2016 (Figure 7). They however slightly increased from 2.2% in 2019. Nevertheless, total **outstanding residential loans to households**, also decreased from EUR 6.6 billion in 2010 to EUR 4.2 billion in 2019⁵¹ (-36.3%).

Figure 7: Mortgage rates for loans over 5 years original maturity (%)



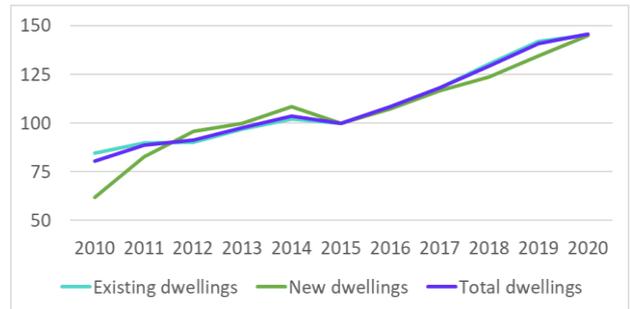
Source: European Central Bank, 2021.

In addition, the **house price index** for total dwelling units increased by 45.8% between 2015 and 2020. This trend is partly driven by the house price index for existing dwelling units, which rose by 45.4% over the same period (Figure 8). At the same time, the increase in house prices has been supported by the steady wage growth of recent years and government supported programmes for house purchase, which was introduced in 2015 and expanded further in 2018.

House prices index for total dwellings between 2015 and 2020 **↑ 45.8%**

According to data published by Eurostat, between 2010 and the second quarter of 2021 house prices in Latvia have almost doubled (+99.0%). Compared with the previous quarter, the highest increase in prices was recorded in Latvia at 6.7% in the second quarter of 2021⁵².

Figure 8: House price index in Latvia between 2010 and 2020 (2015=100)



Source: Eurostat, 2021

Regarding the **building permits** index for residential dwellings, Latvia witnessed an increase of 86.4% between 2015 and 2020. Similarly, building permits for one-dwelling buildings rose by 36.6% over the same reference period. Further, the biggest incline was seen in the building permits for two and more dwelling buildings, rising by 197.9% between 2015 and 2020.

Building permits index for residential dwellings between 2015 and 2020 **↑ 86.4%**

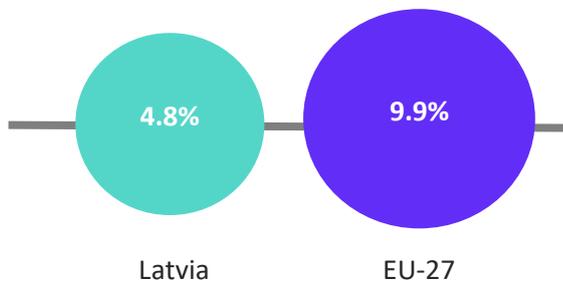
Most of the Latvian **building stock** is owner-occupied, with 81.2% owners occupying buildings in 2020, however below the 2010 level (84.3%). 18.8% of building stock was occupied by tenants in 2020, as compared to 15.7% in 2010. This can be partly attributed to the state policies that favour home ownership.

At the same time, the home ownership rate for the population earning **above 60.0% of the median equalised income** reached 83.9% in 2020 as compared to 87.5% in 2010. Similarly, the home ownership rate for the population earning **below 60.0% of the median equalised income** stood at 71.4% in 2020, below the 2010 level of 72.1%.

In 2020, the **overcrowding rate**⁵³ in Latvia stood as high as 53.7%⁵⁴, surpassing the EU-27 average of 27.4%. Similarly, the **severe housing deprivation rate**⁵⁵ stood at 12.7%⁵⁶ in 2019, three times higher than the EU-27 average of 4.0%. In 2020, it slightly declined to 11.5%. Last, the **housing cost**

overburden rate⁵⁷ has been falling since 2013 (11.4%), standing at 4.8% in 2020, below the EU-27 average of 9.9%. This decline indicates that the pressing issue of housing affordability is being addressed, despite rising house prices⁵⁸.

Housing cost overburden rate in 2020



Infrastructure

According to the 2019 Global Competitiveness Report⁵⁹, Latvia ranks 43rd out of 141 economies in terms of its infrastructure.

With an overall ranking of 52nd out of 141 economies, Latvia performs well in transport infrastructure. In particular, it ranks 15th in efficiency of air transport services, 21st in train services and 27th in road connectivity. Further, it also performs well in terms of railroad density (30th) and efficiency of seaport services (34th). In contrast, the country lags in airport connectivity (82nd), liner shipping connectivity (94th) and quality of road infrastructure (95th)⁶⁰. The country's road density in 2019⁶¹ remained at 29.0km/km² since 2016. It decreased by 6.5% from 31.0 km/km² in 2010.

Latvia ranks third last among the EU Member States in the quality of road infrastructure, after Romania and Malta. Despite recent improvements, the quality of road infrastructure in the country remains well below the European average. In fact, Latvia recorded one of the highest fatality rates on roads at 70 deaths per million inhabitants in 2017 (EU-28⁶² average is 49). The country scores above the EU-28⁶³ average in completion of the TEN-T Core Road Network, with 100% of it being complete⁶⁴. With the purpose of increasing the traffic flow and to move lorry traffic away from residential areas, Latvia has launched its first **public-private partnership** project to design and construct the *Kekava* bypass on the European Route E67⁶⁵. In July 2021, The NIB co-financed the

project through a 21-year loan agreement of EUR 61.1 million⁶⁶.

Also, the construction of **Rail Baltica** project, which will act as a linkage between the three Baltic countries and Poland and therefore to the rest of the European rail network, is not progressing as planned, with the State Audit Offices estimating the project to be delayed by more than two years⁶⁷. In November 2020, General constructor partnership *Bererix*, started the construction of Rail *Baltica* Central Hub in Riga, Latvia⁶⁸. In November 2021, the European Railway Lines, implementer of the Rail *Baltica* project in Latvia, announced a call for tenders for the procurement of the main railway construction work. It is planned to conclude a contract with the winner of the tender at the end of 2022, so that the construction of the new railway line in Latvia can start in the first half of 2023. The project is expected to be completed in 2025⁶⁹.

Further, the country has begun **investing in new trains** to increase the attractiveness of rail commutes and thereby increase the use of public transport for commuting⁷⁰. In August 2021, Latvian Railways began the design and construction of 48 new modern railway stations and stops. The estimated total cost of the project is EUR 44.4 million. The new railway stations and stops will include elevated platforms and several modern equipment, as well as a client-friendly notification system that can be used by all passengers⁷¹.

In May 2021, the construction of the first round of the east highway from *Leriku* street to *Vietalva* street in Riga was launched. The construction of the east highway will provide the possibility to avoid *Rīga* city centre and will relieve the historic centre of *Rīga* and the neighbourhood of *Purvciems* from freight transport. The total cost of the project is EUR 37.8 million and is scheduled to be completed by June 2023⁷².

The Recovery and Resilience Plan of Latvia includes reforms and investments in infrastructure. The plan includes an investment of EUR 295.0 million for creating a multimodal public transport network as well as clean transport infrastructure, including railways, trams, electric buses and cycle lanes⁷³.

4

Key issues and barriers in the construction sector

Company failure

Over the period 2010-2019⁷⁴, **business demography** in the broad construction sector has changed considerably. **Company births** in the narrow construction sub-sector increased from 1,352 in 2010 to 1,770 in 2019 (+30.9%), after reaching its peak in 2015 (2,903), whereas there was a 68.2% incline in the architectural and engineering activities sub-sector, rising from 151 in 2010 to 254 in 2019. However, company births in the real estate activities sub-sector declined by 30.0%, falling from 1,425 in 2010 to 997 in 2019.

Company births in the narrow construction sub-sector between 2010 and 2019

 **30.9%**

Furthermore, except for the architectural and engineering activities sub-sector, all the other sub-sectors registered a decrease in the number of **company deaths** over the same reference period. The narrow construction sub-sector recorded the largest decrease of 13.4% in company deaths (from 1,081 in 2010 to 936 in 2019). This was followed by a 10.5% decrease in the real estate activities sub-sector (1,301 in 2010 to 1,164 in 2019). Conversely, there was a 34.3% increase in the architectural and engineering activities sub-sector (from 99 in 2010 to 133 in 2019).

Company deaths in the narrow construction sub-sector between 2010 and 2019

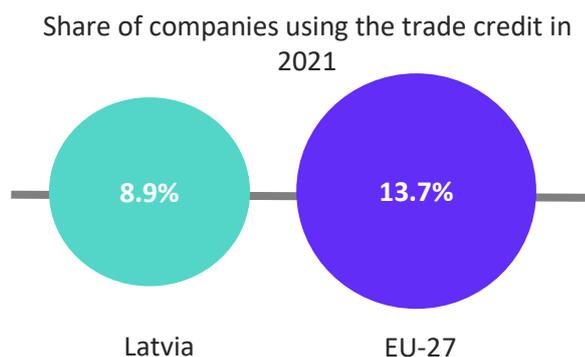
 **13.4%**

According to the Euler Hermes' Insolvency estimates, the number of companies that became insolvent in Latvia in 2020 reduced to 374 from 557 in 2019. However, owing to the recovery from the COVID-19 pandemic, it is forecasted that this number will further fall to 260 by the end of 2021 and 330 by the end of 2022⁷⁵.

Trade credit

According to the SAFE 2021 report, trade credit constitutes a relevant source of financing for only 19.4% of Latvian SMEs, below the EU-27 average of 27.8% in 2021⁷⁶.

As per the report, only 8.9% of the SMEs have obtained trade credit from their business partners in the last six months as compared to the EU-27 average of 13.7%. Further, 28.5% of the SMEs have applied for trade credit in the last six months, while the EU-27 average stood at 29.6%. Out of 29.6% of SMEs who applied for trade credit in the last six months, 70.7% SMEs received everything they applied for. This stands below the EU-27 average of 71.6% in 2021. Also, 61.8% of the SME respondents consider availability of trade credit has remain unchanged over the past six months and 51.9% of SMEs expect trade credit financing to remain unchanged in the six months following the survey⁷⁷.



Late payment



According to the European Payments Report 2021, 54.0% of businesses in Latvia have agreed to accept longer payment terms in order to avoid damaging client relationships⁷⁸.

As per the report, 38.0% Latvian firms consider the widening gap between the payment terms and duration of pay is a real risk to the sustainable growth of the business. On average, business-to-business (B2B) customers in Latvia are allowed 41 days to pay dues, at par with the EU-28⁷⁹ average of 41 days. However, in practice Latvian B2B customers took an average of 52 days to pay dues in 2021, at par with the EU-28⁸⁰ average of 52 days⁸¹.

42.0% of Latvian companies consider that late payments lead to loss of income and prohibit growth potential, with 38.0% of companies believing that the financial difficulties of debtors are the main cause of the problem⁸².

Further, with the ongoing COVID-19 pandemic, the situation has become more difficult. According to the European Payment Report 2021, 55.0% of respondents expect debtors to have liquidity challenges due to the impact of COVID-19, and will likely affect late payments. This is higher than the EU-28⁸³ average of 48.0%⁸⁴.

Additionally, 42.0% of respondents in Estonia ranked “Risk of a pan-European recession” as one of the main challenges in terms of their customers paying on time and in full over the next 12 months⁸⁵. This is above the EU-28⁸⁶ average of 40.0%. At the same time, 57.0% respondents are more concerned than ever before about debtors’

ability to pay on time, below the EU-28 average of 62.0%. Lastly, 70.0% of respondents believe the risk of late/non-payments increasing during the next 12 months, above the EU-28 average⁸⁷ of 66.0%⁸⁸.

As per the SAFE 2021 report, 8.9% of SMEs reported facing late payment issues on a regular basis, below the EU-27 average (11.8%)⁸⁹.

52.9% of SMEs reported that their payments to suppliers have been affected as a result of late payments by customers. For 41.0% of SMEs, late payment affected production or operations, and for 36.2% it impacted investments or new hiring. 23.7% of SMEs also reported that their loan repayments have been delayed, or they have had to seek additional financing, as a result of late payments⁹⁰.

Time and cost of obtaining building permits and licenses

According to the 2020 World Bank’s Doing Business Report⁹¹, Latvia ranked 56th out of 190 economies in ‘dealing with construction permits’, equal to last year’s ranking⁹².

As per the report, it requires 14 procedures and 192 days in total to complete the formalities to build a warehouse⁹³. This is higher than the OECD high-income average (12.7 procedures and 152.3 days) (Table 3). The cost of obtaining a building permit for a warehouse represents 0.4% of the value of the warehouse, below the OECD high-income average of 1.5%.

Table 3: Construction procedures timing and costs in Latvia

Procedure	Time to complete	Associated costs
Obtain topographic survey of the land plot	24 days	EUR 475
Obtain geo-technical study of the land	21 days	EUR 1,000
Request and obtain a building permit ⁹⁴	30 days	EUR 1,409
Obtain technical requirements from the State Environmental Service of the Republic of Latvia	28 days	no charge
Obtain technical requirements from water and sewage company	21 days	no charge
Obtain design clearance from water and sewage company	7 days	no charge
Obtain a note in the construction permit regarding execution of the design	21 days	no charge

conditions		
Obtain a note in the construction permit regarding execution of the conditions for commencing construction work	7 days	no charge
Receive inspection by the State Environmental Service of the Republic of Latvia	1 day	no charge
Receive inspection by Fire Safety and Rescue Department	1 day	no charge
Obtain measurements from State Land Service	27 days	EUR 263
Obtain water and sewerage connection	20 days	EUR 37
Receive on-site inspection and obtain the final handover certificate	5 days	no charge
Register the building in the land book	20 days	EUR 23

Source: Doing Business overview for Latvia, World Bank 2020⁹⁵

Skills shortage



The number of job vacancies in the narrow construction sub-sector experienced an increase of 217.0%, rising from 594 in 2010 to 1,882 in 2020.

However, job vacancies in the narrow construction sub-sector observed a 41.8% decline from 2019. Further, job vacancies in the real estate activities sub-sector increased from 99 in 2010 to 409 in 2020 (+314.2%). In line with this, the **job vacancy rate** in the narrow construction sub-sector stood at 2.9% in 2020 (1.3% in 2010). Further, in the real estate activities sub-sector, job vacancy rate stood at 1.4% in 2020, compared to 0.4% in 2010.

Number of job vacancies in the narrow construction sub-sector during 2010-2020

↑ 217.0%

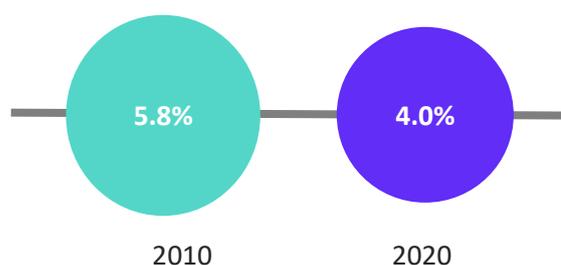
Skills shortages remain as one of the biggest challenges for the sector's growth. A lack of qualified professionals is observable from enrolment in trade schools to engineering and design studies. There is also a need for construction managers, water and wastewater engineers and roofers.

At the same time, the **number of tertiary students** in engineering, manufacturing and construction suffered a decline of 24.6% between 2010 and 2019⁹⁶, falling to 1,859 from 2,465. The number of tertiary students in architecture and building fell (-45.2%), followed by a 28.5% and 9.2% decline in manufacturing and processing and

engineering and engineering trades, respectively, over the same reference period.

Further, **adult participation in education and training** in the narrow construction sub-sector has generally been fluctuating over the years, declining from 5.8% in 2010 to 4.0% in 2020, after reporting a high at 7.2% in 2017. In the real estate activities sub-sector, adult participation in education and training stood at 10.0% in 2017⁹⁷.

Adult participation in education and training in the narrow construction sub-sector



As per the EIB Investment Survey 2020 report, 94.0% of firms in the construction sector reported availability of skilled staff as a long-term barrier to investment⁹⁸.

Skills shortages and mismatches also limits productivity growth. Low and medium-skilled workers can switch between specialisations, depending on the available job offers, because they do not require a document certifying their qualification. While this offers flexibility for construction workers, it does not allow them to acquire a true specialisation and associated skills⁹⁹.

Furthermore, the major gaps in skills include a lack of understanding about energy efficiency solutions, the use of new technologies and nearly zero energy buildings. In particular, regarding roofers, plasterers, carpenters and installers, there is a need to improve their skills on building airtightness and construction leakage prevention, as renovations make up about 90.0% of their work¹⁰⁰.

Latvia adopted a construction industry development strategy for 2017-2024. It addressed various industry issues, such as, ensuring a qualified workforce, increasing productivity, reducing administrative barriers and improving the quality of construction services¹⁰¹.

By 2025, the deficiency of adequately skilled manpower in Latvia is expected to exceed 14,000, with construction and civil engineering, being one of the key sectors affected. Moreover, data from the State Employment Agency suggest that almost 78.0% of vacancies in Latvia in the first quarter of 2021 were registered with profession groups requiring low to medium levels of qualifications like construction workers, bricklayers, builders, carpenters, and unskilled road construction workers, among others. In fact, the number of vacancies in the construction sector has increased in 2020, indicating a severe shortage of manpower across skillsets¹⁰².

Moreover, job opportunities are concentrated in urban areas, but labour mobility remains hindered by the shortage of affordable housing and poor transport connections.

Labour supply is expected to continue falling due to emigration and natural decline in the population. This in turn will lead to further labour shortages and skill mismatches in the country¹⁰³.

To counteract the shortage of skilled workers in a number of sectors in the national economy, the Ministry of Economics drafted a list of 29 sub-groups of professions where there is currently a significant lack of workforce and which could benefit from the influx of foreign specialists¹⁰⁴. To this end, the Ministry introduced **preferential conditions to attract highly qualified specialists from abroad** in the identified professions. Among the shortage occupations feature construction technicians, civil engineers and sustainable construction engineers¹⁰⁵.

Sector and sub-sector specific issues

Material efficiency and waste management

Owing to a rise in economic activity and specifically in construction, **waste generated by the construction sector** has increased in recent years. In the European Union, construction and demolition waste (CDW) constitute one of the biggest waste streams. CDW accounts for approximately 25.0% - 30.0% of all waste generated in the EU. CDW mainly consists of several materials, including concrete, bricks, gypsum, wood, glass, metals, plastic, solvents,

asbestos and excavated soil, many of which can be recycled¹⁰⁶.

The bulk of **CDW** is made up for 81.0% of waste soil and stones, with the remainder segregated wastes such as rubble, concrete, bricks, glass, plastic, wood, metals and mixed CDW. In 2018¹⁰⁷, construction activities alone generated a total waste of 306,730 tonnes in Latvia. This was 1,558.2% higher than the waste generated in 2010, 18,498 tonnes¹⁰⁸.

Waste generated from construction activities in Latvia between 2010 and 2018

 **1,558.2%**

Waste management in Latvia, including CDW, is governed by the **Waste Management Law** of 2010¹⁰⁹. It establishes general requirements and procedures for waste management and prevention. In addition, the **Natural Resources Tax Law**¹¹⁰ imposes mandatory fees to “high polluters” in order to encourage pollution reduction and waste management implementation. The **National Waste Management Plan 2013-2020** also sets out practices and objectives to curb the generation of waste in the country.

More specifically, the Construction Law and Construction Regulations also set principles for environmental protection, fostering sustainable construction and the effective use of natural resources. For instance, recycling and recovery of waste generated during construction activities should be promoted and all hazardous construction waste should be managed in accordance with the regulatory enactments regarding hazardous waste¹¹¹.

The waste management policy of Latvia is stipulated in the **State Waste Management Plan for 2021-2028**. The plan’s primary strategic targets are significant reduction in waste generation, rational use of waste as a resource and ensuring reduction in the amount of waste to be landfilled. The plan aims to reduce the amount of waste stored in landfills so that no more than 10.0% of the total amount of municipal waste is disposed of in landfill by 2035, while recycling would represent at least 65.0% of the total amount of municipal waste¹¹².

The Recovery and Resilience Plan of Latvia envisages the objective that for each of the measures at least 70.0% (by weight) of the hazardous and non-hazardous construction and demolition waste generated on the construction sites will be prepared for reuse, recycling and other material recovery¹¹³.

Climate and energy

Latvia is among EU's top performers in renewable energy, with greenhouse gas emissions per capita being among the lowest in EU¹¹⁴.

Emissions of greenhouse gases (carbon dioxide, methane and nitrous oxides) from the narrow construction and real estate activities sub-sectors in Latvia amounted to a total of 262,953 tonnes and 173,919 tonnes in 2019¹¹⁵, respectively. While emissions in the narrow construction sub-sector increased slightly by 0.3% during the period 2010-2019, emissions in the real estate activities sub-sector declined by 3.9% over time. This indicates that the country is progressing well in containing its greenhouse gas emissions.

Regarding greenhouse gases emissions, Latvia underlines in its Recovery and Resilience Plan its contribution to reaching the 2030 and 2050 targets and considers that the measures implemented under the plan could lead to a reduction of 36,241 t/CO₂ equivalent per year in total. The measures in the plan are expected to contribute to achieving the climate neutrality and the 2030 energy and climate targets entailed in the National Energy and Climate Plan.

As part of the green transition and to reduce greenhouse gases emissions in Riga, Riga Transport reform proposes an investment programme to decarbonise and improve public transport. The plan will focus on railway solutions (electrification of 81 km of railway) and zero-emission electro-mobility (acquisition of four low-floor trams, 17 electric buses and seven electric bus charging stations, construction of a cycle roads). These different investments represent clean urban rolling stock or infrastructure. With a total of EUR 295.4 million, this subcomponent in the Recovery and Resilience Plan represents the second biggest climate contribution to the 37.0% target¹¹⁶.

5

Innovation in the construction sector

Innovation performance

According to the European Innovation Scoreboard 2021, Latvia is classified as an Emerging Innovator, with a continuous increase in performance up till 2020. However, it experienced a decline in performance in 2021¹¹⁷.

As per the report, the relative strong decrease in innovation performance between 2020 and 2021 was mainly due to the sharp decline venture capital investments, from 0.2% to 0.02% of GDP. There was also a decline in the development of environment-related technologies from 12.4 in 2020 to 5.1 in 2021. The top three indicators include population with tertiary education, trademark applications and enterprises providing ICT training. Its main strengths are in the use of information technologies, human resources and digitalisation. On the other hand, Latvia has above average shares of non-innovators with potential to innovate and non-innovators without disposition to innovate. It is also showing below average scores on the climate change related indicators¹¹⁸.

In the broad construction sector, **business enterprise R&D expenditure (BERD)** in the professional, scientific and technical activities sub-sector¹¹⁹ decreased from EUR 6.1 million in 2010 to EUR 3.6 million in 2018¹²⁰. This represents a decline of 41.3% over the 2010-2018 period. BERD in the narrow construction sub-sector attained a level of EUR 0.3 million in 2018, from zero in 2010¹²¹.

BERD expenditure in professional, scientific and technical activities sub-sector between 2010 and 2018

↓ 41.3%

In parallel, the **total R&D personnel** (full-time equivalents – FTE)¹²² in the broad construction sector dropped across all sub-sectors as of 2010.

The total **R&D personnel** in the professional, scientific and technical activities sub-sector declined from 313 in 2010 to 112 in 2018¹²³ (-64.2%). Similarly, FTE in the narrow construction sub-sector declined from 10 in 2010 to seven in 2016¹²⁴ (-30.0%), demonstrating the low levels of private sector engagement in R&D in the Latvian construction sector.

R&D funding in Latvia is also very low, as it stood at 0.6% of GDP in 2019, well below the targeted level of 1.5%¹²⁵. Low investments in R&D will negatively affect the long-term growth in the country and will limit the possibilities of developing knowledge and technology-intensive industries and achieving higher productivity¹²⁶.

Furthermore, the limited innovative capacity of Latvian construction companies is demonstrated by the low number of **construction-related patent applications** registered. The country has not filed any patent application in 2020.

During the 2010-2020 period, only six patent applications have been filed by Latvia. No Latvian construction and materials firms rank within the top 1,000 EU companies by R&D, according to the 2020 EU R&D Scoreboard¹²⁷.

As per the **2019 SBA Fact Sheet**, Latvia has performed below the EU-28¹²⁸ average in terms of innovation. The indicators in Latvia such as share of SMEs bringing product/process, marketing or in-house innovations, share of SMEs purchasing and selling online, turnover from e-commerce, national R&D available to SMEs, and many other indicators rank below the EU-28 average¹²⁹.

Although innovation is an area which has been a top priority for Latvian government since 2014, the overall performance in this area has been moderate. Between the period 2018 and first quarter of 2019, two measures were adopted for promoting innovation in SMEs¹³⁰:

- **support for the development of new products and technologies within competence centres, Round 4** (*Jaunu produktu ieviešana ražošanā 4. kārtā*): As per the measure, the companies will be able to receive support for industrial research, experimental development and technical economic feasibility studies for research projects within one competence centre. An additional funding of EUR 37.0 million has also been allocated from European Regional Development Fund (ERDF)¹³¹.
- an amendment to the existing technology transfer programme, '**Innovation voucher support for SMEs** (*Inovāciju vaučeri*)' had been implemented. This intends to raise interest in this type of support and improve the level of innovation in SMEs. This programme is being implemented by the Latvian Investment and Development Agency, with a total allocation of EUR 2.8 million from the EU Structural Funds. New activities — which form part of the technology transfer programme — include external experts for innovation audit and designer services to introduce new products¹³².

Eco-innovation and digitalisation

According to the **Eco-Innovation Scoreboard (Eco-IS) 2019**, Latvia scored 86 in comparison to the EU-28¹³³ average of 100, falling under the **Average Eco-I performers group**¹³⁴.

As per the report, Latvia's score was above the EU-28¹³⁵ average on two indicators, namely; eco-innovation outputs and socio-economic outcomes. For the remaining three indicators – eco-Innovation inputs, eco-Innovation activities and resource efficiency outcomes, the country scored below the EU-28 average¹³⁶.

According to the **European Commission Digital Economy and Society Index (DESI) 2021**, Latvia ranked 17th with a score of 49.5, out of EU-27 Member States (average score: 50.7). This signifies a rise in the 2021 ranking, although the score itself had not changed in comparison with 2020 (rank: 18th and score: 50.7). As compared with 2020, Latvia improved its score in 2021 in terms of

human capital. However, its score in connectivity, digital public services and integration of digital technology dropped in 2021, as compared to 2020¹³⁷.

Among all dimensions, Latvia ranked highest in digital public services (10th), followed by connectivity (14th), human capital (20th) and integration of digital technology (23rd)¹³⁸.

As per the **EIB Investment Survey 2020**, more than three in five firms (62.0%) have implemented, either fully or partially, at least one digital technology. This brings Latvia in line with the EU-28 average (63.0%). Specifically, in the construction sector, around 50.0% of Latvian businesses adopted using drones, above the EU-28 average of 19.0%. In terms of using 3-D printing, around 19.0% of Latvian businesses reported their usage, more than the EU-28¹³⁹ average (10.0%). Moreover, 12.0% and 11.0% of Latvian businesses have reported using internet of things (IoT) and augmented or virtual reality, in comparison with 22.0% and 11.0% of businesses in the EU-28¹⁴⁰ average, respectively¹⁴¹.

The Latvian National Development Plan 2014-2020, the Transport Development Guidelines 2014-2020 and the National Roads Programme 2014-2020 of Latvia list the investment in the development and modernisation of Latvia's transport infrastructure, in particular, roads and railways, as a priority. In this context, the Latvian public sector is taking steps towards the **building information modelling (BIM)**¹⁴².

With regards to implementation of BIM in Latvia, a public organisation named the **Latvian Building Information Modelling Society (LatBIM)** was founded in 2014. LatBIM aims at promoting development of BIM throughout Latvia and cooperating with state and local authorities, European and global BIM organisations. Amongst others, it prepares technical documentation work orders and quality requirements for BIM construction designs. It also organises events for municipalities, construction boards or trade missions¹⁴³.

In 2019, the Riga Technical University partnered with two other Baltic universities and established a knowledge and innovation contact point – EIT Raw Materials Baltic Hub. The hub aims to address the

shortage of raw materials in construction, energy and water management in the Baltic states¹⁴⁴.

The hub will also focus on innovations in these sectors. The hub will implement three programs successively in the Baltic states (Latvia, Lithuania and Estonia). Each of these programs aims to encourage scientists to reuse and recover raw materials from industrial waste to obtain materials used in concrete-like products. The program will also focus on recovery of several metals and substances from wastewater, to use in construction, energy and water management¹⁴⁵.

In October 2021, the Construction Industry Digitalisation Association of Latvia in cooperation with Riga Technical University, Latvia University of Life Sciences and Technologies, Riga Building College and Vidzeme University of Applied Sciences, organised a Construction Digitalisation Conference 2021 in Riga¹⁴⁶.

The conference was organised with the aim to acquaint all participants of the Latvian construction industry – architects, designers, builders, real estate developers, municipalities – with construction digitisation processes to coordinate the development of the industry internationally, promote cooperation between different countries and create a unified digitisation platform¹⁴⁷.

In December 2020, Zigurat Global Institute of Technology partnered with Innovative Technologies in Engineering & Design (ITED)- a Latvian consultancy firm. Through this, Zigurat will approach a new market in Latvia and the Baltic market. This alliance will allow Latvian Construction companies to access Zigurat's master's programs, which are specialised in Building Information Modelling, Smart Cities, Digital Business, and Blockchain. The collaboration is part of Zigurat's strategy of having a wide network of international collaborators and local promoters to offer the best practices and standards globally¹⁴⁸.

The Recovery and Resilience Plan of Latvia includes almost EUR 384.0 million (21.0% of the total budget) to tackle the main digital challenges. Targeted measures in the digital transformation and innovation of businesses aim to enhance digitalisation capacities through a broad spectrum of actions, such as: establishing a European Digital Innovation Hub (EDIH); grants and financial instruments to support the digital transformation of businesses, including research and innovation, training and advanced technologies. The plan also includes two measures on connectivity infrastructure: last-mile connectivity in rural areas and construction of passive infrastructure on the Via Baltic 5G corridor¹⁴⁹.

6

National and regional regulatory framework

Policy schemes

To boost the Latvian construction sector and increase its productivity and competitiveness, the Ministry of Economics and the Latvian Construction Council (*Latvijas Būvniecības Padomes*) approved the **Latvian Construction Industry Development Strategy for 2017-2024** (*Latvijas būvniecības nozares attīstības stratēģija 2017. – 2024. gadam*) in April 2017¹⁵⁰. The main purpose of the strategy is to establish a common policy for the development of a sustainable and competitive construction industry in Latvia. To achieve this vision, several sector-specific strategic goals are defined:

- reduce construction bureaucracy and decrease the overall duration of the construction process by 50.0% via digital solutions;
- achieve a threefold increase in productivity in the sector and therefore rank among the top 10 EU Member States;
- increase the turnover of the construction sector from the current EUR 1.5 billion per year to EUR 3.0 billion per year;
- improve the system of education and professional qualifications of construction specialists, ensuring the availability of a highly qualified workforce in each construction profession;
- improve the quality of construction services, whilst creating a common quality measurement system.

In order to increase the efficiency of construction processes, a number of strategies have been adopted. This includes a streamlined approach to shorten the building design process, reduced administrative burden, acceleration of approval process through assignment of clear-cut

responsibilities, as well as digital document circulation. With the introduction of a **Construction Design Documentation** (*Būvniecības ieceres dokumentācijas noformēšana*), specific guidelines for construction project documentation, electronic design, and implementation of digital construction ideas were established¹⁵¹.

The housing policy in Latvia is under the responsibility of the Ministry of Economics. The state-owned Development Finance Institution ALTUM oversees its implementation. It administers EU and national funding to provide several financial instruments (loans, grants, guarantees, etc.) for businesses and individuals. Namely, ALTUM offers support schemes for the purchase of dwellings and for energy focused renovation¹⁵².

The Housing Guarantee Programme (*Mājokļu galvojumu programmu*), the main state-aid scheme supporting the purchase and/or construction and renovation of the first home, has supported more than 14,000 housing guarantees as of November 2020¹⁵³.

Initially launched in 2014, it provides guarantees on mortgages for families with at least one child who have a stable income but who do not have enough savings for an initial down payment. The amount of the guarantee depends on the number of dependent children. Families with one child are eligible for guarantees up to 10% of the value of the loan (and up to a maximum of EUR 10,000), whereas families with two children can benefit from a guarantee of 15% (up to EUR 15,000). The amount of the guarantee increases to 20% of the loan (up to EUR 20,000) for families with three or more children. Guarantees can be provided for house purchases/ construction and renovation

costs up to EUR 200,000. A one-off fee equal to 2.5% of the guarantee's amount applies¹⁵⁴.

From March 2018, the program was expanded to include people under the age of 35 that have completed a vocational education programme, as well as persons with at least one dependent child under 24 years of age (as compared to the previous support limited to families with children under the age of 18)¹⁵⁵.

In June 2020, the Latvian government amended the state support program for the purchase of housing, by providing EUR 3.5 million to support nearly 400 large families with the purchase of housing¹⁵⁶.

For this, in November 2020, the support program "Balsts" is designed to provide more support to large families (three or more children, and in some cases, two children and a pregnant woman). Large families who take a loan from the bank for the purchase or construction of a home will be eligible for the support of the "Balsts" program. Subsidy shall be provided if the amount of the real estate transaction does not exceed EUR 250,000¹⁵⁷. The amount of subsidy is based on the following criteria:

- For families with three children (even if the third is still expected), the subsidy is EUR 8,000 for ordinary housing or EUR 10,000 if the housing meets the energy efficiency requirements for near-zero energy buildings.
- For families with four children (even if the fourth is still expected), the subsidy is EUR 10,000 for ordinary housing or EUR 12,000 if the housing meets the energy efficiency requirements for near-zero energy buildings.

In addition, **the Law on Assistance in Solving Apartment Matters** (*Par palīdzību dzīvokļa jautājumu risināšanā*) explains the principles of social housing and housing allowances for eligible beneficiaries. Namely, the types of assistance defined by the document include the provision of temporary living space, housing benefits to support the payment of rent and property management fees, as well as allowances for renovation and adaptation of dwellings¹⁵⁸. These topics are under the remit of the local municipal governments, which are responsible for their

budget allocation and implementation. Following the Law, Local authorities provide services to individuals consisting of renting out social housing, support in exchanging current dwelling for a bigger one, providing temporary accommodation, or providing a specialist housing support-service¹⁵⁹. For instance, the Riga City Council offers eligible beneficiaries (i.e. families with children, people with disabilities, etc.) housing benefits of up to EUR 4.27 per m² to cover a portion of the rent, management fees and other fees related to the use of the living space, based on their income¹⁶⁰.

In addition, the municipality of Riga partially covers utility costs (e.g. 25.0% for heating and 50.0% for water and wastewater) and provides social housing at a rent of EUR 0.06 per m², well below rental market prices¹⁶¹. Finally, the municipality offers a housing adaptation allowance for people with disabilities, enabling them to hire a construction company to carry out adaptation works to improve the accessibility of their residence. The amount of the allowance may not exceed EUR 2,134.3¹⁶².

In April 2021, the Latvian government submitted its Recovery and Resilience Plan to the European Commission. In June 2021, the Commission endorsed the plan, and it was adopted by the Council¹⁶³.

Latvia's plan consists of 6 components, containing a broad range of policy areas and aims to address the country's key challenges with a balanced set of reforms and investments. The key areas for investments are the green and digital transitions, health infrastructure, social and regional infrastructure as well as research and innovation. The measures include direct investments in public infrastructure as well as extensive support programmes for private investment in the twin transitions and innovation. A large share of RRP funding (64.0%) is dedicated to implementing the National Industrial Policy (NIP) 2021-2027. In addition, the RRP is coherent with other national planning documents, such as the National Energy and Climate plan¹⁶⁴.

Building regulations

Construction Law (*Būvniecības likums*), initially introduced in 1995, defines the main provisions related to the procedures of the construction process, rights and responsibilities of parties involved, certification and licensing of construction

participants, principles of construction supervision and control, as well liability and insurance, among others¹⁶⁵.

To simplify the regulatory framework, reduce the administrative burden and thus accelerate and promote the construction of new buildings, a new Construction Law entered into force in 2014. This reduced the number of decisions involved in the construction process. After submitting a construction intention and building design, the second step directly entails the issuing of the building permit. Thus, the authorities no longer take three decisions (issuing the architecture and planning assignment, accepting the building design, issuing the construction permit), but only one (issuing the construction permit)¹⁶⁶.

Moreover, the time allowed to the building authority to decide on issuing the permit is limited to one month. The revised legislation includes the obligation to inform the public about the planned construction work within five days of receiving the permit and regulates the qualifications, certifications and responsibilities of the participants in the construction process in greater detail¹⁶⁷.

Additional amendments to the Construction Law were enforced in 2017, aiming to further reduce the administrative burden and increase the efficiency of the construction process. These amendments introduced more relaxed requirements for changing the construction plan. Namely, it will be easier to deviate from certain initial technical requirements, with the exception of mechanical strength and stability requirements, where deviation will not be possible. Changes in the location of the building, in the construction site and in the facade will also be allowed after their approval by the building board or the institution that carries out the building management. Conversely, changes to the main use of the building are not envisaged¹⁶⁸.

Sustainability of the Industry and eradication of the shadow economy has long been a priority issue on the agenda of both the government and relevant stakeholders. In this context, the electronic working time recording system (*elektroniskā darba laika uzskaites sistēma – EDLUS*), mandated for new civil engineering projects and for all types of new construction works which value exceed EUR 1.0 million¹⁶⁹, was

implemented via amendments to the Law on Taxes and Duties. The amendments require general contractors to implement and maintain the EDLUS at the construction site, as well as for the storage of data until they are transferred to a *Single State database*. EDLUS registers the data of workers and the time they spent on the construction site. Furthermore, following the amendments to the Law on Taxes and Duties of 2019, the threshold of EUR 1.0 million was reduced to EUR 350,000, as of 1st January 2020. Additionally, as of 1st February 2020, general contractors are required to transfer the collected EDLUS data on the previous month to the Single State database, which is unified electronic working time recording system data base - (*vienotā elektroniskā darba laika uzskaites datu bāze – VEDLUDB*) and integrated in the Construction Information System (BIS). In order to eradicate the shadow economy, the minimum sectoral wage was increased in 2019 through, the General Agreement of the Construction Industry (herein after – General Agreement), which is an industry-driven initiative aiming to strengthen fair competition and mitigate labour shortages by setting the sectoral minimum wage. The latter amounts to EUR 780 (EUR 819 for qualified workers) since November 2019. This is 81.0% higher than the statutory minimum wage in Latvia (EUR 500 - amended as of 1st January 2021) and is positively affecting more than 30,000 employees.

In September 2018, an additional amendment to the Construction Law was undertaken to make all documentation required for the construction process fully digital through the introduction of the **Construction Information System** (*Būvniecības Informācijas Sistēma – BIS*). These changes to the Construction Act are due to come into force¹⁷⁰.

BIS is an electronic platform (in the form of a state information system) where information is circulated between the public administration, supervisory bodies and parties to the construction process¹⁷¹.

BIS is expected to minimise the administrative burden through electronic harmonisation of construction documents. Moreover, it will also significantly reduce the time needed to complete a construction project and eliminate paperwork¹⁷².

Under the Construction Act, as of 1 January 2020, it will be mandatory for the construction authorities and institutions (that fulfil the functions

of a construction authority) to run the administrative proceedings, make decisions and coordinate construction plans through the BIS platform. BIS allows the initiator of a construction process not only to authorise construction professionals within construction proceedings but also any other individual. This feature of BIS will allow developers of various sections of building design, construction contractors and – where appropriate – legal services to be involved in the construction process¹⁷³.

In order to speed up the development projects delayed due to appeals from neighbours, NGOs etc., a number of changes concerning the permitting process was made in the construction law effective from May 2021. The amendments include: in case if the supervising institution has taken a decision to reject an appeal of the positive decision taken during the construction process, a further appeal to the court shall not suspend operation of the decision and the developer will be entitled to proceed at its own risk; and an appeal of a note on completion of construction commencement conditions shall not suspend its operation, thus allowing the developer to proceed with the works while the appeal is pending. The amendments will provide more certainty in the development process and possibility to proceed at the own risk. At the same time, the courts still will be able to accept decisions on interim measures suspending operation of the permits which seem prima facie illegal and may result in irreparable damage¹⁷⁴.

In November 2020, the Construction Board of Riga City Council adopted a principle of a Green Corridor for sizeable development projects to assist more speedy advancement of the largest projects. Currently, the Green Corridor is available in the permitting process of buildings of the second and third category if they envisage construction of more than 100 apartments. The Construction Board intends to expand the corridor to other types of projects also¹⁷⁵.

The procedure of Green Corridor involves preliminary review of sketches and parts of the design; issue of a building permit within 14 days (instead of a month); granting of a note on completion of design conditions within 10 days (instead of 15 business days); granting of a note on completion of construction commencement

conditions within one business day (instead of five business days); appointment of a designated project manager for more efficient communication. Thus, the procedure may result in saving 71 days as compared to the regular permitting procedure¹⁷⁶.

In addition to the Construction Law, a variety of other laws and regulations make up the construction regulatory environment, governing topics such as planning, design preparation, design, construction product conformity, hygiene requirements, as well as special building regulations. Instances include the General Construction Regulations (*Vispārīgie būvnoteikumi*), Procedures for the Market Surveillance of Construction Products (*Būvizstrādājumu tirgus uzraudzības kārtība*), Spatial Development Planning Law (*Teritorijas attīstības plānošanas likums*) and the Regional Development Law (*Reģionālās attīstības likums*), among others¹⁷⁷.

Insurance and liability related regulations

In Latvia, according to the Construction Law, contractors have the duty to insure their civil legal liability for the damage caused to the life, health or property of other construction or third parties, as well as to the environment, resulting from their actions or failure to act. Insurance can be taken out either on an annual basis - covering all construction sites and having to be renewed each year - or in relation to a specific construction site, remaining valid throughout the entire construction process¹⁷⁸.

In the case of an annual liability insurance for all construction sites, the limit of the insurance should be at least 10.0% of the building contractor's annual turnover. Similarly, the limit of the insurance in the case of a specific construction project should be no less than 10.0% of the value of the contract¹⁷⁹. The builder may also use other types of insurance, regarding the building or the construction process, in addition to the compulsory construction civil liability insurance¹⁸⁰.

It is common to take out Contractor All Risk (CAR) insurance for medium and large projects, with the liability limit varying between 5.0-18.0% of the contract value, depending on the agreement. For

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large scale projects, 10.0%-15.0% of the contract value is retained by the client upon completion of the construction works for up to two years, in case

defects arise. The amount is returned to the contractor if no such issues occur within that timeframe¹⁸¹.

7

Current status and national strategies to meet Construction 2020 objectives

TO 1 – Investment conditions and volumes

Total investment by the broad construction sector¹⁸², has been fluctuating since 2010 (Figure 10). Particularly, investment by the narrow construction sub-sector grew from EUR 88.2 million in 2010 to EUR 119.7 million in 2020 (+35.6%). Similarly, investment by the real estate activities sub-sector increased from EUR 717.9 million in 2010 to EUR 1233.1 million in 2020 (+71.8%).

Total investment by the narrow construction sub-sector between 2010 and 2020

↑ 35.6%

Total investment by the real estate activities sub-sector between 2010 and 2020

↑ 71.8%

Similarly, investment in intellectual property products by the narrow construction sub-sector reached EUR 4.6 million in 2020 from EUR 0.9 million in 2010, marking a 411.1% increase over the period. Additionally, investment by the real estate activities sub-sector for this category reached EUR 2.4 million.

Figure 9: Investment by the Latvian broad construction sector between 2010 and 2019¹⁸³ (EUR m)



Source: Eurostat, 2021.

Total investments index in the broad construction sector¹⁸⁴ increased by 8.4% over the 2015-2020 period (Figure 11), primarily driven by the investments in non-residential construction and civil engineering, which experienced a growth of 11.1% over time. On the contrary, investments in dwellings registered a decline of 1.8% over the same reference period. In absolute terms, investments in the broad construction sector totalled EUR 3.5 billion in 2018¹⁸⁵, out of which EUR 740.6 million were invested in dwellings and EUR 2.8 billion were devoted to non-residential and civil engineering¹⁸⁶.

Total investment index in non-residential construction and civil engineering between 2015 and 2020

↑ 11.1%

Figure 10: Investment in the Latvian broad construction sector between 2010 and 2020 (2015=100)



Source: AMECO, 2021.

Total inland infrastructure investment¹⁸⁷ as a share of GDP decreased from 1.1% in 2010 to 0.8% in 2019¹⁸⁸, after recording the decade's high in 2015 (1.7%).

Investment in air transport infrastructure registered a rise of 400.0%, rising from EUR 4.0 million in 2010 to EUR 20.0 million in 2019¹⁸⁹. This was followed by a 70.2% rise in road infrastructure investment, which grew from EUR 131.0 million to EUR 223.0 million over time. Conversely, investment in railway infrastructure declined from EUR 73.0 million in 2010 to EUR 13.4 million in 2019 (-81.6%). Further, investment in road maintenance went up, from EUR 113.0 million to EUR 179.0 million, recording a 58.4% incline between 2010 and 2019. Similarly, investment in rail maintenance rose by 15.5% from EUR 98.0 million to EUR 113.2 million over the same reference period.

Air transport infrastructure investment between 2010 and 2019

↑ 400.0%

From January to October 2020, the Latvian government invested EUR 17.5 million into regional roads, EUR 5.8 million into maintenance of state roads and EUR 32.3 million into maintenance of local roads¹⁹⁰.

In parallel, **household renovation spending** in Latvia increased by 47.9% over 2010-2020, rising from EUR 38.6 million in 2010 to EUR 57.1 million in 2020. However, in 2019 it stood at EUR 50.2 million, below the EU-27 average of EUR 73.7 billion. Moreover, **renovation spending as a share of total household disposable income** remained at

par with the 2010 level of 0.3%, below the EU-27 average of 0.9% in 2019.

Riga City Council coalition has committed to renovate and insulate 3,000 apartment buildings in Riga over the next nine years. Financial institution ALTUM will invest EUR 169.0 million in multi-apartment renovation projects by 2023. By 2050, the municipality plans to renovate and insulate 6,000 multi-apartment houses in the capital¹⁹¹.

In July 2021, the Latvian government announced a public loan program for multi-apartment building renovation and surrounding areas. The public loan will be made available to residents for works and space improvements in multi-apartment residential houses, including homes located in less developed regions, small towns or villages, or those which do not comply with commercial banks' lending policy. The total financing of the programme is EUR 31.0 million¹⁹².

According to the **EIB Investment Survey 2020** report, firms in the Latvian construction sector decreased their investments in 2020. The net balance of firms expecting to increase rather than decrease investment has declined by 37.0%. Further, 33.0% of construction sector firms reported investing less over the last three years. Also, the construction sector has the lowest share of firms reporting that they will abandon or delay investments (19.0%)¹⁹³.

In 2019, 217.6 km of national roads were constructed, and an additional 58.1 km of regional roads were restored¹⁹⁴. The total public financing for regional roads for 2016-2019 amounted to EUR 220.5 million, including the EUR 37.7 million received in 2019. During 2020, construction works were completed on 58.7 kilometres of state regional roads, supported by EU funds. Also, until the end of 2020, a total of 335.7 kilometres of state regional roads were planned to be constructed.

Additionally, Latvia conducted several works for restoration of infrastructure objects such as repairs of railway tracks and repairs of railway crossings in 2019. *SJSC Latvijas dzelzceļš* (a state-owned company that provides public railway infrastructure), with the co-financing of the

Cohesion Fund (CF), is implementing several infrastructure development projects, including projects for the modernisation of the most important railway hubs and railway passenger infrastructure modernisation projects¹⁹⁵.

Three agreements on co-financing of the Connecting Europe Facility (CEF) for the Rail Baltica project have been signed until 2020, resulting in the available funding in Latvia amounting to EUR 292.0 million¹⁹⁶.

The **Rail Baltica project** is expected to play a key role to integrating the Baltics with the core European rail network. The project which finally commenced in November 2020¹⁹⁷ is expected to be completed by 2025.

In April 2020, to contribute to the country's economy impacted by COVID-19, the ruling coalition in Latvia allocated EUR 75.0 million for road infrastructure projects. The amount will be used for mature projects that have lacked only funds until now¹⁹⁸.

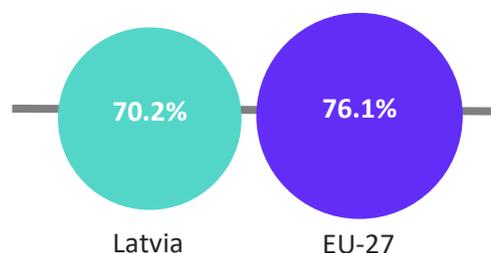
Latvia also benefited from investments from the **European Fund for Strategic Investments (EFSI)**. As of January 2021, financing under EFSI amounted to EUR 285.0 million and is set to trigger additional investments of EUR 1.4 billion. Under the infrastructure and innovation window, 11 projects have been approved, amounting to EUR 247.0 million, which are set to trigger EUR 907.0 million in total investments. Under the SME window, nine agreements have been approved, involving a total financing of EUR 37.0 million, and are set to trigger investments of up to EUR 500.0 million and benefitting 22,198 SMEs and mid-cap companies from improved access to finance¹⁹⁹.

Latvia's national road development strategy from 2020 to 2040 plans to rebuild more than 1,000 km of country's main roads with their current speed of 90 km/h into high-speed roads, with a maximum speed of 130 km/h. According to the plan, there will be three phases of activity. In the ten-year period from 2020 to 2030, 194.3 km of high-speed roads will be built, then in the five-year period from 2030 to 2035, there will be 224.0 km of high-speed roads built. The final period, from 2035 to 2040 involves the construction of no less than 637.5 km of highway²⁰⁰.

TO 2 – Skills

Latvia has taken several initiatives to strengthen the vocational education and training (VET) system. These include curriculum reform, development of education standards and qualifications, teacher training, work-based learning and apprenticeships. Despite these efforts, the **participation in upper secondary VET** stood at 38.9% in 2019, against the EU-27 average of 48.4%. Similarly, the **employment rate of recent VET graduates** in the country stood at 70.2% in 2020, below the EU-27 average of 76.1%²⁰¹.

Employment rate of recent VET graduates, 2020



Latvia is strengthening links between **work-based learning** and professional education. Support is being provided to businesses who offer additional training for staff, and online courses for the unemployed are partially reimbursed. In addition, the upcoming VET reforms will introduce more flexibility in acquiring and improving professional qualification²⁰².

By October 2019, 29 out of 38 VET schools and 469 companies in Latvia were implementing at least one work-based learning programme with 2,011 students participating²⁰³.

Furthermore, **adult participation in learning** (aged 25-64) stood at 6.6% in 2020, a drop from 7.4% in 2019 and well below the EU-27 average of 9.2%²⁰⁴. Latvia's main challenge remains attracting low-skilled adults to learning. The **adult participation in learning for the low-skilled** was even lower, standing at only 3.4% in 2019²⁰⁵. A recent study shows that most learning activities don't target the low-skilled specifically, and so don't reach them due to their lower overall motivation to take part in adult learning. To tackle this, a guide for municipalities on adult education governance is being prepared, and more targeted

education programmes for different target groups would be developed in 2021²⁰⁶.

The **Build Up Skills Latvia (Pillar I)** initiative contributes to enhancing the skill level of the construction workforce, particularly with respect to energy efficiency in buildings. As part of the project, an action plan has been set up to identify the needs for training of the construction workforce. The objective of the programme is to increase the skills and knowledge of the construction workforce in order to meet the Europe 2020 goals on energy efficiency. To this purpose, the programme introduces a number of training sessions targeted at the development needs identified in a status quo analysis²⁰⁷.

The Latvian Builders Association is also active in strengthening the skills of the construction workforce. Notably, amongst the association's goals is the active participation in the development of the industry-specific vocational training system. Furthermore, the association is one of the partners of the Build Up Skills project and provides seminars on construction-related topics²⁰⁸.

The Latvian Association of Civil Engineers provides a series of seminars to enhance the skills of its members, which cover a wide range of topics such as BIM, as well as regulatory aspects (construction law, procurement law, occupational health and safety, etc.)²⁰⁹.

Latvia has increased its focus on providing innovation management courses from educational institutions. One such example being that of Riga Business School (RBS) offering mini-MBA program on Innovation Management. The program, meant for company executives, aims at creating innovation specialists with a focus on business. Participants in the program include construction companies such as *Pavasars Housing Construction*, among others²¹⁰.

Latvia has developed its Education Development Guidelines 2021-2027 which identifies key policy initiatives that are critical for skills development. It aims to improve links between higher and professional education; introduce skills funds and individual learning accounts; and strengthen both work-based learning, and the recognition of qualifications and skills²¹¹.

The strategy for mitigating the consequences of the COVID-19 crisis aims to involve 165,000 people in adult education by 2023. The plan aims to reduce the share of low-skilled people in the workforce by improving the overall skills base (including in digital skills) of the population, while targeting investments in sectors with high export potential. Latvia is implementing a comprehensive reform of higher education which is expected to boost quality and efficiency and increase international competitiveness, with support from the Recovery and Resilience Facility²¹².

Latvia's Recovery and Resilience Plan plans to invest in digital skills, school infrastructure, and higher education reforms. Latvia is also piloting the "skills funds" approach for adult learners, as well as Individual Learning Accounts²¹³.

TO 3 – Resource efficiency / Sustainable construction

In Latvia, the implementation of Energy Performance of Buildings Directives (EPBD) is the responsibility of the Ministry of Economics, which develops and implements the national energy efficiency policy²¹⁴.

The current scheme **Increasing Energy Efficiency in Multi-Apartment Buildings 2014-2020** (*Energoefektivitātes pasākumi dzīvojamās ēkās: 2014-2020*), is aimed at promoting the renovation of multi-apartment buildings to improve their heat insulation. The scheme offers owners financial aid for energy efficiency improvement measures of their multi-apartment residential buildings. Financial support is provided in the form of grants, guarantees and loans. Grant amounts vary between 36-50% of the value of the loan taken out from a commercial bank (or between 25-35% in case of a loan provided by ALTUM), depending on the final heating energy consumption achieved after the works²¹⁵. Guarantees can cover up to 80.0% of a loan taken out from a financial institution, with the maximum guaranteed amount being set at EUR 3.0 million²¹⁶. Loans can be provided by ALTUM in case no loans are available from other credit institutions, with their amount not exceeding the cost of the eligible energy efficiency measures²¹⁷.

Activities supported by the scheme include renovation, reconstruction works, purchase and installation of high efficiency RE-based heat/hot water production equipment, etc. Upon completion of the renovation works, the annual heat energy consumption for heating must not exceed 90kWh/m²²¹⁸. The total budget of the programme is EUR 175.0 million over 2016-2023, of which EUR 150.0 million from the ERDF and EUR 25.0 million from the state budget²¹⁹.

As of January 2020, 881 project applications have been submitted within the support programme for the total expected ERDF funding of EUR 141.5 million for these projects.

The implementation of 155 projects is completed, and 56 projects are still under construction to improve energy efficiency of residential buildings²²⁰.

The ERDF financing for increasing energy efficiency of residential buildings stands at EUR 141.5 million, while for public buildings this amounts to EUR 94.6 million. In case of fulfilment of the performance framework, EUR 3.1 million is reserved²²¹.

The objective of energy efficiency measures for public (state and local government) buildings is to offer financial support to public building energy efficiency improvement projects. This will lead to an improvement in energy efficiency, smart energy management, use of renewable energy sources, reduce greenhouse gas emissions (GHG), thus reducing municipal costs of heat supply.

Under the energy efficiency improvement scheme, by March 2020, 129 project applications for the total funding of EUR 123.0 million from ERDF and state budget were approved²²².

Latvia currently has building stock of around 39,000 multifamily buildings with a floor area of around 55 million m². The current average energy intensity of such multifamily buildings is around 160-180 kWh/m², which is significantly higher than the 100 kWh/m² target of the **Latvian Energy Strategy 2030**²²³. In order to enable deep renovation of such buildings, a company called **Latvian Baltic Energy Efficiency Facility (LABEEF)** was set up in 2016.

LABEEF aims to modernise around 20.0% of these building stocks by 2022, translating to

annual avoided emissions of 21 kg CO₂e per m².

LABEEF supports energy service companies (ESCOs) that implement renovation measures in multifamily buildings based on energy performance contracting (EPC). The ESCO finances a building's renovation measures through a commercial bank and makes an EPC contract with the building owners. Once the renovation is complete, the LABEEF monitors and verifies the effectiveness of these renovation measures. If satisfactory, the LABEEF will, in turn, forfeit the EPC contract and continue to collect EPC receivables from building owners, until the entire investment is collected. This enables a least risk position for the building owners, with the execution risk staying with ESCO and financing risk with that of LABEEF²²⁴.

Finally, the **'Let's live warmer' information campaign** (*Informēšanas kampaņa "Dzīvo siltāk"*), which was already introduced during the previous programming period continued²²⁵. In March 2020, a contest "Most Energy Efficient Building in Latvia 2020" under the 'Let's Live warmer' campaign was announced²²⁶.

The transport and buildings sectors are the largest contributors to rising energy consumption. Latvia has set a renewable energy share of 50.0% in gross final energy consumption for 2030. For Latvia to achieve its energy efficiency target for 2030, it needs to break the trend of rising energy consumption²²⁷.

To achieve its 2030 energy efficiency target, Latvia should speed up building renovation. It involves scaling up current support programmes; reducing the administrative cost of building renovation, including through project standardisation and aggregation; and greater availability of low-cost, long-term financing and private capital to reduce the public cost of renovating private buildings²²⁸.

The long-term renovation strategy (required under the Energy Performance of Buildings Directive) should be used as basis for undertaking renovation measures with a view to decarbonising Latvia's building stock by 2050²²⁹.

The Recovery and Resilience Plan of Latvia allocated EUR 676.2 million towards the green transition. Of this, 46.0% of investments will target energy efficiency in multi-apartment buildings, central government, historical and municipal buildings and the business sector²³⁰.

The measures in the plan include an investment of EUR 57.2 million towards improving the energy efficiency of multi-apartment buildings and transition to renewable energy technologies; EUR 120.6 million for increasing energy efficiency in businesses. Further, the plan allocates EUR 29.3 million for improving municipal buildings by promoting the transition to renewable energy technologies²³¹.

TO 4 – Single Market

Latvia performed well with respect to the 2021 EU Single Market Scoreboard metrics, particularly in terms of Transposition of law, Internal Market Information System and Trade Integration in the Single Market for services²³².

With a transposition deficit of 0.8%, in line with its proposed target of 1.0% (EU-27 average stood at 1.0%). The average delay now stands at 8.8 months, which is above the EU-27 average of 7.4 months. Latvia now has eight overdue directives and only one is more than two years overdue, compared to the two that were last reported. Conformity deficit increased from 0.8% to 1.0%, compared to the EU-27 average of 1.4%. In terms of Infringements, Latvia reported 22 pending cases as compared to EU-27 average of 31 cases. The average case duration also reduced to 21.8 months (EU-27 average 37.3 months) from 25.7 months previously reported²³³.

Latvia performed moderately well in terms of Internal Market Information System, with three out of five indicators standing above the EEA average. Similarly, its trade integration for goods and services is well above the EU-28²³⁴ average. In 2019, trade integration for goods decreased while trade integration for services slightly increased²³⁵.

In addition, Latvia's performance in public procurement is satisfactory. Latvia's main difficulties reside in the share of procedures with a single bidder, i.e., the proportion of contracts awarded with only one bidder (32.0%) and public

procurement procedures negotiated without any call for bids, i.e., the proportion of procurement procedures negotiated with a company without a call for tender (8.0%). This means that there is less competition and therefore public procurers have less options to get better value for money. The low number of tenders in public procurement can be due to insufficient number of suppliers on the market. It can also be linked to the way the technical specifications are drafted and to the awareness of the importance of competition. Moreover, public procurers often lack capacity to prepare and carry out large and complex procurement projects effectively²³⁶. Further, more than a third of Latvian companies believe that corruption has prevented them from winning a public tender. Inter alia, unclear evaluation criteria, collusive bidding, tailor-made specifications for companies are other risk factors commonly identified by companies²³⁷.

In 2019, the Corruption Prevention and Combating Bureau (KNAB) raided several major construction companies as part of large-scale cartel investigations. The KNAB suspects involvement of at least 10 big construction companies of indulging in unfair trade practices such as agreeing prices in state procurements and bribing state officials. The officials, in turn, are suspected of accepting the bribes ranging from EUR 25,000.0 to several hundred thousand euros²³⁸. According to the KNAB, the legislative environment in the construction sector makes it particularly prone to ambiguity, misinterpretation and corruption, due to the complex, often overlapping and contradictory laws and regulations. Bribery is therefore often seen as a way to speed up the issuing of building permits and obtain preferential treatment²³⁹.

The Procurement Supervision Bureau is planning to publish information on low-value procurement, as well as on the real value of contracts (versus the initial ones) in their electronic procurement system to tackle the inefficiency and transparency issues existing in procurement procedures²⁴⁰.

Additionally, in response to the corruption issue, the government is taking several steps, including the adoption of the **Guidelines for Prevention and Combating Corruption for 2015-2020** (*Korupcijas novēršanas un apkarošanas pamatnostādnes*

2015-2020). One of the main priorities of the guidelines is the evaluation of the risk of corruption arising from laws and regulations governing construction procedures and housing policies and to develop proposals for the necessary changes in the legislative framework²⁴¹.

Finally, with respect to the implementation of **Eurocodes**, all Parts are published as National Standards, with 48 parts translated in the national language. The use of the Eurocodes is voluntary and National Regulations are used in parallel with EN 1990, EN 1991, EN 1992, EN 1995 and EN 1996 (except for EN 1994). Further, no National Annexes are published on 13 Eurocodes Parts and even the published ones are not available in English. Moreover, there is no regulatory framework that enforces the use of Eurocodes in public procurement²⁴².

The measures in the Latvia's Recovery and Resilience Plan aim to improve the quality, efficiency and integrity in its public procurement system, improve competition and strengthen capacities as well as to ensure availability of information regarding the execution and actual performance of public contracts concluded²⁴³.

TO 5 – International competitiveness

According to the World Bank Doing Business 2020 report, Latvia ranked 28th out of 190 countries in ease of trading across borders in 2019²⁴⁴.

As per the report, in Latvia it takes 2 hours and 24 hours to be documentary and border compliant, respectively. In terms of costs, business need to spend some 35 USD for documentary compliance and some 150 USD for border compliance²⁴⁵.

The **internalisation of construction products** in the Latvian construction sector has been consistently showing signs of growth since 2010. **The export values of all construction-related products** increased from EUR 591.6 million in 2010 to EUR 1.5 billion in 2020, marking an increase of 155.0% over time. Moreover, Latvia's share of exports of all construction-related products stood at 102.1% of the total value of production in 2019, below the 2010 level of 178.4% and above the

EU-27 average of 11.3%. This further improved to reach 116.2% in 2020.

Export value of all construction-related products between 2010 and 2020  **155.0%**

In the context of **inward FATS (Foreign affiliates statistics)**²⁴⁶, value added at factor cost and turnover in the manufacturing sub-sector increased by 108.8% and 104.7% between 2010 and 2018²⁴⁷. Similarly, in terms of number of persons employed, it experienced an increase of 46.5% over time. In the narrow construction sub-sector, value added at factor cost and turnover registered growth of 125.7% and 144.4% respectively, over the same reference period. The number of persons employed in the sub-sector also grew by 49.1% between 2010 and 2018. This trend of consistent growth in the value added at factor cost and turnover was also witnessed in the real estate activities sub-sector, which rose by 130.9% and 133.1% over time, respectively. Similarly, there was a 73.3% incline in the number of persons employed in the real estate activities sub-sector during the same reference period.

According to the SBA Fact Sheet report 2019, Latvia performs in line with the EU-28²⁴⁸ average in terms of internationalisation. The country performs particularly well in areas of information availability, advance rulings and formalities – automation²⁴⁹.

As per the report, Latvia is the third worst performer in border agency cooperation. Despite remaining below the EU-28²⁵⁰ average, the share of SMEs engaging in extra-EU online exports increased in 2015-2017²⁵¹.

The Latvian government launched the **'International promotion of competitiveness'** programme to support SME activities to enter foreign markets. Also, a one-stop-shop to access export support services is managed by Latvian Investment and Development Agency (LIDA). The agency also operates representative offices in foreign markets to ensuring strong links to major business partners and locations²⁵².

The international competitiveness support programme is available to SMEs and offers a wide range of services. The cluster programme, with EUR 6.2 million available from the European

Regional Development Fund, supports SME internationalisation and the development of new products and services. The programme has funded 15 clusters so far, with export volumes of their members increasing 3.5 times since 2014²⁵³.

Trade missions are organised by the **Investment and Development Agency of Latvia** (*Latvijas Investīciju un attīstības aģentūra* – LIAA) and the **Latvian Chamber of Commerce and Industry**. For instance, in 2018, construction trade missions to Sweden and Denmark took place²⁵⁴. 10 Latvian construction companies also participated in 'Nordbygg 2018', Scandinavia's largest construction industry trade fair, during which participants obtained business contacts, such as future cooperation business agreements²⁵⁵.

Typical obstacles faced by Latvian construction companies wishing to operate abroad includes

insolvency of foreign customers, late or non-payments as well as fluctuations in economic and political contexts of third countries, which can result in significant losses²⁵⁶. To this end, ALTUM offers both short-term and long-term **Export Credit Guarantees** (*Eksporta kredīta garantiju programme*), protecting exporters against the commercial as well as political risks. Precisely, the export credit guarantee covers up to 90.0% of the value of the export transaction in the case of commercial risks, and up to 95.0% for political risks. Moreover, the guarantee covers late payments of up to two years, and its value can amount up to EUR 2.0 million²⁵⁷. Guarantees are provided only for exports to third countries (excluding the EU, EEA, USA and other industrialised countries), such as all African, Asian, and South American states²⁵⁸.

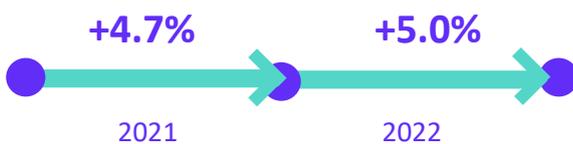
8

Outlook

After witnessing a decline of 3.6% in 2020 due to the COVID-19 pandemic, the Latvian economy is expected to revive and register growth driven by significant developments in exports, private consumption and investments.

Latvia's GDP is expected to grow by 4.7% in 2021 and then rise by 5.0% in 2022, reaching EUR 29.4 billion.

Expected GDP growth in 2021 and 2022



Similarly, the **volume index of production** in the broad construction sector is expected to increase by 6.9 ip in 2021, mainly due to a 3.7 ip and 6.6 ip declines in the construction of buildings and the construction of civil engineering in 2021, respectively.

In turn, the **turnover** in the broad construction sector is forecasted to grow by 5.9% in 2021, reaching EUR 9.6 billion. Similarly, the **total value added** of the broad construction sector is expected to increase by 6.0% in 2021, reaching EUR 3.0 billion in 2021.

Following the same trend, the number of **persons employed** in the broad construction sector is expected to increase by 6.2% to 153,818 in 2021. This incline is projected to come from the all the sub-sectors including the architectural and engineering activities (+9.9%), the narrow construction (+6.1%), the real estate activities (+5.7%) and the manufacturing (+5.6%) sub-sectors in 2021.

The housing market in Latvia is slowly growing with average apartment prices (particularly in the Riga region) rising. Moreover, the Recovery and Resilience Plan of Latvia includes investments in the energy efficiency of public and private buildings through a large scale renovation initiative. Additionally, in November 2020, the Construction Board of Riga City Council adopted a principle of a Green Corridor for sizeable development projects to assist more speedy advancement of the largest projects.

The **civil engineering** sector is expected to be driven by the government's focus on the development of transport infrastructure, particularly railway, with the EU's support. The development of the **Rail Baltica** project remains a priority. The construction, which started in November 2020, is expected to be completed in 2025 thereby boosting construction activity and investments. Further, the country has begun **investing in new trains** to increase the attractiveness of rail commutes and thereby increase the usage of public transport for commuting.

The reforms and investments in the Recovery and Resilience plan will help Latvia become more sustainable, resilient and better prepared for the challenges and opportunities of the green and digital transitions. The measures in the plan are expected to create jobs and promote the economic growth potential of Latvia.

The outlook for the Latvian construction sector remains positive particularly due to long-term infrastructure projects and investments in housing. Also, the projections of GDP recovery, increasing turnover and employment make the construction sector optimistic and promising.

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