

## Latvia – 20 Years After its Independence (or a trade-off?)

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Example of the former Soviet Union country Latvia

EVA MAURINA

[eva.maurina@inbox.lv](mailto:eva.maurina@inbox.lv)

Vienna University of Economics and Business, Vienna

Following famous words of my professor Anis Bajrektarevic that: “the Atlantic Europe is a political power-house (with the two of three European nuclear powers and two of five permanent members of the UN Security Council, P-5), Central Europe is an economic power-house, Russophone Europe is an energy power-house, Scandinavian Europe is all of that a bit, and Eastern Europe is none of it.”, I wanted to examine the standing of my own place of origin in the ‘new European constellations’. What happens to a country which suddenly is free to govern its own territory and people? What is the biggest fear? Is it the inability to satisfy its population or a threat from the former conqueror? Should a country opt for the ‘shock therapy’ or experience gradual changes? How to deal with the privatization of state-owned institutions? The following lines objectively question how the well-being of the East-European nation has changed in 20 years since the collapse of the Soviet Union, and in the course of the country’s integration into the EU. The authoress also answers whether a small country like Latvia can actually preserve both its political and economic sovereignty. On a bigger scale, the findings suggest that the well-being in the Latvian SSR was better than it is today, while others strongly disagree. Furthermore, the authoress concludes that Latvia had to sacrifice its economical sovereignty in order to preserve its political independence. Is any other choice conceivable, now or in future?

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The Republic of Latvia is a small country situated on the Baltic coast, in Eastern Europe. The estimated population of 2012 slightly exceeds 2 million. 60% of the population is ethnic Latvians, while a significant part, i.e. 27.3%, is Russian, demonstrating the legacy of the past. (Eurostat, 2012)

Just slightly over 20 years ago Latvia was under the Soviet rule and Communists were the ones who had the power to make decisions. The government of Latvia was not recognized by the international community. The nation itself experienced the Soviet economic and political system. In other words, during the time of occupation, Soviet Union introduced the Russian language into all aspects of everyday life. The intelligence was deported and a 5-year economy plan led to empty store shelves and starving people. Even though the productivity of the agricultural sector was high, all

harvest was transported to other Soviet territories. Nevertheless, industrial capacity was significantly improved, employment was high, education was for free, and most of the basic needs of the nation, such as housing, were satisfied.

Latvia's de facto sovereignty was recognized in 1991, and the first years of independence were spent developing a functioning state. The most difficult tasks facing the government were the creation of administrative bodies, reforms in the health and education sector and also a much needed shift from a planned economy to a market economy. When a political stability was reached and reforms initiated, the nation became increasingly concerned about the preservation of its statehood, so in 1995 the Latvian authorities adopted a statement defining foreign policy goals. They argued that the sovereignty can be strengthened through early integration into the European and world-wide security and political and economic structures. Latvia became a member state of the UNO in 1991, and joined the EU and NATO in 2004. (Jundzis, 2010)

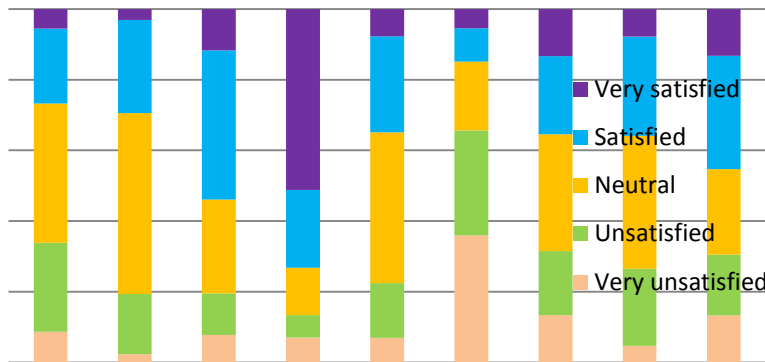
However, clear existence goals for the country were absent for the first decade of independence. While political sovereignty was at the top of the agenda, the majority of the society believed that the continuous increase of average human well-being and a long-term conservation of cultural heritage and Latvian language should be the goals. Even though the initiated reforms strived for improved living standards, similar to those of many Western countries, and increased individual freedom and protected rights, many question whether these reforms and integration into the EU have supported the achievement of one of the main goals – improved human well-being in Latvia. (Pabriks & Purs, 2001)

The Human Development Index, published by UNDP, assesses the long-term progress of human development regarding a long and healthy life, access to knowledge and a decent standard of living. The overall human development value in Latvia has been positive as the HDI value has risen from 0.693 (1990) to 0.805 (2011). Hence, the statistics rank Latvia among other high human development countries. (UNDP, 2011)

The majority of indicators, compared from 1990 to 2010, have followed a positive trend. Very often the development was slow during the first years of independence when the reforms were launched. Years later, in the 21<sup>st</sup> century, especially after Latvia's accession to the EU, human well-being improved more rapidly until the crisis in 2008 which resulted in its decrease. Nevertheless, improved absolute numbers should not be overestimated.

The previously centralized health sector has experienced notable reforms in the last 20 years; thus, the health condition of the inhabitants of Latvia has improved. The system was decentralized; hence, it entitled the foundation of private health care institutions; thereby, the health care became more accessible and more qualitative, as displayed in Figure 1. Furthermore, as the health expenditure of the state's budget has increased and the money from European funds can also be received, new technologies have been implemented. At the same time, more and more people are unable to afford the health care services due to the growing prices.

**Figure 1** Satisfaction of surveyed population of health care system (quality, price, accessibility) in Latvia during three different time periods

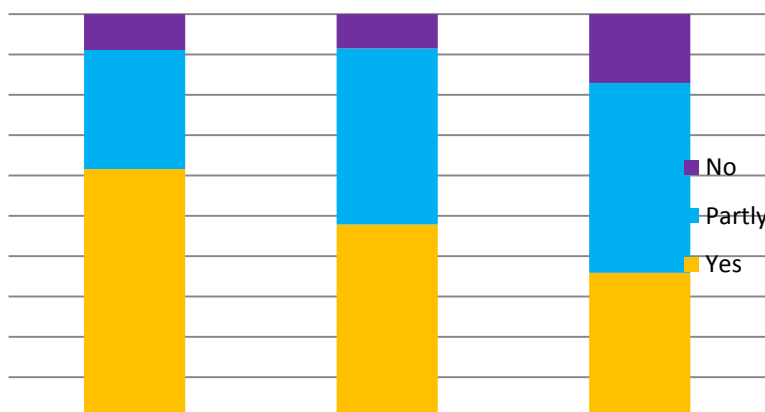


One can say that in the Soviet Latvia general care was easily accessible, but, when it came to a very specific treatment, it was challenging to find a proper physician. On the plus side, nowadays there are various physicians specialized in their fields; however, sick people might have to pay for treatment out of their own pockets in order to receive help without waiting. Consequently, many people are unsatisfied with prices of medical care in Latvia. On the bright side, the quality of care provided has definitely improved over the past 20 years.

Despite advancements and reforms in the health care system, demographics are in recession, which is a serious threat to the country's succession. A natural decrease of population due to lower fertility rates and a considerable migration outflow (especially within the first years of the collapse of USSR and after Latvia's accession to the EU) has contributed to the fact that the population has decreased from 2.67 million in 1990 to 2.24 million in 2010. As a consequence of smaller number of newborns and rising life expectancy, the population is aging, which imposes an increasing burden to the economically active part of the population to finance the retired people.

Unfortunately, not only is financing the retired people a serious issue, but also a complete burden to costs of primary goods which have increased. Thus, paying for one's own needs is becoming harder. The results of surveying 130 people suggest that in the Latvian SSR more than 60 per cent of the representative sample had funds to pay for all basic needs, such as food, housing, health care, education. Currently, less than 40 per cent of respondents have means to pay for all these needs. The proportion of people who can finance their needs just partially has risen from 29 to 47 per cent.

**Figure 2** Ability to finance the basic needs (food, education, health care, housing etc.)



Even though the absolute income has increased, the amount of people earning less than the subsistence minimum is rising, especially in the rural areas. It has to be mentioned that the content of Latvia's subsistence basket has not been revised since the first year of renewed statehood; thus, in reality, it does not contain all goods and services required for living decently. Furthermore, since the accession to the EU, prices have risen rapidly. For instance, total housing costs have increased significantly - in the USSR the rent and public utilities were highly subsidized by the government, whereas in 2005 the average housing costs amounted to 80 US dollars and 170 dollars in 2009. (Central Statistical Bureau of Latvia, 2011) These costs are borne by the private sector and the burden is becoming heavier due to lower income compared to the costs themselves. The situation is even worse, considering the fact that the proportion of overcrowded households is one of the highest within the EU. If people lived in and paid for apartments so that they were not characterized as overcrowded, the housing costs would be even higher compared to their income. Many people agree that they enjoyed much better housing conditions when they were a part of the communism country.

Similarly, the respondents of the survey mentioned that the Soviet Times guaranteed a certain security regarding employment. The majority of the economically active population was employed in the Latvian SSR compared to the 16 per cent unemployment level in 2009. (Central Statistical Bureau of Latvia, 2011) Even though the absolute remuneration was considerably lower in the Soviet times, it had more purchasing power. On the other hand, the labor market is becoming more knowledge intensive, and the workers – more educated and better specialized in their professions. Working conditions have also improved significantly, partly because of the regulations of the ILO.

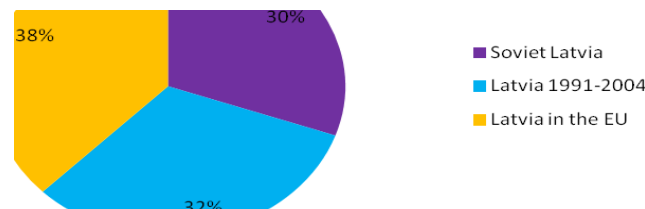
Transformation to knowledge-based economy has been supported by the development of the education system which is highly recognized by international surveys. High literacy and enrollment ratios are requirements for the nation to educate people who can efficiently participate in such natural resource-scarce economy. Smart people are one of Latvia's major assets. Nevertheless, the state has to further advance its education system, as remarks from the Soviet system are still present (books, teaching concepts, teachers etc.). Furthermore, the government has to understand the role of education expenditure. Ongoing budget cuts on education sector deteriorates the quality, as teachers and professors lose their motivation and pupils and students become more motivated to enroll in universities abroad.

The EU has provided significant advantages to the Latvian population, especially the youth which now is eligible to study permanently or temporarily at foreign universities, enjoying the same terms and conditions. Also, to the people who are entrepreneurial, open-minded and have a certain understanding of how to take an advantage of new business opportunities. The EU has also contributed to the modernization of hospitals, schools and the infrastructure. Furthermore, the EU sets standards as well as observes the development of human well-being; therefore, Latvia is motivated and under a pressure to demonstrate continuous advancement. As a result, the nation believes that the health and education systems have been improved and provide higher quality and accessibility. Nevertheless, given their income level, they are discontent with the prices of the tertiary education and specialized health care services. On the other hand, the Soviet government paid for housing, education and health care thus more resources were available for food items, leisure time, clothing, and also the employment ratio in the Latvian SSR was close to 100 per cent.

Therefore, there are people who believe that the communism times ensured better well-being. In addition, the equality within the population was much higher. However, as very often respondents mentioned, everybody was equally poor. Nowadays, the income polarization is a significant issue.

To complete the picture about human development trends in Latvia, which have followed different directions, it is worth referring to the final question of the conducted survey. It asked the respondents when, in their opinion, the well-being was the highest: in Soviet Latvia, in Latvia before joining the EU or in Latvia which is a member state of the EU. As the graph illustrates, the opinions vary – approximately every third of the respondent pool shares a different view, which simply further proves the finding that there are indicators which have improved along the movement towards Europe and there are aspects which so far the sovereign Latvia has not been able to offer its people as it was done by the USSR.

**Figure 3** The period of the highest human well-being in the opinion of the respondents



In order to succeed and reach the well-being benchmark set by the Union, first of all, a sustainable economic growth is needed, resulting in means which could shift into a social system. Additionally, the political powers have to cooperate with the society – finding a common ground, establishing goals that are seen as important and beneficial to the state itself and its population. It is of utmost importance to assure that the population lives decently, meaning, their basic needs, such as food, housing and health care, are satisfied. It should be the main goal of the government, thereby increasing the satisfaction and loyalty of the population to the state. Hence, the society would be willing to contribute to the development process, also by properly paying taxes.

Furthermore, lessons from the past should be learned. One of the main arguments for Latvia entering the EU was the economic advancement. As tariff and non-tariff barriers would be abolished, the trade between the EU and Latvia, especially the export originating from Latvia, would further increase. Productivity would be increased when people started working into more productive sectors. Furthermore, fixed and human capital investments were expected to be attracted via low labor costs, the adoption of EU legislations and additional privatizations. Investments would initiate an upward growth spiral. Nonetheless, skeptics argued that not every person residing in Latvia would benefit. Citizens who benefited the most would be young people, as they would enter better paid jobs, whereas the pensions of retired people would not increase as rapidly as the prices of goods and services. Latvian farms would face serious hardship due to a surplus in the market resulting from foreign competitors that are subsidized by their own governments. (Memo, 2000) They were right. The EU has suppressed the Latvian economy as a result of shutting down industrial plants, uncontrolled FDI inflows, enabling cheap credits, a significant inflation and price increase, and foreign companies creating a competition which

small Latvian companies and farmers cannot defeat. The smaller economy led to an increasing budget deficit, external borrowing and, finally, budget cuts demanded by the IMF and the EU, which have harmed the population as their adjusted income is not as high as living costs. One can say that Latvia traded a part of its economic sovereignty in order to ensure its political independence and the population is paying the price.

However, the people living in Latvia have been willing to pay this price for the sake of Latvia's sovereignty. In a survey, carried out by the national news portal TVNET, it was asked what the biggest threat to Latvia's sovereignty is. 53 per cent of the 5311 respondents indicated Russia and unknown money influx as the biggest danger. Contrary, just seven per cent perceive integration into the EU and NATO as imminent danger to Latvia's independence. (LETA, 2004) On one hand, if Latvia had not joined the EU, the threat imposed by a money influx would have been limited, but political independence would have been significantly less insured, suggesting that preservation of economic and political sovereignty is impossible for a small country like Latvia. In words of my former professor: *'difference between a dialectic and cyclical history is a distance between success and fall.'* (Bajrektarevic, 2012)

If Latvia had not joined the EU in 2004, it could have taken its time to develop the industries which correspond to the society's interests, not to the EU regulations. In addition, the migration outflow would have been smaller; therefore, people who are desperately needed in Latvia to cultivate the economy would have been available. Hence, the money influx into an economically stronger country would not have resulted in such a crisis. In this case Latvia would have experienced a slow and stable economic and social welfare growth. However, at some point in time, say 10 years later than the original accession date, Latvia should have joined the EU, as it is too small to be acting alone on the global stage. Latvia does not have significant raw materials or highly developed industries; thus, it lacks international power. Its needs and ideas are heard and pushed forward only in cases when stronger partners share the same interests. The EU is a platform where Latvia can find like-minded countries; therefore, it can find "allies" and together strive for developments and economic and political stability.

As for the Latvia's situation in the EU, in 2014, Latvia is expected to join the Eurozone if it fulfils the requirements. At the moment, it is believed that Latvia will succeed and be allowed to join, but opinions whether the country really needs to adapt the Euro vary. In September 2012, the public opinion on the Euro adaptation was record low, as only 13% of Latvians support the idea. Being a member of Eurozone would further disable Latvia to control its monetary policy and raise the prices which would not correspond to the income earned by a less productive workforce and industries compared to the ones in other EU states. Therefore, many experts believe that Latvia should postpone its adoption of the Euro until the future of the Eurozone is clearer and Latvia recovers from the economic recession and advances its production regarding productivity and value added.

Once Latvia substitutes its Latvian Lats for the Euro, it will be economically even more dependent from the EU and its regulations, but it would also present new trade opportunities for Latvian companies and therefore cultivate the economy and increase human well-being. The state would also become more creditworthy to foreign investors. Nevertheless, one should not forget how the FDI affected the economy three years ago. Swedish banks, which acquired Latvian banks, issued loans excessively and irresponsibly during the pre-crisis period; thus, fuelling unsustainable

and imaginary private consumption and property prices in the country. Sweden's position, demanding severe budget cuts that affected education and the health sector, was indicative of their fear of losses in case the loans issued decrease in value due to devaluation. Latvia has to be well prepared before welcoming Euro as a replacement for its Lats, which was only reintroduced in 1993.

**Keywords:** Latvia, European Union, Soviet Union, political sovereignty, economic sovereignty, independence, human well-being, human development, Human Development Index

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