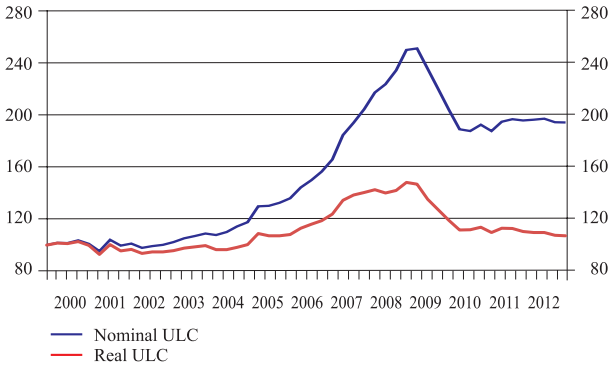
3. In Focus

Labour market revival broadens the base for sustainable economic development

Real wages have recovered, posting 1.5% year-on-year growth in Q2 2012, the strongest since the wage-productivity gap has closed. Together with the increase in employment this provides a solid foundation for the private consumption recovery.

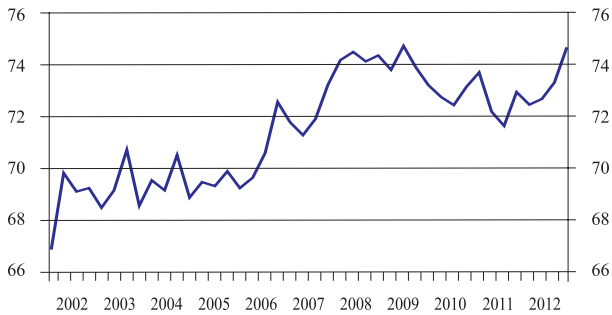
The purchasing power of wages has improved as a result of the dropping inflation, whereas the nominal wage rise has remained moderate and stable at 3.7% year-on-year. The wage growth is sustainable and does not create an upside risk to inflation as it is broadly in line with the labour productivity developments. Thus, Latvia's commitment to fulfil the Maastricht criteria in spring 2013 is not under major challenge. The return to competitiveness observed during the recent years has been sustainable: overall, unit labour costs have lost 23% and 28% in nominal and real terms respectively compared to their peak in the second half of 2008, and the year-on-year growth is still negative. Sizeable competitiveness gains have promoted a significant increase in Latvia's export shares in the imports of other countries.

ULC index
(2000 Q1 = 100; seasonally adjusted)



Source: Bank of Latvia calculations based on Eurostat data

Participation rate
(% of population aged 15-64)



Source: Bank of Latvia calculations based on the CSB data

As a result of robust labour productivity development, this was not a jobless economic recovery. Employment started to recover in Q2 2010 (two quarters later than GDP) and, according to the Eurostat national accounts concept, Latvia ranked second among other EU Member States in terms of the pace of employment creation in Q2 2012. Strong employment growth is confirmed by all available statistical data sources (Labour Force Survey, Business Survey, National Accounts, State Revenue Service data) and comes, almost entirely, from the private sector. However, both the closure of a major part of the public temporary jobs programme in Q4 2011 and Q1 2012 as well as the strong growth in the economic activity have resulted in a sticky unemployment rate that (disregarding the employment data) might be wrongly interpreted as a jobless recovery.

Real wage improvements in combination with higher employment have increased the real wage bill, thereby notably accelerating the retail turnover, with private consumption becoming a significant GDP growth driver recently. Given the deteriorating business confidence and the economic prospects of Latvia's main trading partners, broadening of the base for sustainable economic development requires the revival of private consumption.