

SABIEDRĪBA CITAI POLITIKAI

PAK LAIĀM PĀRMAIŅĀM!

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Viedokļi



Gatis Kokins
Sustainable Business
Choice in the High-Cost
Economy



Atis Lejiņš
Aicinājums Latvijas
oligarhiem!



Gatis Kokins
DB :: "Latvijā kopš padomju
gadiem ir būtiska
strukturālā bezdarba
problēma"



Atis Lejiņš
23. augusts: pārdomas par
nākotni



Gatis Kokins
Pilsoni



Gatis Kokins
Pirmā aktīvākas monetārās
politikas bezdelīga no
Latvijas Bankas? [1]



Gatis Kokins
Par Latvijas valsts virsmērķi
[1]



Jānis Ošlejs
Nevienlīdzība aizskar dziļi,
līdz kaulam



Valdis Krastiņš
Es apskaužu grieķus!



Gatis Kokins
Lafērs iztraucēts [1]

Gatis Kokins

| vairāk par autoru



SCP

Sustainable Business Choice in the High-Cost Economy

15.10.2010

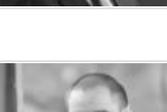
Latvia's transition to market economy was not a subject of public discussion in early nineties. Post-war generation was starving for capitalism during last 45 years and was ready to accept changes at any cost. Total market liberalization was applauded, thus making sure that planned economy will have no ground to return. Latvia installed free capital movement principles a way before joining EU and removed prohibitive import barriers opening local market for international competition. This, subsequently, was well prized by foreign investors and growing FDI started to offset negative trade balance of the country.

However, already after Russia's default in 1998 it become apparent that industrial production in Latvia is not increasing at the sufficient pace. Service, especially financial intermediation, was booming. Country with no tax on capital gains was slowly transforming into speculative paradise and tax heaven for rich.

Currency board arrangement maintained by the Bank of Latvia has ensured stable local currency - Lats, but this also has led to excessive borrowing in euro (90% of loan portfolio) – it was cheaper and no currency risks were foreseen by households. At the same time Bank of Latvia had no instruments to raise interest rates for euro loans and thus – no possibilities to apply brakes on mortgage lending. Massive inflow of cash (commercial banks doubled international borrowing in 2006-2008) was not digested by weak Latvian economy: CPI skyrocketed, followed by wages increase. Real exchange rate increased by 30% and industrial production slumped – products were not competitive globally due to their high cost base. Investors were tempted to invest in real estate (returns were higher and tax rate was close to zero), rather than in industrial production.

Collapse of Lehman Brothers and international money markets in 2008 revealed frightening truth: Latvian economy is "naked". Creditors suddenly were unwilling to finance world-record 25% of GDP current account deficit based on consumption of imported goods financed by consumer lending. Latvia avoided default by turning to IMF for assistance and faced the most severe adjustment in EU – GDP per capita dropped from 52% of EU average in 2007 to 42% in 2010.

At the same time real exchange rate was not adjusted during the crisis: it is still around 30% higher than in 2006. Desired "internal devaluation" with deflation and decrease of wages did not happen and adjustment went along the easiest path – through high unemployment (peaking at 21%).

	Gatis Kokins Latvijas Industrializācijas Programma [4]
	Gatis Kokins Delfīns un bute [3]
	Jānis Ošlejs Plūdi un atplūdi [3]
	Gatis Kokins Elegants veids cīņai pret apkāršņu algām un Neo [5]
	Gatis Kokins Advokāti nākotnes nodokļu stratēģijām
	Gatis Kokins Lafērs un divas Aīšas [4]
	Gatis Kokins Esi vienkāršāks, un tauta tev sekos?
	Guntis Stirna Rīga – zīmols, kura nav [3]
	Jānis Ošlejs Atdot vai neatdot [14]

Aldis Greitāns
Par nelegālo nodarbinātību

1/11



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Pievienot

Today optimism is back in the neighbouring Nordic countries and foreign investors' mood seems to be bullish again. Latvian business confidence index also has turned back to positive due to prudent and sustainable fiscal policy of the new government. Latvia obviously is entering next business cycle, but without sufficiently adjusted cost base, i.e. country is still not competitive to experience hype for industrial production. Government has installed capital gain tax, has increased consumption taxes, therefore, hopefully, this business cycle will not turn into next speculative bubble driven by real estate price appreciation and consumption. But due to high price level (70% of EU average) Latvia will not be able to compete with Poland (55% of EU average) in attraction of global producers to establish their cost sensitive production facilities here.

With such a simplistic monetary policy Latvian industries can be competitive only in business branches with extremely high value added, where cost fraction is an insignificant part of sales price. This can be found in high-tech areas, ITC sector and also by developing so called "design economy".

As an example for Latvia's further growth potential we can look at *Lattelecom's* success at installing GPON fibre-to-the-home (FTTH) **500 Mbps high-speed broadband internet**. This service now is available to 49% of households, making **Latvia #2 in the world** (after South Korea) in terms of average internet download speed. Such a groundbreaking bandwidth enables developers and consumers to develop and use interactive IP TV technologies, cloud computing applications and solutions – in few years GPON availability will become a competitive advantage for the whole country! And when you are at the frontier of the cutting edge technologies, high real exchange rate is not the biggest obstacle.

Probably, the only choice for successful Latvian business is a global excellence. The excellence of mastering cutting-edge solutions may also secure a good deal of the Latvian economy's future competitiveness on the global market.