

- Euro area industrial production up by 1.5 % in November 2016
- British government considers GBP 1,000 levy for EU guest workers after BREXIT
- Baltic States: new light-vehicle registrations +14 % in 2016

1 Key economic indicators

Key Economic indicators of Latvia							
Variable / Date	2014	2015	2016	2016			
				Q1	Q2	Q3	Q4
Real sector							
Real GDP, yoy, %, sca	2.1	2.7	-	1.2	0.8	0.3	-
Nominal GDP per capita, EUR thou., nsa	11800	12300	-	2800	3200	3300	-
Industrial production index, yoy, %, ca	-0.9	3.5	-	3.6	4.4	1.4	11,0 (Nov)
Volume index of construction production, yoy, %, ca	7.9	-1.2	-	-19	-19	-22	-
Retail trade, deflated turnover, yoy, %, ca	3.6	5	-	2.1	2.4	1	4,6 (Nov)
Gross fixed capital formation, yoy, %, sca	0.1	2.8	-	-14.9	-25	-26.3	-
Prices							
GDP deflator, sca	1.3	0.4	-	0.7	0.5	-0.3	-
HICP, eop, yoy, %	0.3	0.4	-	-0.6	-0.6	0.5	1.2 (Nov)
PPI, eop, yoy, %	0.3	-1.5	-	-3.2	-3.5	-1.7	-1,6 (Nov)
House price index, yoy, %, eop	-4.5	6.6	-	7.1	10.3	-	-
Labour market							
Minimum wage, EUR, biannual, eop	320	360	370	370		370	
Unemployment rate, sa, LFS, %, sa	10.8	9.9	-	9.9	9.5	9.8	9.6 (Nov)
Real labour productivity per hour worked, yoy, %, nsa	2.9	3	-	2.7	0.9	2	-
External trade & external position							
Exports of goods, yoy, %, sca	3.9	2.6	-	0.5	2.8	2.4	-
Imports of goods, yoy, %, sca	0.5	2.1	-	5	6.5	1.2	-
Current account balance, % of GDP, sca	-1.9	-1.1	-	0.0	0.3	1.7	-
FDI inflow, % of GDP, nsa	2.5	2.5	-	-2.0	-2.7	3.6	-
Economic sentiments							
Economic sentiment indicator, SA	102.9	102.2	103.9	103.6	104.7	104.7	103.9
Industrial confidence indicator, SA	-7.1	-6.2	-1	-5.4	-3.2	-3.3	-1
Construction confidence indicator, SA	-21.5	-31.7	-24.4	-32.2	-36.7	-30.2	-24.4
Retail confidence indicator, SA	7.5	3.5	4.5	9.6	7.9	7.8	4.5
Services Confidence Indicator, SA	2.7	0.8	6.5	5.3	7	5.5	6.5
Consumer confidence indicator, SA	-7.5	-8.4	-18.3	-9.5	-8.7	-7.5	-18.3

[Source: Eurostat, Bank of Latvia, author's calculations]

2 Economic news of past week

<p>Euro area industrial production up by 1.5 % in November 2016</p>	<p>In November 2016 compared with October 2016, seasonally adjusted industrial production rose by 1.5 % in the euro area (EA19) and by 1.6 % in the EU28, according to estimates from Eurostat. In October 2016 industrial production rose by 0.1 % in the euro area, while it fell by 0.1 % in the EU28. In November 2016 compared with November 2015, industrial production increased by 3.2 % in the euro area and by 3.1 % in the EU28. (Eurostat)</p>
<p>British government considers GBP 1,000 levy for EU guest workers</p>	<p>The British government is considering charging employers GBP 1000 (EUR 1200) a year for every skilled worker they recruit from the European Union after the UK leaves the bloc. Britain has already approved such a levy for foreign workers from non-EU nations. It takes effect in April 2017. Currently, citizens of the 27 other EU member states have the right to live and work in Britain. But that freedom of movement is likely to end once Britain quits the bloc. (baltic-course.com)</p>
<p>Baltic States: new light-vehicle registrations +14 % in 2016</p>	<p>New light-vehicle registrations in the Baltic States increased 14.1 % to 69000 units in the full year 2016. All three countries reached positive full-year results: Estonian market still remains obvious leader by volume, but its growth rate was the slowest (+9.7 % to 27350 units), Lithuanian market outpaced the others by growth rate once again and was 2nd by volume (+18.7 % to 23075 units), Latvian market was second by growth rate and the smallest by volume (+15.3 % to 18575 units). (baltic-course.com)</p>
<p>Registered unemployment in Estonia 4.5 % in December 2016</p>	<p>Last year the unemployment rate in Estonia totaled 4.5 %, which is 0.1 percentage points (ppt) more than in 2015. At the end of December 28438 people were registered as out of work, which is 4.5 % of the labor force. Of them 5328 were with limited capacity for work. Recipients of the unemployment insurance benefit numbered 10239 in December, making up 32 % of the registered jobless. The average benefit per calendar month was 433 euros and the sum total disbursed was roughly 3.8 mln euros. The basic unemployment allowance of 137 euros a month was paid to 7020 persons, 22 % of the total number of registered jobless. (baltic-course.com)</p>
<p>Registered unemployment in Latvia 8.4 % in December 2016</p>	<p>The registered unemployment in Latvia increased by 0.4 percentage points (ppt) in December 2016 to 8.4 %. In early December last year there were 75348 people registered with the State Employment Agency as jobless but their number increased by 3,009 people to 78357 jobless at the end of the month. At the end of November 2016, registered unemployment in Latvia was 8 %, but in October and September the jobless rate stayed at the same level – 7.9 %. (baltic-course.com)</p>
<p>Latvian Finance Ministry for greater tax progressivity</p>	<p>The Finance Ministry is ready to move towards a greater progressivity of the tax system. The nontaxable minimum income already ensures certain progressivity, but the Finance Ministry is ready to move towards even greater progressivity in its proposals for Latvia's new tax strategy. As it is about to work out its new tax strategy, Latvia has to choose between two alternative paths - either to differentiate personal income tax rates or reform the nontaxable minimum income. The current nontaxable minimum income system is rather complicated and a differentiated nontaxable minimum might be simplified by setting constant rates and figures. (baltic-course.com)</p>

3 Economic insights

In United Kingdom European Union membership referendum on 23rd June 2016, 52 % of UK voters decided to vote for leaving the EU. UK Government intends to invoke the Article 50 of the Treaty on European Union (as formal starting of the procedure withdrawing from the European Union) at the end of first Quarter of 2017.

The Sunday Times reported, that Prime Minister Theresa May is to present her plans for a "hard Brexit" in a speech scheduled for Tuesday (2017-01-17) in London. Apparently May will prepare to withdraw from tariff-free trade with the region in return for the ability to curb immigration, strike commercial deals with other countries, and escape the jurisdiction of the European Court of Justice.

Markets reacted to the idea of UK leaving the EU, and the following events by selling British Pound (Ssince end-2015), as can be seen in chart below.



Figure 1: British Pound to Euro exchange rate. Source: Yahoo Finance

There are different channels how weakening British pound may affect Baltic economies:

1. Decreasing value of the British Pound makes imports from UK to Euro area countries cheaper, but by weakening the British purchasing power - exports more expensive. That could boost the imports from UK to euro area countries, but reduce the exports.
2. Due to many emigrants from the Baltic countries working in UK remittances from UK to euro area countries could fall in value, due to falling GBP to EUR exchange rate.
3. Until UK leaves the EU, there might be a stronger emigration from the Baltic countries to UK, due to lack of information about the future rules on immigration policy in UK.

Only the change in trade patters will be briefly discussed in this bulletin (see next page).

Variables/Date	Estonia				Latvia				Lithuania			
	IMP	EXP	NET	SHARE OF TT	IMP	EXP	NET	SHARE OF TT	IMP	EXP	NET	SHARE OF TT
Jan.-Oct. 2014	376.1	242.6	-133.5	2.9%	273.1	429.0	156.0	3.5%	946.4	769.5	-176.9	4.1%
Jan.-Oct. 2015	283.6	277.6	-6.0	2.7%	245.9	456.6	210.7	3.5%	615.2	858.1	242.9	3.7%
Jan.-Oct. 2016	279.9	238.5	-41.4	2.5%	250.2	473.6	223.4	3.7%	540.9	772.5	231.6	3.4%
Change Jan.-Oct. 2015 to Jan.-Oct. 2014	-24.6%	14.4%	-95.5%	-4.6%	-9.9%	6.4%	35.1%	0.6%	-35.0%	11.5%	-237.3%	-10.5%
Change Jan.-Oct. 2016 to Jan.-Oct. 2015	-1.3%	-14.1%	594.4%	-9.6%	1.7%	3.7%	6.0%	6.0%	-12.1%	-10.0%	-4.7%	-7.3%

Table 1: Trade patterns of the Baltic countries with the UK. Source: Eurostat, author's calculations

- Imports:

The speed of imports-decrease has slowed in all three Baltic states. In Jan. - Oct. 2015 compared to Jan. - Oct. 2014 Estonian imports decreased by 24.6 %, Latvian imports decreased by 9.9 % and Lithuanian by – 35 %. In Jan. - Oct. 2016 compared to Jan. - Oct. 2015 Estonian imports decreased only by 1.3 %, Lithuanian imports decreased only by 12.1 %, while Latvian imports increased by 1.7 %.

Slowdown in decrease of imports from UK to Estonia and Lithuania, and even an increase of imports from UK to Latvia support the theory, that EUR gaining strength against the GBP makes imports in euro area countries cheaper and thus increases the demand for British goods.

- Exports:

In Jan. - Oct. 2015 compared to Jan. - Oct. 2014 Estonian exports increased by 14.4 %, Latvian exports increased by 6.4 % and Lithuanian by – 11.5 %. In Jan. - Oct. 2016 compared to Jan. - Oct. 2015 Estonian exports decreased by 14.1%, Lithuanian exports decreased by 10 %, while Latvian exports increased only by 3.7 %.

Slowing speed of exports in Latvia, or even negative change in exports in Estonia and Lithuania are in line with the expectations of decreasing purchasing power of UK. Decreasing purchasing power makes imports from euro area countries more expensive and thus reduces the British demand.

- Trade with UK as share of total trade

Trade with UK as share of total trade is defined as total imports and exports to UK divided by total imports and exports to the world.

Trade with UK as share of total trade in Estonia has been on decrease, but the pace of the decrease has increased: from -4.6 % in Jan. - Oct. 2015 compared to Jan. - Oct. 2014 to -9.6 % in Jan. - Oct. 2016 compared to Jan. - Oct. 2015. In Lithuania, trade with UK as share of total trade has been decreasing as well, though the speed of decrease has not increased as in Estonia. In Jan. - Oct. 2015 compared to Jan. - Oct. 2014 trade share decreased by 10.5 % , but only 7.3 % in Jan. - Oct. 2016 compared to Jan. - Oct. 2015. On the other hand, Latvian trade with UK as share of total trade has been increasing and has additionally gained in pace. In Jan. - Oct. 2015 compared to Jan. - Oct. 2014 trade share gained 0.6 %, and in Jan. - Oct. 2016 compared to Jan. - Oct. 2015 trade share increased by 6.0 %.

There is a clear need for further analysis and Brexit-effects estimation for the Baltic states. Severe effects for the trade can be expected in the future, if UK chooses the "hard Brexit" scenario . That would affect the profitability of companies in trade sector in specific, and employment and economic growth in general.